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JOURNAL OF RESPONSIBLE FINANCE

Knowledge Series on Emerging Trends

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Knowledge Series on Emerging Trends

ESG Reporting as a Tool and Driver for Risk Assessment, Transparency and Performance

Volume 2 | May 2015

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MESSAGE FROM GIZ

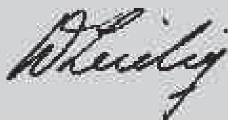
Global and local contexts are profoundly transforming owing to ongoing political, economic, environmental, social and technological developments. The speed of change is unprecedented. Complexity and uncertainty surrounding decision makers, both in politics and business, are manifold higher than ever before. Consciousness among people for their right to well-being is sharper and better articulated than it has ever been. Even as people across the globe have benefited from innovation and progress over the past few decades, these benefits have neither been equitably distributed and accessed; nor been generated in a sustainable manner. It is evident that if these risks are not managed, the fault lines will lay bare open in a variety of ways, lowering the quality of life of people instead of improving it.

It is important to understand the role and power information can exercise in enabling governments, business and industry, and people to tackle these current and future risks. This Volume focuses on disclosure and reporting that businesses and financial institutions have begun to do and what it may mean for their performance. Research shows that good reporting practices result in businesses doing better not only vis-à-vis their target stakeholders, but also in their management practices—beyond mere financial performance. This can only be good news to drive sustainability-oriented growth at a cumulative level.

With each successive volume, the Journal of Responsible Finance will delve deeper into several interconnected aspects of sustainability and responsible financing. GIZ, along with its partners and stakeholders, intends to take the idea of responsible financing from concept to wide practice—of which building and sharing knowledge is a key aspect.

We hope that you will find this Volume engaging and useful.

Kind regards



Wolfgang Leidig
Director
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FOREWORD—IBA

India continues to be one of the few economies in the world where long-term fundamentals for growth are strong. Among several others, a recent study, "Global Business and Spending Monitor 2015" by American Express, in partnership with CFO Research, indicates India's finance leaders are looking at fresh spending, investments, acquisitions, new business partnerships and new markets. Policymakers are therefore expected to lend an impetus to a step up in industrial and infrastructure sector growth.

At the same time, however, it is important that against this background, businesses and investors strengthen their vigil on the potential ESG (environmental, social and governance) risks to sustainability of existing and new ventures. Here, financial institutions have a significant role to play in encouraging and supporting this required integration of ESG factors into investment decisions and business strategies.

It was to build the momentum on this vital front that last year, GIZ, in collaboration with SIDBI and IBA, had launched the Journal of Responsible Finance (JRF) to be disseminated among Indian banks and financial institutions. The first volume titled, "The Next Generation of Finance—Taking a systemic perspective on risk and opportunities" introduced the fundamental concepts, rationale and issues in the field of responsible finance, with articles that linked the Indian context to ESG, both as risks and opportunities.

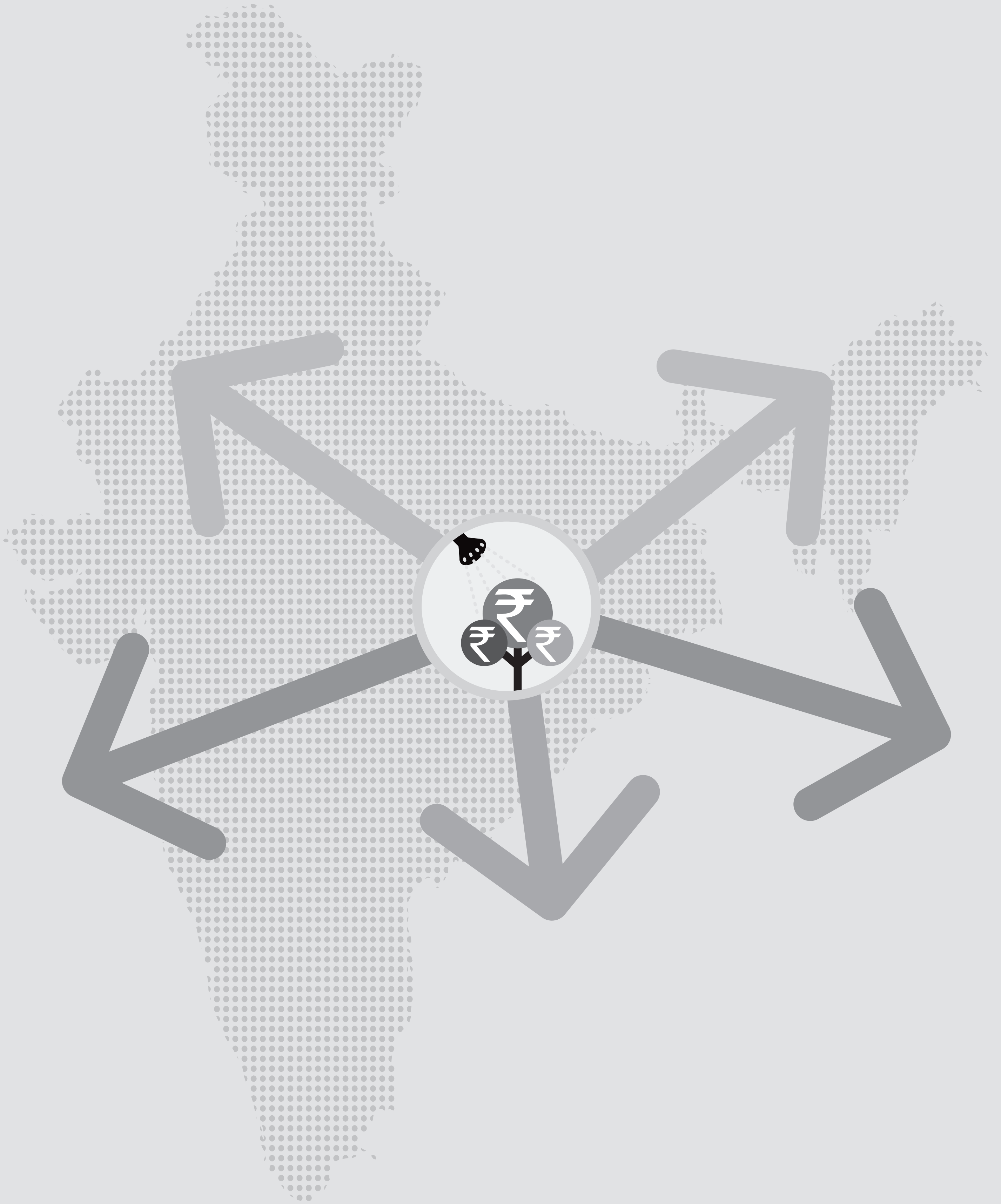
We are now pleased to introduce Volume II with a focus on the theme "ESG reporting as a tool and driver for risk assessment, transparency & performance". This volume covers a relevant mix of articles, such as Indian trends in ESG reporting as it moves from disclosures to performance management; an industry perspective on voluntary disclosure as an opportunity; a roadmap for regulation to further promote sustainability measurement and reporting, including that of Stock Exchanges; and insights and evidence on what can make sustainability metrics meaningful. This volume also covers a special section introducing various existing tools for stakeholders who want to use ESG disclosures to assess companies' performance.

