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eBook | Ask the EHSQ Expert

Unpacking ESG: 6 Questions You Were Too Afraid to Ask

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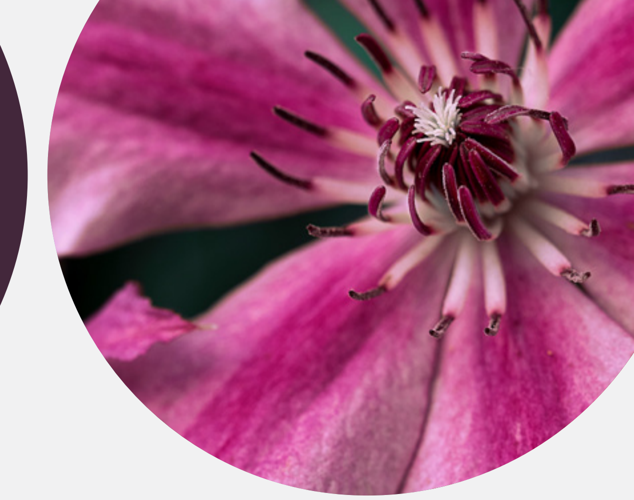
Introduction

For Environmental, Health, Safety and Sustainability (EHS&S) professionals, being inundated with a slew of industry acronyms to learn is nothing new – GHG, SDS, TRI – the list is long. But a newer term that is popping up with greater frequency among the EHS&S practitioners we speak with is Environmental, Social, and Governance (ESG).

Why? There's significant overlap with the type ofdata EHS&S professionals have been collecting and reporting on for years with the type of information shareholders and the investor community now want to see from an ESG reporting perspective.

This is good news for EHS&S professionals. That said, as an emerging field, a lot of questions remain which is why industry experts, Christine McCarty, Product Marketing Manager at Cority, and Jessica Francisco, Head of Sustainability for North America at Arcadis, got together to answer six of the most frequently asked questions we get about how to get started with ESG reporting.



Christine McCarty

Product Marketing Manager, Cority

Jessica Francisco

Head of Sustainability for North America, Arcadis

Question 1

I often hear the terms ESG and Sustainability used together. How is ESG different from Sustainability?

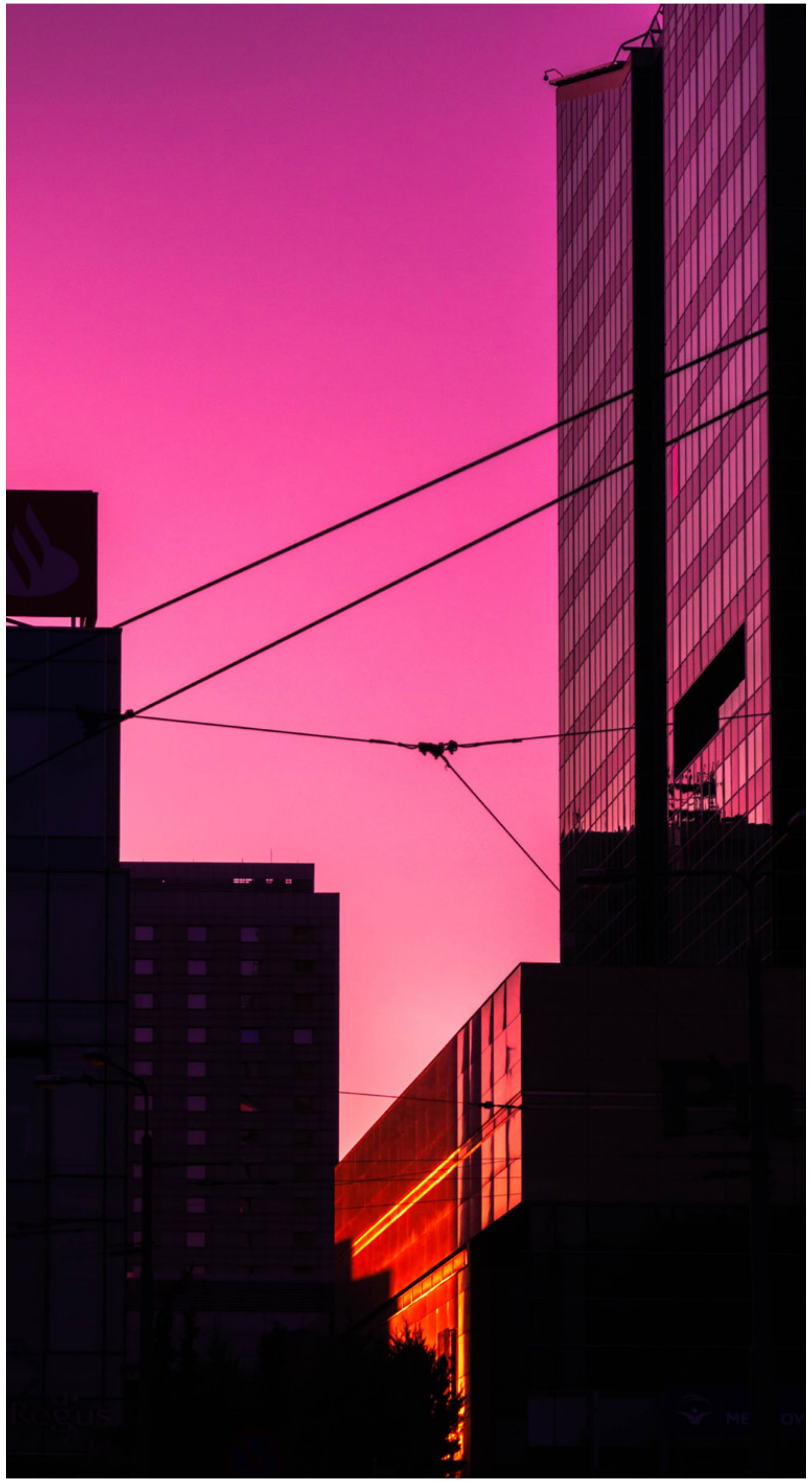
Christine: Sustainability is a term that has been around for many years to describe the idea that corporations should generally "do good" and take steps to protect the planet and avoid depletion of natural resources. It's also associated with the "triple bottom line", an economic concept which suggests that in addition to the standard bottom line (profit), companies should also be concerned with people and the planet. These terms have been used over the last thirty years and Jessica will share the most widely used definition of sustainability in a moment.

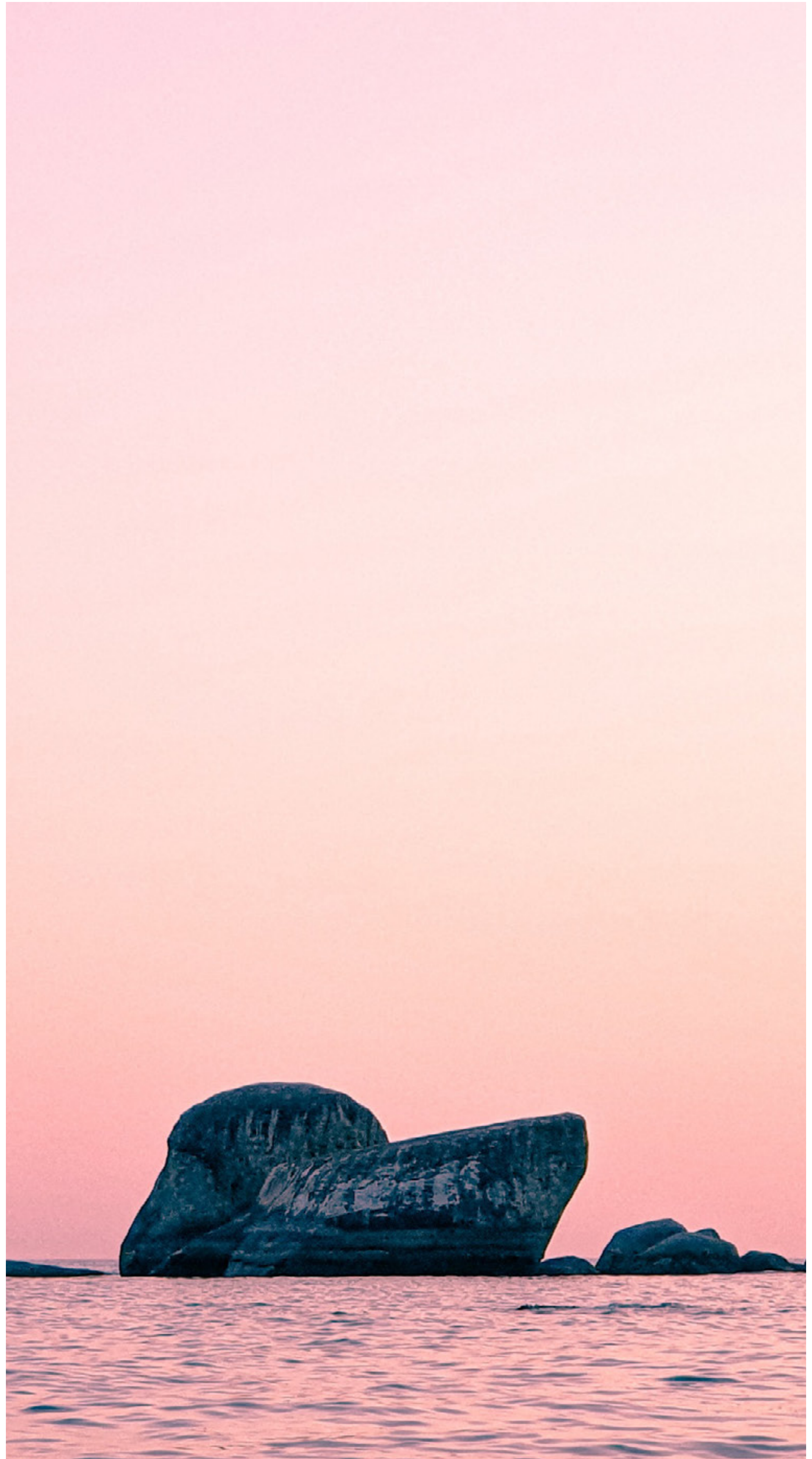
Some practitioners I've talked to say they believe ESG is just a synonym for sustainability, or the latest buzzword. However, the interest that financial institutions and investors have taken in ESG radically differentiates it from sustainability.

