Schulte Roth & Zabel Webinar

Meeting Investor and Stakeholder Expectations Under the Conflict Minerals Rule

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Patricia Jurewicz
Director
Responsible Sourcing Network

Azadeh Sabour
Associate Director, Advisory Services
Sustainalytics

Andrew Arriaga
Research Analyst
Responsible Sourcing Network
The Problem

- Democratic Republic of the Congo (DRC)
- Large variety and abundance of minerals
- Eastern DRC in conflict since the mid-1990s
  - Ethnic tensions
  - Border disputes
  - Over 5 million casualties
- Minerals funding armed groups
  - Up to $185 million/yr
  - Conflict Minerals = Tin, Tantalum, Tungsten, Gold
RSN Response

- **July 2010**: Dodd-Frank Act became law
- **2010-2011**: RSN coordinated 5 MSG consensus comments; cited in the final SEC rule 48 times
- **Jan 2013**: RSN published *What’s Needed: An Overview of Multi-Stakeholder and Industry Activities to Achieve Conflict-Free Minerals*
- **Sept 2013**: RSN and the Enough Project released *Expectations for Companies’ Conflict Minerals Reporting*
- **2014**: RSN released *Expectations Shortlist* with endorsement by 26 NGOs and SRIs
- **2015**: RSN released *Indicators Shortlist* and *Longlist, Step-by-Step Guidance*
Mining the Disclosures

- Formalization of relationship with Sustainalytics
- Focus on the Investment Community
- Development of 18 Indicators
- Quantitative analysis of Social Performance
- Inclusion of public company content in addition to SEC filings
- Development of a Baseline
- Focus on a Sample Group
Sustainalytics is the largest independent investment research provider dedicated to RI and ESG research.

- **200 staff**: 100+ ESG analysts with multidisciplinary and industry expertise.
- **Offices in 14 locations**: headquartered in Amsterdam, with offices in Toronto, Boston, New York.
- **Clients**: 250+ institutional clients globally (e.g. financial institutions, asset managers, asset owners, pension funds, etc.)
Sustainalytics: What We Do

For over 20 years, we have been helping clients process environmental, social and governance (ESG) information into insightful, value-added analysis to enable more informed investment decisions:

- Sustainalytics supports investors around the world with the development and implementation of RI/ESG integration approaches, across investment strategies and asset classes.

- Our standard research framework for evaluating ESG performance of public companies is comprised of roughly 170 core and sector-specific indicators, coupled with a sector focused weight matrix.

- We offer broad coverage of major global markets and flexible research tools, including ESG reports on 4,000+ public companies and controversy assessments for over 10,000 public companies.
How Investors Use ESG Research

- Active Ownership/Engagement
- Positive/Negative/Norms-based Screening
- ESG Integration
- Positive Thematic and Impact investing
Rapid Growth of ESG/RI

76% Increase in AUM incorporating ESG between 2012-2014 in the United States

- In 2014, AUM incorporating ESG reached USD 6.57 trillion – accounts for 1 of every 6 dollars invested in the US

- Globally, ESG incorporation is also experiencing a rapid growth rate of 61% from 2012-2014

- US market is the fastest growing

- Evidence of increasing sophistication in how ESG information is being embedded into investment processes

- The number of signatories to the Principles for Responsible Investment (PRI) has exceeded 1200 in 2014 - AUM backing these signatories is USD 45 Trillion.

Sources: US SIF, Global Sustainable Investment Alliance, and unpri.org
What is Driving ESG Considerations?

Primary Drivers:

- **Regulatory Risk** (e.g. Section 1502 of Dodd-Frank Act)
- **Search for Materiality** - Growing body of evidence to support the recognition that ESG issues can be financially material. Academic and sell-side research strongly supports this view.
- **Alignment with Mission/Contribution to Sustainable Development**

Growing Focus on Social Impact – the “S” in ESG

- Sustainalytics has observed a growing trend among investors that are focused on labour and human rights impacts.
- Sustainalytics has contributed to a number of social impact initiatives that rank corporate performance:
  - **Access to Medicine, Access to Seeds, Access to Nutrition**
  - **Ranking Digital Rights** (measuring freedom of expression and privacy practices of major telecom and internet companies)
  - **Humanity United and 12 partners’ “KnowTheChain” Campaign** (which sheds light on the issue of slavery and human trafficking in the supply chain)
Sustainalytics’ Framework

Defining Methodology
- Define indicator scope, scoring methodology, and weight matrix
- Determine sample group of companies to research

Stakeholder Engagement
- Engage stakeholders to solicit feedback on key considerations of the methodology

Methodology Refinement
- Apply any necessary improvements

Data Gathering
- ESG analysts research sample group of companies

Data Analytics
- Project team aggregates data and draws insights
Sustainalytics offered RSN guidance on indicator scope, scoring methodology, and weight matrix development:

- RSN designed 18 performance indicators, divided among four Measurement Areas
- Framework designed to be scalable and to aim for objective assessments

1. **Measurement Area 1**
   - Assessing Exposure and Responding to Risk
   - Investors can be confident in the filer’s risk assessment.