We believe Volume II takes the dialogue forward in highlighting several specific aspects in the ESG domain and find that it needs to be read by all members of the Indian financial community.

The Indian Banks' Association's (IBA) vision is to work proactively for a healthy, professional and forward looking banking and financial industry in a manner consistent with public good. IBA believes that Indian institutions will vastly benefit from the knowledge that JRF will bring to its audience, both in terms of the progress and the challenges that still need to be addressed. JRF seeks to provide a much-needed structured platform for sharing of trends and evolving insights in the journey of responsible finance, the world over and in India.

We hope you find this second volume informative and stimulating.

Mohan V. Tanksale
Chief Executive, Indian Banks' Association (IBA)



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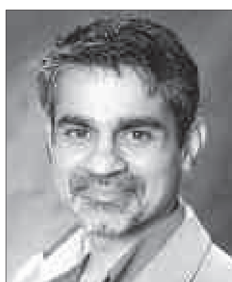
2015: The Year when ESG Reporting in India Enters the Mainstream:

Moving from Disclosure to Performance



›› Pawan Mehra

Pawan Mehra is co-founder and Managing Director of cKinetics, a specialised Sustainability Advisory firm that provides end-to-end solutions for investors and businesses. Pawan leads cKinetics' engagements that involve design and launch of new solutions that feed into the emerging sustainability market space. Pawan was earlier involved in building and scaling early-stage ventures, first as a venture capital investor in his early career with GVFL and McKenna Capital and, since then, as an entrepreneur with Parsec Interact and Intellecap. He has served on the board of the Global Impact Investing Network which represents global investors looking to make socially relevant investments.

›› Shradha Kapur

Shradha Kapur is Engagement Manager at cKinetics and has been working at the intersection of Sustainability and finance. She was the lead author of *Cracking the Conundrum*, the landscape report that has set the tone for investors and businesses to engage on ESG in India. Prior to initiating her career in sustainability at cKinetics, Shradha built her experience in the financial services sector at BNP Paribas and Capital IQ (Division of S&P).

In 2013, a study by cKinetics found that, even as sustainable and socially responsible investing (SRI) had been on an upswing globally, these investors had been on the periphery of the Indian market for the past few years. Only about USD 10 billion of the global SRI capital had found its way into India by then. These investors have been in an exploratory mode, waiting to see a critical mass of businesses reach a stage where it becomes feasible to implement responsible investment practices.

Of late however, the Indian market has become a growing opportunity for SRI funds as more businesses are measuring and disclosing their ESG practices. The study *Cracking the Conundrum*[1] estimates that this increase in disclosure could lead to a growth of Rs. 4.4 trillion (USD 80 billion) in annual capital flows into India in the next 10 years. The study indicates that as ESG reporting grows further in India, the Assets Under Management (AUM) of SRI funds and those using ESG information is expected to grow from the current Rs. 3 trillion (USD 55 billion) to Rs. 5.5-9.6 trillion (USD 100-175 billion) in five years and is forecasted to touch levels of Rs. 13.2-17.3 trillion (USD 240-315 billion) in 10 years.

Table 1: Capital that uses ESG Information (as in 2013)

Social investors	USD 260 million
E&S seeking funds	USD 1.8 billion
Indian SRI focused funds	USD 170 million
Global SRI funds allocated towards India	USD 10 billion
Developmental Financial Institutions (Indian and global)	USD 40 billion
Indian banks	USD 48 billion
Global banks	USD 32 billion

ESG Disclosure and Financial Attractiveness: A Quantifiable Linkage

cKinetics has developed a framework to quantify and demonstrate the impact of voluntary adoption of ESG disclosure by businesses on their capital inflow. The framework establishes the correlation between (financial) attractiveness of business to responsible investors and ESG disclosure[2]; the model has been centred on the relationship between ESG Disclosure and reporting Score (ESDS) and the KZ Index (which represents the capital constraint of businesses)[3].

Public reports of the top 100 listed Indian companies were examined for prevalence of disclosure and reporting on 35 key ESG parameters over three reporting periods (2010-13) and ESDS was arrived at by taking into account three key factors:

$$ESDS = f\begin{pmatrix} \textit{Level of disclosure of an indicator} \\ \textit{Longevity of disclosure} \\ \textit{Assurance conducted on the disclosure} \end{pmatrix}$$

The KZ Index is widely recognised as a measure for capital constraint of a business, i.e. the degree to which the businesses are limited in their ability to raise capital. As a corollary, lower the capital constraint, greater the ability of a firm to raise capital.

A linear regression[4] model was run over three years and across multiple sectors, with KZ Index as the dependent variable and ESDS as the independent variable, which revealed that as disclosure (ESDS) increases, businesses become more financially attractive.

A few sectors stood out where the linkage between disclosure and financial attractiveness was reasonably strong. These included:

- Business and consumer services
- Industrial, manufacturing and extractive industries
- Energy and related infrastructure

There were some sectors where such a linkage was quite weak. These included:

- Construction and housing
- Consumer goods and retail

It is important to note here that the linkage (or correlation) should not be confused with causation. While a correlation may exist between ESG disclosure and financial attractiveness, the cause may be very different. Some investors, for instance, use disclosure and reporting as a proxy for management quality. Hence, in such cases, management quality is the cause for greater investment and greater disclosure and reporting.

Table 2: Relationship between disclosure and reporting for select sectors

Sector	Coefficient (establishing linkage)	Standard Deviation	T-stat (linkage strength)
Business and consumer services	0.08	0.02	3.76
Industrial, manufacturing and extractive industries	0.07	0.03	2.27
Energy and related infrastructure	0.04	0.03	0.95
Construction and housing	0.03	0.05	0.53
Consumer goods and retail	0.04	0.16	0.27

Source: cKinetics research report: *Cracking the Conundrum*

The data analysed on ESG disclosure of 100 listed Indian businesses between 2010 and 2013 aimed to link ESG disclosure with the KZ index. Based on the estimated ESG disclosure (ESDS) scores (independent variable), the following regression equation is used to calculate the KZ score for each sector for different time horizons:

KZ = Intercept - Coefficient * Disclosure

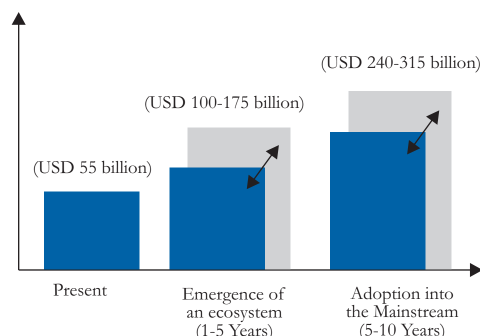
The coefficient has been subtracted from the intercept since a lower KZ means that the firm had lesser capital constraints. A larger positive coefficient above indicates the relative linkage and the T-stat indicates the strength of the linkage.

Predicting how Increased ESG Disclosure will Attract More SRI Capital

In order to predict the impact of ESG disclosure on capital flows into companies, a model was built with the following approach:

1. Create a forecast for ESG disclosure over a 5-year and a 10-year period. Forecasts were developed independently for each sector, based on the existing ESG disclosure in the sector and the prevalence of external pressures on the businesses within the sector vis-à-vis disclosure and reporting.
2. Modelling the change in capital flows based on the linkage between financial attractiveness and ESG disclosure.
3. Estimating Assets under Management (AUM) for different SRI fund types.

