

# ESG disclosure: standards, ratings, and regulation

Knowledge perspective

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# Agenda

## ESG reporting ecosystem

Deep-dive on ESG standards

Deep-dive on ESG ratings

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# Executive summary

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## ESG standards guide the disclosure of ESG information

- GRI, ISSB, and TCFD are emerging as ESG standards leaders. Each framework has unique breadth / depth of ESG topics and focus of impact (financial impact v. double materiality), and level adopted. Commonly used standards include GRI, TCFD, CDP, SASB, IR, WEF.
- Pressure to report on ESG is increasing from investors, regulators, and stakeholders – they aim to better understand ESG risk and impact, both financial and societal, and ESG frameworks offer a structured approach to reporting this impact externally
- Increasing consolidation and standardization is expected to simplify reporting and help companies communicate consistently across stakeholders

## ESG ratings measure companies' performances and/or exposure to ESG risks

- ESG rating market is crowded, but quickly consolidating. Commonly ESG ratings are CDP, MSCI, Sustainalytics, Refinitiv, S&P Global, and ISS ESG. **MSCI and Sustainalytics are emerging as leading rating agencies however, each has unique advantages and limitations**
- There's a lack of conviction in ESG ratings due to varying methodologies which result in low correlation between scores, and low correlation with financial performance
- ESG ratings look at ESG performance that may have financial implications and assign them associated scores. However, they are an incomplete way to assess value creation from ESG
- ESG ratings are gaining attention as investors are increasingly using ratings agencies as an outside-in perspective. Coverage of ESG rating agencies is on the rise, especially in North America and Europe

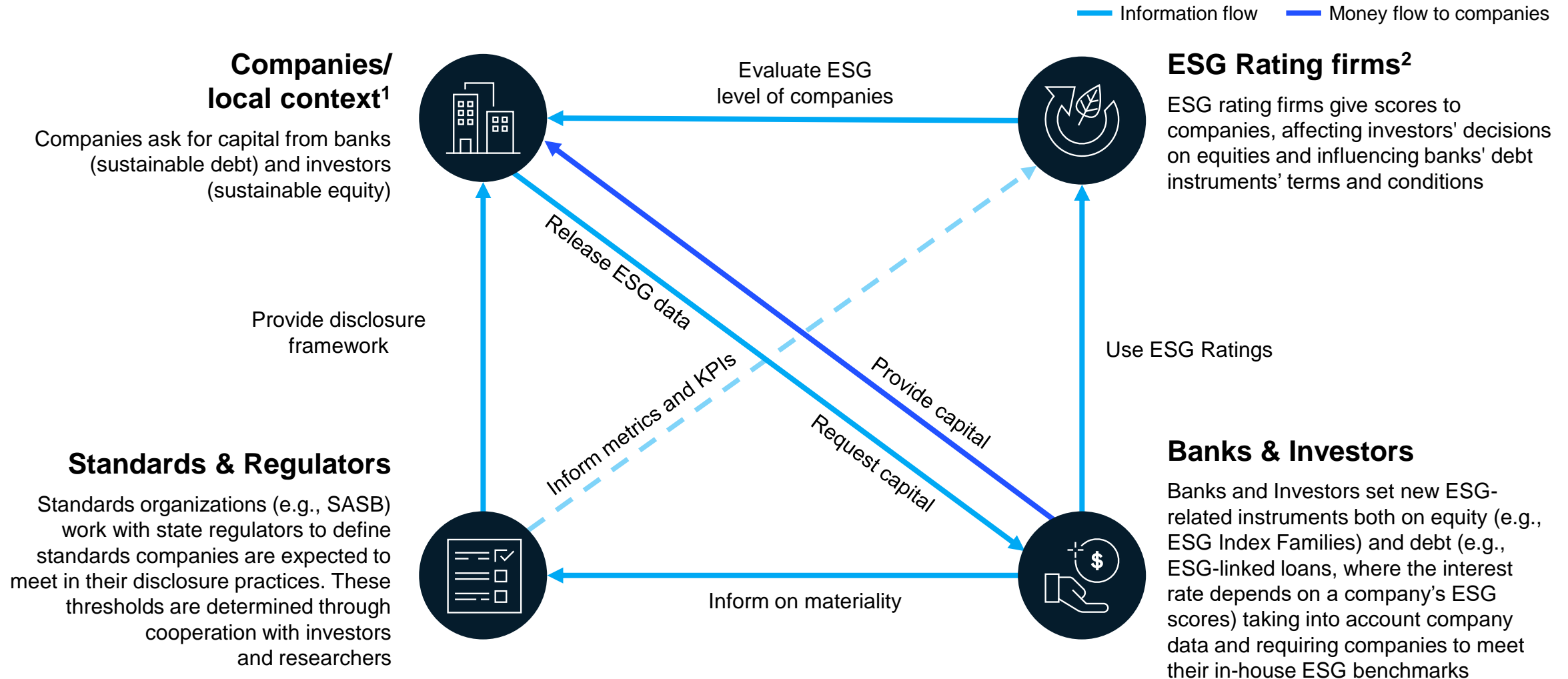
# ESG reporting is defined by standards, ratings, and regulation

