10 ESG REPORTING QUESTIONS DIRECTORS SHOULD CONSIDER

Environmental, social and governance (ESG) reporting has come into its own as a discipline, with most public companies now issuing sustainability reports. What's the board's role in ensuring these reports are responsive to investors' needs?

ESG reporting is here to stay, with nine out of 10 S&P 500 companies issuing reports during the 2019 reporting season. This is up from 75% in 2014, delivering a clear message that the proverbial train for ESG reporting has left the station. To top it off, according to the Governance & Accountability (G&A) Institute, there is now an undeniably intensive emphasis on ESG and corporate sustainability by fiduciaries, asset owners and asset managers.[1] Even the U.S. Securities and Exchange Commission is commenting on the topic.

As of February 2020, over 1,000 companies boasting $12 trillion in total market cap had endorsed the Task Force on Climate-related Financial Disclosures (TCFD) recommendations for sustainability disclosure. These companies include more than 473 financial firms representing $138.8 trillion of managed capital. Meanwhile, the Sustainability Accounting Standards Board (SASB) has seen a 180% increase in reporting using its framework over the last two years. And, according to BlackRock, ESG data will evolve into even more of a common language among issuers and investors over the next few years.[2]

[1] "90% of S&P 500 Index® Companies Publish Sustainability/Responsibility Reports in 2019," G&A Institute, July 16, 2020: www.ga-institute.com/research-reports/flash-reports/2020-sp-500-flash-report.html.

[2] "RE: Financial Factors in Selecting Plan Investments; 29 CFR Part 2550; RIN 1210–AB95," BlackRock letter to the U.S. Department of Labor, July 30, 2020: www.blackrock.com/corporate/literature/publication/dol-financial-factors-in-selecting-plan-investments-073020.pdf.

protiviti®
Face the Future with Confidence

Inspired by the global rise of reporting beyond financial results, below are 10 questions for boards to ask themselves and their management teams. This discussion applies to companies issuing sustainability reports.

1. **Have we set compelling sustainability targets and goals that appeal to the marketplace?** Directors should understand how the company's ESG initiatives compare to those of competitors. ESG should be integrated into the overall corporate strategy rather than be a mere afterthought, making it equivalent to a compliance activity.

2. **What story are we telling the street?** Directors should inquire whether the company's ESG storyline is resonating in the market and impacting the company's valuation. They should understand how the company's message compares to that of peers, leaders in the industry and key competitors. The company should articulate how ESG initiatives make a difference in executing the strategy and identify areas where it sees the greatest opportunity to create value.

3. **Can we integrate our ESG reporting with financial reporting?** ESG investments and initiatives enable key strategies, create new revenue sources and achieve operating efficiencies, all of which affects both present and future financial returns. Thus, it may be more meaningful to investors to integrate ESG reporting into financial reports, quarterly earnings calls and investor roadshows consistent with the convergence of investor interest in financial and ESG performance. Such alignment may result in time and cost savings.

4. **What reporting framework are we using, and why?** With the proliferation of standards in the market and various frameworks in play,[3] reporting against multiple authoritative frameworks may be necessary to address the investor needs for common industry metrics to compare and contrast performance. Until a universal framework is adopted, this reporting practice may become expected. The use of an established framework, such as the SASB's, is an effective way to avoid "greenwashing," or overstating ESG efforts.

5. **What accountabilities have we set for ESG-related performance?** ESG performance should be integrated with financial and operational performance monitoring; otherwise, it may become an appendage and receive less C-suite attention. Performance expectations and metrics should be linked to incentive compensation plans to drive progress and establish accountability for results. Executive sponsorship of ESG initiatives is an imperative.

6. **Is our ESG reporting satisfying the needs of the investment community and other stakeholders?** The board should inquire as to management's process for engaging and understanding the expectations of ESG stakeholders. Institutional investors and asset managers with a stake in the company may convey their expectations for the criteria management should use in reporting ESG performance in a given industry. It is also useful to monitor the company's ESG ratings and understand what makes them change.

7. **What are our ESG risks, and how well are we managing them?** ESG objectives and activities present new and unique risks and opportunities that should be considered through the company's enterprise risk management lens. Note that there is guidance on how to do this.[4] ESG-related risks should be incorporated into public risk disclosures (e.g., the disclosure of risk factors).

[3] For example, the following frameworks show varying usage based on a survey of the S&P 500 by the G&A Institute (usage noted parenthetically): the CDP (formerly the Carbon Disclosure Project) (65%), Global Reporting Initiative (GRI) (51%), the United Nations Sustainable Development Goals (UN SDGs) pursuant to the 2030 Agenda for Sustainable Development (36%), SASB (14%) and TCFD recommendations (TCFD report) (5%). Other standards are available or in development.