Here's why: ESG is a specific set of financial criteria that has roots in a 2005 report called Who Cares Wins by the UN Global Compact that included recommendations by the financial industry to better integrate environmental, social, and governance issues in analysis, asset management, and securities brokerage.

ESG reporting provides transparent data to enable stakeholders (including investors) to understand and evaluate companies' performance - the same way companies use information internally to drive decision-making.

Jessica: The United Nations Brundtland Commission has provided the most referenced definition for sustainability: "Sustainability is meeting the needs of the present without compromising the ability of future generations to meet their own needs." While sustainability is a broad term, it typically addresses an organization's environmental protection, social advancement, and economic development efforts. Through their activities, all organizations have both positive and negative impacts on the environment, society, and economy.





> "Sustainability is meeting the needs of the present without compromising the ability of future generations to meet their own needs."

Jessica Francisco
Head of Sustainability for North America, Arcadis

ESG performance is used as an important capital market measure. One that is used to identify superior risk-adjusted returns and indicates a more precise measurement of an organization's ESG performance. As such, investors are increasingly using ESG criteria in their analyses to identify material risks and growth opportunities for companies.
Let's take a closer look at what falls into each pillar of ESG:

The Three Pillars of ESG

Environmental Pillar

- Climate change
- Greenhouse gas emissions
- Energy
- Resource scarcity
- Biodiversity
- Water
- Waste
- Pollution
- Environmental compliance

Social Pillar

- Employee relations
- Health and safety
- Training and education
- Diversity and equal opportunity
- Non-discrimination
- Human rights
- Privacy and security
- Union relations
- Local community impact

Governance Pillar

- Board diversity and structure
- Executive compensation
- Bribery and corruption
- Political lobbying and donations
- Procurement practice
- Risk management

Question 2

What is driving the intense interest in ESG?

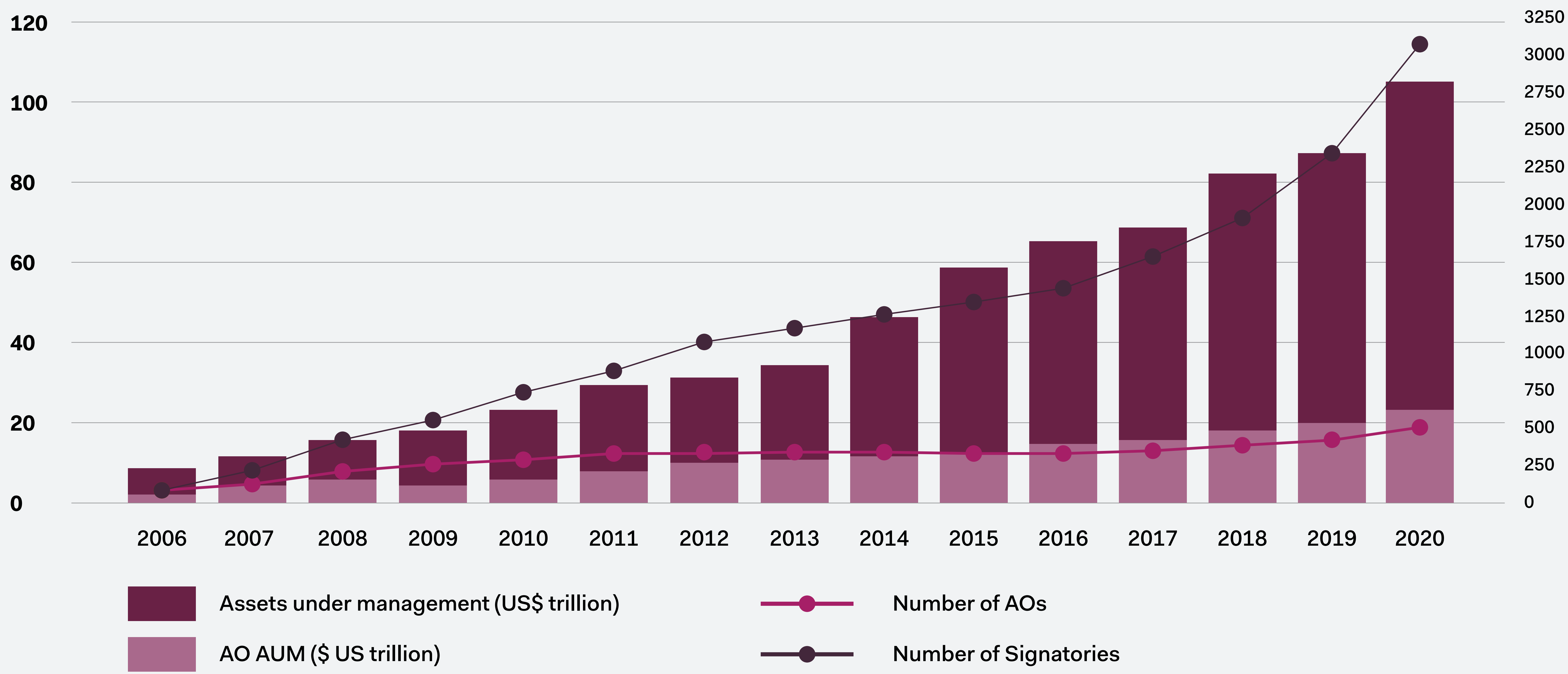
Jessica: While many stakeholders influence sustainability actions for organizations, investors and shareholders are now driving the intense interest in ESG. With a wide range of complex, global sustainability risks on the rise, investors are increasingly considering ESG factors in their investment decisions.

In 2006, the Principles for Responsible Investment (PRI) were developed by an international group of institutional investors reflecting the increasing relevance of ESG issues to investment practices. There are now more than 3,000 investors who collectively manage over $100 trillion in assets globally that have become PRI signatories. This represents the majority of the world's professionally managed investments.

There's plenty of evidence that companies prioritizing ESG issues actually generate superior long-term financial performance across a range of metrics. As such, investors are driving companies to disclose their ESG risks as well as their strategies for addressing those risks over the long term.

> "For a long time, there was a belief that investing in sustainability meant sacrificing financial performance, but ESG has really proven that this thinking is incorrect."
>
> **Christine McCarty**
> Product Marketing Manager, Cority

Total Assets Under Management and PRI Signatories



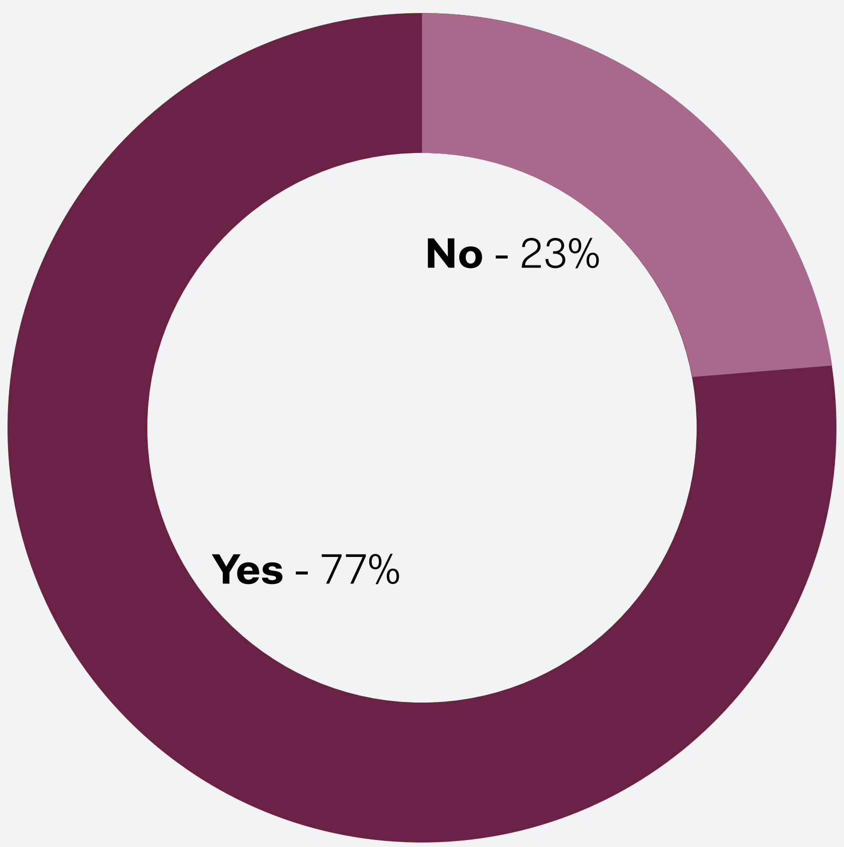
Source: “About the PRI.” PRI: Principles for Responsible Investment. December 01, 2017.

