Weyerhaeuser Company

USA, Consumer Goods & Services

Accounting		Climate Assumptions		Audit		Date of analysis: May 10 2021
Judgements	Consistency with other reporting	Visibility	Paris alignment	Visibility in CAMs	Consistency check	Year end: December 2020 Report date: February 2021 AGM: May 14 2021
						Climate Action 100+ company, so seen by investors as key to driving global net zero emissions.
Significant concerns	Significant concerns	Significant concerns	Significant concerns	Significant concerns	Significant concerns	

Summary view:

- As a forest management company producing cut logs and manufactured wood products, the company faces significant climate-related risks, both physical risks relating to its timberlands and mills, and transition risks. These include disruption to timber growth cycles, damage due to weather events or fires, potential limits placed on harvesting levels, and changes to energy use and building practices. The company is also assessing potential opportunities including interest in its forest lands for climate mitigation, and development of forest carbon offset markets.
- While the company reports some progress in reducing Scopes 1 and 2 emissions, it has yet to report on Scope 3. Ambitions announced in July include a commitment to setting a company-wide, science-based GHG reduction target, but the timeframe for this is not clear.
- Given wide-ranging risks associated with climate, the lack of clear consideration in the company accounts and in the auditor's report is concerning, particularly in relation to estimates of timberland depletion and impairment considerations.

Background

The Business

- Weyerhaeuser owns 9.9m acres, controls another .8m acres of timberlands in the US and manages a further 14.1m acres under long-term licences in Canada. It primarily sells cut logs and manufactured wood products including structural lumber, oriented strand board and engineered wood. These products are manufactured at 35 facilities in the US and Canada, and supplied to residential, industrial, light commercial, and repair/remodel markets. In 2020, 87% of group sales to external customers were in the US, 7% were Canadian.
- It operates through 3 segments:1) Timberlands 2) Real Estate, Energy and Natural Resources (RE/ENR) and 3) Wood Products. External sales of Wood Products were nearly 77% of 2020 sales. The segment also contributed 94% of total earnings before tax and interest expense.
- Timberland properties that exhibit higher value in uses other than as commercial timberlands are monetised via the Real Estate business, which sells tracts for recreational, conservation, commercial or residential purposes. Energy & Natural Resources sells rights to extract construction aggregates, industrial materials, oil and natural gas; to generate wind and solar electricity; and for communications, pipeline, powerline and transportation rights of way.
- External sales of the Timberlands segment were just under 76% of its total sales in 2020; the rest were intersegment sales to the Wood Products segment. Raw materials of the Wood Products segment also include externally sourced fibre and chemicals.
- 2019 TCFD reporting indicates that Scope 1 emissions were 0.41m MtCO2e, and Scope 2 0.70m MtCO2e (down 53% overall compared to a 2000 baseline, versus a 40% reduction target set for 2020). Weyerhaeuser has "chosen not to conduct Scope 3 reporting until customer requests increase to a significant level and industry-specific guidelines are developed to ensure comparability with other forest product companies".

Approach to climate change

- The company's analysis of risk factors includes direct consideration of climate change, both physical risks (relating to timberlands and manufacturing facilities), and legal and regulatory (transition) risks. It notes that no insurance coverage is maintained for damage to timberlands.
- Physical risks include slower growth and changes to forest species, affecting both its own forests and the availability, cost and quality of the wood fibre used in its mill operations. Risk commentary is somewhat overlapping, with other topics also describing aspects that could be construed as related to climate change, such as: disruption of supply and demand due to fires,

weather events, growth cycles, insect infestation, disease, prolonged drought, flooding, severe weather and other natural disasters and their impact on harvest.

- Regarding transition risks, the company indicates that "Climate change effects, if they occur, and governmental initiatives, laws and regulations to address potential climate concerns, could increase our costs and have a long-term adverse effect on our businesses and results of operations". Areas highlighted include costs to comply with stricter CO2 emission controls, and limits on harvest levels. The company also expects developments to address renewable energy and fuel standards, the monetization of carbon, and potentially mandated changes to energy use and building codes, which could affect homebuilding practices.
- TCFD reporting also says that "climate change will result in the disruption of normal business patterns" and "there are opportunities and risks to each of our businesses". It references efforts to assess and manage physical risks as well as proposals for carbon legislation and public policy choices concerning renewable energy and biomass. Opportunities might include changes to tree growing conditions in certain areas, increased interest in its forest lands for climate mitigation, and development of forest carbon offset markets.
- In July 2020, the company announced new sustainability 'ambitions' for 2030, referred to as '3 by 30' and described quite generally, under the headings of Climate, Homes, and (Rural) Communities. For Climate, the company wants "a world where the value of working forests – and the products that come from these forests – is fully recognised as one of the key solutions to slowing and managing climate change". Actions (also quite general) include helping to position working forests and wood products in carbon offset markets, and carbon removals accounting initiatives. Slightly more tangible (but lacking a deadline) is an 'early action' that commits to setting a company-wide, science-based GHG reduction target. The company plans to incorporate the net carbon sequestration on its land and carbon stored in its wood products.

