Navigating the complexities of ESG Reporting Frameworks

Report

The direction of travel is more comprehensive ESG reporting

Reporting on Environmental, Social and Governance (ESG) strategy and performance in disclosures made both to investors and publicly has, over recent years, become less of an optional decision and more of a business imperative for companies and financial institutions the world over. There is now, more than ever before, market expectations for comprehensive finance-grade, auditable and comparable ESG reporting.

One of the biggest drivers of this is of course risk. For decades investors have scrutinised conventional financial reporting for wanting to understand the level of financial risk involved in their investment decision-making. Now, as ESG risk increasingly encroaches on financial performance of investments, reviews of ESG information have become necessary to enable a comprehensive view of risk – sustainability risk can be viewed as synonymous with investment risk.

The need for sustainability information was initially addressed by voluntary reporting frameworks and benchmarks such as the Global Reporting Initiative (GRI), the Carbon Disclosure Project (CDP) and the Global ESG Benchmark for Real Assets (GRESB). As a pioneer of sustainability reporting standards the GRI, established in 1997, now has over 10,000 reporting organisations, covering more than 100 countries, with 73% of the world's 250 largest companies reporting to their framework. GRESB has also confirmed the number of participants making submissions to their benchmarking assessment, both to quantify their sustainability progress and satisfy rising investor expectations, has grown each year. GRESB's 2021 benchmark saw the largest ever growth in total numbers, with 1,520 entities now participating worldwide, with significant growth in Europe.

Alongside market expectations for higher quality and coverage of ESG reporting, the other major reason for companies to create detailed ESG disclosures has been to comply and keep apace with increasingly stringent legislative requirements.

So how should ESG disclosures be made? The selection of the most appropriate framework is certainly a critical decision as it may determine how the organisation is viewed through an ESG lens. This is no easy task; even within existing guidelines from the European Investors in Non-Listed Real Estate (INREV), there is scope for choice of methodology.

Selecting the most appropriate ESG framework

Understanding the wealth of ESG reporting standards and requirements can be challenging and burdensome, particularly as they are continually and rapidly evolving. Even those businesses considered at the forefront of sustainable investment are being pushed further by framework bodies to drive the market shifts necessary to address the breadth and depth of sustainability issues that the world is facing. Those that are making slower progress can feel like they are merely treading water or even moving backwards in relative terms, with exposure to increasing levels of financial risk as a result.

Within the real estate industry this can be exacerbated when frameworks are not tailored to the nuances and specificities of the sector, as development and operational management of real estate assets can be unique when compared with other industries. However, some sector-specific frameworks and guidelines have strived to address this challenge. To aid the decision-making process, consideration of various elements, as discussed below, can help with navigating the ESG reporting landscape and determining the most appropriate and valuable option to your organisation.

1. **Audience**

   Who do you want reading your disclosure and analysing your ESG performance? The disclosures made can display your organisation's dedication to ESG issues and topics that resonate with them. For example, investors are likely to be interested in different metrics to employees. Therefore, it is vital to understand the interests of each stakeholder and how these requirements can be met.

2. **Stakeholder Expectations**

   Understanding what insights are needed by your internal and external stakeholders is crucial to deciding on your approach. Internally, different teams across the business will require different information to inform management decisions. Finance, risk and compliance teams will be seeking to assess performance data, whilst asset management and development teams may be more interested in utilities consumption and supply chain data to analyse supplier risk profiles, particularly with growing focus on Scope 3 GHG reporting.

External stakeholders such as investors, boards or creditors are likely to prefer the more recognised frameworks such as the Taskforce for Climate-related Financial Disclosures (TCFD), the United Nations' Principals of Responsible Investment (UN PRI) or the Sustainable Accounting Standards Board (SASB) Standards. Should compliance with regulators, such as the Financial Conduct Authority (FCA) be required, they will likely favour reporting to government legislated reporting such as Streamlined Energy and Carbon Reporting (SECR) for UK based companies, or National Greenhouse and Energy Reporting (NGER) for Australian organisations.

3. Resourcing

It is acknowledged that ESG Reporting can take significant amounts of time. Do you have sufficient resources internally to report robustly, or will additional personnel and expertise be required? With more limited resources, you may be required to reconsider you reporting strategy. Selecting a reporting framework which is less demanding may be more suitable. However, should your current resourcing levels appear insufficient to meet your reporting disclosure aspirations, it does not mean you have to change plans. External support from ESG and Sustainability Consultants can bolster your internal team and provide additional expertise.