	 Standards	 Ratings	 Regulation & Policy
Description	Standards <b>guide the disclosure of ESG information</b> (e.g., tons CO <sub>2</sub> /yr, Executive Gender Diversity %, etc.) by companies to their investors and <b>help businesses communicate their impacts</b>	Ratings <b>measure companies' performances and/or exposure to ESG risks</b> (e.g., AAA, C) that may have financial implications and assign them <b>associated scores</b>	Regulation <b>provides mandatory ESG disclosure rules</b> and legal requirements for companies to operate in a specific region
Example organizations	        	     	  

# The ESG ecosystem is maturing through consolidation of standards and ratings

	Current state of market	Likely state once market matures	Evidence of market maturing
1 Standards	<ul style="list-style-type: none"> <li>• <b>Multiple voluntary organizations</b> providing frameworks and standards (often regionally focused)</li> <li>• <b>Overlapping “Civil society”</b> (e.g., GRI) and <b>“Investor material”</b> (e.g., SASB) reporting</li> <li>• Some <b>large investors requiring companies</b> to report according to some ESG disclosure frameworks</li> </ul>	<ul style="list-style-type: none"> <li>• <b>Consistent &amp; comprehensive global system</b> of frameworks and standards</li> <li>• Demand for <b>mandatory, transparent and assured reporting</b> based on <b>officially agreed global framework/standards</b></li> <li>• Consolidation of frameworks with regulatory requirements to satisfy investors' needs</li> </ul>	<ul style="list-style-type: none"> <li>• <b>GRI continues to be a leading framework</b> with global adoption, high flexibility, and emphasis on double materiality (both financial and stakeholder impact)</li> <li>• <b>Formation of ISSB (International Sustainability Standards Board) by IFRS</b> which is consolidating VRF (formerly, SASB &amp; IIRC) and CDSB</li> <li>• <b>TCFD capturing support from regulators and investors globally</b>, including forming the structure of SEC proposed climate disclosure rule in March 2022</li> </ul>
2 Ratings	<ul style="list-style-type: none"> <li>• Numerous ESG rating agencies, poorly correlated</li> <li>• Evaluation criteria <b>inconsistent and incomparable scales</b></li> <li>• ESG ratings agencies still seen as less credible – <b>“garbage in, garbage out”</b></li> </ul>	<ul style="list-style-type: none"> <li>• <b>Fewer well-correlated ESG rating agencies, consolidation of smaller agencies</b></li> <li>• <b>Consistent evaluation criteria and comparability</b></li> <li>• <b>Better credibility and relevance across agencies</b> with improved alignment and standards</li> </ul>	<ul style="list-style-type: none"> <li>• <b>Merging of ratings</b> such as: Morningstar acquiring Sustainalytics in 2020 &amp; S&amp;P Global acquiring RobecoSAM's ESG rating business in 2019</li> <li>• Businesses not traditionally linked to sustainability <b>are expanding product offerings to include ESG Rankings</b>, example: Fitch Ratings' ESG Relevance Score</li> </ul>
3 Regulation	<ul style="list-style-type: none"> <li>• Regional regulation upcoming in <b>certain geographies</b> (e.g., EU and US) – limited clarity as to applicability for international companies</li> </ul>	<ul style="list-style-type: none"> <li>• <b>Globally aligned regulations consistently enforced</b> to cover a reasonable amount of clarity</li> </ul>	<ul style="list-style-type: none"> <li>• In Europe, <b>European Commission will issue “Taxonomy Regulations”</b> which will classify all economic activity as “sustainable” or not (effective 2022)</li> <li>• February 2022 the UK announced <b>mandatory climate-related financial disclosures</b> by public companies and large private companies</li> </ul>