Christine: I'll echo what Jessica said: financial success of ESG funds is really what's driving the intense interest right now. ESG funds are providing strong financial returns for investors. **For a long time, there was a belief that investing in sustainability meant sacrificing financial performance, but ESG has really proven that this thinking is incorrect.**

If anything could have dampened enthusiasm for ESG, it should have been the tumultuous markets of 2020 during the global COVID-19 pandemic. However, multiple analyses have demonstrated that ESG funds consistently outperform non-ESG funds. For example, a Bloomberg analysis found that the average ESG fund fell by only 12.2% in March 2020, which was almost half the decline of the Standard &Poor's 500 Index. Index funds investing in companies that rate highly on ESG factors have received a boost overall during the pandemic.

It's also becoming increasingly common for investment managers, banks, and asset owners to commit to setting portfolio targets

Vast majority of institutional investors plan to stop investing in non-ESG products by 2022



Do you intend to stop investing in non-ESG products within the next 24 months? (Institutional Investors)

Source: PwC Global AWM Research Centre

that are aligned with the Paris Agreement. For example, as part of the United Nations Net-Zero Asset Owner Alliance, thirty of the world's largest investors with $5 trillion assets under management have collectively agreed on concrete portfolio decarbonization targets. In January 2020, the CEO of BlackRock (the world's largest asset manager) announced initiatives to place sustainability at the center of their investment approach because they believe that climate risk is investment risk. But, for those who still aren't convinced that ESG is going to be a critical financial factor in the future, consider that a PWC survey found that 77% of institutional investors intend to stop investing in non-ESG products by the end of 2022.

This all underscores that climate change is a pressing concern around the world and financial institutions are looking for ways to mitigate risks.

Moving away from just the financial aspect, when it comes to companies being evaluated on the merits of their ESG disclosures, many are using it as another opportunity to distinguish themselves to their customers. Of course, companies are looking for ways to maximize profits, but they are also beginning to see that environmental performance can be a differentiator for their products and their brands – which in turn can help companies be more resilient and increase sales.

Question 3

Are there Different Approaches to ESG Across the World?

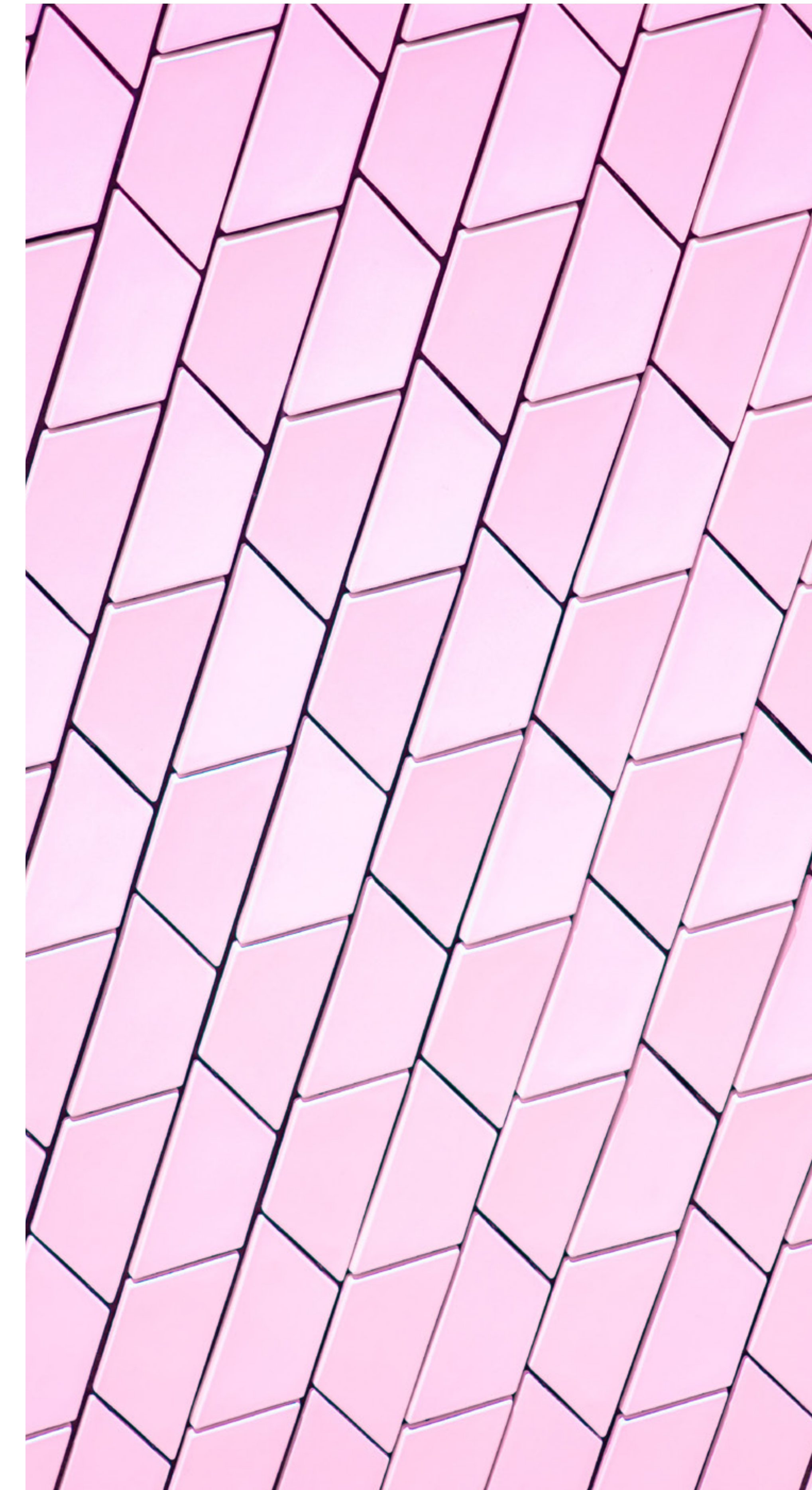
Jessica: With global reporting and disclosure frameworks providing the backbone for most organizations, there are generally similar approaches to ESG across the world. However, there may be local or regional differences in ESG topics reported and regulatory reporting requirements.

Carrots & Sticks reviews ESG reporting regulations around the world. The 2020 edition of Carrots & Sticks noted a substantial increase with 614 regulatory reporting requirements – an increase of over 60% from the 383 requirements in the previous report in 2016 – across 80+ countries. This increase in reporting requirements is driven by governmental bodies, financial market regulators, and stock exchanges.

Of the approximately 100 exchanges in the Sustainable Stock Exchanges (SSE) initiative, 55 exchanges have written ESG guidance and 24 exchanges have mandatory ESG requirements. *These stock exchanges reference the following reporting frameworks in their guidance documents:

While there are many reporting and disclosure frameworks for ESG performance, the investment community has typically prioritized the GRI, IIRC, SASB, CDP, and TCFD frameworks – and Christine will cover these in more detail in the next section.

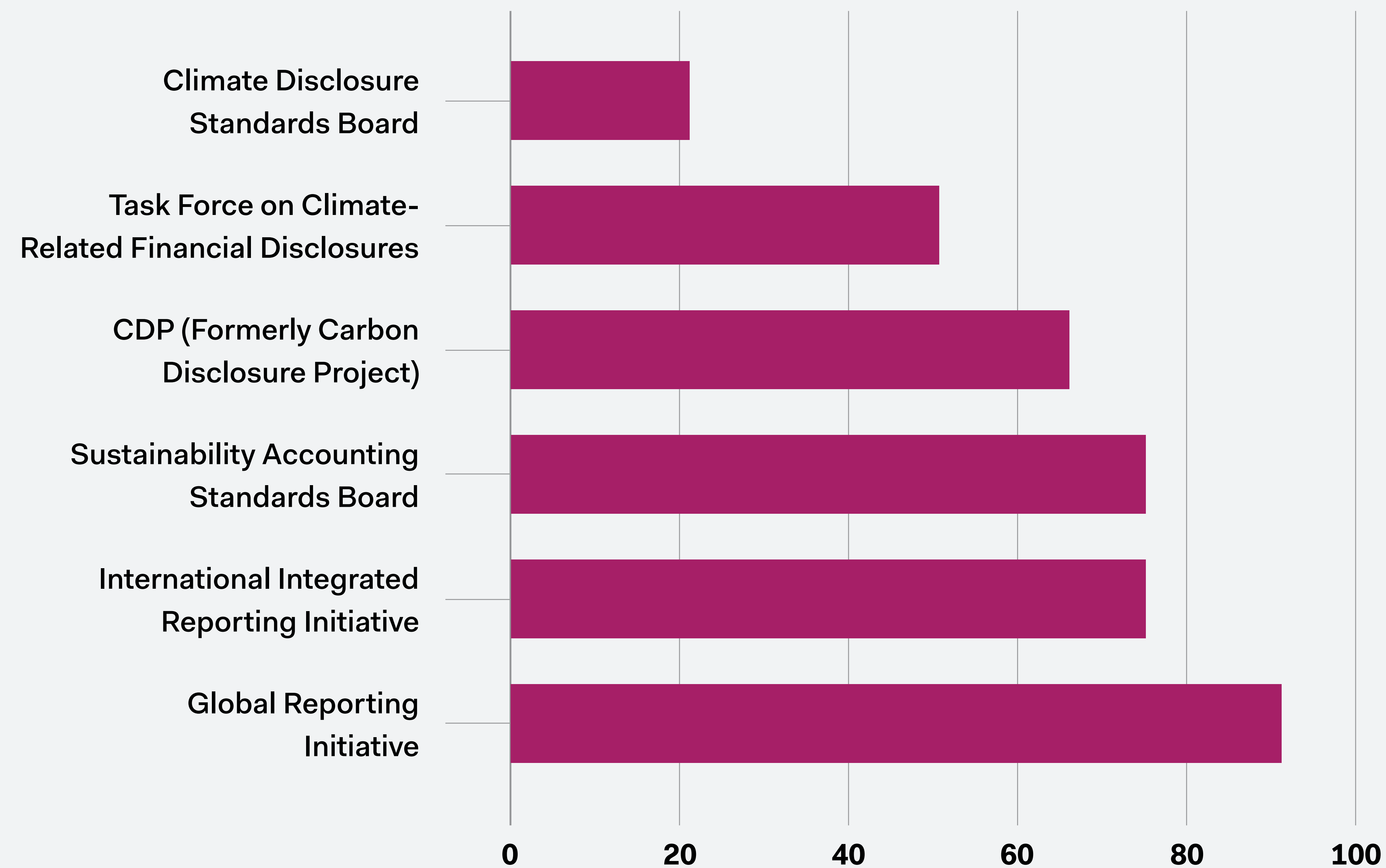
Christine: We do see some differences based on geography. At this point, a majority of sustainable assets are in Europe, so we are certainly seeing more of a drive there. However, this is rapidly expanding to the rest of the world. For example, with the new Biden administration's public interest in carbon reduction, GHG regulations, and setting net-zero targets, we may see more intense focus on ESG in the United States over the next few years – a significant shift from recent years.