2. **Measurement Area 2**
   - Policies and Management Systems
   - There is internal buy-in and commitment throughout the company to engage in substantive conflict minerals supply chain due diligence.

3. **Measurement Area 3**
   - Transparency and Reporting
   - The filer is reporting thoroughly on its due diligence.

4. **Measurement Area 4**
   - Promoting a Conflict-Free Minerals Trade
   - The filer’s approach to risk management is rounded out by an understanding of its impact on communities.
Sustainalytics offered RSN guidance on defining a sample group of companies to be researched for the pilot study:

- Among 1300+ SEC filers, a sampling of companies (51) was chosen to provide the most meaningful insights.

- Sample group consisted of:
  - The 3 largest companies by market cap/per industry
  - Industries with highest exposure to conflict minerals (17)

**Three criteria were used to determine high exposure industries:**

1. Company’s product lines contained mostly 3TG minerals, or, a little 3TG was used, however, in vast quantities of products (e.g. automobiles).
2. Industry faces significant reputational risk for its exposure to conflict minerals, through suppliers, products/services, or through stakeholder activism.
3. Companies in the industry face higher reputational risk due to brand recognition.
Sustainalytics’ industry analysts supported RSN in determining the following 17 high exposure industries, which fall in 6 sectors:

<table>
<thead>
<tr>
<th>Information Technology</th>
<th>Industrials</th>
<th>Consumer Discretionary</th>
</tr>
</thead>
<tbody>
<tr>
<td>Communications Equipment</td>
<td>Aerospace and Defense</td>
<td>Auto Components</td>
</tr>
<tr>
<td>Electronic Equipment, Instruments, and</td>
<td>Electrical Equipment</td>
<td>Automobiles</td>
</tr>
<tr>
<td>Components</td>
<td>Industrial Conglomerates</td>
<td>Household Durables</td>
</tr>
<tr>
<td>Semiconductors and Semiconductor Equipment</td>
<td>Machinery</td>
<td>Leisure Products</td>
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<tr>
<td>Technology Hardware, Storage, and Peripherals</td>
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<td>Specialty Retail</td>
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<td>Textiles, Apparel, and Luxury Goods</td>
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<tr>
<td>Materials</td>
<td>Healthcare</td>
<td>Energy</td>
</tr>
<tr>
<td>Containers and Packaging</td>
<td>Healthcare Equipment and Supplies</td>
<td>Energy Equipment and Services</td>
</tr>
</tbody>
</table>

Figure 3: High Exposure Industries Index
Data Gathering

Sustainalytics’ ESG analysts reviewed publicly available sources to assess performance of the sample group in RSN’s 4 measurement areas.

<table>
<thead>
<tr>
<th>Filer</th>
<th>Industry</th>
<th>Pilot Study Sources Used by Analysts</th>
</tr>
</thead>
<tbody>
<tr>
<td>3M Co.</td>
<td>Industrial Conglomerates</td>
<td>Form SD: SD, Conflict Mineral Report: CMR, Company Website: Web, Other Public Reporting: Other</td>
</tr>
<tr>
<td>ABB Ltd.</td>
<td>Electrical Equipment</td>
<td>Form SD: SD, Conflict Mineral Report: CMR, Company Website: Web, Other Public Reporting: Other</td>
</tr>
<tr>
<td>Abbott Laboratories</td>
<td>Healthcare Equipment and Supplies</td>
<td>Form SD: SD, Conflict Mineral Report: CMR, Company Website: Web, Other Public Reporting: Other</td>
</tr>
<tr>
<td>Apple, Inc.</td>
<td>Technology Hardware, Storage, and Peripherals</td>
<td>Form SD: SD, Conflict Mineral Report: CMR, Company Website: Web, Other Public Reporting: Other</td>
</tr>
<tr>
<td>Ball Corp.</td>
<td>Containers and Packaging</td>
<td>Form SD: SD, Conflict Mineral Report: CMR, Company Website: Web, Other Public Reporting: Other</td>
</tr>
</tbody>
</table>
Sustainalytics’ data team developed an analytics tool to help RSN compare results on a company and industry level basis, so RSN could draw meaningful insights for its report – *Mining The Disclosures.*