Accounting: judgements and consistency with other reporting

Accounting judgements		Significant concerns

- There is no explicit reference to climate change in the notes to the US GAAP financials. It is not apparent that any consideration of climate change has been built into the numbers.
- At the end of 2020, the value of timber and timberlands was \$11.8bn, just over 72% of total assets. These assets are accounted for at cost, less depletion.
  - Capitalised costs generally relate to initial site preparation and first planting. Subsequent costs (such as fertiliser, vegetation and insect control, pruning, pre-commercial thinning, and property taxes) are expensed as incurred or over the period of benefit.
  - Depletion represents the carrying value of timber that is harvested or sold. It is based on the net carrying value of timber, divided by the related volume of timber estimated to be available over the growth cycle. On average, the company harvests around 2% of its forests each year. The estimate of depletion relies on assumptions regarding regulatory and environmental constraints, management strategies, growth rates, and known dispositions and inoperable acres. Assumptions of climate change (and its risks and mitigations) are implicit in this, but are not evident in the company's disclosures.
- Long-lived assets that are subject to impairment consideration include the company's timber and timberlands, PP&E (\$2bn) and mineral rights (\$.3m), nearly all of which are in the US. The company states that it reviews the carrying value of long-lived assets whenever an event or a change in circumstance indicates that the carrying value may not be recoverable through future operations. It seems that no such assessment was triggered in 2020.
- No changes to estimated depletion were apparent in 2020, apart from a timber casualty loss of \$80m for the September 2020 forest fires in Oregon. The company estimated the book value of timber and related assets that could not be salvaged, and revised its harvest plans. Disclosure indicates it is reasonably possible that this could increase by \$30-40m. No update is provided in the 2021 Q1 Form 10-Q.

- While not necessarily related to climate, the company has relatively limited accruals for asset retirement obligations ($33m at end 2020), including reforestation obligations under the forest management licences in Canada and obligations to close and cap landfills. It also discloses accruals for environmental remediation of $57m, and notes that it is reasonably possible that costs for identified sites may exceed this by a further $121m.

Consistency with other reporting		Significant concerns

- The company's climate-related commitments and targets are at a relatively early stage, and they appear to be disclosed only outside of the 10-K. Additionally, there is a considerable range of risks disclosed within the 10-K, including risks to growth and harvests of its own forests (and that of external suppliers of fibre), incremental costs associated with steps to mitigate these risks or comply with transitional steps that could even limit harvests or use of the company's wood products. This seems to be at odds with financials that seem to ignore these developments, particularly in estimates of depletion and impairment considerations.
- The latest TCFD reporting notes 2019 spend of $7.7m on forest productivity research to improve forest management practices and the resiliency of forests. The company's total reported R&D expense is less than this amount, and while it is small in relation to overall group profitability measures, it illustrates the questions arising on consistency of reporting on steps to address climate issues, and visibility in the financials.

Climate assumptions in accounts: visibility and Paris alignment

Visibility of climate assumptions in accounts		Significant concerns

- There are no apparent climate-related assumptions. There is thus no sensitivity analysis.

Paris alignment		Significant concerns

- With no visibility, there can be no alignment with the goals of the Paris Agreement.
- While not impacting the financials, the company notes in its latest TCFD reporting that it conducts "climate risk assessments which include studying the effects of changing temperature, precipitation, and other climate-related factors on tree growth and harvest ability", but that it does "not publish the results of these analyses" and has "not yet conducted a full two-degree warming scenario analysis", let alone a more challenging 1.5°C assessment.

Audit: visibility in CAMs and consistency check

Audit firm: KPMG LLP	Responsible partner: Richard David Callahan
Audit standards: PCAOB standards	

Visibility in Critical Audit Matters		Significant concerns

- There is no explicit reference to climate change in the auditor's report, and only a single CAM, related to the discount rate assumed for the projected benefit obligations for pensions.

Consistency check		Significant concerns

- PCAOB audit standards require the auditor to read other information that is presented together with financial statements and the auditor's report thereon. The auditor's report is silent on the outcome of the review, which implies that no material inconsistency was identified in the other information within the 2020 10-K.
- Given the wide-ranging risks highlighted in the 10-K, including those related to the valuation of the company's largest assets by far (timber and timberlands), the lack of clear consideration by the auditor is concerning.

The Climate Accounting Project is an independent investor-led project to reinforce the statements of the IASB and IAASB that material climate change issues are incorporated within their standards. This analysis seeks to understand the extent to which companies and auditors are delivering against this aspect of these standards and similar local standards.		**Key**
		Good practice
		Few concerns
		Some concerns
		Significant concerns

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