"Given the Biden administration's interest in carbon reduction, GHG regulations, and setting net-zero targets, we may see more intense focus on ESG in the United States over the next few years."

Christine McCarty
Product Marketing Manager,
Cority

Referenced Reporting Frameworks in the Sustainable Stock Exchanges (SSE) Initiative*



Source: Sustainable Stock Exchanges Initiative

Question 4

Why are there so many reporting formats?

Christine: There's currently a multitude of sustainability frameworks and standards, though some investors are now calling for convergence around a single framework that will bring consistency and comparability (which Jessica will speak to in a minute).

Why? There's a general feeling that companies are overburdened with the different standards and there's a strong argument for consolidating into a single framework coming from both investors and companies providing ESG disclosures. Some have even suggested that mandatory reporting might be a way to accomplish this consolidation. In the future, we are likely to see some consolidation, though for the moment, these are some of the most common reporting standards companies should expect to see (see table page 18)

Jessica: As sustainability has expanded to address more and more topics, so has the desire to obtain more and more information on these topics. With each stakeholder group seeking a little bit more or a little bit

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Jessica Francisco
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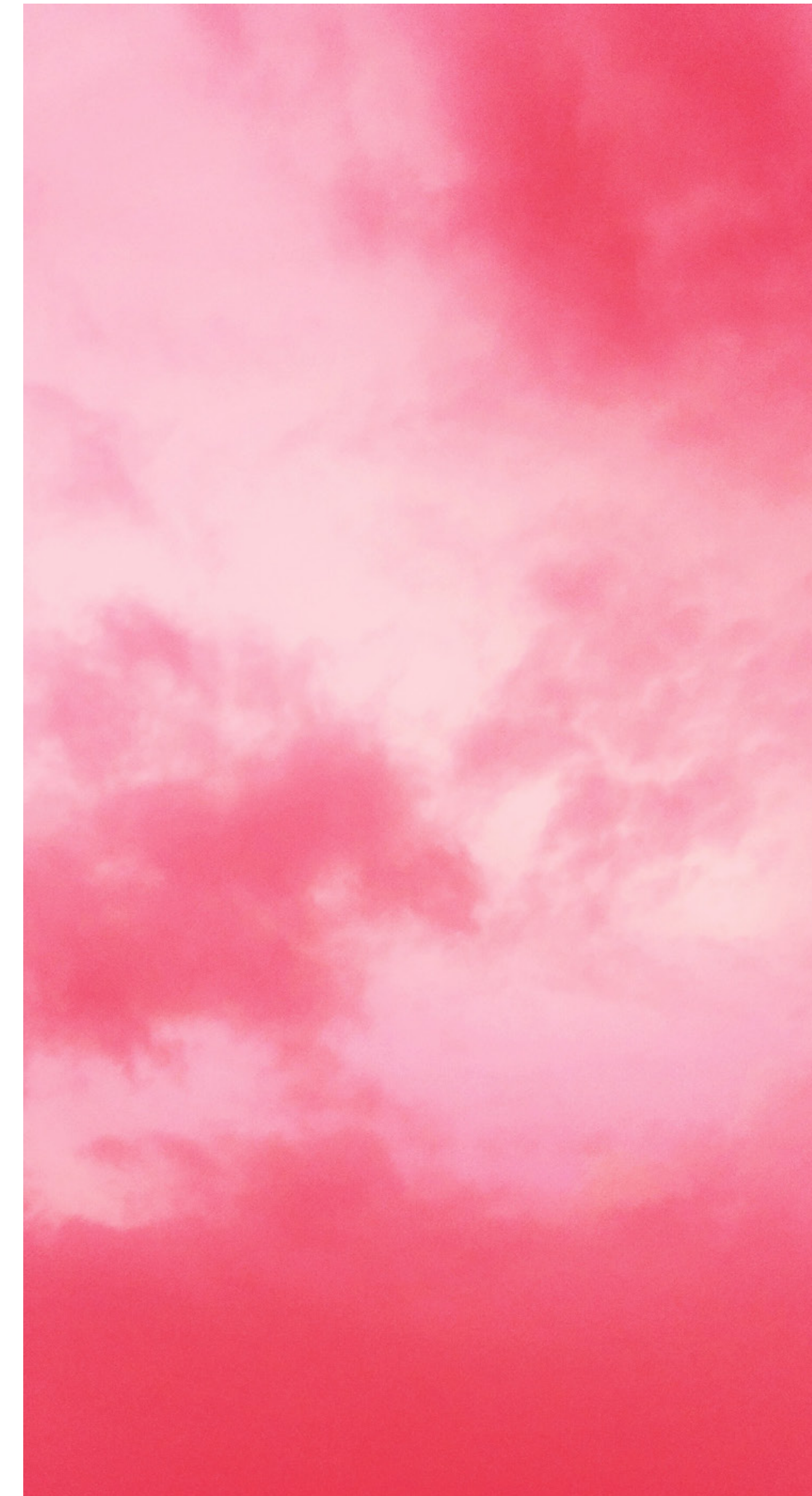


The Most Common Reporting Standards Companies Should Expect to See

GRI - an internationally recognized broad framework of standards for reporting on sustainability with requirements, recommendations, and guidance on 900 sustainability topics

CDP - the CDP is one of the largest investor-led reporting frameworks used internationally

Sustainable Development Goals (SDGs) - 17 ESG goals with 169 associated targets, set by the UN

UN Global Compact - 10 UN sustainability principles addressing broad sustainability issues with which companies can voluntarily demonstrate alignment

SASB - an investor-led sustainability framework focused on financially material issues

TCFD - recommendations intended to help companies account for climate-related risks in their disclosures

IIRC - an integrated reporting framework focused on how an organization's strategy, governance, performance, and prospects, in the context of its external environment, lead to the creation of value in the short, medium, and long term

GHG Protocol - a voluntary reporting standard for many companies and mandatory in the United States for large emission sources

EcoVadis - a sustainability framework that provides performance ratings for companies with global supply chains

different information, we have seen new sustainability reporting and disclosure frameworks emerging to meet those needs. As a result of this, we now have an alphabet soup of sustainability reporting frameworks and standards today, per the examples that Christine shared.

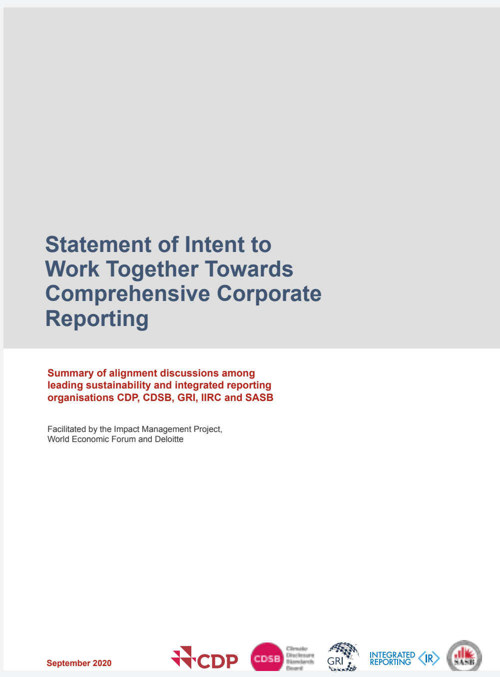
This has led to some onerous reporting requirements for many companies and confusion for the stakeholders trying to figure out what really matters. The good news is that there is growing consensus that there needs to be a globally recognized and adopted approach that enables comparable, consistent, and comprehensive ESG reporting.

At the 2020 World Economic Forum (WEF) Annual Meeting in Davos, 120 of the world's largest companies supported efforts to develop common metrics and disclosures on ESG factors for their investors and other stakeholders.

Additionally, BlackRock continued to advocate for more widespread and standardized ESG reporting in their Q3 2020 BlackRock Global Quarterly Steward Report. BlackRock stated that "the proliferation of disclosure initiatives, many of which are overlapping, has led to duplicative efforts by reporters and a lack of consistent and comparable data. We believe that this could be resolved by aligning and converging to establish a globally recognized sustainability reporting framework and set of standards. Ideally, these would be developed by those with domain expertise in the private sector and supported by public policy makers as they move to require more comprehensive corporate reporting."