Figure 1: Forecast for assets under management by funds using ESG and targeting India (USD billion)



The results of this model have been published in *Cracking the Conundrum*[5] which estimates that as more businesses begin to measure and disclose their ESG practices, it will lead to growth of Assets managed by SRI funds, which in turn would lead to adoption of ESG information by mainstream investors (and their models) in less than 10 years.

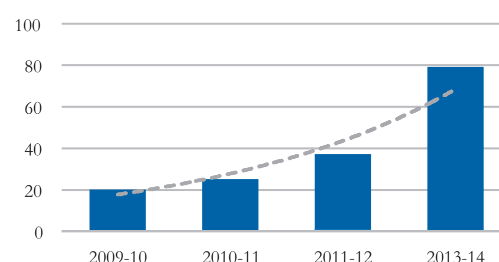
Tracking the level of ESG Disclosure in India: ESG Dashboard

To understand and analyse the market pulse on ESG practices, the India Responsible Investment Working Group[6] launched the ESG Dashboard and has been developing ESG information instruments that will inform investors, businesses as well as the market at large on the ESG performance of Indian companies.

Annual Benchmarking Report

The India Responsible Investing Group has been tracking the ESG disclosure of the top 100 listed businesses in India since 2009, over which period, there has been a significant improvement in both the number of people disclosing as also the quality of disclosure. In this context, the 1st Annual ESG Scorecard provides an overview of the ESG disclosure of Indian companies and (for the first time) introduces ESG benchmarking—a tool for investors to rank and compare businesses. The report analyses trends in ESG disclosure and reporting of more than 120 large businesses in India, to inform investors on the ESG performance and risks of their stock portfolio.

Figure 2: Indian businesses with Sustainability Reports



Source: Sustainability Outlook

ESG Market Pulse India

A quarterly information dashboard that captures ESG actions of Indian businesses, investors, policy makers and other stakeholders and enables investors and other stakeholders to

- Track Environmental, Social and Governance related actions, news and disclosure of top listed Indian businesses
- Monitor key ESG risks and opportunities facing Indian businesses
- Obtain ESG snapshots of eight high-risk sectors, a synopsis of prevailing sectoral trends and their impact on company valuations

ESG Benchmarking Tool

For investors, in particular, ESG disclosure can be considered as a proxy for business responsibility practices and management quality and commitment to sustainability. To help investors in assessing the same, the working group has developed a (self-evaluating) benchmarking tool, which has established sector benchmarks for different ESG parameters and metrics and allows investors to evaluate investees' performance vis-à-vis their peers. The objective of the tool is to answer the following questions:

- How complete and comprehensive is the ESG disclosure of listed businesses in India?

- Where does a particular company rank vis-à-vis its peers in providing satisfactory amount of material ESG information that is consistent over time?
- What key material indicators are not being addressed by the companies?
- What are the outstanding metrics in which the company has been able to benchmark the level of material disclosure?

With recent government initiatives and increasing awareness about the business case for ESG disclosure, the reporting trend has been accelerating in the country. The National Voluntary Guidelines for Social, Environmental and Economic Responsibilities of Businesses (NVGs) and the ensuing mandate from SEBI requiring the top 100 listed businesses to disclose[7], were the primary drivers. Additionally, growing investor interest, as well as ESG considerations being entrenched in businesses' "social license to operate" led to intensification of efforts on both, ESG-related initiatives and communication. This is evident from the fact that over the past two years (since the BRR was mandated) the number of companies disclosing as well as the quality of disclosure has improved.

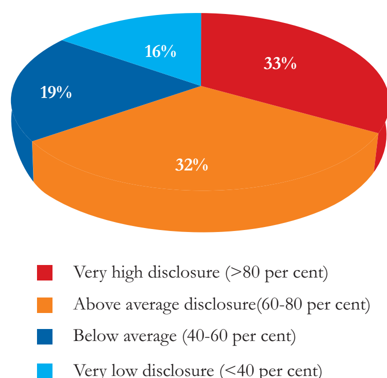
The reporting period 2013-14 saw 79 companies release a sustainability report compared with 37 in the pre-BRR mandate period (2012-13); this represents an increase of more than 100 per cent.

Quality of Disclosure

An increase in prevalence of reporting across E, S and G parameters

Despite the mandate by SEBI, the BRR framework allows businesses a degree of flexibility in both adoption of the principles and disclosure; they are required to adopt the nine principles, or explain why they have not been able to do so. However, an analysis of the level of disclosure indicates that most businesses have displayed eagerness in adopting and disclosing on different principles.

Figure 3: Extent of disclosure (percentage of companies)



As can be seen in Figure 3, there is a marked change in the prevalence of disclosure (actual data) on different parameters, over the past 2-3 years, with over 33 per cent of businesses disclosing on over 80 per cent of the metrics (that are considered material to them) and an equivalent percentage of businesses disclosing on over 60 per cent of the metrics considered relevant. (Source: cKinetics research and analysis)

Indian companies are considering both, risks as well as opportunities

The ESG Dashboard developed by the working group tracks news, press releases, quarterly filings and other publicly-disclosed information across 120 listed companies in India. During 2014, the ESG Dashboard tracked 900 ESG-related data points and the information was analysed with respect to three dimensions.

1. Sector dimension: This captures the level of activity across sectors on disclosing ESG information. Information has been categorised into the following:
   a. Environmental information related to biodiversity management, climate change and emissions management, product life cycle sustainability, environmental compliance, energy management, waste management and water management
   b. Social information related to employee well-being, inclusive growth, customers and community engagement and development and CSR spending
   c. Governance information related to corporate policies and standards, board engagement, corruption and bribery and other controversies such as criminal cases against the management, sexual harassment cases and regulatory inquiries
2. ESG opportunity dimension: publicly-cited information about opportunities for businesses, such as inclusive banking and sustainable chemicals. Opportunities have been categorised into the following:
   a. Accessing new markets
   b. Building reputation capital
   c. Differentiation in the market place
   d. Operational effectiveness
   e. Product innovation
   f. Better compliance

3. ESG risk dimension: publicly-shared information related to risk. Risk has been categorised into:
    a. Personnel risk
    b. Legal risk
    c. Operational risk
    d. Political risk
    e. Reputation risk

Figure 4: Disclosure was distributed rather evenly across sectors

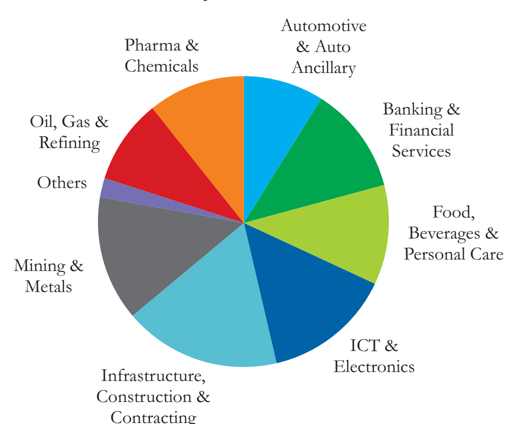


Table 3: In 2014, about 900 ESG-related information items were released by top 100 businesses. Information was distributed across E, S and G parameters