# ESG reporting ecosystem is dependent on companies, financiers, and regulators



1. Data aggregators also sit at this point in the diagram

2. Financial regulators (e.g., the Securities and Exchange Commission (SEC) in the United States) also sit at this point in the diagram

# ESG data and reporting is important across stakeholders

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Stakeholder	Impact from successful ESG reporting
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<b>Companies</b>	<ul style="list-style-type: none"><li>• Company diagnostics and benchmarking against peers using metrics and ratings can help pinpoint ESG strengths and weaknesses in an organization</li><li>• Benchmarking with ratings from multiple vendors can assist in triangulating a company's performance on a specific issue</li></ul>
<b>Investors and banks</b>	<ul style="list-style-type: none"><li>• Strong ESG performance may increase investor diversity and potentially open-up access to lower cost capital available to companies in reputable ESG indices</li><li>• Used alongside corporate financial data, ESG data can enable analyses to understand which ESG metrics are most correlated to a company's financial performance</li></ul>
<b>Regulators</b>	<ul style="list-style-type: none"><li>• Regulations can address specific topics that may be aligned to ESG standards and reporting</li><li>• Potential to better prepare firms for wide variation in regulatory requirements across different geographies and levels of government</li></ul>
<b>Society</b>	<ul style="list-style-type: none"><li>• Requires companies to take a deeper, inward-looking view into their organization, positioning companies to make more informed choices and acknowledge present and future risk</li><li>• Increases stakeholders' transparency into companies and industries, further incentivizing companies to strategically approach ESG topics</li></ul>

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# Agenda

ESG reporting ecosystem

**Deep-dive on ESG standards**

Deep-dive on ESG ratings



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# Executive summary






















## ESG Standards

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- **ESG standards landscape is saturated with many players** – each with unique breadth / depth of ESG topics and focus of impact (financial impact v. double materiality), and level adopted. Commonly used standards include GRI, TCFD, CDP, SASB, IR, WEF
- **GRI, ISSB, and TCFD are emerging as leading frameworks for ESG reporting**
  - GRI: widely adopted (10K companies reporting), covers ESG topics broadly, addresses double materiality (investor and stakeholder impact), and offers flexibility in reporting process (three universal standards, 40 industry standards, 30+ topic-specific standards)
  - ISSB: newly formed collaboration with several organizations (including EU Commission, SEC, World Bank) to standardize ESG reporting and consolidate major existing frameworks (e.g., SASB, IR, CDSB), several which already have high adoption (e.g., 13K companies report on SASB)
  - TCFD: climate-specific framework, quickly growing with companies (e.g., 2,600 organizations publicly supported in 2021), investors, and regulators (e.g., SEC climate disclosure proposal leverages TCFD for mandatory reporting)
- **Pressure to report on ESG is increasing from investors, regulators, and stakeholders** – they aim to better understand ESG risk and impact, both financial and societal, and ESG frameworks offer a structured approach to reporting this impact externally
- **Increasing consolidation and standardization is expected to simplify reporting and help companies communicate consistently across stakeholders**