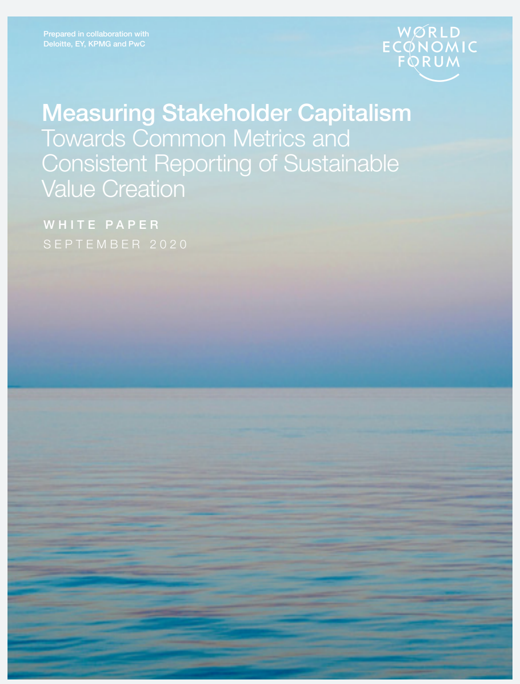
The good news is that there are currently multiple initiatives underway to develop global ESG reporting frameworks and standards. While many of these initiatives are still underway, I am optimistic that this increased collaboration will lead to consolidation of reporting frameworks – at least for ESG reporting for the investment community.

Examples of Intitiatives Underway to Develop Global ESG Reporting Frameworks and Standards

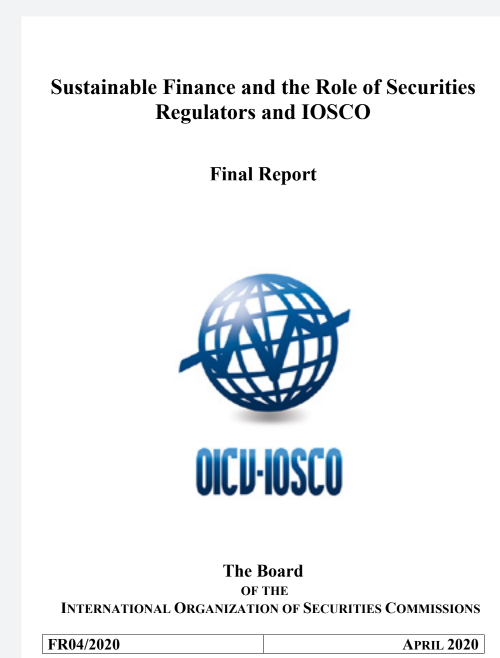


In September 2020, IIRC, GRI, CDP, CDSB, and SASB released a document announcing their joint effort to develop a comprehensive, globally accepted, corporate ESG reporting system.

The International Financial Reporting Standards (IFRS) will create a new Sustainability Standards Board (SSB) under the governance structure of the IFRS Foundation to develop global sustainability standards.



In September 2020, the World Economic Forum (WEF) with Bank of America, the Big Four (Deloitte, EY, KPMG, and PWC), and the International Business Council (IBC) released a set of universal ESG metrics and disclosures.



International Organization of Securities Commissions (IOSCO) established a Task Force on Sustainable Finance to improve ESG disclosures and enhance coordination of regulatory and supervisory approaches.

Question 5

Are there Ways I Can Be More Efficient When It Comes to ESG Reporting?

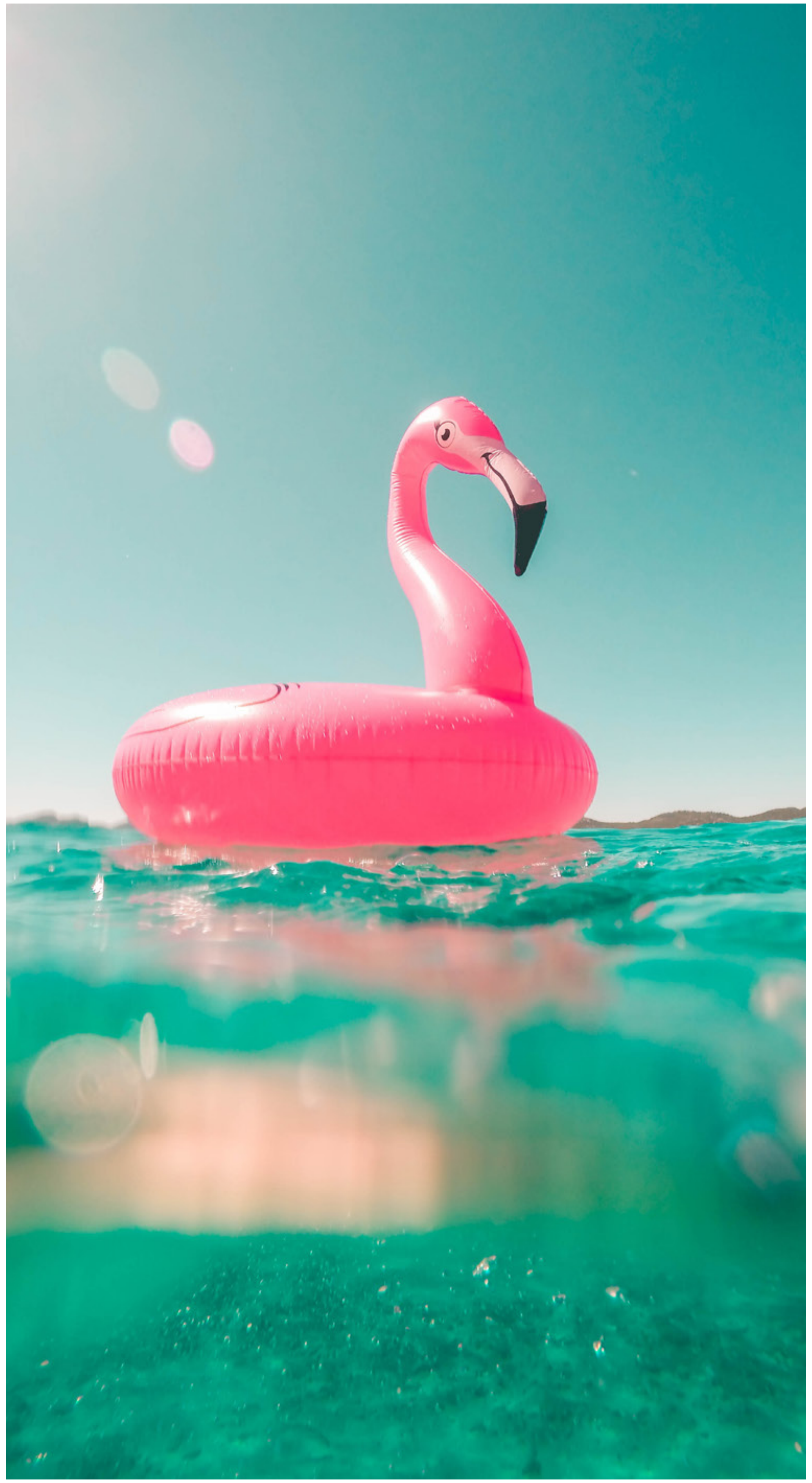
Christine: As we wait to see if a consolidated approach will emerge, there are some steps companies can take today to be more efficient with ESG reporting:

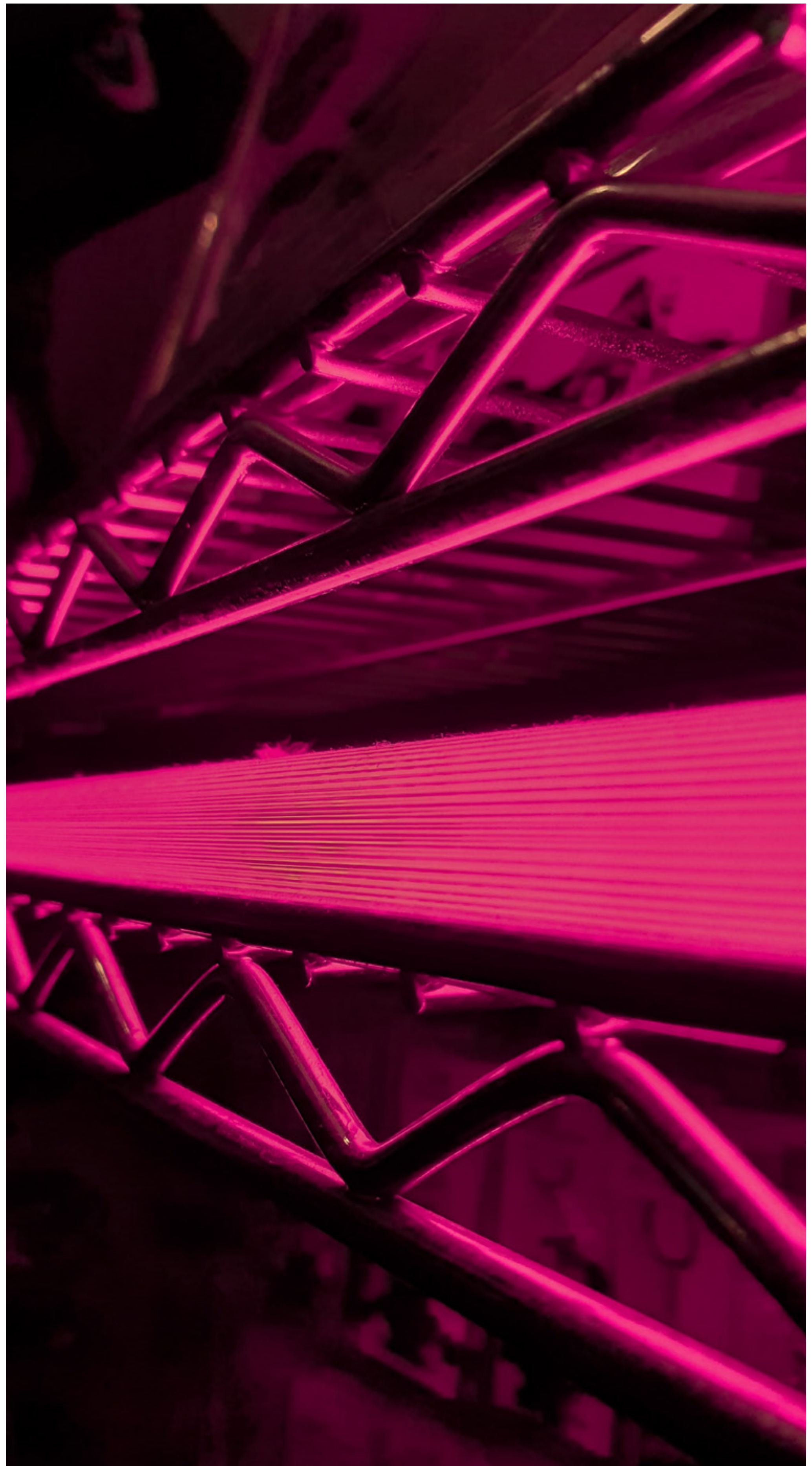
Having a single, unified platform that holds all your environmental data can be beneficial for the environmental component of ESG reporting. Whether you are monitoring utility usage and employee travel for GHG reporting or managing more robust environmental programs like air emissions, hazardous waste, and chemicals management, having this data in a single place enables you to enter once and then generate accurate reports for a variety of purposes including voluntary ESG reporting and mandatory government reporting.