ESG Information category	Number of disclosures
E	
Biodiversity management	16
Climate change and emissions management	68
Products Life Cycle Sustainability	57
Environmental compliance	38
Operations	39
Energy management	15
Waste management	9
Water management	6
S	
Customer/Consumer satisfaction	52
Employees' well-being	90
Inclusive growth	84
Other Social related information	155
G	
Corruption and bribery	35
Corporate policies/standards	54
Board engagement	39
Other Controversies[8]	150
Total	**900**

Table 4: Disclosures about risks by top 100 listed companies

	Personnel risk	Legal risk	Operational risk	Political risk	Reputation risk	Total
Automotive & Auto Ancillary	5	3	30	3	6	47
Banking & Financial Services	5	18	23	2	14	62
Food, Beverages & Personal Care	2	8	4	2	7	23
ICT & Electronics	4	7	2	6	18	37
Infrastructure, Construction & Contracting	3	32	28	6	11	80
Mining & Metals	3	53	18	12	5	91
Oil, Gas & Refining	1	22	13	5	6	47
Pharmaceuticals & Chemicals	2	38	7	2	11	60
Others	1	6	4		1	9
	21	187	129	38	79	459

Expectedly, much of the information about risks is related to legal risks that are required to be disclosed and acted upon. Interestingly however, there is proactive public disclosure in the form of press releases and official company statements on items related to operational risk.

influence the way capital is deployed into publicly-traded companies in India. There are indications of certain key emerging trends in the way sustainability performance is getting reviewed and managed by companies. These key trends include:

1. Top management is getting more involved in sustainability-related issues

Table 5: Disclosures about opportunities by top 100 listed companies

	Accessing new markets	Building Reputation Capital	Differentiation	Operational effectiveness	Product innovation	Better compliance	Total
Automotive & Auto Ancillary	3	7	3	8	12	2	35
Banking & Financial Services	22	9	1	8	3	2	45
Food, Beverages & Personal Care	9	17	4	29	14	5	78
ICT & Electronics	17	32	5	21	7	8	90
Infrastructure, Construction & Contracting	31	7	3	26	5	6	78
Mining & Metals	3	12	2	10		8	35
Oil, Gas & Refining	8	10	3	13	1	4	39
Pharmaceuticals & Chemicals	4	7		6	11	6	34
Others				7			6
Grand Total	97	101	21	128	53	41	441

441 information items (out of the 900) disclosed by the top 100 listed companies were about opportunities i.e. how they were pursuing aspects of E, S and G - related opportunities for their businesses. Most of these disclosures were made on a multitude of platforms, including press releases, and news portals. This indicates that most businesses aim to target any voluntary communication to all stakeholders (rather than limiting the same to investors).

Outlook for 2015: from Disclosure to Performance

From the perspective of investors, not only should disclosure metrics be standard and comparable across businesses, they should also translate into monetary value for investors through risk mitigation and identification of opportunities.

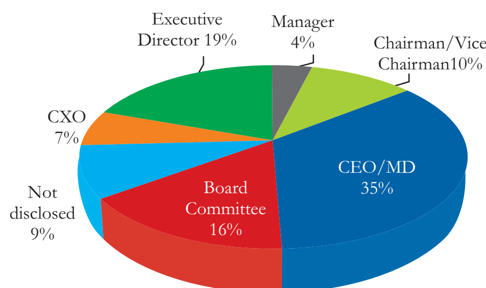
The BRR (Business Responsibility Report) has enabled a standard framework for disclosure. In 2015 we expect more standardised data to emerge that will

2. Pointed quantitative data is likely to become a part of investor-business dialogues
3. There will be ongoing refinement of the benchmarks being developed and wider adoption by both investors and businesses, to gauge and improve upon long-term business continuity and performance

1. Increased involvement of the top management in sustainability-related issues

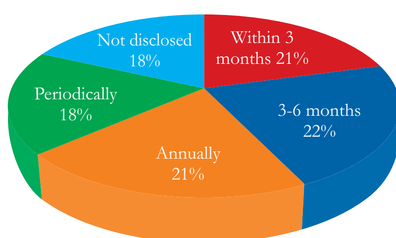
In response to the BRR question "who is responsible for the sustainability practices and performance of the company" (Figure 4), more than 50 per cent of the respondents have mentioned the involvement of top management. The response to this question indicates how integral sustainability is to businesses, and who has the executive responsibility for managing sustainability performance. While answers varied across sectors and type of business (private, state-owned, etc.), it is clear that an important performance benchmark is the involvement of top management in making sustainability a priority.

Figure 5: Who is responsible for sustainability performance?



As a corollary to the above question, the frequency and review of business responsibility performance also determines how integral it is. From an investor standpoint, this is an important indication of how serious a business is about sustainability.

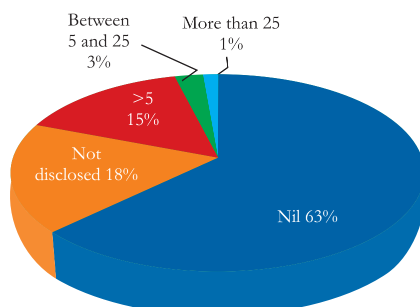
Figure 6: Frequency of review of sustainability performance



2. Pointed, quantitative data to become a part of investor-business dialogue

The current BRR framework has some pointed questions, which reveal to investors and other stakeholders, the key regulatory risks that the businesses face. From an investor perspective, information contained in these metrics (pertaining to cases on the companies or fines being paid by them) is crucial in assessing how well the company is being governed and what regulatory challenges is the company running into.

Figure 7: Cases filed by stakeholders

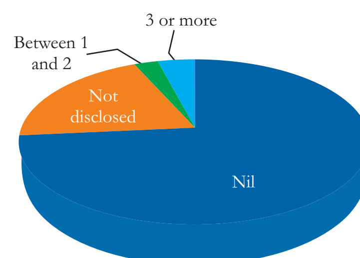


Examples of cases include:

Cases filed by stakeholders regarding unfair trade practices, irresponsible advertising and/or anti-competitive behaviour: Number of formal stakeholder complaints is an interesting metric to determine a company's standard of governance. While many businesses have not revealed this data this year, it seems that the achieving a status of nil complaints and cases through the year is the benchmark at which corporate India is holding itself accountable, as more than 50 per cent businesses have already reported to have achieved the same.

Number of show cause or legal notices received from central and state pollution control boards (CPCB/SPCB) still pending (i.e. not resolved to satisfaction) at end of the financial year: There seems to be a trend that most companies deal with such notices in an expedited manner. This is the reason why most companies have reported that there are no notices pending. While it will be important to get businesses to report on the overall number received, it seems if those are addressed in a timely fashion is also important for investors to understand.

Figure 8: Number of legal notices



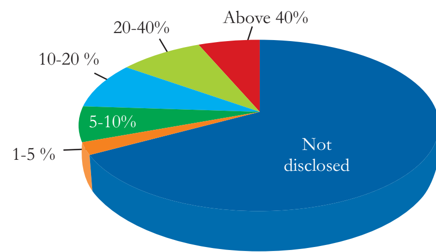
Source: ESG Score of Indian Companies, 2014

3. Measures impacting long-term business continuity and performance will start getting benchmarked

Currently, although quantitative data is being reported, it is not in a standardised format. Therefore, this data, although useful for investors, is not comparable.

