

# FACEBOOK, INC.

TICKER: FB

RATING DATE: May 23, 2012

IVA INDUSTRY: Internet Software & Services

PREVIOUS RATING: n/a

GICS SUB-INDUSTRY:

COUNTRY: US

## IVA RATING

# B

### ESG PILLAR PERFORMANCE

	Score	Weight*
ENVIRONMENTAL (E)	6.4	28.0%
SOCIAL (S)	2.7	58.0%
GOVERNANCE (G)	3.6	14.0%

*Intangible Value Assessment (IVA) measures and analyzes companies' risk and opportunities arising from environmental, social and governance issues. By assessing indicators typically not identified by traditional securities analysis, IVA Ratings uncover hidden risks and value potential for investors. Ratings range from AAA (best) to CCC (worst). Scores range from 10 (best) to 0 (worst). This report should be read in conjunction with the IVA Industry Report, where the Key Issues are explained in further detail.*

### COMPETITIVE SET

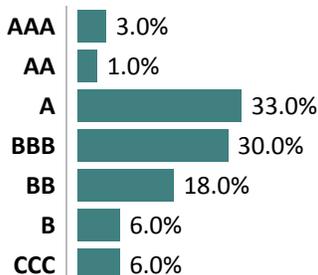
#### Top 3 Companies

SAP AG	AAA
International Business Machines Corporation	AAA
Accenture Plc	AA

#### Bottom 3 Companies

OTSUKA CORPORATION	CCC
DeNA Co.,Ltd.	CCC
Gree,Inc.	CCC

### Industry Rating Distribution



### RATING COMMENT

We initiate coverage of Facebook at 'B'. The company's privacy practices present the single biggest risk to its business from an ESG perspective, and we have serious concerns about Facebook's vulnerability on this issue in the medium to long term. Although adept handling of user privacy is key to the company's long term success, its history of missteps and frequent changes to policies and user privacy management tools make it exceptionally vulnerable to lawsuits and regulatory action, as well as the possibility of user migration.

While Facebook is taking a smart, forward-looking approach to energy consumption by its proliferating data centers, its strategy is still less comprehensive than we see at more established peers and competitors, such as Google. We also have concerns about the company's likely global expansion, and particularly the possibility of its entry into China, where concerns about censorship and civil liberties could present substantial threats if the company does not tread carefully.

### KEY ISSUE OVERVIEW



	Pillar	Score	Average	Weight
<b>HUMAN CAPITAL DEVELOPMENT</b>	<b>S</b>	<b>4.4</b>	<b>5.0</b>	<b>29.0%</b>

Facebook has moderately high exposure to challenges in the area of human capital, mainly because of its heavy reliance on highly skilled employees and the fierce competition for top talent in its industry. However, the company offers competitive employee benefits and a strong on-boarding program, thereby ranking in the second quartile.

*Average: All industry averages are calculated on the basis of the companies of the MSCI World Index.*

\* Pillar weights may not add up to 100%. For industries published prior to Q3 2011, up to 20% of the rating reflected performance on a variety of social and environmental indicators that are not Key Issues facing the industry. These non-key issues do not contribute to pillar scores or pillar weights. Please refer to the Industry Report for more details. Where there are no governance key issues, the governance score is derived from the ISS GRId and ESG Impact Monitor products. Please note that governance scores may be updated in between rating updates. Please refer to the IVA Methodology for further details.

	Pillar	Score	Average	Weight
<b>PRIVACY &amp; DATA SECURITY</b>	<b>S</b>	<b>0.9</b>	<b>5.1</b>	<b>29.0%</b>
<p>Facebook faces extremely high exposure to risks associated with privacy and data security as one of the largest social networks in the world, with nearly a billion users sharing sensitive personal data online and targeted advertisements that provide the company with revenue. The company has faced enormous criticism over its privacy practices, as well as serious controversies involving leaking of users' data to third parties without their full consent, placing the company in the bottom quartile despite recently strengthened privacy enforcement mechanisms.</p>				
<b>ENERGY EFFICIENCY</b>	<b>E</b>	<b>9.2</b>	<b>6.4</b>	<b>14.0%</b>
<p>Like most companies in the Software &amp; IT Services industry, Facebook's exposure to risks associated with energy cost increases is moderately low but rising as data centers expand and proliferate. Although the company's energy use is massive and growing, we believe Facebook is preparing itself well to withstand rising energy prices, and the company ranks in the second quartile.</p>				
<b>OPPORTUNITIES IN CLEAN TECH</b>	<b>E</b>	<b>3.6</b>	<b>4.6</b>	<b>14.0%</b>
<p>Although some Internet Services companies have developed various aspects of clean technology, such as smart grid applications, infrastructure-as-a-service, and applications to monitor energy use or carbon footprint for customers, Facebook has done little to explore this space, placing it in the third quartile.</p>				
<b>CORRUPTION &amp; INSTABILITY</b>	<b>G</b>	<b>3.7</b>	<b>3.8</b>	<b>9.0%</b>
<p>Due to the nature of the social networking services it provides, Facebook faces growing risks associated with possible censorship and other government efforts to monitor or control citizens' activities on the Internet. The company's recent sign-up for observer status with the Global Network Initiative signals its awareness of the risks it faces, though it does not represent any notable commitments at this point.</p>				
<b>CORPORATE GOVERNANCE</b>	<b>G</b>	<b>3.3</b>	<b>7.0</b>	<b>5.0%</b>
<p>Our initial research of the company's corporate governance revealed very serious issues related to shareholders' rights. Facebook has a dual-class share structure and the founder and CEO controls 57% of the voting rights.</p>				