Often, the data that is required for different disclosures and reports is common, but companies may need to do calculations and formatting in different ways. Having a single system to pull the data and run the necessary calculations can help to get accurate, consistent outputs. For some industries like utilities, oil & gas, manufacturing, and mining, there are heavy requirements for environmental reporting regarding air emissions, water effluents, and chemical releases in addition to voluntary ESG disclosures. Practitioners who leverage a unified platform to manage all these different programs can reap a few key benefits from using the same data sources across their programs:

- Gain efficiencies by not hosting, entering, and troubleshooting data in two places
- A unified platform helps with data integrity and consistency

If you are managing ESG disclosures, water, air, and GHG through siloed processes, you increase the likelihood that there will be inconsistences between your reports – rather than all your reports telling the same story. This is starting to be noticed by regulators. As we are seeing a proliferation of data that is now online and publicly accessible, there is more cross-checking happening.





> " If you are managing ESG disclosures, water, air, and GHG through siloed processes, you increase the likelihood that there will be inconsistences between your reports – rather than all your reports telling the same story."

Christine McCarty
Product Marketing Manager,
Cority

Jessica: Many companies are opting to report their ESG performance using multiple, voluntary frameworks and standards, many of which are overlapping. To more effectively and efficiently report your ESG performance, I recommend that you develop a deliberate ESG reporting strategy driven by the answers to the following four questions:

- ☐ Why are you reporting ESG performance?
- ☐ Where will you be reporting?
- ☐ What ESG metrics and indicators will you report?
- ☐ How will you track, monitor, and report your performance?

ESG Reporting Strategy Questions

Why are you reporting ESG performance?

The reasons for reporting your ESG performance will directly influence its quality, quantity and characteristics. Potential reasons for reporting may include, but are not limited to, the following:

- Comply with regulatory requirements
- Align with peers or competitors in your industry
- Satisfy stakeholders including shareholders, investors, customers, employees, or non-governmental organizations
- Explain how the company has assessed and responded to climate change risks
- Communicate ESG strategy, goals, and targets to stakeholders
- Demonstrate how ESG initiatives drive value for the company

Where will you be reporting?

To determine where your company will report ESG performance, it's important to first understand your intended audience:

- Start by mapping out all your potential stakeholders
- Once you have identified each stakeholder group, then you can determine the most appropriate channel(s) to reach those stakeholders
- Reporting channels may include everything from your intranet to your annual integrated report or sustainability report to specific questionnaires or disclosure platforms

What ESG metrics and indicators will you report?

Once you have determined why and where you will report your ESG performance, you will need to identify what ESG frameworks or standards you will follow and what ESG information you will report:

- For each ESG framework or standard, it's important to determine which metrics and indicators are appropriate for your company – keeping in mind your reporting objectives as well as the material topics for your company
- It's easy to become overwhelmed by the volume of information desired by stakeholders, so it's important to anchor on the information that is relevant, material, and reliable for your stakeholders
- You do not have to track, monitor and report every metric in the frameworks or standards you use

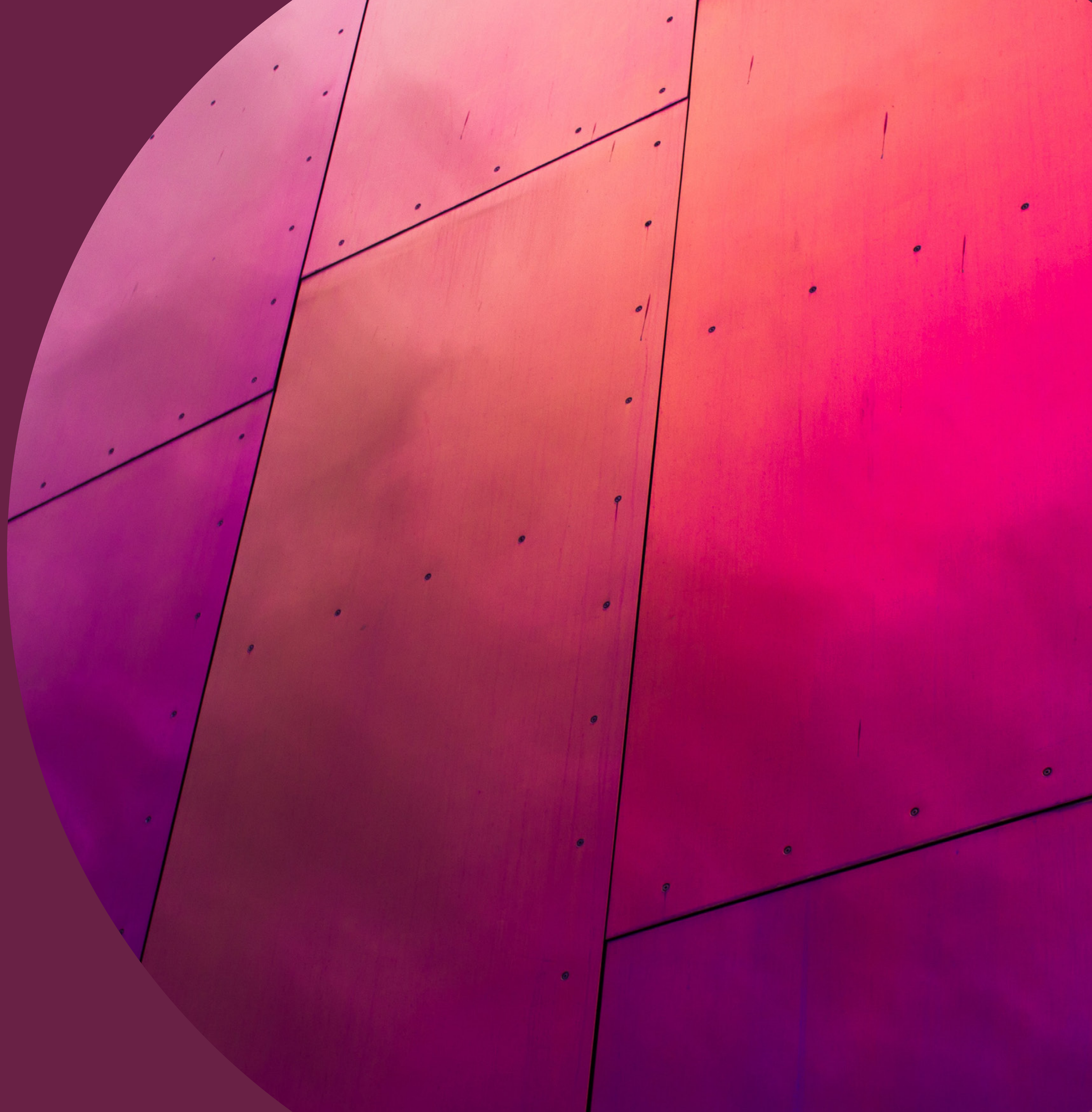
How will you track, monitor, and report your performance?

Finally, you will need to determine how you will collect information for the ESG metrics and indicators you have prioritized for your company. **Given that you will typically be gathering information for many departments across your organization, investment in a digital tool or software platform can drive significant benefits for your company.** These benefits typically include:

- Achieving value creation such as reducing costs or enhancing brand
- Improving business performance
- Controlling ESG risk
- Providing evidence of ESG performance

Question 6

What Are Some Current ESG Reporting Trends I Should Be Aware Of?



Christine: Sustainability and ESG reporting are continuing to rapidly evolve. Let's look at five key trends happening in the industry right now:

- Investors and shareholders are driving more and more companies to voluntarily report their ESG performance. In 2019, more than 8,400 companies also voluntarily disclosed to CDP their practices to measure and manage their environmental impacts. From 2018 to 2019, an additional 20% of global companies completed the CDP disclosures for climate change, water and/or forests.[i]

- New regulatory reporting requirements will continue to emerge globally. As we mentioned earlier, ESG reporting regulations around the world have increased over 60% in the last 4 years. There is every indication that this will continue in the future as more countries establish reporting requirements. Both the U.S. Federal Reserve and the U.K. Treasury released positions supporting climate risk disclosure in November 2020.

