SURMOUNTING THE WILD WEST OF CORPORATE ESG EXPECTATIONS

ESG reporting frameworks, ratings, rankings, and data providers continue to proliferate. Focused Corporate ESG strategy and approaches can help IROs navigate the landscape.

BY PAM STYLES

Corporate leaders today largely recognize that environmental, social and governance (ESG) disclosure is here to stay and are including expanded ESG factors in ongoing operations and communications strategy.

Frustrations loom large, however, in dealing with the "Wild West" of constantly changing stakeholder expectations across rugged trails of possible disclosures and ESG frameworks, raters, rankers, data providers and third-party influencers.

These issues are being raised with regular frequency.

Resources and Advice

The Conference Board recently released an excellent practical guide for companies to think about how they might tell their sustainability story while dealing with dynamic and rapidly evolving regulations, reporting frameworks and ESG ratings firms. The guide also addresses active SEC considerations of various potential ESG reporting mandates.

I interviewed the Conference Board Guide author—Thomas Singer—and several other ESG experts to gather perspective about how corporate leaders and management are working to meet investor and stakeholder expectations while the field of third-party influencers and ESG information providers evolves.

"There was a time when companies could get away with not reporting, but those days are pretty much over, even though still largely voluntary," Singer says.

In terms of a Wild West analogy, he agrees that "ESG is going through a messy period right now," noting the increasingly complex landscape and jockeying for survival among hundreds of players in the ESG field. Common estimates suggest that the ESG landscape includes more than 100 voluntary ESG reporting frameworks and as many as 600 or 650 raters, rankers and data suppliers.

Singer encourages companies not to expect a lot of change in the near term, but to "take ownership as you can as a company and have conviction in your decisions." He suggests taking these steps:

- Be involved in [legislative/regulatory/framework/rater] comment periods to influence change.
- Be more proactive in communication directly with investors and stakeholders to not be dependent on frameworks or raters.
- Be selective in active focus on a handful of raters that have clear value in their applicability and methodology to your company and sector; be a bit more passive with the rest and don't react to every poor rating.

"Currently there is no one perfect framework nor perfect rater that can satisfy all stakeholders. Investors are relying on multiple information sources and developing their own ESG assessment methodologies to offset weaknesses in any one particular ratings or other source," Singer explains.

The frustration of dealing with raters and frameworks that do not understand the nuances of the individual company and its industry have led some companies to work collectively within their industry groups to develop their own approach to ESG reporting guidelines suited to specifics of their particular industry. Two examples include the ESG-focused forum begun within the Edison Electric Institute (EEI) for its utilities and power generators members and the ESG framework by GRESB for real estate assets.

The AEP Approach

ESG veteran Sandy Nessing, Managing Director of Corporate Sustainability at American Electric Power (AEP) offers some thoughts about the current Wild West.

AEP is a $42 billion market cap domestic utility company with annual revenue of about $15 billion and approximately 17,000 employees. AEP has been a significant leader in ESG reporting within its industry and spearheaded greater sector awareness and participation in ESG through active encouragement of the EEI to develop ESG research and reporting guidelines specifically appropriate to domestic utility and power generating companies.

Nessing has seen a lot. She explained that AEP focused on ESG long before the company approached EEI around 2006/2007 to communicate that action was needed to do something constructively about reporting as an industry in terms of ESG guidelines.

From her perspective, "You have to figure out what is important and what isn't. You have to focus, because you can't do it all. You've got to cut through the noise and hold your ground.

"You need to give management and the board the bigger picture, so they don't just focus on one rater's rating or another or react to new expectations of various stakeholder groups and organizations that do not have a practical understanding of the business or sector(s) in which your company operates."

Instead of reacting to every ESG rater, ranker, database or other, Nessing started asking AEP stakeholders what research resources they used. That resulted in purposefully choosing to ignore certain "opportunities" to engage with some well-known raters and/or rankers, because the heavy lift of engagement was not commensurate with the likely interest in outcome by AEP stakeholders.

Nessing shared that example because she believes the most important thing is "to not lose sight of why we're doing this work. Don't just chase the ESG data and shiny ratings. Don't lose track of the stuff that really matters. This is amazing work and it's going to facilitate amazing change."

Value of ESG KPI Content Indexes

Lou Coppola, EVP and Co-founder of the Governance & Accountability Institute (GAI) offers some insight on including ESG key performance indicator (KPI) content indexes in corporate reports. He is recognized as an expert in ESG research, data, disclosure and aggregation.

These ESG KPI content indexes have effectively become the fourth leg of a company's critical reporting, after the profit-and-loss statement, balance sheet and cash flow financial statements. The indexes present organized and consistent data to analysts, investors, data miners and stakeholders.

"An ESG content index (or several) using a hybrid standards approach is critical on the front end to enable more reliable and efficient investor and rater analysis; structured information is also much more readily found by artificial intelligence (AI) mining tools, all which promote accuracy and usefulness of data," Coppola explains.