<table>
<thead>
<tr>
<th>Company Name</th>
<th>Industry</th>
<th>Percentile Rank</th>
<th>4 Theme Level Scores</th>
</tr>
</thead>
<tbody>
<tr>
<td>Intel Corporation</td>
<td>Semiconductors and Semiconductor Equipment</td>
<td>100%</td>
<td>0.00</td>
</tr>
<tr>
<td>QUALCOMM Incorporated</td>
<td>Communications Equipment</td>
<td>98%</td>
<td>0.00</td>
</tr>
<tr>
<td>Apple Inc.</td>
<td>Technology Hardware, Storage and Peripherals</td>
<td>96%</td>
<td>0.00</td>
</tr>
<tr>
<td>General Electric Company</td>
<td>Industrial Conglomerates</td>
<td>94%</td>
<td>0.00</td>
</tr>
</tbody>
</table>
Evaluating 2014 Reports: Four Measurement Areas

Measurement Area 1
Assessing Exposure and Responding to Risk
Investors can be confident in the filer’s risk assessment.

Measurement Area 2
Policies and Management Systems
There is internal buy-in and commitment throughout the company to engage in substantive conflict minerals supply chain due diligence.

Measurement Area 3
Transparency and Reporting
The filer is reporting thoroughly on its due diligence.

Measurement Area 4
Promoting a Conflict-Free Minerals Trade
The filer’s approach to risk management is rounded out by an understanding of its impact on communities.
Assessing Exposure and Responding to Risk

Can investors be confident in the filer’s risk assessment?

Performance Indicators

1) Filer described products.
2) Filer described Reasonable Country of Origin Inquiry.
3) Filer used a template.
4) Filer engaged suppliers.
5) Filer verified survey responses.
6) Filer engaged smelters or refiners.
Policies and Management Systems

Is there internal buy-in and commitment throughout the company to engage in substantive conflict minerals supply chain due diligence?

Performance Indicators

8) Filer followed 5 OECD framework steps.
9) Filer described internal risk-management.
10) Filer obtained an independent, private-sector audit.
Measurement Area 3

Transparency and Reporting

*How thoroughly is the filer reporting on its due diligence?*

**Performance Indicators**

11) Filer published disclosure on website.
12) Filer gave the quantity of verified conflict-free smelters.
13) Filer identified SOR sources.
14) Filer described plans for continuous improvement.
Promoting a Conflict-Free Minerals Trade

Does the filer measure **social outcomes**? Does filer engage partners to effectively address the root problems? Does filer ensure its response does **not create new problems**?

**Performance Indicators**

15) Filer requires suppliers to source only from verified conflict-free SORs.
16) Filer took leadership in engaging SORs or in-region mining efforts.
17) Filer committed to supporting a conflict-free minerals trade in the DRC region.
18) Filer does not embargo the DRC region.
Aggregate Results

- Most of the 51 companies in the pilot study received less than 50 of 100 points.
- Performance was weak in Transparency and Reporting.
- Performance was strongest in Policy and Management Systems.
- Pleased to see most of the 51 companies rejected the embargo effect.
Leading & Lagging

- Leading industries contain many leading companies. Our expectations are high but achievable: Leading companies demonstrated leading practices.

- Lagging industries do not contain high-performing companies. This correlates to what we know about the lack of leadership or engagement in these sectors.
Industry Score and Percentile Distribution by Sector

- **Technology Hardware, Storage, and Peripherals**
  - Apple
  - EMC
  - Qualcomm

- **Communications Equipment**
  - Texas Instruments
  - Intel

- **Semiconductors and Semiconductor Equipment**
  - General Electric
  - Boeing

- **Electronic Equipment, Instruments, and Components**
  - Garmin
  - Sony

- **Information Technology: 75th Percentile**
  - Samsung

- **Industrial Conglomerates**
  - Ford

- **Aerospace and Defense**
  - Boeing

- **Machinery**

- **Electrical Equipment**

- **Industrials: 58th Percentile**
  - General Electric
  - Boeing

- **Household Durables**
  - General Electric
  - Boeing

- **Auto Components**

- **Textiles, Apparel and Luxury Goods**

- **Automobiles**

- **Leisure Products**

- **Specialty Retail**

- **Consumer Discretionary: 48th Percentile**
  - Ford

- **Containers and Packaging**

- **Healthcare Equipment and Supplies**

- **Healthcare: 22nd Percentile**

- **Energy Equipment and Services**

- **Energy: 7th Percentile**

- **Materials: 22nd Percentile**
Industry Score and Percentile Distribution by Sector