While for most environment-related parameters, the data is disparate, businesses are consistently providing information on their energy consumption and use of renewable energy. One such metric, where quantitative and very useful data is being reported is "Use of renewable energy as percentage of total energy consumption". Given the escalation in diesel pricing, the operating margins of businesses are, in no small way, linked to energy security. Therefore, it is important to encourage standardised disclosure for this metric.

Figure 9: Use of renewable energy as percentage of total energy consumption



Source: ESG Score of Indian Companies, 2014

Continuing to Track the Market Pulse

The above analysis indicates that Indian companies are clearly moving towards integration and mainstreaming of non-financial disclosure. While this is an encouraging indicator to those striving for inclusive, sustainable and responsible growth in India, it is also certain that the country's financial sector will have to play a leading role in promoting this trend.

In this context, to create a systematic change, it is important that ESG information is aligned and made consistently available and tools and initiatives, such as those outlined above, continue to be developed and evolved in a bid to mobilise, enable and equip financial institutions to invest responsibly. Moreover, it is also necessary to continually engage financial institutions and sensitise them towards the "why", "what" and "how" of responsible finance—a key activity to ensure rapid transformation of the financial sector.

Therefore, with the overall objective of increasing the adoption of responsible finance practices in India, the India Responsible Investment Working Group continues to provide access to ESG information and trends to investors and companies. Information resources include:

1. Quarterly ESG dashboard that tracks developments at listed companies
2. Tracker on Business Responsibility Reports
3. Annual scoring of ESG performance of Indian companies

The group is also beginning to host investor-analyst discussions with businesses and tracking SRI fund flows.

The Sustainable Business Leadership Forum (SBLF) has been working closely with businesses, investors, catalyst organisations and policy makers to identify links between capital flows and Environmental, Social and Governance (ESG) disclosure in India and promote dialogues about the expectations, concerns, challenges and realities surrounding ESG measurement, management and disclosure in the Indian market.

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2 Adapted from the working paper titled "Corporate Social Responsibility and Access to Finance" by Beiting Cheng, Loannis Loannou, George Serafeim. Published in the Strategic Management Journal in May 2011; http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1847085

3 ES Disclosure and Reporting score is arrived from reporting on 35 key indicators by top 100 listed businesses in India and KZ Index = -1.001909 x Cash Flows / K + 0.2826389 x Tobin's Q + 3.139193 x Debt / Total Capital + -39.3678 x Dividends / K + -1.314759 x Cash / K

4 Log and quadratic regressions were also tested; but linear regressions had the best fit

5 http://ckinetics.com/crackingtheconundrum/

6 The Working Group was convened under the Sustainable Business Leadership Forum (SBLF) and constitutes the Indian Institute of Corporate Affairs, Deutsche Deutsche Gesellschaft für Internationale Zusammenarbeit GmbH (GIZ), and cKineticshttp://SBLF.SustainabilityOutlook.in/about-the-forum/sustainability-disclosure-and-reporting

7 In 2012, SEBI (the capital markets regulator in India and the watch-dog for investors) mandated that the top 100 listed businesses (by market capitalisation) annually furnish Business Responsibility Reports http://www.sebi.gov.in/cms/sebi_data/attachdocs/1344915990072.pdf

8 No "rumoured" controversies were taken into considerations. Only those that the company was actually embroiled in criminal cases against company officials, regulatory inquiries etc.

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We have seen a major opportunity in making voluntary disclosures"—Beroz Gazdar

Head Sustainability, Mahindra & Mahindra in conversation with JRF editors

›› Beroz Gazdar

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1. How has the sustainability journey at Mahindra Group evolved? What are your views on internal struggles between related functional departments within a company as it embarks and progresses on this journey?

Mahindra's sustainability journey started around the end of 2007 when conversations around non-financial disclosures and business risks from climate change had just started. Concepts of green mobility and green technology were being discussed at various forums and India had announced the National Action Plan for Climate Change. At Mahindra, concepts such as ethical business, governance, social responsibility, quality, and customer-centricity were already intrinsic to the way business was carried out. Subsequently a clear requirement from a foreign financial institution gave the final nudge for our Board to look at a triple bottom line approach as it seemed like a logical thing to do.

We got started by building on our strengths and identifying what we needed to do. As mentioned earlier, our strengths were our well-defined codes of conduct for directors, senior managers and employees, high employee commitment to the organisation's core values, the Group's commitment to governance transparency and ethics, and our commitment to contribute to social welfare aligned to the national inclusive growth agenda. Moreover, since our mainstay businesses are manufacturing-centric, issues such as energy management, quality, and health and safety were already ingrained.

On the other hand, our assessment of organisational dynamics within the group highlighted two major challenges.

The diversity of business verticals in the Group, all at different levels of maturity, was the first challenge. Realities with regard to competitors, customers and value chains of companies in the manufacturing, financial services, IT, real estate and retail are completely different. Developing a common and shared understanding of sustainability across various industry groups was identified as the bigger issue. Addressing this meant dealing with thousands of professionals having different priorities, domain knowledge and their own business challenges that needed to be considered.

Complete lack of awareness and misconceptions about sustainability was the second big challenge. Initial interactions with employees in various businesses and at different levels showed that people had a vague understanding of various aspects of sustainability. The relevance of 'climate change' to business was hardly ever discussed or debated. Initial discussions on the subject threw up much cynicism. While businesses in the services sector felt that this was relevant to only manufacturing businesses, those in the manufacturing businesses felt that any change would necessarily mean a financial burden.

There were also a few external factors to be dealt with. Internationally, the scope of 'business

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responsibility' was getting expanded from within the operational boundary to a 'Cradle to Grave' approach, and companies were expected to be responsible for human rights violations, corruption, employee health and safety even in their supply chains. Lastly, voluntary disclosure of non-financial performance from investor groups was catching up.

2. How did you address these diverse and conflicting views in context of manufacturing and services businesses?

First, we needed to have everyone on the same page. So we branded the initiative and called it 'Alternative Thinking', and developed an awareness strategy building around this concept, borrowing from Albert Einstein who had postulated that the level of thinking that created the problem would not help in solving the same. You needed 'Alternative Thinking'. The operational aspects of sustainability i.e. energy, water, resource conservation, waste reduction and GHG reduction, were then explained in a manner that every employee could relate to. This was propagated through Sustainability Walls, E-mailers, posters, pledges, quizzes, articles in in-house magazines etc., creatively and continuously over a couple of years.

Simultaneously, communication to the CEOs, CXOs, Plant Heads, and Function Heads was focused on the business case relevant to each business and each set of managers within each business. This brought the required buy-in and corrected certain myths and biases, and got everyone to run the same race together.

3. What was the approach taken for mainstreaming the sustainability agenda in the Group?

In order to ensure that the sustainability dimensions get meaningfully integrated, a phased approach was taken. The first phase was to focus on awareness building and creating systems for base lining, measuring and monitoring of data and performance. Sustainability champions and data owners were identified across all plants and business locations and all internal stakeholders were sensitised on the business case for sustainability. In the second phase, the focus was on operationalising sustainability through roadmaps for various aspects such as reduction in resource-use and emissions and waste management. This had a direct impact on cost where managers started seeing tangible benefits. The third phase was a focus on integrating sustainability dimensions in strategy and in the risk-mapping exercise. Now, issues such as resource-use efficiencies, sustainable supply chains, identifying risks from climate change are gaining relevance among business managers.