"A well-developed content index includes KPIs designed to respond directly to multiple investor ratings methodologies and is proving invaluable on the back end as an indisputable reference for the company's use to push back on raters and data providers that they find have inaccurate data on their company."

Coppola and his team have developed a proprietary internal platform to help companies monitor multiple raters and ESG data providers' platforms for data accuracy and flag inaccuracies or missing information to the respective entities for corrective attention. Capabilities such as these will surely prove to be a game changer for companies frustrated by gross inconsistencies and in ESG information. But a company needs to start by helping itself first by publishing (or referencing) its ESG data in an organized way that a content index facilitates.

If you have read this far and are saying to yourself, "My company is too small and too far behind to participate in ESG disclosure and engagement to this level of sophistication," check your hesitancy and read on.

FIS Launches Award-Winning Inaugural ESG Report

It is naturally daunting for company boards and internal ESG leaders just getting started in their public ESG reporting and positioning journey to feel like they can never get to the mode of offense instead of defense. The other way to look at it is that companies that have waited until now to place greater emphasis on their ESG journey can often leap ahead in their inaugural efforts, because others have been trailblazers before them. One such company that succeeded is FIS.

FIS produced an inaugural corporate responsibility report that won an IR Magazine award in 2021 for Best ESG Reporting—right out of the gate.

Andrew Ciafardini, Chief Sustainability Officer at FIS, led this effort. FIS is a $70 billion market cap global company with annual revenues of approximately $13 billion and more than 60,000 employees.

While the size and resources of FIS might seem intimidating to smaller companies, just think about how daunting a task it was for FIS to figure out how to organize and tailor its inaugural sustainability report to suit its priorities, and to synthesize its ESG performance factors into a cogent report. The simplicity of the FIS approach included:

1. Established unique FIS pillars of growth based on materiality assessment.
2. Organized the report flow of priority topics germane to the company. In this instance FIS found United Nations Sustainable Development Goals (SDGs) useful.
3. Selected GRI as its primary reporting framework to provide a robust ESG KPI content index in accordance with GRI Standards with linkages to SDGs, then provided additional selective response to another framework, in this instance SASB.

FIS chose the voluntary framework(s) that worked in parts or as a whole to convey the message the company wanted to convey. While it took nearly 60 pages to do so, given the size of FIS, the simplicity of the approach can be right-sized for any company to emulate. The FIS approach established flexibility to adapt company messaging across multiple reporting frameworks that will be important going forward while the Wild West of ESG frameworks, raters, rankers and data suppliers continues to evolve.

"First, before getting started, it's critical for a company to step back and identify the 'Why,'" Ciafardini says. "What are the main reasons spurring the need to begin ESG reporting? Who are the stakeholders driving the discussion? And what are you hoping to achieve with your disclosures? Clear objectives are vital.

"Second, it's important to recognize that it's not always the loudest voice that should guide your strategy and selection of

ESG disclosure topics, but rather the topics that you are consistently hearing about across your shareholder and stakeholder bases. This can be done passively or by intentionally soliciting input from investors and other stakeholders to maintain focus on what they really need and want to know. If you try to address every issue for every audience or reporting framework, your disclosures won't be manageable.

"While traditional governance agencies have also become ESG raters, it's important to understand that rating agency scores are sometimes just one factor for an investor's assessment scorecard and decision-making process. If you need to, due to capacity constraints, address shareholder disclosure needs first and build from there."

"Third, when working on the report, the key is to build in agility and flexibility in your approach, and by all means stay focused on the most material ESG topics. It's critical to be able to tell an integrated sustainability narrative vs. a collection of ESG metrics. Don't worry about the length of the sustainability report, but rather focus on what you need to say to address your company's particular stakeholders' expectations."

"Finally, it's important to embrace ESG as a team sport that requires the ability to pull experts across the company to be successful. Leveraging your colleagues and external partners is vital, and where possible utilizing an outside consultant for your first report can be immensely helpful."

FIS demonstrated that just because your company may only be starting to focus more attention on your ESG journey and public positioning, you are not doomed to feel behind forever.

Key Takeaways

Hank Boerner, Chairman and Chief Strategist at GAI, has been involved with ESG and sustainability since the inception of this field.

Boerner observes, "We are now seeing companies considering ESG in all complex elements of corporate strategy and competitive positioning to deliberate purpose." ESG is effectively being integrated as an everyday part of company strategy and operations management.

He is also monitoring "emerging topics and trends across the ESG supply chain, activism and legislative/regulatory areas to anticipate what might evolve in ESG reporting expectations."

He adds, "It is important to remain flexible right now in terms of reporting and disclosure so your company can adapt to changes that are bound to come in the process of this developing Wild West episode."

As you (re)position your company in its developing ESG journey, aim to make the ESG reporting frameworks, raters and data providers work for you, instead of the other way around. IR

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