- With the increased pressure from stakeholders, many organizations are demonstrating their commitment to sustainable business practices by publicly disclosing ambitious ESG targets. Approximately 58% of global companies have carbon reduction targets and approximately 25% have water reduction targets. [ii]

- To support their sustainability programs, companies are seeking information on ESG performance from their partners throughout their supply chain. According to CDP's Supply Chain Report 2018/19, 35% of the 115 program members reported that they are engaging suppliers on climate change in 2019 – in comparison to just 23% in 2017. [iii]

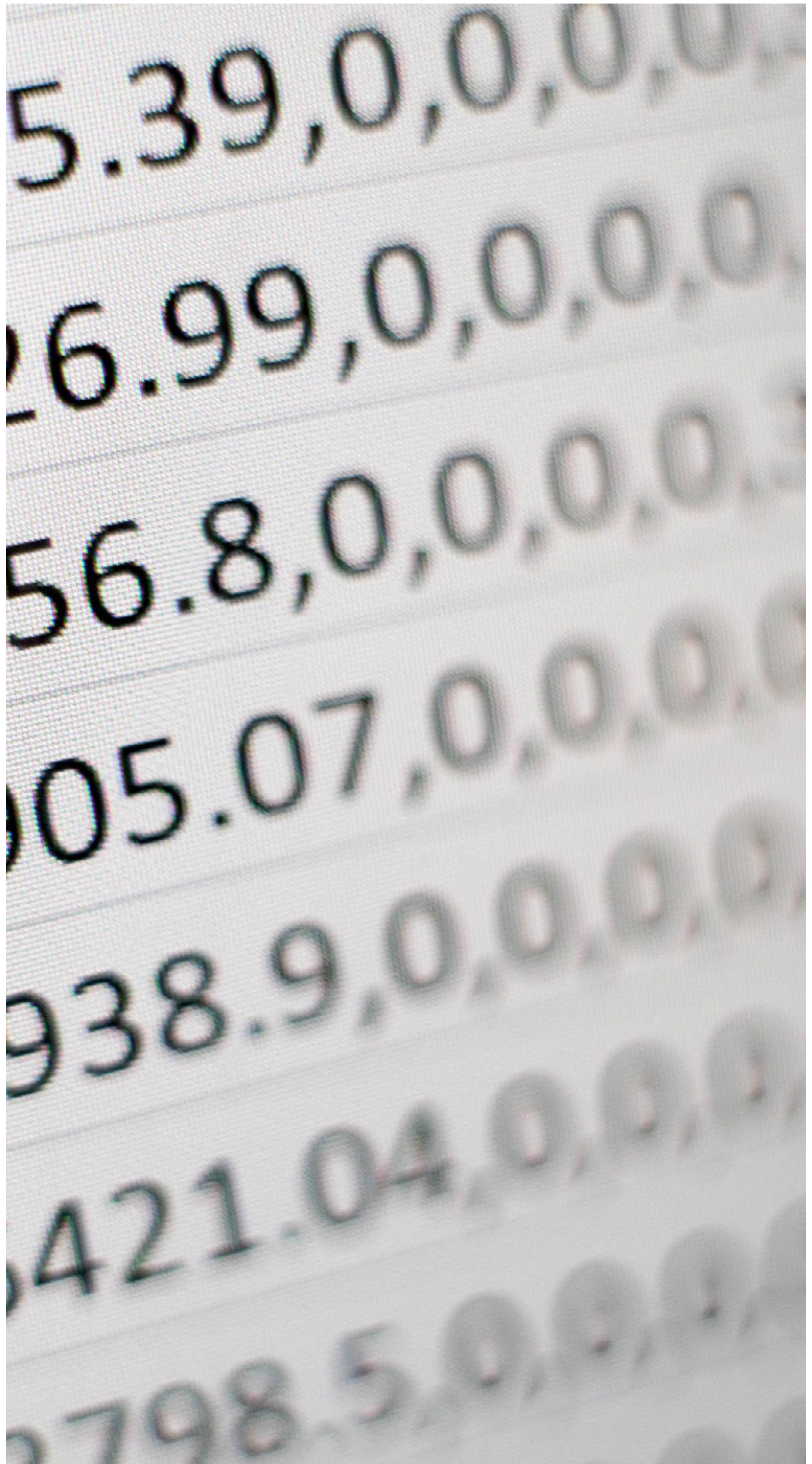
- To support efforts to track, monitor, and report ESG performance, companies are investing in ESG digital solutions. The global sustainability and energy management software market size was valued at US$ 987.7 M in 2019, and it is

[i] https://www.cdp.net/en/companies/companies-scores

[ii] These numbers are based on an analysis completed for global companies listed on the S&P Global 1200 Index and US companies listed on the S&P 500 Index (State of Green Business 2020, GreenBiz).

[iii] Cascading Commitments: Driving ambitious action through supply chain engagement. CDP Supply Chain Report 2018/2019.

[iv] Sustainability & Energy Management Software Market Analysis. Coherent Market Insights. Report Code CMI3894. June 2020.



estimated to grow to $2.3 B in 2027 (CAGR of 11.4%). [iv]

Christine: When it comes to ESG reporting, one of the key trends I think EHS&S professionals should keep an eye on is the movement towards requiring data to be assurable. In a recent Ernst & Young survey, 75% of respondents indicated that it would be “valuable” or “very valuable” to have a third-party firm provide independent assurance over the robustness of an organization’s processes and controls for ESG reporting.

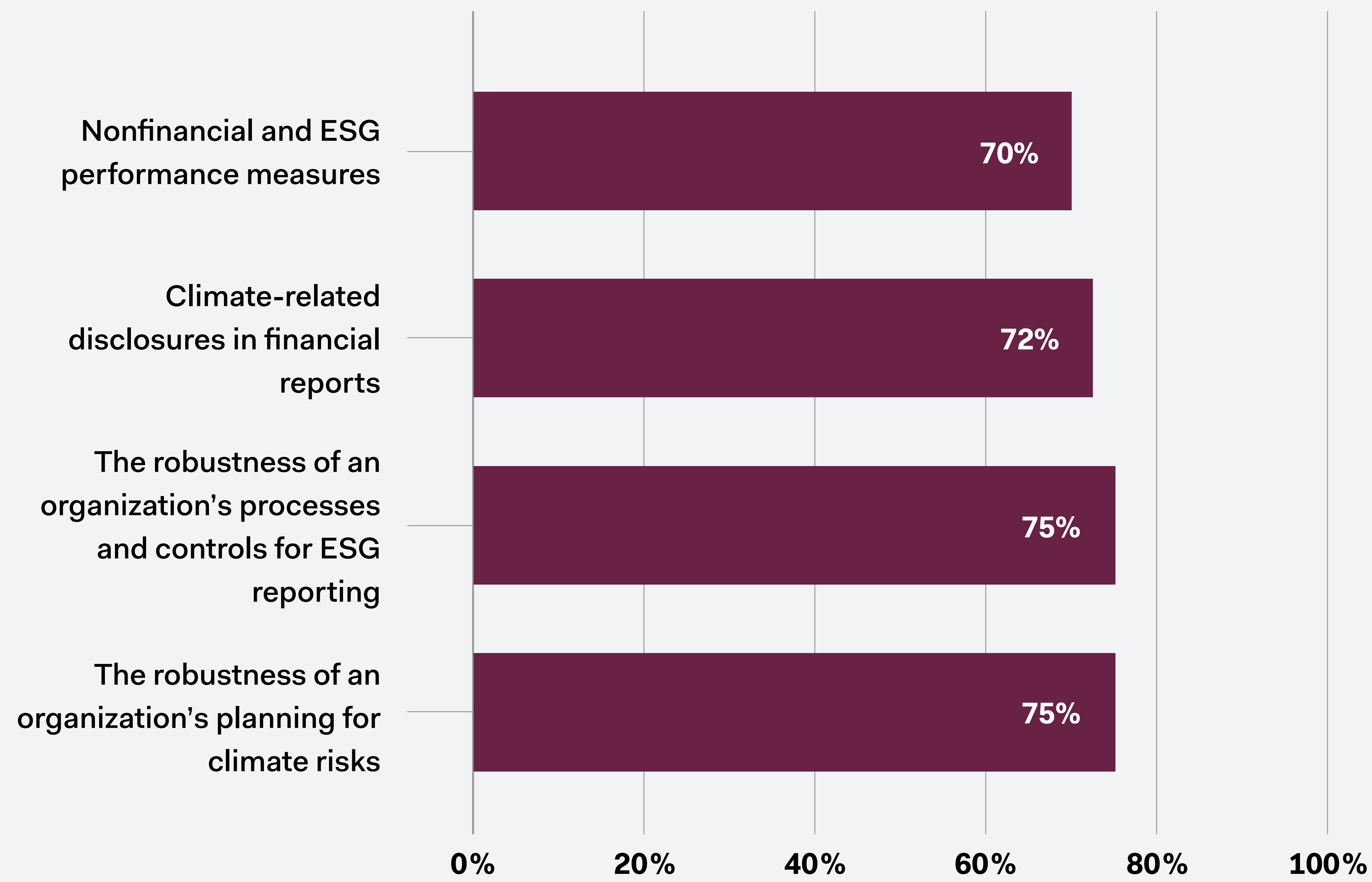
There is a growing movement toward ESG data being held to the same standards as financial data - the information needs to be verifiable. You don’t want to be accused of greenwashing or providing inaccurate information. **Many companies are still using spreadsheets to track and monitor a lot of their ESG data, especially their environmental programs, and this could become a growing risk in the future as spreadsheets don’t offer features required for auditing and securing data.**

Additionally, as we continue to see increased scrutiny on environmental performance, it’s important for companies to consider not only how to efficiently report on ESG performance, but how to actively work to reduce their own carbon footprint. For many companies, software solutions that help track emissions and waste streams and convert to C02 equivalents across their different environmental programs can help identify ways to improve environmental performance.