*Average: All industry averages are calculated on the basis of the companies of the MSCI World Index.*

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## KEY ISSUES

### Human Capital Development

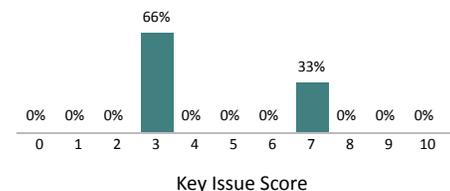
Pillar	Key Issue Score	Average	Weight
S	4.4	5.0	29.0%

Facebook has moderately high exposure to challenges in the area of human capital, mainly because of its heavy reliance on highly skilled employees and the fierce competition for top talent in its industry. However, the company offers competitive employee benefits and a strong on-boarding program, thereby ranking in the second quartile.

Our model evaluates companies' ability to attract, retain and develop human capital as well as their exposure to risks of increased costs associated with high turnover or reduced productivity resulting from poor morale. Companies that have comprehensive compensation and benefits packages, provide formal employee engagement channels as well as broad-based professional development and training opportunities are best positioned to mitigate operational risks in this area.

Facebook has compensation programs that strongly link employees' interests to the success of the firm, including stock options and bonuses for rank-and-file employees, though we do have some minor concerns about the conflict that could arise between employees that received stock grants prior to the firm's IPO and new joiners, who will not be as richly rewarded. Facebook also has an intensive employee development training program for all new software engineers that includes a 6-week bootcamp and a formal mentoring program, which may help ensure that new hires are successful at the company. And while the company does not disclose other details of leadership training, talent management programs, or employee engagement initiatives that are important and common among more established companies, we believe Facebook is well positioned to manage this key resource in the near to medium term.

Score Distribution:



<b>Exposure Score:</b>	7.6
<b>Management Score:</b>	5.0

## Headline Indicators

### Management & Performance

#### Employee Engagement and Retention

Formal grievance reporting or escalation procedures:	<b>No evidence</b>
Company monitors employee satisfaction on a regular basis:	<b>Not Disclosed</b>

#### Professional Development

Training or professional development programs for employees:	<b>Yes</b>
Regular performance appraisals and feedback processes:	<b>Not Disclosed</b>
Job-specific development training programs:	<b>Yes</b>
Leadership training and talent management programs:	<b>Not Disclosed</b>

## Controversies

All controversies are assessed as part of the annual review of a company's ESG rating. MSCI ESG research updates the controversies sections of the IVA Company Profile every month. Monthly updates to controversies will not impact the existing company rating except in exceptional circumstances.

No major relevant controversies have been uncovered.

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## Privacy & Data Security

Pillar	Key Issue Score	Average	Weight
S	0.9	5.1	29.0%

Facebook faces extremely high exposure to risks associated with privacy and data security as one of the largest social networks in the world, with nearly a billion users sharing sensitive personal data online and targeted advertisements that provide the company with revenue. The company has faced enormous criticism over its privacy practices, as well as serious controversies involving leaking of users' data to third parties without their full consent, placing the company in the bottom quartile despite recently strengthened privacy enforcement mechanisms.

