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# A PRACTICAL APPROACH TO ESG FROM A CORPORATE VANTAGE POINT

## Launching and maintaining a successful ESG reporting program requires internal and external strategies and resources.

BY PAMELA STYLES

Environmental, social, and governance (ESG) issues and associated reporting on ESG practices to external stakeholders are increasingly important to investor relations professionals and their companies. While still voluntary in the United States, ESG reporting is increasingly demanded by investors and other stakeholders.

This article explores a practical understanding and approach to ESG for IROs. It explores these areas:

- Internal opportunities and pitfalls such as internal operational realities, individual expert professional capabilities, staff capacity, and team cooperation.
- External perspectives including the optimal use of voluntary ESG reporting standards and frameworks; ESG ratings and ranking organizations and third-party influencers; and ESG data suppliers.
- Resource allocation and budgeting and the need for focus and prioritization.

Ultimately, the goal is to establish a public ESG profile of your company that is right-sized, defensible, and constructive for your company in competition with its peers.

### Internal Opportunities and Pitfalls

To gain internal buy-in and commitment to ESG, consider emphasizing these points to executive leaders, subject matter experts (SMEs), and your team members:

- Benefits of ESG in recruiting and retaining talent to reduce turnover.
- Another way to monitor supply chain sustainability.
- Opportunities to attract and retain investor interest.

- Rise in ESG focus from fixed-income investors that is rapidly catching up with equity investment.
- Potential to lower your company's overall cost of capital. (The CFA Institute recently surveyed investors and found, "Among practitioner survey respondents, 73% expect the influence of ESG ratings on firms' cost of capital to be greater in the next five years.")
- New strategic opportunities to differentiate your company and gain competitive advantage.
- Access to favorable financing and investing opportunities not previously attempted on the asset or liability side of the green bond world.

### *Build Your Team*

Gaining support from your company's board of directors and C-suite is critical. Remember to also get needed support from departments such as corporate communications, human resources, environmental and health services, community affairs, finance, and legal, all which may play an important role in gathering, reviewing, and approving ESG disclosures.

### *Crawl, Walk, and Then Run*

If your ESG reporting program is new, keep it tight. Increasing investor expectations for ESG disclosure can create pressure and sustainability reports can take on a life of their own.

It is better to start small and build on sustainability disclosure each year as opposed to immediately publishing a long sustainability report that is loaded with greenwashing and information that investors do not need.

If your company's core ESG disclosure is well organized, it can be communicated in many manageable ways and combinations including websites, stand-alone topic collaterals, corporate policies and position papers, KPI content indexes and/or sustainability reports, and proxy statements, which are growing in popularity for expanded sustainability-related content).

There is nothing cast in stone that says your company must produce a sustainability report immediately out of the starting gate. Instead, you can take a building-block approach, as your SMEs are able to support you in appropriate disclosure and performance progress on dedicated topics. A modular approach can provide flexibility initially and for ongoing updates, to align with limited resource availability and budget considerations.

Producing a full sustainability report initially can be daunting, so look for other means online that may be instructive. For example, British Petroleum (BP) provides a simple ESG data sheet on its website to point stakeholders to ESG performance data and ESG-related publications.

If your company has already produced a few years of sustainability reports, the BP example could also be helpful in considering how modular updates can spread out sustainability-related disclosure updates throughout the year, smoothing out internal resource assignments and controlling needs for increased budget allocations.

Consistent with the modular approach concept, the Global Reporting Initiative (GRI) shifted its ESG Standards to a modular format a few years ago to allow companies greater flexibility.

There is no need to reference more than one reporting framework for your inaugural effort, but you may find that several subcategory KPIs in the primary framework chosen have parallel KPIs in other frameworks (i.e., CO2 emissions) that enable selective reference to other frameworks and respective KPI numbering systems.

GRI provides information about linking GRI reporting to other frameworks and reporting guidelines. A current example of this approach can be found on page 9 and an appendix in the recently published FIS Sustainability Report. Also realize that it is not necessary to respond to every KPI included in any of the voluntary framework standards guidelines. In fact, Nasdaq suggests smaller companies attempt to just focus on 30 KPIs initially and build from there.