# Standards and frameworks attempt to standardize ESG disclosure within ESG reporting

Section focus

	 <b>Standards</b>	 <b>Ratings</b>	 <b>Regulation &amp; Policy</b>
Description	<p>Standards <b>guide the disclosure of ESG information</b> (e.g., tons CO<sub>2</sub>/yr, Executive Gender Diversity %, etc.) by companies to their investors and <b>help businesses communicate their impacts</b></p>	<p>Ratings <b>measure companies' performances and/or exposure to ESG risks</b> (e.g., AAA, C) that may have financial implications and assign them <b>associated scores</b></p>	<p>Regulation <b>provides mandatory ESG disclosure rules</b> and legal requirements for companies to operate in a specific region</p>
Example organizations	        	     	  

# There are six commonly used standards

Non-Exhaustive							Deep-dive to follow
	Standard / framework	Overview	Audience / geography	Level of guidance	ESG focus	Coverage <sup>2</sup>	Measurement for adoption
ESG standards	<b>Sustainability Accounting Standards Board (SASB)</b>	 Non-profit which sets standards to guide the disclosure of financially material sustainability information by companies to their investors	Investor, businesses US-focused	Specific, detailed, and replicable requirements	Overall sustainability / ESG	13,000	No. early adopter companies reported SASB metrics publicly
	<b>Global Reporting Initiative (GRI)</b>	 Provides most widely used standards for sustainability reporting to help businesses communicate their CSR/ESG impacts	Broad set of stakeholders Global	Universal standards with additional topic standards	Overall sustainability / ESG	10,000	No. organizations published report based on GRI guidelines or standards
	<b>Integrated Reporting (IR)</b>	 Promotes communication about value creation as the next step in the evolution of corporate reporting	Investors, businesses Global	Map how all company activities leading to value creation	Overall sustainability / ESG	~1,600	No. companies using the principles of integrated reporting
	<b>World Economic Forum (WEF)</b>	 Independent international organization prioritized 21 critical metrics across industries and 34 less established	Investors Global	Common core set of metrics and recommended disclosures	Overall sustainability / ESG	<500	No. companies, investors and other interested parties that consulted
Climate standards	<b>Carbon Disclosure Project (CDP)<sup>3</sup></b>	 CDP helps investors, companies, cities, states and regions to manage and disclose their environmental impacts	Investors, employees, customers Global	Specific requirements to assign score	Environment & (some) Governance	14,000	No. companies that disclosed via CDP in 2021
	<b>Task Force on Climate-Related Financial Disclosures (TCFD)</b>	 Created by FSB to develop consistent climate-related financial risk disclosures for use by companies, banks, and investors	Investors, lenders, insurers Global	Framework providing principles-based guidance	Environment (financial impact lens), Governance	~2,600	No. firms supporting the TCFD recommendations

On 3<sup>rd</sup> November 2021 at COP26, the IFRS Foundation Trustees announced the International Sustainability Standards Board (ISSB) to deliver a comprehensive global baseline of sustainability-related disclosure standards integrating several existing standards

1. Qualitative view on relevance based on participant companies (type, size and volume), investors (type, AUM), and coverage of topics/data sought by investors; 2. Number of organizations that have adopted or recognized these standards; 3. CDSB is a part of CPD