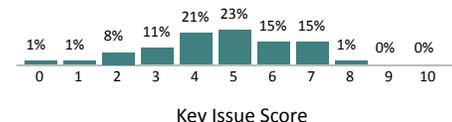
Privacy and data security is the largest risk to the company from an ESG perspective as social networks must find a way to monetize the data that users share without violating their trust. In the absence of modern, strict, and consistent privacy laws in all the geographies in which its users are located, the company risks litigation or legislation aimed directly at its practices, particularly following some of its high profile privacy blunders. Ongoing privacy controversies can scare users off of the service, limit the company's ability to generate revenue from advertisers, and provide openings for other social networks with more robust data security and privacy practices. Given its controversial history in this area, we are particularly concerned that Facebook may fail to live up to its existing privacy policies or the terms of its 2011 settlement with the FTC, thereby risking fines, litigation, user migration, and regulatory action that could threaten its business model.

While the evaluation of any company's privacy policy is a snapshot in time, Facebook's privacy policies have changed frequently since the company was incorporated in 2004, often in the direction of eroding users' privacy, although the company tends to enhance certain privacy tools even while weakening others. At incorporation, Facebook enticed users to share personal information online with a privacy policy that guaranteed the data would not be shared with any user of the website that was not a member of a group the user specified in his or her privacy settings, but over the years, the company has changed its privacy policy and data handling practices to make more of that information available to more users as a default option. In our May 2012 assessment of the company's privacy policies, we located the strength of its privacy policy near the median for the Internet Software & Services sub-industry, with notable commitments to allow users to delete all data collected on them and to download a copy of everything they've put into Facebook.

In November 2011, the company rolled out strong privacy enforcement mechanisms including two Chief Privacy Officers, one focused on policies, the other on products. The other enforcement mechanisms - privacy audits for the next 20 years and employee privacy training - were mandated through a settlement with the U.S. Federal Trade Commission (FTC) over what the government agency alleged were deceptive practices in the area of privacy. The most serious charges were that the company violated its own privacy policy by sharing users' personal information with advertisers and stating that it complied with the U.S.-EU Safe Harbor Framework (which governs data handling between the U.S. and the European Union) when it in fact did not. Google settled with the FTC over similar allegations around the same time and is also required to undertake the mandated privacy audits. Both companies are under threat of a USD 16,000/day fine if they are found to violate the settlement agreements in the future.

Following criticism over its privacy changes in 2010, Facebook added layers of complexity to users' privacy controls that would allow users to demarcate privacy settings on individual posts, while simultaneously introducing recommended privacy settings that encouraged users

Score Distribution:



<b>Exposure Score:</b>	9.4
<b>Management Score:</b>	3.3

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to share content with everyone, including non-Facebook users. While privacy advocates have criticized the company's progression on the issue as an attempt to propel users to share more information without their full understanding and consent and ahead of their comfort level, Facebook's founder and CEO stated in 2010 that its privacy approach has evolved following changing social norms with regard to privacy.

While Facebook's users are active participants in the sharing of their private information with other users, the company has faced criticism over the ways advertisers are able to target its users. Additionally, its alleged use of tracking cookies that collect browsing history even after users log out of Facebook, along with other violations of its privacy policies, have resulted in one of the world's largest ever privacy class action lawsuits. The high profile controversies throughout the company's short history leave us very concerned about the sustainability of Facebook's business model.

## Headline Indicators

### Management & Performance

### Policy

#### Abide by (or commit to abide by) the following best practices:

Not collecting personal information from third-party sources:	<b>No</b>
Limiting access to personal data to designated personnel (employees or contractors):	<b>No</b>
Monitoring employees' and contractors' access to data in real time (as a means of detecting suspicious use):	<b>No</b>
Providing customers an option to opt out from internal direct marketing:	<b>No</b>
Not renting, selling, or providing personal (non-aggregate) information to external parties for the benefit of those external parties (as opposed to for processing or analysis on behalf of the company itself):	<b>No</b>
Allowing customers (or non-customers on whom data have been collected) to delete all data on them (not just deactivate, but delete):	<b>Yes</b>
Deleting data after a certain amount of time:	<b>No</b>
Informing customers whenever their data is transferred to or handled by external data providers:	<b>No</b>

## Controversies

All controversies are assessed as part of the annual review of a company's ESG rating. MSCI ESG research updates the controversies sections of the IVA Company Profile every month. Monthly updates to controversies will not impact the existing company rating except in exceptional circumstances.

### Severe Controversies

**Date:** December 2011

**Assessment:** Severe

#### US FTC Settlement Regarding Deceptive Practices and Privacy

Facebook has been repeatedly criticized by online privacy organizations, consumer groups, and U.S. legislators for its alleged breaches of user privacy protocol. In 2011, the U.S. Federal Trade Commission (FTC) ordered an on going 20-year audit of the company's privacy practices as part of a settlement of complaints filed by a coalition of privacy organizations and consumer groups.