### *Avoiding Pitfalls*

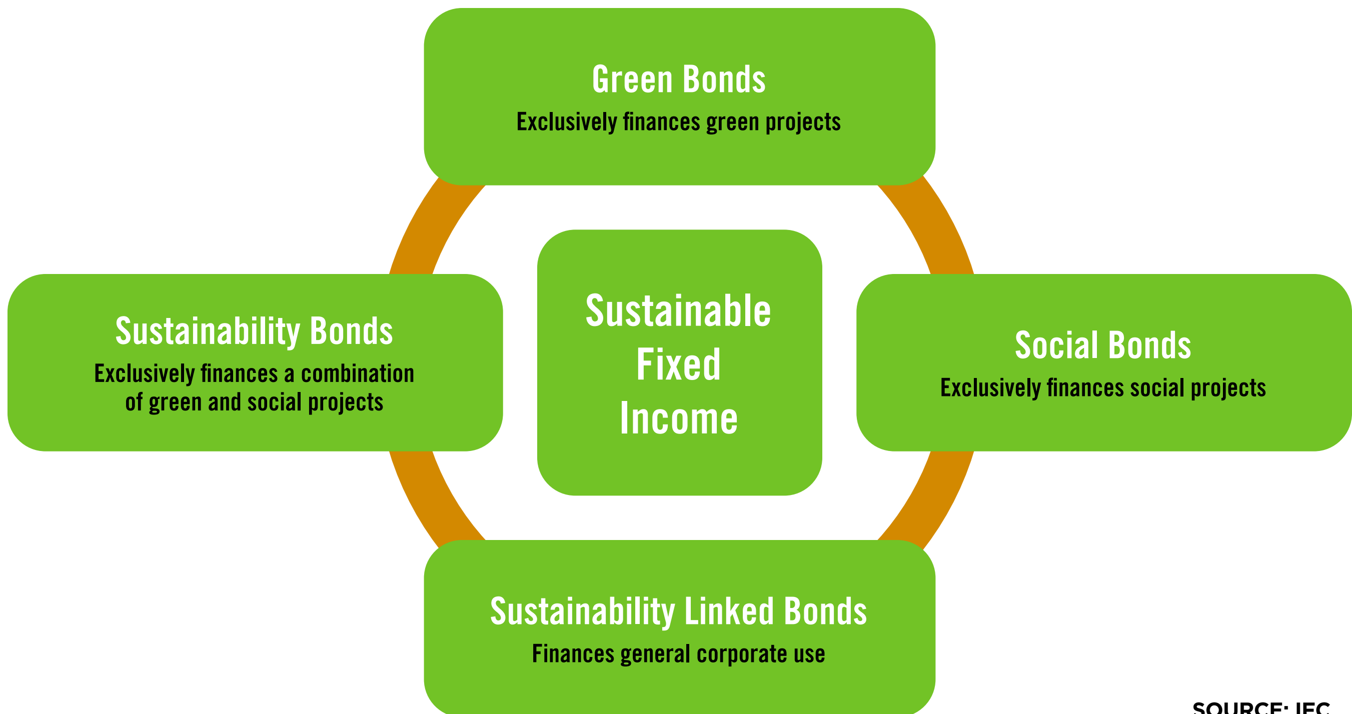
What are some common pitfalls in ESG reporting? The structure of reporting systems and incompatible (or difficult to gather) data are two that are often encountered.

Take a moment to shift from a "glass half empty" to a "glass half full" mindset to address these challenges.

First, review what your company already discloses or will soon disclose in its public SEC filings. Where is this information consolidated internally, how is it done, and who controls it? Think about how to coordinate use of this information in your company's voluntary sustainability report and collaterals.

The SEC will soon require greater disclosure related to human capital and human capital management (also check for other germane ESG-related interpretive SEC guidelines), so that is an opportunity to align your information to meet these new mandates.

A recent article titled, "ESG Disclosure Trends in SEC Filings," published by the law firm White & Case, provides a trove of other examples where you may find existing consolidating systems and disclosures. The article authors indicate, "[While] the trend




SOURCE: IFC

towards increased ESG disclosure in SEC filings is pronounced . . . companies should assess their investors' policies and consider engaging with investors in order to determine which ESG information about their company is important to them . . . [and] carefully consider where to place the ESG disclosure. Investors seeking ESG information do not necessarily expect any or all of that information to be presented in SEC filings, and sustainability disclosure on corporate websites can provide effective vehicles for this disclosure to investors."

Second, take a look at materiality and pare back. Just because your peers are disclosing various aspects of ESG is not necessarily a reason for your company to do so. This is where it is vital to get your CFO on board with the internal ESG team efforts.

Third, have confidence that third-party raters, rankers, and data providers have adapted their proprietary databases and analytical frameworks to take in inputs from whatever voluntary ESG reporting framework(s) a company chooses to use. Their analysts already know how to "map" the different voluntary KPI numbers to their proprietary system(s) purpose.

### External Perspective

Prioritizing which reporting framework(s) to reference, which investors to target, which raters and rankers to heed, which data providers (and now artificial intelligence analysis tools to monitor) is a challenge, since the collective third-party influencers with respect to ESG keep shifting as the field continues to mature.