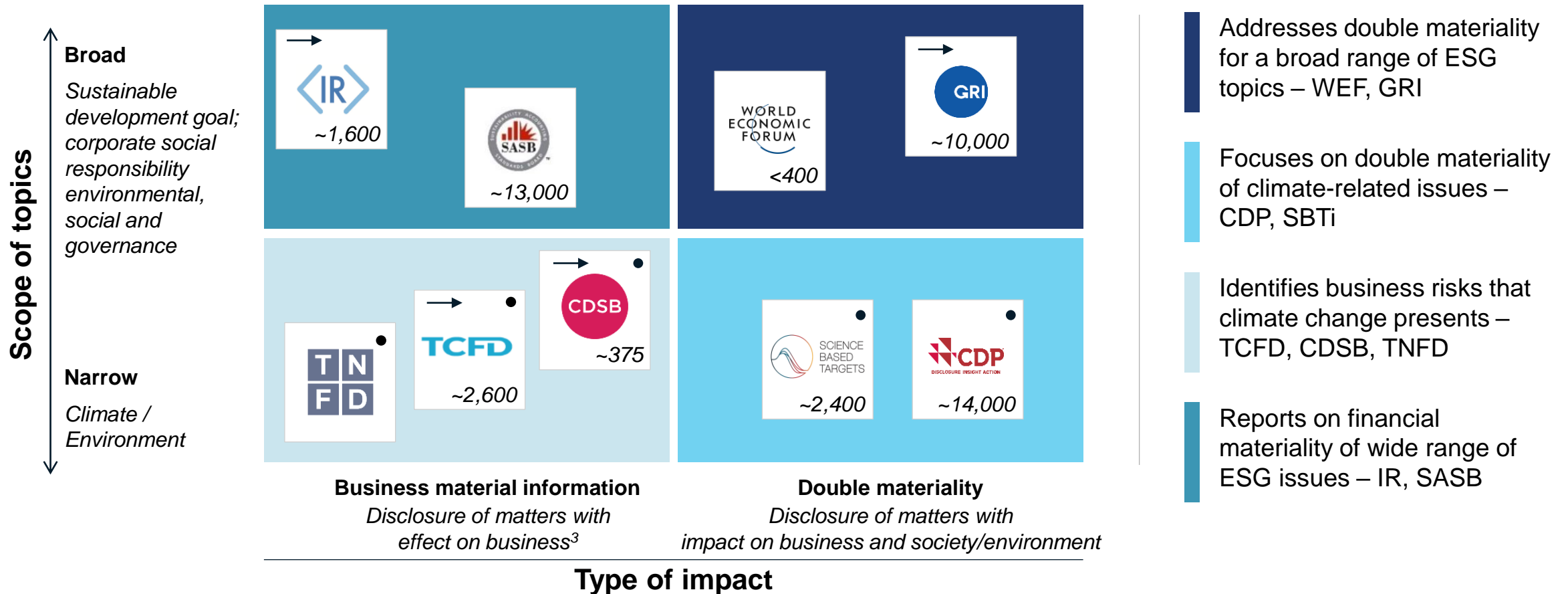
# ESG reporting frameworks address different types of impact and breadth of topics

