# Explainer

# A Look Inside Four Proposed ESG Standards

By Rheaa Rao December 30, 2020

Several organizations have this year developed frameworks that lay out the ESG metrics that they think public companies and funds should disclose.

Now it's up to the Securities and Exchange Commission to pick one and enforce it, analysts say.

## Reporting on ESG Metrics

**Several organizations either are creating their own ESG-reporting frameworks or have joined the efforts of others to do so. Below is a look at those initiatives.**

| Organization | Objective of ESG Standards/Framework |
|---|---|
| **Sustainability Accounting Standards Board*** | Companies can disclose activities across five dimensions of sustainability: the environment, social capital, human capital, business model and innovation, and leadership and governance |
| **Global Reporting Initiative*** | Companies can report sustainability information that help them describe their impact on the economy |
| **Climate Disclosure Standards Board*** | Companies can disclose information about environmental and climate-related risks and opportunities |
| **Carbon Disclosure Project *** | Provides a structure for companies and investors to disclose climate change and other environmental information |
| **International Integrated Reporting Council*** | Companies can disclose relevant, material sustainability-related information. The organization is merging with the SASB. |
| **Task Force on Climate-Related Disclosures** | Companies can disclose information about climate-related financial risks |

| Organization | Objective of ESG Standards/Framework |
|---|---|
| **CFA Institute** | Asset managers can spell out how they define certain ESG terms and concepts on a fund level. Still in progress. |
| **Deloitte, EY, PwC and KPMG** | Consists of 55 ESG metrics on topics ranging from emission targets to pay and gender ratios |

*Source: Each organization's website. *Groups are working together to establish a framework for public company disclosures.*

One proposal that has gained prominence has been developed by the Sustainability Accounting Standards Board. The organization is working with the Global Reporting Initiative, Climate Disclosure Standards Board, Carbon Disclosure Project and International Integrated Reporting Council to establish which ESG-related data public companies should disclose, as reported.

The Big Four accounting firms also jointly developed a reporting framework for ESG standards. And they're encouraging members of the International Business Council, which consists of 130 or so global companies, to incorporate the standards next year.

The CFA Institute, meanwhile, is workshopping metrics it thinks fund firms should disclose to investors about their ESG products. Doing so will fill a disclosure gap, says John Wilson, director of corporate engagement at Eaton Vance. In recent years, more asset managers have started integrating ESG considerations into their investment approaches.

The differences between each standard are becoming clearer as organizations look to build consensus, Wilson explains. For example, the Global Reporting Initiative's standards enable companies to report on how they impact the economy. SASB standards and the Climate Disclosure Standards Board's industry-agnostic approach, meanwhile, help firms report on sustainability-related information that is material to them.

And the Task Force on Climate-Related Disclosures — whose recommendations were included in the collaboration between the five organizations — is focused on understanding a company's vision for how it intends to transition to a low-carbon economy, he adds.

Under current practice, ESG disclosure standards are voluntary. As a result, firms share only the data that present them in the best light, says Louis Coppola, cofounder of Governance & Accountability Institute, a sustainability consulting, research and advisory firm. This makes it difficult to compare firms even in the same industry.

However, some of the responsibility to accurately assess firms regardless of what they disclose falls upon fund managers, says Venk Reddy, chief investment officer at Zeo Capital, a sustainable credit specialist that offers mutual funds. Fund shops poised to excel must dig deeper into existing data and disclosures, he notes.

The SEC, however, should bring together different stakeholders to address ESG issues, Eaton Vance's Wilson says. They can lean on the standards developed by the SASB and Task Force on Climate-Related Disclosures that have already gained prominence, he adds. Coopting what's out there would help them enforce certain disclosures instead of convincing firms of the necessity of such disclosures, he adds.

Earlier this month, the Investment Company Institute backed the SASB and the Task Force on Climate-Related Disclosures' frameworks.

Such standards will help fund managers get useful information to make important decisions that are consistent with the investment objectives of funds, said George Gatch, ICI chairman and JPMorgan Asset Management's CEO.

The lobbying group rejected the CFA's fund-level disclosure attempt, saying that the institution should let regulators take the lead.

If the SEC does take up ESG-related disclosures, though, it should make sure such requirements are neither too loosely defined nor overly prescriptive, says Sara Crovitz, partner at law firm Stradley Ronon. The regulator should also make sure that the new standards are harmonized globally as much as possible so they're not a burden to multinational firms, she notes.

"It's going to have to be an iterative process," she says. "It's never going to be perfect."

For fund-level disclosures, the SEC's role should be to ensure that the regulator can judge whether the manager is representing what it does fairly, Zeo Capital's Reddy says. It is not the SEC's responsibility to evaluate how sound a manager's investment is, he notes. Investors and advisors can assess the actual viability of the strategies, he adds.

The SEC isn't the only entity that can weigh in on ESG standards, Coppola says. While the SEC would have the loudest voice, other groups can play a part too, he adds.

Stock exchanges may ask firms for certain disclosures as part of their listing requirements, Coppola notes. The incoming Environmental Protection Agency could also mandate disclosures for certain industries, he adds.

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