In November 2011, Facebook agreed to settle eight administrative complaints regarding privacy concerns brought forward by the FTC in 2010. The complaints charged that Facebook made privacy promises to its users which were not met, and that it had violated federal law. As part of the settlement, Facebook agreed to stop misrepresenting

the security of users' personal information, to obtain users' express permission before making changes that would override their privacy settings, to prevent anyone from accessing data from a deleted account more than 30 days after its deletion, and to develop a comprehensive privacy program to address its services' privacy risks. The settlement also required Facebook to subject its privacy practices to third-party audits every two years for the next 20 years to certify that it complied with the FTC order. According to the FTC, any violation of the settlement order could result in a daily penalty of up to USD 16,000. Facebook acknowledged that the company had made mistakes and said that it was committed to addressing the FTC's complaints.

Several U.S. legislators, consumer groups, and privacy organizations subsequently expressed doubts that the settlement would sufficiently address privacy concerns. In December 2011, the Electronic Privacy Information Center (EPIC) sent a letter to the FTC requesting that it determine whether Facebook's implementation of a new profile layout called the "Timeline", was consistent with the terms of the settlement. A number of U.S. legislators also wrote to Facebook's CEO requesting information, including the site's privacy policy statement, information collection practices, and utilization of user information.

In September 2011, consumer organizations including, Consumer Watchdog, EPIC, and Privacy Activism, among others, wrote a letter asking the FTC to investigate allegations that Facebook used "cookies" to track users' online activity after they had logged out of Facebook. The groups also expressed concerns over Facebook's new information-sharing features which gave the site the power to automatically share information about users' online activities. The organizations claimed these practices were deceptive and violated the site's own policies.

In October 2011, several U.S. lawmakers wrote to the FTC requesting an investigation of Facebook over similar concerns.

In June 2011, a number of privacy organizations including EPIC, the American Civil Liberties Union (ACLU), and the Center for Digital Democracy, filed a complaint with the FTC regarding Facebook's automated tagging of users in photos using facial recognition technology. The organizations urged the FTC to require Facebook to suspend the program pending a full investigation, the establishment of stronger privacy standards, and a requirement that the feature would only be activated with users' consent.

In 2010, the U.S. FTC received several complaints about Facebook's data-collection practices from a coalition of organizations including EPIC and the Center for Digital Democracy. The complaints reported that privacy changes made by Facebook in December 2009 exposed user information that could previously be made private, and that automatically signed users up for new features without their expressed consent. The FTC accused Facebook of making deceptive privacy claims, and also alleged that the site did not respect the Safe Harbor Framework governing the transfer of data between the U.S. and the European Union. In 2010, the FTC brought forward eight administrative complaints and called on the company to offer more granular privacy controls that would enable users to choose to share or make private specific information that they posted.

**Date:** December 2011

**Assessment:** Severe

#### **Probe by European Union Data Protection Regulators**

In December 2011, Facebook Ireland agreed to improve privacy protections in Europe after an investigation into its practices by the Irish Data Protection Commissioner two months prior. Facebook Ireland agreed to give users more information on how the site and third-party applications handled their information, and to minimize the collection of data from users while they were not logged onto the site. Facebook Ireland, which is responsible for all of the site's users outside the US and Canada, also agreed to inform European users that it used facial recognition software for "tagging" suggestions in posted photos.

The Irish Data Protection Commissioner started an investigation into Facebook's privacy practices in October 2011 following numerous complaints about the site's treatment of users' personal information from individual users and groups such as the Norwegian Consumer Council and the Europe-versus-Facebook group.

In August 2011, Germany's Hamburg Data Protection Authority started an investigation into Facebook's photo-tagging software and asked Facebook to deactivate it due to concerns that its facial recognition feature violated European privacy laws. Facebook denied that it was breaching privacy regulations but said it would consider the issues raised by German authorities.

In June 2011, a member of the European Union's Data Protection Working Party announced that a group of privacy regulators from the European Union (EU) would probe Facebook over a new feature that used face-recognition software

for photo-tagging suggestions, without users' permission. EU regulators said the automatic tagging suggestions could pose risks to users and should only happen with their prior consent. The UK Information Commissioner's Office also reported that it was looking into the privacy concerns raised by the facial recognition feature. Facebook defended the feature, saying it only suggested tagging people within the network of the user who posted the picture. The company also claimed it provided instructions on how users could disable the function.