## Simplified view

→ Incorporates forward-looking elements

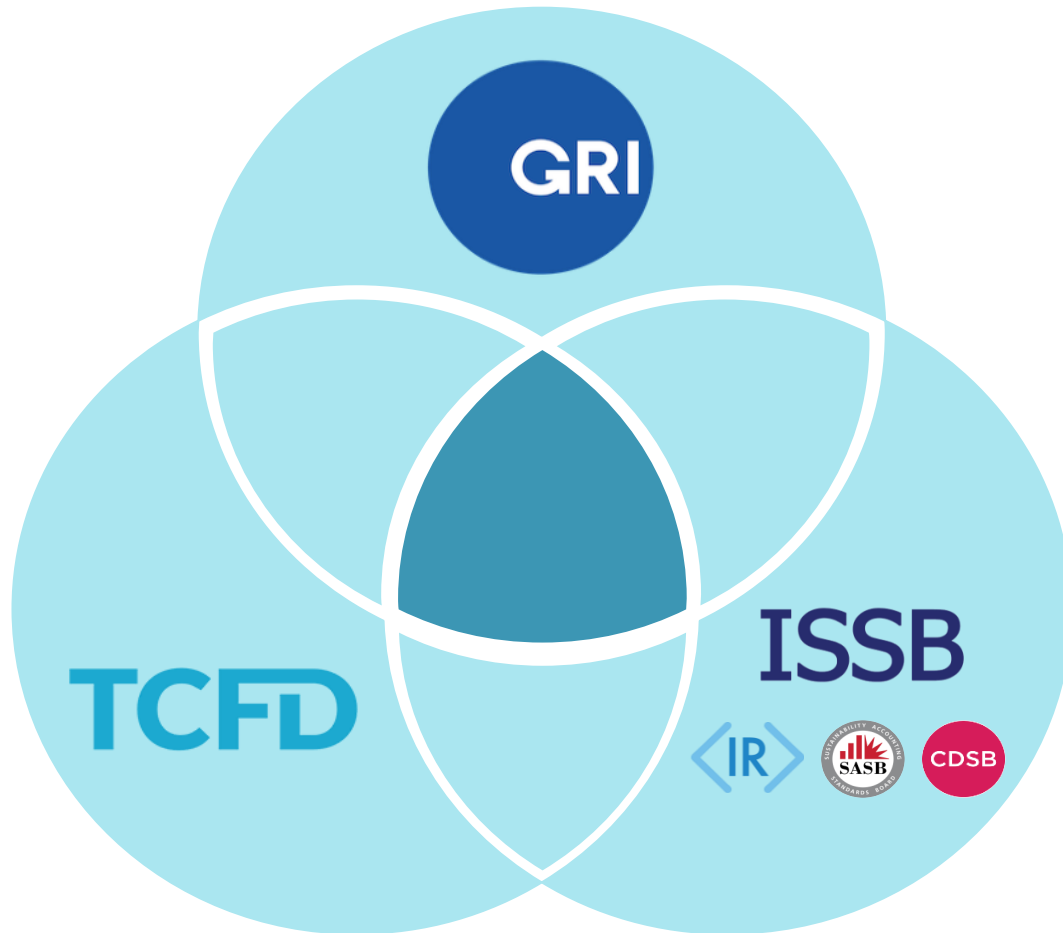
● Scope of environmental information only

# organizations who have adopted



1. CDSB is a part of CDP and will be consolidated into the ISSB before February 2022; 2 CDP works collaboratively with other standards and frameworks by sharing corporate data on environmental sustainability collected through their questionnaire and specialist system; 3 E.g., Impact on business strategy execution, financial performance, value creation. 4. SBTi offers both ESG standard and rating services, deep-dives included in the ESG rating portion of the deck

# GRI, ISSB, and TCFD are emerging as leading ESG standards



## GRI

- High prevalence with +10,000 companies reporting
- Focused on double materiality, both investor and stakeholder impacts
- Universal and deep-dive standards for various topics

## ISSB

- Intended to be go-to sustainability disclosure in 5 years merging several major existing standards
- In development via collaboration between standards and other stakeholders (e.g., EU commission, World Bank)
- Focus is financial materiality for investors / capital markets