4. What was the role of the Board Room in this process?

A governance structure was put in place to start with. The Group Sustainability Council was formed with the CEOs and CXOs of different businesses right at the outset—sometime in 2007 with a clear mandate. Mr. Anand Mahindra announced the Council with a set ofclear objectives and responsibilities. This Council reports into the Board CSR Committee, which reviews performance twice a year.

5. Businesses' perception tends to be that publicly disclosing any data beyond compliance could create a competitive disadvantage. Voluntary reporting allows for self-selecting disclosure and lack of transparency about material ESG performance. Your comments on the classic "prisoner's dilemma" in which it is in no one's interest to take the first step, notwithstanding that all players could benefit?

Actually, we have seen a major opportunity in making voluntary disclosures. We found there was a business case for measuring and reporting, and going beyond compliance. Prevailing frameworks such as GRI actually helped us understand future expectations of stakeholders and markets. Subsequently, as we began articulating our global aspirations and once we received a request for information from an international investor, our understanding of the business case was further strengthened. Further, from the Inter-Governmental negotiations on Climate Change, it was clear that there would be regulation around carbon. Hence there was an advantage in being proactive rather than having an archaic view that disclosures would result in a competitive disadvantage. I think what needs to be understood is that this is about transparency and accountability of non-financial parameters and not about divulging trade secrets.

6. So you see a clear business case for ESG performance assessment and disclosure? Have any competitive advantages for your group emerged from the alternative thinking approach embedded in your sustainability strategy?

Yes there have been clear business benefits. First, once business managers started measuring and monitoring energy, water, waste in greater depth, actions were taken for conservation, as that resulted in a direct benefit of cost reduction. Second, there were internal and external recognitions which motivated people further. And third, our voluntary disclosures under CDP (Carbon Disclosure Project) and DJSI (Dow Jones Sustainability Index) and the high rating we got from these raters, caught the attention of the investor community. Today, two of our listed companies, i.e. M&M Limited, and

Mahindra Finance are listed on the DJSI Emerging Markets and three of our companies i.e. M&M Limited, Mahindra Finance and Tech Mahindra are in the list of top 10 in the Carbon Disclosure Leadership (India) Index, thereby contributing to the Mahindra Brand equity.

7. The reporting frameworks used in India are largely BRR and GRI. Then there are disclosure requirements from investors. How do you assign responsibilities and manage the different requirements? How do you see these tools getting embedded into various relevant layers of the organisation?

The reporting under any framework is meaningful only if the responsibilities lie with the concerned department and hence it has to get embedded in the various layers. Otherwise it becomes a tick-in-the-box exercise. At Mahindra we have created an IT-based process for data collection from the various departments which are as per the GRI framework but get fed into all external disclosures including the BRR. The responsibility of data integrity lies at the point where actual action takes place. The sustainability reporting team's responsibility is to collate the data and place it in public domain in appropriate formats.

8. Apart from regulators and investors, what about the role of other stakeholders, particularly, customers' interest in ESG disclosure?

The key stakeholders who demand ESG disclosure so far have been government, civil society and now, increasingly, investors. In the case of customers, there is a clear difference between B2B and B2C segments. In case of the former, ESG disclosure has actually become a competitive parameter as more business customers seek such information from their vendors. In the latter case, however, retail customers have still not shown much interest in ESG performance of products they purchase. For example customer preferences in the personal vehicle market is guided by aspiration and not by the product impact on the environment or society. Investors, of course, are interested from the perspective of assessing how competitive a company is in the global market, and this now includes ESG.

9. How do you address at M&M (including supply chains) some of the following key challenges in reporting? A) Lack of standardised disclosure metrics which results in ambiguous interpretation of ESG performance parameters. B) Lack of in-house capacity for measurement and reporting across firms. C) Absence of legal requirements and adequate incentives working as a roadblock to adoption of meaningful ESG disclosures.

A) We haven't faced any major issue with disclosure metrics. However, there will always be debates and discussions when a new regulatory requirement for reporting comes up. E.g. when SEBI made BRR mandatory, there were preliminary doubts and discussions but since the basic systems for data collection were in place, all it required was some realignment. Of course, there are a few indicators in the BRR for which we do not have measures yet. For example, the percentage of "entities that we deal with" that are covered in our BRR. Here we restrict the response to only suppliers and dealers. Other examples include reduction of resource use in sourcing, production and distribution; product-wise reduction in resource use and percentage of products and waste recycled. We have however, initiated the process for tracking and monitoring such information. Some issues would be more challenging than others. For example, product-wise information would be relatively easy as it is under the company's control, while aspects such as resource efficiency or life cycle assessment of GHG emissions across the value chain for a manufacturing company would be a humungous task. Here, capacities would have to be built not only with the tier 1 suppliers and vendors but further across the sub-tiers. This would be a prolonged exercise which would take a few years.

Mapping supply chain sustainability continues to be a big challenge for business across sectors, even though it is well understood business is as strong as the weakest link in its supply chain. There is need to build capacities at large that can help make undertaking life cycle assessments feasible across sectors.

B) The first thing that we did when we got started was put monitoring and reporting systems in place for in-house capacities to be built. That is a must.

C) Wherever there is an absence of legal requirement, a business case is first prepared and shared with the concerned department. For example, we have just signed up for the IBBI Declaration with CII for conservation under the India Business Biodiversity Initiative. A clear business case was presented to the Council as to how understanding, measuring and monitoring bio-diversity around our plant locations would mitigate future regulatory and business continuity risks in relation to each of our businesses. This then becomes an incentive.

10. How have you strengthened your reporting and communication with investors?

Even before the BRR disclosure became mandatory, we have been including ESG disclosures as a separate section in our annual report. For institutional investors our CDLI and DJSI ratings are of great help. Moreover all presentations and documents to investors include our ESG performance and targets.

11. Disclosures by Indian firms on environmental and social management systems and corporate governance would be of value to investors—A) as a signal of a firm's proactive approach to mitigate operational risks and B) in the form of additional data that allows investors to better assess risks to the business. Yet there is lack of clear communication between business and investors on ESG. What does your experience indicate?

Yes this is the case with Indian banks and financial institutions (FIs) which needs to change. Actually, almost seven years back, RBI had issued a circular for banks to follow the Equator Principles, which set out the principles of responsible lending. Internationally, banks and FIs sign up to these principles, to show their commitment to responsible lending. Today IDFC is the sole signatory to these Principles from India. As long as banks and FIs in India do not consider ESG performance and non-financial risks in their lending policies, there will be little conversation between businesses and investors on this issue.

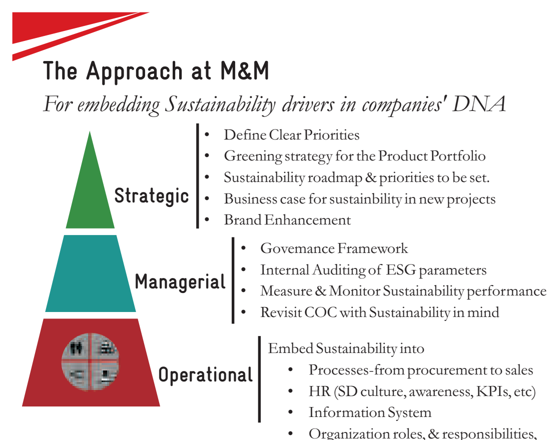
Internationally, various Stock Exchanges such as the NYSE, Singapore Stock Exchange, and Johannesburg Stock Exchange have made non-financial disclosures mandatory for companies tapping the securities market for funding. There are consortiums of large lenders including financial institutions and pension funds that analyse and rate companies based on specific disclosures on Carbon, water, supply-chain, human rights, anti-corruption, governance and social equity etc. Examples of ranking include Carbon Disclosure Project, Dow Jones Sustainability Index etc. Some trade analysts just assess companies on these parameters based on data available in the public domain which includes press reports. Somehow the banking and financial services sector in India needs to realise that only those companies which have a holistic approach to growth will be resilient to change, and thereby be good business for the financial sector in the long run.