4. Mandatory or voluntary

Over recent years growing policy debate has led to mandatory sustainability reporting regulations being introduced at country level as well as across economic and political unions such as the EU. As introduced above, SECR requires the disclosure of annual energy and carbon performance for companies that exceed two out of three thresholds: £36m annual turnover, £18m balance sheet and over 250 employees. TCFD reporting is now

mandatory in the UK (required from 6th April 2022 for listed companies with over 500 employees) with around 1,300 organisations affected by the mandate in the first instance. Other countries the TCFD is also mandatory include those within the EU, Switzerland, Hong Kong, Japan, Singapore and New Zealand.
Voluntary disclosures provide a greater breadth and detail that is currently not required by governments or regulators. They allow investors to understand more quantitative information, often in the form of carbon accounting disclosures, but also across water, waste and social indicators. Although a framework may be voluntary, aligning to a framework is now frequently expected, if not demanded, by the investor community.

5. Impact potential

Materiality to the organisation is to be considered by undertaking risk assessments of their primary risk area and associated consequences. A commercial property investment company may consider operational carbon (environmental), health safety & well-being (social) and bribery & corruption (governance) to be the most material. A framework that covers these would be most valuable to track ongoing performance and monitor progress of these principal factors.

Double materiality assessment is increasingly being expected, which requires both looking at the inward financial materiality and risk, and the outward materiality of the impacts the organisation's operations have on people and the environment. Whilst the exact meaning of double materiality is still up for debate, it is acknowledged that material factors are environmental risks that transform into financial risks, or what is important to a 'reasonable person' other than direct financial consequences.

6. Sector relevance

Within the real estate industry GRESB is well established. The voluntary reporting framework requires completion of an ESG questionnaire inclusive of quantitative datasets, to assess either real estate and infrastructure portfolios. It provides investor-focused output reports, ESG quantification and overall scoring, including highly coveted 'Green Star' ratings. Through their assessment GRESB have conducted alignment mapping to a number of recognised reporting frameworks such as European Public Real Estate Association (EPRA) Sustainability Best Practice Recommendations Guidelines (sBPR), the UN PRI Direct Property module, and the CDP, giving organisations confidence that they can address the majority of requirements contained within other reporting framework requirements if already submitting to GRESB.

7. Location

In different countries certain frameworks will be more recognised or relevant. EPRA, which provides a consistent way of measuring sustainability performance for listed real estate companies in Europe, will be more recognised and relevant in this jurisdiction as a result of the bodies' active involvement with policy debate at both country and EU level.

8. Metric Coverage

Reporting frameworks cover a wide range or ESG elements. Whilst some focus on covering most or all of these, some are more specific and dedicated, honing in on an area of focus to deliver more granular information on this subject matter. As an example, the GRI and SASB Standards provide comprehensive coverage across a wide range of sustainability metrics, whilst the CDP and TCFD focus more exclusively on climate.

Comparison of reporting frameworks: GRI, SASB

With the wealth of frameworks, guidance and reporting assessments now occupying the reporting landscape uncertainty on both how to report and what to report on is abound. Verco's Reporting Framework Matrix has identified two established reporting frameworks to strongly consider, both well-recognised globally and comprehensive in their coverage of ESG metrics. Here we will discuss why you may consider aligning your ESG reporting to one of them.

It is important to note the different focuses of each. The GRI Standards focus on an organisation's ESG impacts which affect a wide range of stakeholders, whereas the SASB Standards' attention is on ESG issues that have a financially material impact on the organisation, and therefore are more tailored towards the interests of investors.

Global Reporting Initiative (GRI) Standards (www.globalreporting.org)

The GRI is an international independent not-for-profit organisation founded in 1997 whose standards assist in identifying the key environmental, social, and economic impacts your organisation has based on the nature of your business. GRI has been devised as a modular system of interconnected standards under three series, as shown in Figure 1.