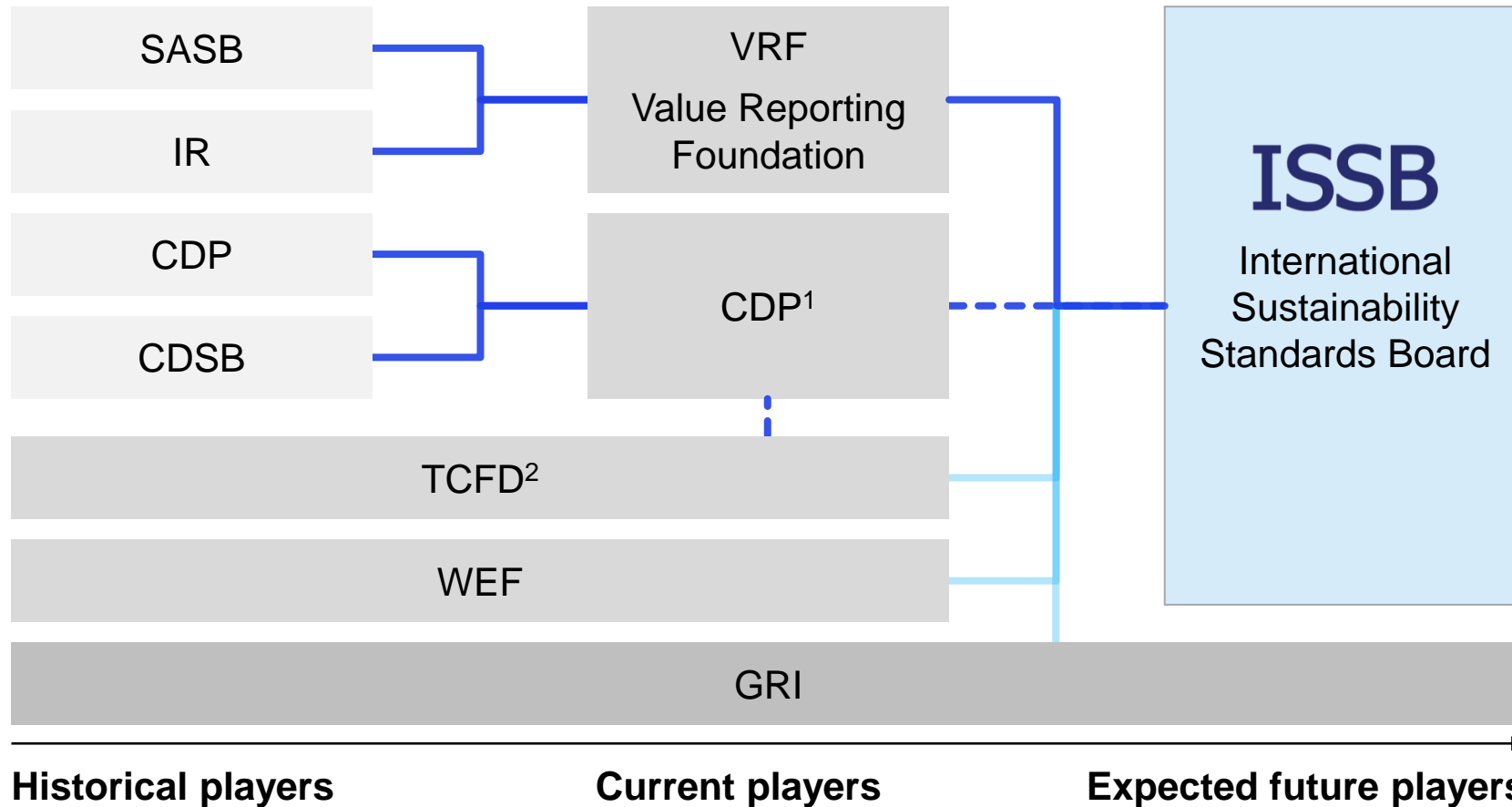
## TCFD

- 2,600 companies expressed support for TCFD in 2021
- Increasing adoption by regulators and investors (e.g., SEC proposed climate disclosure rule)
- Emphasis on financial materiality of “E” and some “G”
- Coverage of globally material issues on ESG
- Frameworks applicable for public & private companies
- Recommended and recognized by various stakeholders: regulators, investors, companies, public

# Many of existing standards will consolidate into ISSB and most other major players will serve an advisory role

Simplified view   Non-Exhaustive

■ Partially integrated   ■ Fully integrated   ■ Serve as advisory role



## Benefits of standards consolidation

- ① Improves quality of standards from synergistic effects of each player's expertise
- ② Streamlines reporting process and frees capacity for organizations
- ③ Decreases noise and improves stakeholder understanding of reporting landscape
- ④ Enhances ability to make meaningful decisions on ESG risks and impact