[4] "Applying Enterprise Risk Management to Environmental, Social and Governance-Related Risks," Executive Summary, Committee of Sponsoring Organizations of the Treadway Commission and World Business Council for Sustainable Development, October 23, 2018: www.coso.org/Documents/COSO-WBCSD-ESGERM-Guidance-Full.pdf.

8. **What have we done to ensure that our ESG-related disclosures are reliable?** Directors should gauge management's confidence that the company's disclosure controls and procedures are effective as they relate to ESG metrics and reporting. This may be an opportunity for the internal audit function to include important aspects of the company's ESG reporting in the audit plan to provide assurance to management and the board as to the fair presentation of the underlying data.

9. **Does — and if not should — our independent auditor have a role in ESG reporting?** Note that 29% of S&P 500 companies use external assurance.[5] Increased investor reliance on ESG reporting may elevate the importance of independent attestation over time, particularly for companies active in the capital markets. For example, in a securities offering, underwriters may request comfort letter attestation for selected ESG disclosures.

10. **How has the COVID-19 pandemic affected our ESG reporting?** With the pandemic's effects on customer behavior, workplace design, global supply chains and the communities in which they operate, the focus on ESG matters has shifted for many companies. For example, the approach to social issues around health and safety, the distributed workplace, and overall employee wellness has changed. Companies are also revisiting and highlighting how they address their carbon footprint as the market transitions into reopening from the pandemic. The question is, how are these and other pandemic-induced impacts altering company discussions of ESG strategies and initiatives, including the balancing of short-term needs and decisions with long-term resilience?

In addition to focusing sufficient attention on ESG strategies and initiatives, the board should consider its review responsibilities for ESG reporting in the context of how it approaches Form 10-K and other public filings. ESG-related risks should be included within the scope of the board's risk oversight process. Some companies even disclose the board's oversight role in ESG matters in their public filings.

The above discussion applies to companies issuing sustainability reports. As noted earlier, 90% of S&P 500 companies issue these reports; thus, some S&P 500 companies are *not* currently issuing them. And there are many other non-issuers as well. For such companies, the board should inquire of management why a report is not issued, for they have become outliers. What are the repercussions of not issuing an ESG report? Are competitors issuing them? Are major shareholders raising concerns about the lack of disclosures they expect?

ESG reporting presents an opportunity for companies to share what they are doing to sustain the long-term interests of shareholders while also addressing the interests of customers, employees, suppliers and the communities in which they operate. More importantly, it is an inevitable response to the rapid growth of sustainable, responsible and impact investing assets across the world.

Bucking this undeniable trend could mean much more than just being left behind. It can lead to high-profile proxy battles over ESG-related topics, threats to board seats, institutional investors redirecting capital elsewhere, and brand erosion. That is why quality and transparent ESG reporting should be a board priority.

[5] "90% of S&P 500 Index® Companies Publish Sustainability/Responsibility Reports in 2019," G&A Institute.

How Protiviti Can Help

Protiviti assists executive management and the board with the enterprise's assessment of its risks and the effectiveness of its capabilities for managing those risks, including risks related to ESG performance. Protiviti supports organizations throughout their sustainability journey by offering a holistic and integrated approach, encompassing all of the following elements to help businesses confidently face the future.

For example, Protiviti can assist management with:

- **Discovery and strategy-setting —** Defining sustainability objectives and related strategic guidelines, assessing the maturity of the sustainability program, and understanding material topics for the business and stakeholders.
- **Data management and development —** Identifying data supporting the analysis of material sustainability topics and building the data collection, aggregation and validation process for selected sustainability disclosures.
- **Performance and reporting —** Monitoring the sustainability program objectives and reporting comprehensively and transparently the organization's ESG performance to stakeholders.
- **Governance and risk management —** Designing or enhancing the governance framework to better address ESG risks and compliance requirements and strengthen the internal control environment enabling ESG reporting.

Audit Committee Self-Assessment Questions

*In these dynamic times, it is best practice for boards and their standing committees and individual directors to self-assess their performance periodically and formulate actionable plans to improve board performance based on the results of that process. To that end, audit committees should consider the illustrative questions we have made available at **www.protiviti.com/US-en/insights/bulletin-assessment-questions-audit-committees**. These comprehensive questions consider the committee's composition, charter, agenda and focus and may be customized to fit the committee's assessment objectives in light of current challenges the company is facing.*

Protiviti partners with the National Association of Corporate Directors (NACD) to publish articles of interest to boardroom executives related to effective or emerging practices on the many aspects of risk oversight. As of January 2013, NACD has been publishing online contributed articles from Protiviti, with the content featured on https://blog.nacdonline.org/authors/42/. Twice per year, the six most recent issues of *Board Perspectives: Risk Oversight* are consolidated into a printed booklet that is co-branded with NACD. Protiviti also posts these articles at protiviti.com.