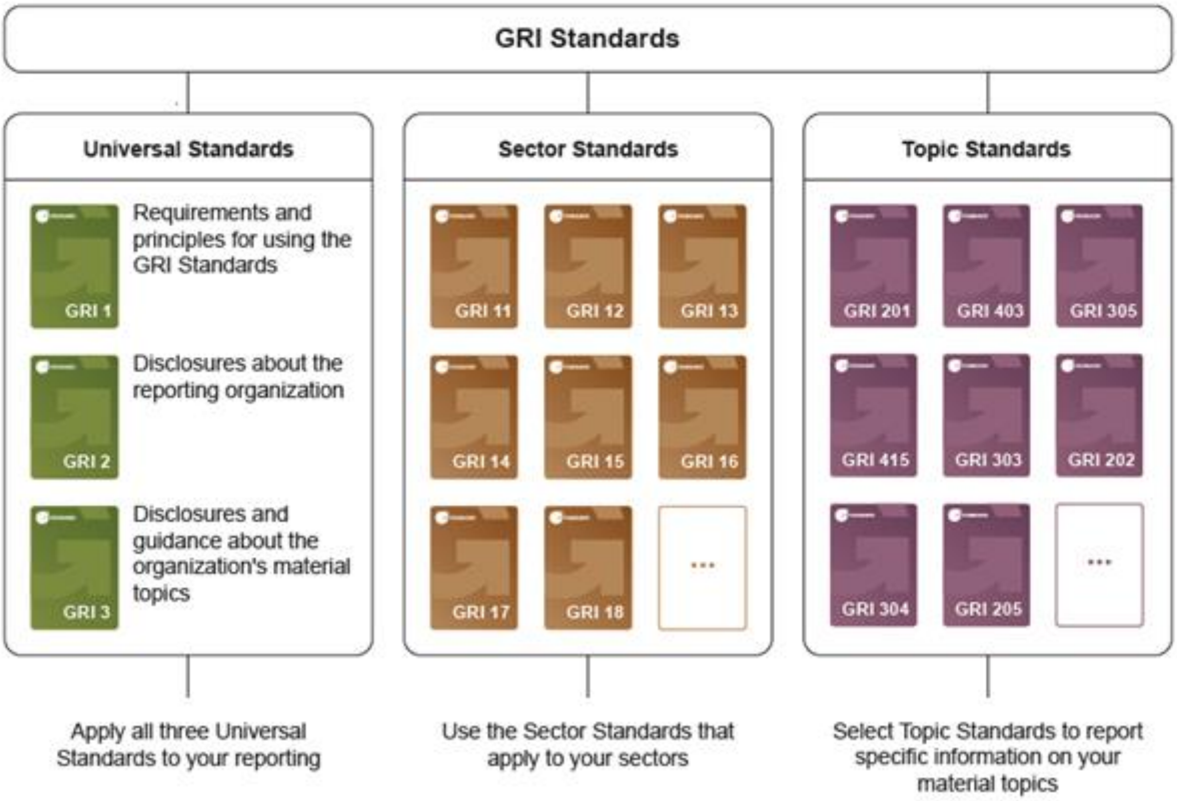

Figure 1: GRI Standards: Universal, Sector and Topic Standards (source: GRI)

There are 10 mandatory sets of disclosures, and 29 optional sets of disclosures which are dependent on the materiality to the organisation. The GRI Universal Standards apply to all organisations and span topics including climate change, human rights and corruption. Topic Standards cover individual focus areas – for example GRI-305: Carbon and GRI-303: Water and Effluents. Sector Standards are currently available for the Oil & Gas, Coal, Agriculture and Mining industries. Whilst there is not currently a Sector Standard available for Real Estate, this is expected to be developed in due course by the GRI in line with their prioritisation strategy.

The GRI recommends reporting **in accordance** with the GRI Standards. Under this approach all material topics, including the related impacts and how these are managed, are to be disclosed. Alternatively, an organisation can report **with**

reference to GRI Standards if some of the requirements cannot be fulfilled to report in accordance with the GRI Standards.

Key benefits of reporting to the GRI are:

- **Credibility** – The GRI created the first set of sustainability reporting standards in the world, achieving a globally trusted reputation. 190 of the 250 largest corporations use GRI Standards to report their sustainability performance.

- **High quality data** – Research indicates that reporting using the GRI Standards can help your company share the most relevant ESG data with investors. A GRI study in partnership with Baruch College of the City University of New York scored 572 companies based on the information quality and degree of verification of their ESG disclosure. The 481 companies that used the GRI framework scored higher on average for each element disclosed compared to the 91 companies that did not use the GRI Standards. (source: http://ga-institute.com/Sustainability-Update/research-results-using-the-gri-sustainability-reporting-framework-improves-the-quality-of-esg-disclosures-joint-research-from-ga-institute-and-baruch-college-shows/)

- **Commonality** – The UNPRI have aligned their reporting requirements with GRI, as well as the 17 United Nations Sustainable Development Goals (UNSDGs), meaning that by reporting in accordance with the GRI you will more simply be able to report to other frameworks.

Sustainability Accounting Standards Board (SASB) Standards (www.sasb.org)

SASB STANDARDS
Now part of IFRS Foundation

The Sustainability Accounting Standards Board is a non-profit organisation founded in 2011. Governance changes were completed in 2021 through the merger of The International Integrated Reporting Council (IIRC) and the Sustainability Accounting Standards Board (SASB) to form the Value Reporting Foundation (VRF). In August 2022, the International Financial Reporting Standards (IFRS) Foundation then assumed responsibility for SASB Standards when it merged with the Value Reporting Foundation, which previously maintained these Standards.