1. Only CDSB is merging to form ISSB, CDP will remain a separate entity

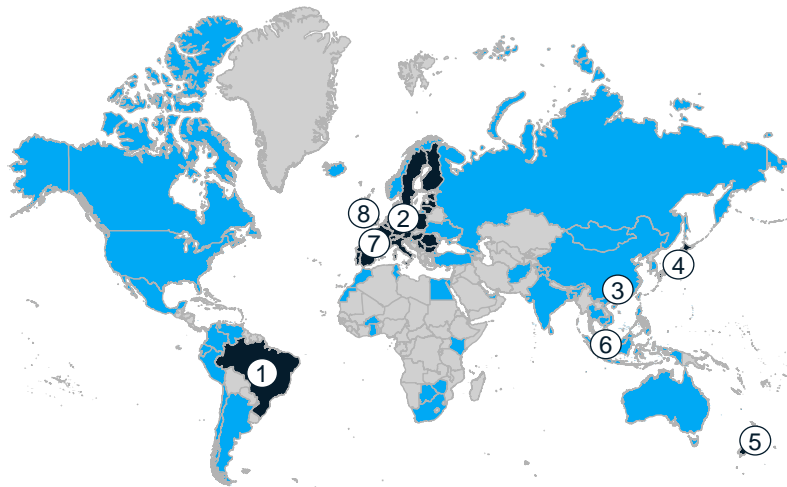
2. TCFD is not formally apart of CDP however, reporters to CDP also fulfill the requirements of the TCFD framework

# TCFD in gaining momentum with global adoption by regulators and investors, including 30% increase in supporters from 2020-2021

## TCFD has 2,600+ supporters, including 8 countries with official requirements

### Country-level TCFD support

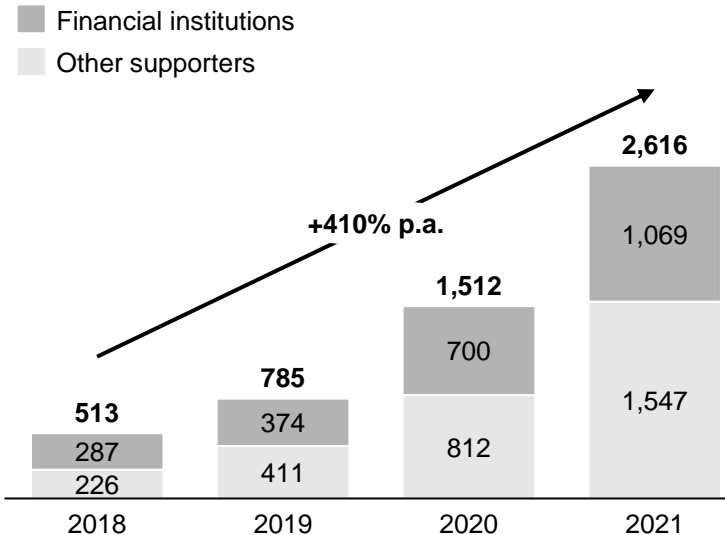
- Jurisdictions with TCFD-aligned reporting requirements
- Countries/jurisdictions with TCFD supporters



### Select examples of TCFD regulatory support

- **European Union:** April 2021, European Commission issued proposed Corporate Sustainability Reporting Directive (CSRD), which is expected to include TCFD reporting for 50K large companies across Europe
- **UK:** December 2020, Financial Conduct Authority introduced new rules for companies with a UK premium listing to disclose climate related risks and opportunities in line with the TCFD recommendations
- **Japan:** June 2021, Tokyo Stock Exchange published revised Corporate Governance Code requiring certain listed companies to enhance climate-related financial disclosures based on TCFD
- **Brazil:** September 2021, Central Bank of Brazil announced mandatory TCFD-aligned disclosure requirements for regulated institutions

### Number of TCFD supporters



## Investors are trending towards TCFD

### Select examples of TCFD investor support

- **“Maple8”** – eight of Canada’s largest pension plan investment managers: published statement for TCFD-aligned disclosures from companies (includes Canada Pension Plan Investments, Ontario Teachers’, and Public Sector Pension Investments)
- **BlackRock:** Larry Fink, CEO of world’s largest asset manager, used annual Letter to CEOs to call for TCFD-aligned disclosures
- **State Street Global Advisors:** expectations set by SSGA in January 2022 is company disclosure aligned with TCFD recommendations
- **Aviva:** January 2022 the UK investment fund announced expectations for reporting on climate transition roadmap and aligned to TCFD
- **Ceres Investor Network:** covers \$30T+ between 180 financial institutions in NA and promoted adoption of TCFD recommendations