- **Technology Hardware, Storage, and Peripherals**: Apple, EMC
- **Communications Equipment**: Qualcomm
- **Semiconductors and Semiconductor Equipment**: Intel, Texas Instruments
- **Electronic Equipment, Instruments, and Components**: TE Connectivity
- **Information Technology: 75th Percentile**
- **Industrial Conglomerates**: General Electric
- **Aerospace and Defense**: Boeing
- **Machinery**:
- **Electrical Equipment**:

**Industrials: 58th Percentile**
Industry Score and Percentile Distribution by Sector

Consumer Discretionary: 48th Percentile

- Household Durables
- Auto Components
- Textiles, Apparel and Luxury Goods
- Automobiles
- Leisure Products
- Specialty Retail

Materials: 22nd Percentile

- Containers and Packaging
- Healthcare Equipment and Supplies

Healthcare: 22nd Percentile

Energy: 7th Percentile

Energy Equipment and Services

Companies scoring at or above 80th percentile:
- Garmin
- Sony
- Ford
<table>
<thead>
<tr>
<th>Category</th>
<th>Companies</th>
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<tbody>
<tr>
<td>Leading</td>
<td>(1) Intel Corp. (2) Qualcomm, Inc. (3) Apple, Inc.</td>
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<tr>
<td>Strong</td>
<td>3M Co.</td>
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<td></td>
<td>Boeing Co. (The)</td>
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<td>Cisco Systems, Inc.</td>
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<td>Deere &amp; Co.</td>
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<td>Delphi Automotive plc</td>
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<td>EMC Corp.</td>
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<td>Ford Motor Co.</td>
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<td>Garmin Ltd.</td>
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<td>Hewlett-Packard Co.</td>
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<td>General Electric Co.</td>
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<td>Illinois Tool Works, Inc.</td>
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<td>Magna International, Inc.</td>
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<td>Nike, Inc.</td>
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<td>Sony Corp.</td>
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<td>TE Connectivity Ltd.</td>
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<td>Texas Instruments, Inc.</td>
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<td>United Technologies Corp.</td>
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<td>Adequate</td>
<td>ABB Ltd.</td>
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<td>Abbott Laboratories</td>
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<td>Ball Corp.</td>
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<td>Caterpillar, Inc.</td>
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<td>Emerson Electric Co.</td>
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<td>Ericsson</td>
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<td>Hasbro, Inc.</td>
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<td>Honeywell International, Inc.</td>
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<td>Kyocera Corp.</td>
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<td>Lowe’s Companies, Inc.</td>
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<td>Luxottica Group SpA</td>
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<td>Mattel, Inc.</td>
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<td>Schlumberger Ltd.</td>
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<td>TJX Companies, Inc. (The)</td>
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<td>Minimal</td>
<td>Baxter International, Inc.</td>
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<td>Corning, Inc.</td>
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<td>Danaher Corp.</td>
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<td>Eaton Corp. plc</td>
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<td>Halliburton Co.</td>
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<td>Home Depot, Inc. (The)</td>
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<td>Honda Motor Co., Ltd.</td>
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<td>Johnson Controls, Inc.</td>
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<td>Medtronic plc</td>
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<td>National Oilwell Varco, Inc.</td>
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<td>Polaris Industries, Inc.</td>
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<td>Rock-Tenn Co.</td>
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<td>Sealed Air Corp.</td>
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<td>Taiwan Semiconductor Mfg. Co., Ltd.</td>
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<td>Toyota Motor Corp.</td>
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<td>V.F. Corp.</td>
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<td>Whirlpool Corp.</td>
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Recommendations

Companies

- Fully implement the 5 steps of OECD due diligence
- Be transparent, report on goals
- Engage with multi-stakeholder efforts
- Source conflict-free from the DRC

Investors

- Reduce Material Risk
- Compare and Collaborate
- Measure Performance
- Understand different filing statuses
- Engage companies in 17 high exposure industries, especially laggard companies

www.sourcingnetwork.org/mining-disclosures-2014
Continuous Improvement

- Refine certain indicators to be more specific and objective.
- Increase and expand sample group.
- Weighting indicators for SD-only filer to CMR filer.

- RSN welcomes your feedback as we evaluate and improve the pilot study.
Methodology can be replicated, scaled, and adapted to other issues.

1502 creates an opportunity for investors to expand mandatory social performance data and analysis.

Stakeholders can apply pressure to more industries to reach a critical mass of companies promoting a conflict-free minerals trade.
Download the report:

www.sourcingnetwork.org/mining-disclosures-2014
Q&A

We welcome your feedback. Please send comments and questions to:

Patricia Jurewicz
patricia@sourcingnetwork.org

Andrew Arriaga
andrew@sourcingnetwork.org

Azadeh Sabour
azadeh.sabour@sustainalytics.com