In March 2010, European regulators started an investigation into Facebook's privacy policies and practices, focusing on the practice of allowing users to upload information about non-users, such as email addresses and photographs. The investigation raised the question of how much responsibility social networking platforms should take for the content uploaded by its users.

### Moderate Controversies

**Date:** May 2012

**Assessment:** Moderate

#### Lawsuit over Privacy Issues

As of May 2012, Facebook faced a USD 15 billion lawsuit seeking class action status, filed on behalf of all U.S. users who joined the site from May 2010 to September 2011, alleging that the company violated its site users' privacy by tracking their internet usage even after they had logged out of their accounts. The lawsuit was a consolidation of 21 separate cases filed over similar complaints in various states in 2011 and early 2012. The complaint claimed that Facebook was in violation of the U.S. Wiretap Act, the Computer Fraud and Abuse Act, and the Stored Communications Act. Facebook denied the claims and reported that it would contest the case.

**Date:** December 2011

**Assessment:** Moderate

#### Lawsuits Alleging Misappropriation of Users' Names for Marketing Purposes

In December 2011, the San Francisco Federal Court allowed a group of Facebook users to proceed with a class action lawsuit alleging that Facebook unlawfully exploited their preferences on the site for commercial gain and without their permission. According to the plaintiffs, the image and name of a user who clicked "like" on a brand's Facebook page could be used by the site in an advertisement for that company. Facebook reportedly defended the practice by saying that users' clicking the "like" button was effectively giving consent for their name to be used in an advertisement. A spokesperson for the company claimed the case was without merit.

In May 2011, an individual filed a lawsuit against Facebook alleging that the site misappropriated the names or likenesses of his child and of other minors in order to promote products or services. The lawsuit, which was filed in a US district court in New York, claimed Facebook used the names and images of underage users in "Social Ads" when they clicked on "like" for certain brands, without obtaining permission from the minors' parents or guardians. Facebook stated that the suit was without merit.

**Date:** December 2011

**Assessment:** Moderate

#### Canadian Privacy Lawsuit

In December 2011, Facebook agreed to pay USD 74,600 (CAD 76,000) to settle a class-action lawsuit over privacy concerns filed on behalf of users in Canada. As part of the settlement, Facebook agreed to keep its privacy policy substantially the same for three years since publishing an updated version, which supposedly made privacy controls clearer for users.

The lawsuit was filed in July 2010 in Winnipeg, Canada, and alleged that the site's privacy policies misled users into letting their information be sold to advertisers and data miners. The lawsuit claimed that changes to Facebook's privacy settings during the previous 18 months had led users to believe that their information was more secure, but actually resulted in their information being moved into the public domain and opened it up to "harvesters". The suit included all Canadians who were members of Facebook between December 2009 and January 2010.

**Date:** September 2010

**Assessment:** Moderate

#### Violations of Canadian Privacy Legislation

The company has faced concerns about its privacy practices and policy in Canada.

In April 2012, Canada's federal Privacy Commissioner's office released the results of three investigations into complaints about Facebook. The investigations were launched in September 2010 to dig into the privacy practices of the company

based on complaints by users of the company's social networking site. One complaint was based on users' concerns that Facebook was accessing users' email address books without consent as part of its "friend suggestion" feature. Another complaint was filed by a user regarding the potential collection and sharing of users' data related to the site's social plug-ins, while the third complaint was filed by a user who claimed Facebook required too much personal information to create an account.

At that time, the commissioner reported that while Facebook had violated the Personal Information Protection and Electronic Documents Act by accessing non-users' email address books without consent, the case was closed as the site had already addressed the issue. The other two complaints were concluded to be "not well-founded." The commissioner called on Facebook to design privacy controls in anticipation of privacy concerns.

In April 2010, experts on privacy, ethics, and technology expressed concerns about a new Facebook application that allowed users to publicly connect with other websites and share them with their social network. Experts describe the practice as "soft surveillance" and said the application could be used by advertisers to target users based on their personal preferences and those of their friends. They also pointed out that while Facebook users could opt out of the feature, few online users exercised privacy options. Facebook claimed the new service would not affect its privacy policies. In May 2010, a spokesperson for the Canadian Internet Policy and Public Interest Clinic (CIPPIC) claimed that Facebook's privacy practices continued to be questionable.