On the flip side, there a few proactive players that have made a beginning. For example, YES Bank has products and processes that are based on the principles of responsible lending. The bank has an Environment and Social Policy and a prohibitive lending list. Disclosures on basic ESG parameters is a pre-requisite for all lending, and big-ticket financing goes through an environmental and social risk assessment process. These ESG requirements are part of the Letter of Credit system and are monitored across the lending cycle. Secondly, in November 2012, the Bombay Stock Exchange launched BSE CARBONEX, the first carbon-based thematic index in the country, to take a strategic view of organisational commitment to climate change mitigation. This index has been launched with the aim of creating a benchmark, and increasing awareness about the risks posed by climate change. This should give some impetus to ESG parameters getting mainstreamed in disclosure requirements of the financial sector.

12. Does your experience show any correlation between proactive management and disclosure of ESG data and a firm's ability to attract investment capital? What has been your biggest achievement?

Yes, we see that correlation. In general, the examples would be in form of negative screening or outcome, i.e. companies not getting funding or there is a foreclosure or pull out if investors find that the company has violated an ESG standard.

In our case, so far our disclosures have been for existing investor groups and not for fresh funding. Our biggest achievement is the external ratings and listings which signal to the world that the company is sustainable in the long run.



3 A Roadmap for Policymakers and Stock Exchanges to Promote Sustainability Reporting

By Sudeep Rathee and Anthony Miller, Ph.D

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Capital market stakeholders play a crucial role in facilitating more firms adopting sustainable business practices and in helping make financial systems more responsible. A key function of both, stock exchanges and regulators is to improve corporate performance on environmental, social and governance (ESG) issues, and promote responsible investment for funding the global sustainable development agenda. Stock exchanges, in particular, provide a central platform for interaction among investors, companies, policy makers and regulators. They are uniquely placed to provide sustainability leadership, with a variety of measures at their disposal. These include listing requirements related to sustainability reporting, voluntary initiatives, guidance documents and training for companies and investors, and sustainable investment products such as indexes that focus on ESG issues.

Financial institutions and civil society groups have been encouraging policymakers to even consider making sustainability reporting a sustainable development goal (SDG) in the post-2015 UN development agenda. For example, the Corporate Sustainability Reporting Coalition, which represents financial institutions, professional bodies, NGOs and investors, called on governments at Rio+20 conference, to develop a policy framework for promoting corporate sustainability disclosure amongst listed companies. The policymakers also recognised this need and highlighted in Paragraph 47 of the outcome document, the need 'to develop models for best practice and facilitate action for the integration of sustainability reporting'). The Report of the High-Level Panel of Eminent Persons on the Post-2015 Development Agenda[2], further proposed that '*in future—at latest by 2030—all large businesses*

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should be reporting on their environmental and social impact—or explain why if they are not doing so'.

Some progress on implementation of sustainability reporting initiatives is already noticeable. For example, in its review of sustainability initiatives worldwide, the SSE 2014 Report on Progress[3] found that:

- 19 members of the G20 have at least one regulation in place requiring disclosure of social and/or environmental metrics by companies;
- Of the 32 regulators represented on the board of the International Organisation of Securities Commissions (IOSCO), more than one-third have introduced a sustainability reporting initiative;
- At 55 exchanges over one-third of the exchanges provide either sustainability reporting guidance or training to the listed companies on their exchange; and, 12 of the 55 exchanges require aspects of environmental and social reporting for at least some of their companies, with seven of those exchanges requiring such reporting for all listed companies.

> Stock exchanges and regulators can begin by assessing the degree to which existing rules are meeting investors' information needs and where the new regulations might fill a disclosure gap

In spite of this steady progress, the adoption of sustainability disclosures by companies is fairly low. Globally, less than 10 per cent of the estimated 80,000 transnational corporations produce sustainability reports. Some part of the problem can be related to the different market structures and regulatory frameworks across countries. As a result, a common sustainability reporting agenda cannot ideally fit all markets in the same way, and requires stock exchanges and regulators to carefully understand the scope, disclosure models and implementation choices for designing sustainability reporting frameworks.

Challenges in Implementing Sustainability Reporting Initiatives

In implementation of a sustainability reporting framework, the first major dilemma faced by stock exchanges and market regulators is—the choice between mandatory versus voluntary structure of reporting. Some stock exchanges and regulators might advocate adopting the voluntary or "comply or explain" rules, whereas others could merit the mandatory sustainability reporting frameworks as more appropriate. The choice might mot be that straightforward and depends on consideration of various other aspects as well, such as—existing market rules and regulations, scope of coverage—listed and/or private companies, defining the scope of sustainability subject matter, level of capacity and readiness of to-be-covered companies.

Second, there arises the need to analyse how authority is separated in the market between stock exchanges and regulators, i.e. who should be doing it—the government, stock exchange and or regulator. For fair-play and transparency, several countries in recent past have demutualised their stock exchanges and entrusted the major regulatory powers with separate entities. The structures of these regulatory entities are also varied: some are government-backed agencies (e.g. the Monetary Authority of Singapore, the Hong Kong Securities and Futures Commission and the Mexican Comisión Nacional Bancaria y de Valores) and some are private companies (e.g. the Tokyo Stock Exchange Regulation). As a result, the self-regulatory powers of stock exchanges now differ greatly, as does the extent of regulatory oversight that they are subjected to. In countries where stock exchanges retain regulatory powers to set listing rules, the degree to which the exchange competes with other local or global exchanges, is also an important contextual consideration. Stock exchanges need to ensure that any disclosure requirements do not significantly discourage potential listee companies from listing on their exchange.

Another problem arises due to existing regulations that cover the related sustainability reporting elements. Particularly in developed markets where sustainability issues tend to be more heavily regulated, a number of environmental and social disclosure rules may already exist. In markets where various issue-specific disclosure rules exist, it can lead to a "spaghetti bowl" system of numerous *ad hoc* single-issue disclosure rules that can lack coherence and be confusing for companies to follow. To avoid this problem, stock exchanges and regulators can begin by assessing the degree to which existing rules are meeting investors' information needs and where the new regulations might fill a disclosure gap or help facilitate or enhance investor access to such disclosures. In turn, stock exchanges and regulators should consider introducing a more comprehensive reporting initiative wherein different government entities and/or stock exchanges will come together to develop an overarching structure. In India, for example, when the Ministry of Corporate Affairs came out with the National Voluntary Guidelines on

Social, Environmental & Economic Responsibilities of Business in July 2011, the Securities and Exchange Board of India (SEBI) decided to require listed companies to prepare business responsibility reports based on the guidelines.