Despite these various changes, and the associated concern that the standards may be phased out and become obsolete, the IFRS has committed to building on the SASB Standards and encourages continued support and use until they are replaced by IFRS Sustainability Disclosure Standards.

The SASB standards, applicable globally, identify the categories of sustainability issues most relevant to financial performance across 77 industries. SASB Standards are focused around financial materiality to enable businesses to identify, manage and communicate financially-material sustainability information to their investors. Notwithstanding, the standards also allow non-financial risks and opportunities to be identified.

Key benefits of reporting to SASB are:

- **Rigor** – the standards are set utilising a rigorous and transparent standard-setting process using evidence-based research and involvement from investors, companies and subject matter experts.

- **Impact dial on company performance** – the standards assist in communications to investors regarding sustainability issues that are expected to impact the ability to create value over the long term.

- **Industry specific** – Focus can be placed on the issues that are most likely to impact financial performance within the real estate industry through the 'Real Estate Services Sustainability Accounting Standard'.

- **Commonality** – by reporting to SASB Standards you will be covering half of the disclosure requirements contained within the GRESB Real Estate Assessment. SASB and TCFD are also purposefully aligned to facilitate more seamless reporting of climate-related disclosures.

So can you report to both? Certainly. The standards are intentionally aligned to make disclosure more straightforward for organisations. In July 2020, the GRI and SASB announced a collaborative workplan which sought to provide clarity on the application of their reporting standards and assist organisations in successfully using both standards. Both sets of standards can be used together to meet your ESG reporting needs, to provide the depth and breadth of disclosure that their many stakeholders, including investors, require. There can be several benefits of using both frameworks together:

- **Comprehensiveness** – a complete picture can be drawn, bringing together both sustainability and financial information.
- **Investor needs** – the broader range of disclosures made ensures more investor requirements are met.
- **Value** – key insights are provided from both frameworks that can be actioned to deliver enhanced sustainability and financial performance.

How reporting is undertaken in practice can vary with a number of different approaches available. For example, separate GRI and SASB tables of disclosure can be published within the same integrated report, or alternatively a combined GRI and SASB content index can be prepared.

So why should your organisation align to particular reporting standards?

With global pressure mounting from governments, investor and the general public to now go beyond the targets and promises set, the focus is turning towards delivery against these objectives, implementation of measures to improve performance and the overall progress that has been made on organisation's Net Zero and their wider ESG journey towards more sustainable products, operations and developments. ESG Reporting has never been under such a focused spotlight and scrutiny.

Aligning to a reporting standard can certainly go a long way to solving the reporting conundrum. The following benefits and considerations can be seen from using reporting frameworks in disclosures:

- **Consistency:** Reporting Frameworks are consistently updated to ensure your reporting is up to date and relevant considering the rapid speed of change. Reporting out-of-date and unintentionally omitting key information could potentially lead to divestment as well as reducing the attraction of your portfolio to new investment.

- **Comparability:** Through use of frameworks comparisons can be made year-on-year both internally as well as by external stakeholders - both current and prospective investors.
    - **Internal tracking** of performance against recognised metrics to facilitate management decision making. Reviews can be conducted against industry peers and leading companies in other sectors to ensure that you are making an informed assessment of progress with a broader cross-industry view.
    - **External tracking** by investors can be undertaken as comparison to other funds and companies can be undertaken. This can help attract additional investment, particularly for ESG leading firms. In recent years there have been record inflows of capital into more sustainable funds, as well as to dedicated ESG funds. One of the main reasons for this trend is the direct link that is being seen between ESG and financial performance.

- **Recognition:** The organisations that construct the reporting frameworks spend a significant amount of time and allocate extensive resources to curate, review and iterate their guidance and requirements. By reporting to a framework you ensure that your reporting is to an exemplary global standard.

- **Investor confidence:** reporting will be viewed as robust, auditable and investment-grade. Whilst their own due diligence will no doubt be conducted, reporting to a recognised framework will enhance confidence in their investment decision-making process.

Next steps

If you are still uncertain on where to start in your ESG Reporting journey, you are definitely not alone. Preparing your organisation for ESG disclosure can be an intimidating undertaking. Fortunately, there is expert support available to make this task more straightforward.

Conducting an ESG materiality assessment is an excellent way to help you understand your organisation's current position, identify key stakeholders, set ambitious yet attainable ESG goals and create a structured approach for achieving them. The outcomes of performing a materiality assessment will assist and enable the most relevant and impactful ESG disclosure framework to be selected.

Verco provides comprehensive solutions and advisory to address the ESG reporting challenge. We also help organisations aim, report and deliver ESG initiatives that in turn can assist in attracting and retaining investment, mitigate risk and fast-track sustainable performance.

Should you like to arrange a meeting with an expert, please contact us via this link.

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