Earlier in July 2009, the Privacy Commissioner released a report claiming that Facebook violated Canadian privacy legislation by keeping user accounts on file indefinitely after they were deactivated and by sharing users' information, without their expressed consent, with third-party software developers. According to the Commissioner, Canadian law requires organizations to retain personal information only for as long as it was necessary to meet purposes that it was collected for. The report expressed concerns that Facebook offered confusing or incomplete privacy information to its users. The privacy watchdog gave Facebook one year to implement changes that would safeguard users' privacy. It also called on the company to make privacy policies and options more transparent to ensure that users could properly manage personal information. As of August 2009, Facebook had agreed to make worldwide changes to its privacy policy and to be more transparent about what data it collects. It also said the site would make it clear that users can deactivate or delete their account.

In June 2009, a group of students at the University of Ottawa filed a complaint with the Privacy Commissioner alleging that Facebook violated the country's privacy laws. The students reported that the site sent users' personal information to third parties for advertising and marketing activities without the users' knowledge or expressed consent.

In May 2008, CIPPIC filed a complaint with Canada's privacy commissioner regarding Facebook's policies on sharing users' personal information with applications developers. A spokesperson for Facebook reported that the complaint had "serious factual errors" and pointed out that "almost all Facebook data is willingly shared by users."

**Date:** May 2010

**Assessment:** Moderate

#### **Australian Privacy Investigation**

In May 2010, Australia's Privacy Commissioner launched an investigation into Facebook regarding changes to its privacy controls. The social networking site also faced growing criticism from civil society, including the online civil liberties group Electronic Frontiers Australia, which claimed that Facebook was reluctant to simplify its privacy settings because the company used members' information for profit. An Australian senator and Communications Minister criticized Facebook's privacy practices, alleging that the company showed "complete disregard for users' privacy." Later in May 2010, Facebook announced new privacy controls that were intended to give users more control of how they shared information.

## Energy Efficiency

Pillar	Key Issue Score	Average	Weight
E	9.2	6.4	14.0%

Like most companies in the Software & IT Services industry, Facebook's exposure to risks associated with energy cost increases is moderately low but rising as data centers expand and proliferate. Although the company's energy use is massive and growing, we believe Facebook is preparing itself well to withstand rising energy prices, and the company ranks in the second quartile.

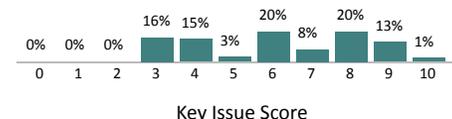
Companies in this industry are less energy dependent than those involved in heavy manufacturing or extractive operations. However, numerous trends are driving energy usage increases for these companies, including, in Facebook's case, exponential growth in the generation of data by its users, which the company must process and store. Energy represents this industry's most substantial environmental challenge and attention to energy consumption and efficiency is likely to result in financial savings, while failure to adequately address efficiency may result in medium term cost increases.

While Facebook lags better established peers such as Google in developing formal programs and setting quantitative improvement targets for energy efficiency, the company has nonetheless taken an aggressive approach to maximizing data center efficiency. Like other Internet services companies, data centers represent the bulk of the company's energy needs. In 2011 Facebook adopted open architecture for its servers and data centers, allowing its designs and achievements in efficiency to be shared by the broader industry. Facebook's collaborative approach to data center energy efficiency is rare in the industry, with most companies considering their data center designs to be a competitive trade secret. The company has also joined The Green Grid, an industry group focused on data center energy efficiency.

The company's efforts appear to be yielding dividends, as Facebook's newest data center in Oregon achieved an extremely low Power Usage Effectiveness (PUE) ratio of 1.08 in late 2011. PUE is the amount of energy powering IT equipment in a data center divided by the total amount of energy coming into the facility. Perfect efficiency would be a score of 1.0 - all energy powering IT equipment and none used for cooling or other purposes. Typical scores are in the range of 1.7-1.9, according to the U.S. EPA. Google, a clear leader in the industry, achieved an average PUE across all data centers of 1.14 in 2011.

In addition to its focus on pure energy efficiency, Facebook has adopted a data center siting policy that includes a preference for the availability of renewable energy. The siting policy was adopted following a high profile campaign against the company by Greenpeace in an example of the greater external pressures we anticipate the company will see on environmental and social issues as it grows. While cleaner energy sources may raise the per watt cost of electricity in the short term, by adopting them now, the company prices into its operations some of the risks associated with rising energy prices as well as the possibility that climate change legislation would require it to switch to renewable energy sources that may be more expensive.

### Score Distribution:



<b>Exposure Score:</b>	2.8
<b>Management Score:</b>	5.0

### Headline Indicators

### Management & Performance

### Controversies

This key issue assesses energy consumption data to determine companies' environmental impact. Controversies are not covered under this heading.