For example, at Cority, we work with a major retailer and a large oil & gas company to manage their waste. By tracking waste pickup schedules, volumes, and streams, both companies now have the data to know how often they really need waste pickups to be performed and are able to reduce transporter emissions. This data has also helped them identify ways to reuse and recycle some of the waste, resulting in less waste and thus, reduced emissions from waste – contributing to a circular economy model.

Another one of our oil & gas customers has found that using a SaaS solution to manage air emissions and GHG has enabled them to be proactive and meet their quarterly carbon reduction targets by being responsive in real-time to issues in the field. For example, if there is a meter providing erroneous values in the field, they have ranges set on the values coming into Cority and if data coming in is out of the expected range, it notifies the GHG team, who can then immediately respond to those meter variances occurring in the field. The EHS&S team has the data they need to take action as opposed to waiting until annual GHG reporting comes around and the time to fix issues has long passed. Overall, having that visibility helps them be nimble and improve environmental performance, which is then reflected in their ESG reporting.

How valuable is it to have a third-party firm provide independent assurance?



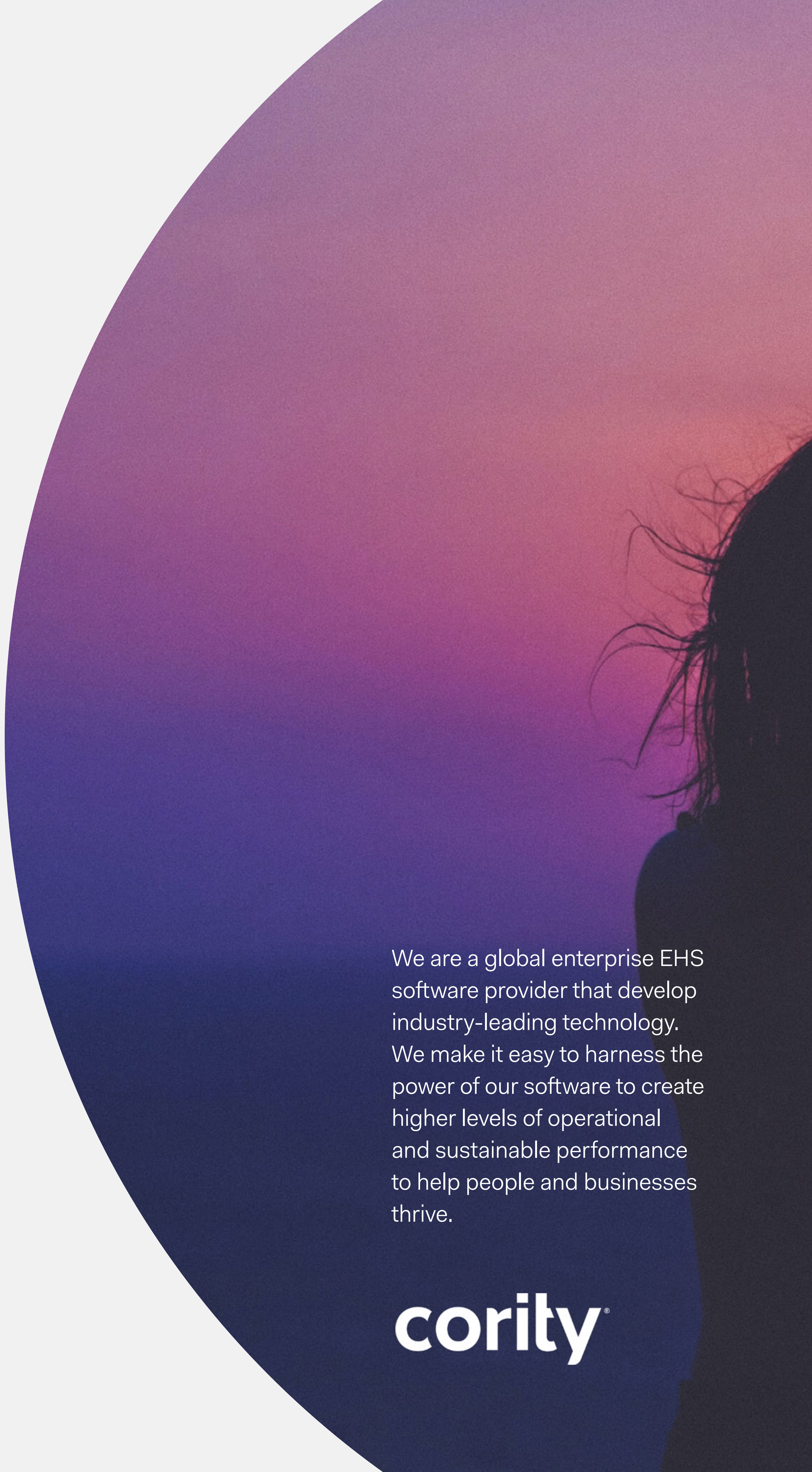
Source: "How will ESG performance shape your future?", Ernst & Young, 2020.

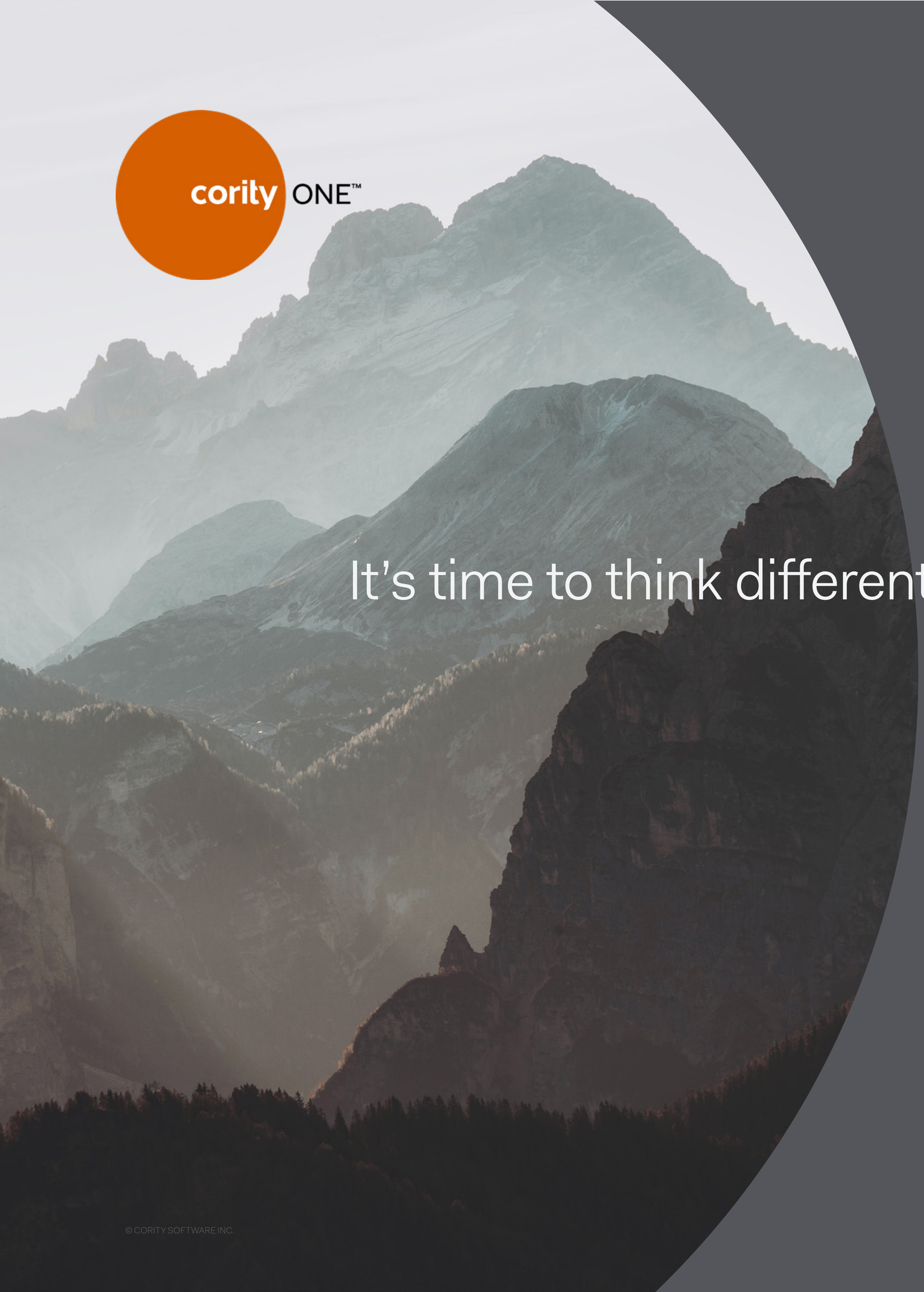
Final Thoughts

For many EHS&S professionals, collecting environmental information is something they have routinely been doing for years.

As the benefits of ESG continues to make themselves known to the investment community, companies should anticipate more pressure to provide complete, accurate and timely information that demonstrates a commitment to environmental, social and governance objectives.

Now is a good time for EHS&S teams to take a look at their programs and laser focus on improving performance in these areas in order to help their companies remain competitive. Technology could be a piece of the puzzle to help identify areas of improvement, increase efficiency and create defensible audit trails.





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