A few recent announcements from 2020 capture just how fluid things are in the ESG area:

- November 25: SASB announced it will merge with IIRC, their combined entity will be called The Value Reporting Foundation.
- November 17: Deutsche Börse announced it will acquire ISS.
- October 20: Data provider FactSet announced it is acquiring TrueValue Labs, a pioneer in AI-driven ESG data.
- October 11: ISS announced it will acquire FICO® Cyber Risk Score Business.
- September 22: The Big Four announced a joint initiative to unveil a coordinated ESG reporting initiative together with the International Business Council (IBC) that entails 21 core metrics and 34 extended metrics, in their drive to create a common accounting framework.
- September 11:CDP, GDSB, GRI, IIRC and SASB announced they would join forces to work together toward comprehensive [ESG] corporate reporting.
- August 19: CFA announced plans to develop its own ESG disclosure standards framework.
- July 13: GRI and SASB announced a collaborative workplan to help stakeholders better understand how the standards may be used.

### *Standards and Frameworks*

There have been over 100 ESG standard-setting initiatives to date. There have also been many ESG partnerships and association initiatives that address various environmental and social issues, themes, and hot topics germane to the sector.

See the article, *"The Complexity of ESG Reporting Frameworks, Emerging Convergence Trends,"* by Louis Coppola, EVP at the Governance and Accountability Institute, on page 12 of this issue for a more detailed perspective on reporting frameworks.

In the process of prioritizing which framework(s) your company chooses, make sure that those third-party raters, rankers, and data providers that your company or board follows closely are aware of newly released company ESG updates and make sure they are easy to find on your company's website. Don't be shy to contact them directly to ask for a re-review of their ratings/rankings on your company, if your team has achieved substantial additions to your company's ESG-related disclosures.

### *Third Parties and AI*

There are hundreds of third-party raters, rankers, and data providers out there too that are consuming whatever ESG information they can find on your company.

Including a framework content index at the end of your sustainability report or publishing a content index on your company's website, even before investing time and expense into producing a full sustainability report, can go a long way to making sure your company's ESG efforts and performance progress can be easily accessed by external stakeholders.

The emerging application of artificial intelligence to ESG makes it especially important for your company's ESG reporting to be well organized and easy to find and "read."

### *Emerging Investment and Fixed Income Opportunities*

There is a burgeoning arena of green and sustainable fixed income opportunities through the bond and loan markets. One example of a forerunner in this approach is the International Finance Corporation (IFC), the private sector arm of the World Bank Group (WBG), that provides loans and equity investments to companies that meet or demonstrate a commitment to robust environmental and social performance standards. On the other side of its balance sheet, IFC has led the creation of AAA-rated sustainable bond opportunities for investors seeking to embed ESG criteria in their portfolios.

Esohe Denise Odaro, Head of Investor Relations at IFC, says, "One of IFC's institutional mandates is capital market development, so sustainable and green capital market products are a natural haven for us given our long-established efforts in the ESG domain. The market recognizes that our clients are held to stringent environmental and social values."

Working with Global Pension Investment Fund (GPIF), the largest pension fund globally, IFC and the WBG published a report that makes practical recommendations to support the broadening of ESG investing across fixed income asset portfolios.

### Resource Allocation and Budgeting

Up-front work to assess the scope, scale, scheduling, and expectations regarding your ESG disclosure and positioning efforts, whether inaugural or advanced, can make a huge difference in cost, return on effort (ROE), and return on investment (ROI).

ESG disclosure efforts can be expensive but maximizing internal resources can contain costs as much as possible.

Since ESG disclosure, voluntary reporting, and proprietary framework mapping can get exponentially complicated, it is very important to take the time up front to conduct some level of peer benchmarking and materiality assessment of your company's risk and impact profile.

Be brutal in prioritizing only those aspects that are truly material to your company and be bold to clearly indicate when any individual KPI is not relevant. The latter is important for third-party raters, rankers, and data suppliers to know, so they don't ding your company for non-disclosure or, worse, attempt to interpolate an answer to fill in the blank by looking at what some other sector peers might have indicated.

Third-party raters, rankers, and data providers have adapted their proprietary databases and analytical frameworks to accept input from voluntary ESG reporting framework(s) or other sources of company ESG-related disclosures. So, if it is an established framework, their analysts and system logics should know how to map different KPI numbers and responses into their proprietary system(s).

Be watchful that these third parties do not try to get your company to do their work for them to populate their databases, which then becomes your staff cost instead of theirs.

The ultimate reward to hard work is to realize tangible and intangible return. Having a right-sized and defensible ESG positioning for your company can open unexpected doors and strategic opportunities. IR

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