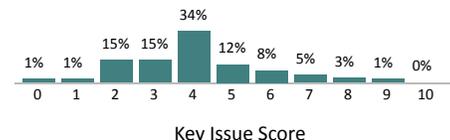
## Opportunities in Clean Tech

Pillar	Key Issue Score	Average	Weight
E	3.6	4.6	14.0%

Although some Internet Services companies have developed various aspects of clean technology, such as smart grid applications, infrastructure-as-a-service, and applications to monitor energy use or carbon footprint for customers, Facebook has done little to explore this space, placing it in the third quartile.

The company has begun to develop content that will engage users in addressing their home's energy use through a partnership with the Natural Resources Defense Council and it has launched what it refers to as a 'social energy app' through which users can benchmark their energy use, share tips on energy efficiency, and participate in energy efficiency competitions. Further efforts to create applications that appeal to users' carbon consciousness could provide the company with an opportunity to retain and attract users to its site.

### Score Distribution:



Exposure Score:	5.1
Management Score:	3.2

## Headline Indicators

### Management & Performance

### Performance

#### Energy Efficiency

Smart Grid: **No involvement**

#### Applications

Other: **No involvement**

#### Air Quality

Environmental Information Technology: **Servicing or minor component manufacturing or other non-core involvement**

## Research & Development

### R&D Expenses (USD million)

Year	Amount
2011	388.0 USD

**FACEBOOK, INC.**

<b>Year</b>	<b>Amount</b>
<b>2010</b>	144.0 USD
<b>2009</b>	87.0 USD

**R&D/Sales**

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<b>Year</b>	<b>Percentage</b>
<b>2011</b>	10.46%
<b>2010</b>	7.29%
<b>2009</b>	11.2%

**Controversies**

This key issue assesses how companies take advantage of their opportunities. Controversies are not covered under this heading.

# FACEBOOK, INC.

## Corruption & Instability

Pillar	Key Issue Score	Average	Weight
G	3.7	3.8	9.0%

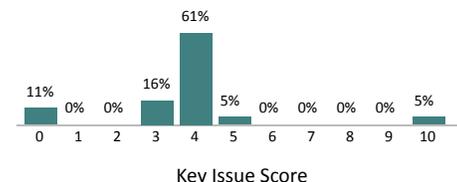
Due to the nature of the social networking services it provides, Facebook faces growing risks associated with possible censorship and other government efforts to monitor or control citizens' activities on the Internet. The company's recent sign-up for observer status with the Global Network Initiative signals its awareness of the risks it faces, though it does not represent any notable commitments at this point.

Censorship and other threats to free expression present a complicated set of challenges to companies offering Internet services directly to users. Facebook shares a high level of risk with other Internet services companies that serve users in regions where political freedom is under threat, such as Google, Microsoft, and Yahoo!. Some politically repressive regimes, of which China is the best known, direct companies to block websites or services, require service providers to monitor users' online speech and other modes of expression, block or remove "inappropriate" content, and sometimes turn in dissidents. In these markets, compliance with such requirements is a condition of doing business.

While Facebook has been the subject of much hype regarding its perceived role in facilitating communication between dissidents and activists under repressive regimes, as the company considers expansion into a broader array of such markets - most particularly, China - it could find itself the subject of less laudatory attention. As Yahoo! learned to its chagrin several years ago, a single high profile incident resulting in the jailing of a dissident can do substantial damage to the company's reputation and could impede growth in that market.

There are various measures that companies can take to mitigate this type of risk while continuing to do business in countries such as China. The Global Network Initiative, of which Google, Microsoft and Yahoo! are founding members, has laid out best practices for companies in these scenarios. According to GNI principles, steps that should be taken include notifying users when mandatory censorship occurs, limiting the services hosted in-country in order to limit the government's jurisdiction over information held on its servers, and insisting on going through formal legal channels to process any requests for user data. While Facebook has not gone so far as to join the GNI at this point or officially adopt any of these practices, the company has been accepted for a year in 'observer' status, which will allow it to learn more about how GNI members implement these risk mitigation measures.

Score Distribution:



<b>Exposure Score:</b>	5.4
<b>Management Score:</b>	2.1

### Headline Indicators

#### Management & Performance

#### Policies & Commitments

Policies on civil liberties and freedom of speech:

Commit to external standards for ethics, or signatory to sector-specific ethical groups or codes:

External standards: :

**Policy articulated**

**Signatory to other external standards**

**Observer Status (not a signatory), to the Global Network Initiative**

#### Programs and Structures

Internal auditors ensure compliance with ethical standards:

**No**

External independent auditors ensure compliance with ethical standards:

**No**

Employee training on ethical standards :  
Whistleblower protection:

**Not Disclosed**  
**Not Disclosed**

### Controversies

All controversies are assessed as part of the annual review of a company's ESG rating. MSCI ESG research updates the controversies sections of the IVA Company Profile every month. Monthly updates to controversies will not impact the existing company rating except in exceptional circumstances.

