How to approach ESG reporting: Part 1

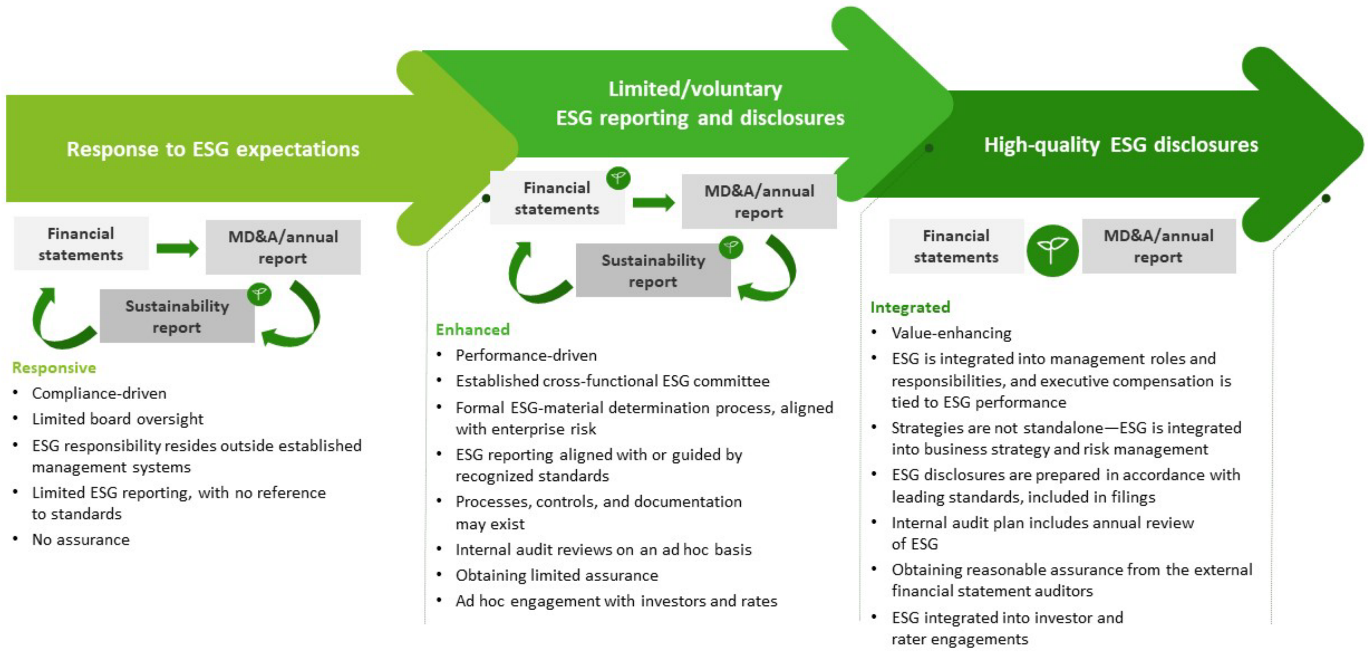
In the first of a three-part series, we explain the latest developments in ESG reporting and how your organization can adapt.

What is ESG reporting?

There is growing awareness that material environmental, social, and governance (ESG) factors connect to an organization's long-term growth potential and overall success. As a result, companies now need to deliver a more holistic view of corporate performance to their stakeholders. It's becoming the norm in financial reporting across industries and sectors to embed progress against ESG goals in mainstream financial reporting.

The evolution of ESG reporting

Organizations are increasingly integrating ESG into their operations, making sustainability core to their missions. They use sustainability reports or integrated disclosures to communicate their findings.



There are several best practices to keep in mind when reporting on ESG. The most effective organizations recognize stakeholder needs, choose an appropriate reporting framework, integrate their ESG strategies into their business plans, and provide consistent disclosure across all reports.

Why it matters

This paradigm shift in reporting is adding pressure to organizations large and small to recognize complex ESG risks and opportunities and to articulate them strategically to their stakeholders. Reputational risk threatens companies that are hesitant or unwilling to disclose their sustainability practices in a meaningful way–because when ESG reporting is insufficient, investors may feel compelled to commit their capital elsewhere. Organizations need a robust long-term strategy to address relevant ESG factors and they need to ensure their efforts are reflected in their corporate disclosures. Those that can manage the ESG revolution may be better positioned for the challenges ahead than those that are reactionary, and may face fewer costs and time pressures.

ESG-reporting drivers

Demand for disclosure
Investors, customers, employees, and other stakeholders are demanding that companies take demonstrable action to incorporate ESG updates into their corporate purposes, operations, and reporting.

Performance potential
Businesses recognize that adopting an ESG mindset can be essential to creating value. ESG investing is empirically well-founded, with companies that rank high in ESG practices outperforming others on a variety of key financial metrics.[1]

Current and future regulations
Given the current accelerated pace of changes to ESG-reporting regulations worldwide and the increased governmental focus on ESG factors, organizations need to be mindful of global as well as local requirements.

Access to capital
ESG-linked corporate lending is here, whereby terms are linked to borrowers meeting specified ESG criteria. Due to increased focus on ESG analysis and the popularity of socially responsible investment products, ESG principles have been incorporated into financing programs. Growing evidence shows that companies with high ESG scores, on average, enjoy lower capital costs compared with those that have poor scores.[2]

A road map for ESG reporting

A lack of ESG term, metrics, and framework standardization can make reporting on an organization's sustainability initiatives seem daunting. Implementing an agile methodology paves the way for a smoother journey, allowing for an overarching strategy for achieving an ESG mindset across the organization in addition to setting targets and tracking and monitoring progress against defined goals.

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[1] Friede, Gunnar, Timo Busch, Alexander Bassen. "ESG and financial performance: Aggregated evidence from more than 2,000 empirical studies." Journal of Sustainable Finance & Investment 5.4 (2015): 210–233
https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2699610&mod=article_inline

[2] Ashish Lodh. "ESG and the cost of capital." MSCI, Feb 25, 2020, https://www.msci.com/www/blog-posts/esg-and-the-cost-of-capital/01726513589.

Best practices

- Identify ESG risks and opportunities, including financial-statement impacts
- Incorporate ESG factors into business strategies
- Reflect ESG mindset in risk-management processes
- Establish appropriate governance structures for ESG-related oversight
- Develop indicators to measure progress against milestones
- Embed ESG goals in executive compensation
- Communicate goals and progress to all stakeholders (not just shareholders)

Getting started

Knowing where to begin with ESG reporting can be confusing. The process should be treated as a journey over time that starts with gaining consensus on how to define ESG within your organization and accounting for the needs of your stakeholders. Companies that recognize how ESG, financial, and operational results intersect set themselves up to create value in the long term.

The power of Deloitte

At Deloitte, we work with companies of all sizes and across all industries to find the right way to infuse sustainability practices into their operations, while staying true to their organizational values. We take our clients through all aspects of ESG strategy, controls, systems, and reporting, as well as provide assurance on ESG reporting. By developing in-depth, business-driven, individualized road maps to manage the opportunities and risks that sustainability brings, we can help your organization thrive in the new reality of business and make the world a better place for everyone.

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