No major relevant controversies have been uncovered.

# FACEBOOK, INC.

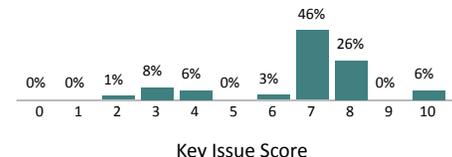
## Corporate Governance

Pillar	Key Issue Score	Average	Weight
G	3.3	7.0	5.0%

Our initial research of the company's corporate governance revealed very serious issues related to shareholders' rights. Facebook has a dual-class share structure and the founder and CEO controls 57% of the voting rights.

The Corporate Governance score is derived from a combination of Institutional Shareholder Services' (ISS) Governance Risk Indicator (GRId) assessment, where available, and controversies assessment from MSCI ESG Research Impact Monitor. A full GRId assessment of Facebook is not yet available; it will be completed later in 2012. For details please refer to the IVA Methodology Document.

Score Distribution:



### Headline Indicators

#### Management & Performance

#### Governance

##### Shareholder Rights

Shareholder Rights Grade:  
Shareholder Rights Analysis:

**High Concern**  
**The ability of shareholders to exercise their rights as owners is significantly restricted.**

### Controversies

All controversies are assessed as part of the annual review of a company's ESG rating. MSCI ESG research updates the controversies sections of the IVA Company Profile every month. Monthly updates to controversies will not impact the existing company rating except in exceptional circumstances.

#### Moderate Controversies

**Date:** February 2012  
**Assessment:** Moderate

##### Facebook Scrutinized over Dual-Class Shares Structure

Facebook uses a dual-class shareholder structure. The company offers two classes of shares wherein one class will have ten votes per share (Class B) compared to the usual one-is-to-one (Class A). In addition to owning most of the Class B shares, Facebook's CEO and chair had also negotiated with other shareholders to gain "irrevocable proxy" over their shares. This gives Facebook's CEO and chair control over 57 percent of voting rights despite owning only 28.4 percent of the company. Shareholder rights groups have been critical over concerns of diminished board accountability and shareholder proxy voting rights.

In February 2012, Institutional Shareholder Services (ISS, an MSCI company) released a report, entitled "The Tragedy of the Dual-Class Commons", criticizing this kind of governance structure for having diminished board accountability and shareholder proxy voting rights. The report mentioned several US companies, including Facebook, that used a dual-class structure. A Facebook investor, California State Teachers' Retirement System has stated that it was scrutinizing the governance structure, in relation to the report.

## OTHER RISKS &amp; OPPORTUNITIES

## Protection of Minors

Facebook faces ongoing risks related to the use of its site by minors. According to its terms of service, Facebook requires users to be at least 13 years old in order to use the social networking site. Websites in the United States are required by the Children's Online Privacy Protection Act (COPPA) to obtain verifiable parental consent before collecting, disclosing, or using personal information related to children under 13. Facebook has recently considered allowing children to open accounts and according to a survey by 2011 Consumer Reports, as many as 7.5 million users under 13 already had accounts on the network. The company has come under fire by authorities in the US and Australia that have called on Facebook to better safeguard the security of users, particularly underage users, who could be exposed to predators who use the site to lure victims. Given the particularly high profile of controversies related to sexual predators on social networks, we are concerned that Facebook's approach to this issue may not be adequately robust to manage this risk. Websites that allow underage users to have accounts can utilize parental tools such as parental ability to change privacy settings or accept friend requests for their minor children.

## IPO Troubles

Immediately following the company's IPO in May 2012, Facebook and its lead underwriter, Morgan Stanley, were facing lawsuits, inquiries by regulators, and US Congressional scrutiny over whether the company had misled investors, omitted facts, or submitted false statements in its IPO documents.

During the first week of trading, the head of the Financial Industry Regulatory Authority (FIRA) said his agency would examine whether Morgan Stanley shared negative news with larger clients prior to the IPO. The chairman of the Securities and Exchange Commission (SEC) stated that her agency would be looking into issues related to the IPO. The shareholder suit centered on allegations that Facebook was more pessimistic in its revenue projections shared with its underwriters than it was in its initial filing documents.

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