Decide among Disclosure Models: Mandatory or Voluntary

Sustainability reporting initiatives can be categorised into two main types: mandatory and voluntary. Mandatory approaches can be based on a comply or explain or a prescriptive framework, while voluntary approaches leave reporting to the company's discretion but have the potential to be effective where certain drivers exist. The two approaches can be used simultaneously with mandatory reporting reserved for only some issues or some companies. They can also be used sequentially, with voluntary reporting used for an initial period to allow companies to develop capacity, eventually to be supplanted by mandatory reporting to ensure a harmonised approach among all companies.

Evidence[4],[5] shows that companies are more likely to report specific information if such disclosure is made mandatory by a stock exchange or regulator. Consequently, some member States, for example, France, Denmark and Sweden, have made sustainability reporting mandatory for at least some corporations, in particular large enterprises and state-owned enterprises.

Analysis also shows that some voluntary initiatives have been very effective, while some mandatory rules have been largely ignored. In the area of sustainability reporting, many countries show far more reporting than would otherwise be required by mandatory rules. For example, the UNCTAD study[6] found that on corporate governance disclosure, only 56 per cent of 25 emerging markets require this item, yet 91 per cent of 188 of the largest companies in those markets were disclosing this. Therefore, while mandatory rules generally produce more disclosure overall, well-designed voluntary approaches can also be an effective option, particularly for jurisdictions introducing a sustainability reporting initiative for the first time.

Comply or explain framework for disclosure

Stock exchanges and regulators should consider using a comply-or-explain framework when requiring sustainability disclosures from companies. This approach is common among existing mandatory sustainability reporting initiatives and is also the model proposed by the United Nations High-Level Panel of Eminent Persons on the Post-2015 Development Agenda. Under a comply-or-explain framework, companies typically report against a specified standard set of disclosure items, or they are asked to produce a sustainability report and explain their approach to the selection of information included in the report. In the former case, companies should explain any gaps in disclosure as compared with the specified standard; and here the regulator should provide guidance on how to explain such gaps. Alternatively, companies are simply required to explain why they do not publish a sustainability report at all, if that is the case.

Australian Stock Exchange (ASX), for example, has adopted a comply-or-explain model for its Corporate Governance Principles and Recommendations[7], which contain provisions for sustainability issues. Companies are encouraged to apply the recommendations set out in the guidelines and are required to provide a statement in their annual report disclosing the extent to which they have followed these. Companies also need to identify the recommendations that they have not followed and explain the reasons why.

Similarly, the Johannesburg Stock Exchange (JSE) expects all issuers to address the principles set out in the King Code of Corporate Governance, which currently covers 75 principles[8], including on sustainability and integrated reporting, disclosing how each principle has been applied or explain why or to what extent they were not applied. In addition, the assessment of the principles must be documented in the form of a register that must be made available on the website of the issuer.

The frameworks used by ASX and JSE are examples of a principles approach versus a rules-based approach to non-financial reporting. A principles approach in corporate governance, typically coupled with a comply-or-explain framework, establishes a high-level set of basic principles, while acknowledging that the specific implementation of those principles in different companies and industries may take different forms that are equally effective and appropriate. As the ASX guidance states, a principles approach tied to a comply-or-explain framework allows a company to explain how its practices accord with the spirit of the relevant principle. Companies are still required to demonstrate that they understand the relevant issues and have considered the impact of any selected alternative approach.

Begin with a voluntary initiative

Voluntary sustainability reporting initiatives also have the potential to be effective where certain drivers

exist. Companies may be more likely to comply with a voluntary disclosure recommendation when there is significant demand for sustainability information from their key stakeholders (investors, customers, government officials), and companies consider that there are benefits (operational and reputational) to such reporting.

The effectiveness of a voluntary approach can be demonstrated by the rise of corporate sustainability reporting on the part of thousands of companies not legally required to do so. An important tool for enhancing the effectiveness of a voluntary sustainability reporting initiative is the creation of a related sustainability index. Such indices typically highlight top performers, allowing public pressure and competiveness between firms to drive disclosure and ultimately performance (International Finance Corporation, 2011). In Brazil, for example, the BM&FBOVESPA stock exchange launched its carbon efficient index in 2010 which, within 24 months of its launch, led to a 44 per cent increase in the number of companies voluntarily reporting emissions data.

Employing a voluntary scheme can be particularly appropriate when introducing a sustainability reporting initiative for the first time, and especially when doing so in a jurisdiction that has little experience producing such reports. Such voluntary schemes can be a useful educational phase for companies, allowing them to build the necessary capacity to produce high-quality sustainability reports.

Consistent policy direction

Stock exchanges and regulators should consider advising relevant stakeholders on the future direction their policy will take, and companies should be allotted sufficient time to adapt. When the initiative is intended to evolve from one disclosure model to another, for example from voluntary to mandatory, clarity on its direction enhances the uptake of sustainability disclosure in a market. For example, in 2012, the Hong Kong Stock Exchange included a voluntary environmental, social and governance reporting guide[9] in its listing requirements with a view to implement the rule to comply or explain by 2015. Since then, in last two years, the exchange has provided training to its listed companies on this ESG reporting guidance and held surveys to gauge their readiness for a comply-or-explain implementation in 2015[10]. Similarly, Singapore Exchange (SGX) launched[11] a sustainability reporting guide for listed companies in 2011, and then in 2013 CEO of the SGX announced[12] their plan to ultimately move to a comply-or-explain reporting regime in the future. Latest, in Oct 2014, the exchange has announced[13] a one-year period for companies to prepare their internal process before the exchange will implement a mandatory sustainability reporting in 2016.

Several stock exchanges that initially promoted voluntary sustainability disclosure among listed companies have moved to mandating sustainability disclosure. For example, Bursa Malaysia introduced its corporate social responsibility framework in 2006. Since the end of 2007, however, listed companies must, according to the stock exchange's listing requirements, disclose their practices that support sustainable business. If there are none to report, a statement must be provided to that effect.

Identify Scope of Sustainability Reporting Initiatives

Stock exchanges and regulators, when determining the appropriate scope of application and subject matter for a sustainability reporting initiative, should consider the existing capacity of companies to report on sustainability issues and focus on the disclosure of information that is material to investors and other stakeholders.

Scope of application: Number and types of companies included

Sustainability reporting initiatives may seek to focus on those enterprises with the most significant environmental and social impacts, while taking into the consideration the capacity of companies—especially small and medium-sized enterprises (SMEs)—to prepare such reports. Particularly in the case of mandatory disclosure initiatives, one policy option is to only require a subset of companies to disclose on sustainability issues, such as only large enterprises, enterprises that operate in specific high-impact sectors, or state-owned enterprises. For small enterprises, either mandatory initiatives with differential reporting standards appropriate to their capacity or voluntary reporting schemes could be considered.

Since 2012, the listing agreement of Indian Stock Exchanges mandate that business responsibility reports addressing environmental, social and corporate governance issues must be disclosed as a part of annual reports for the top 100 listed entities by market capitalisation. This reporting requirement in India is currently voluntary for all other listed entities. Such an approach—mandatory sustainability reporting for only the 100 largest companies—can be part of a gradual introduction of reporting requirements with the aim of eventually covering a broader group of large enterprises.

In addition, regulators should seek to avoid creating disproportionate burdens on listed companies versus private companies and consider the application of sustainability reporting initiatives to both private and listed companies. In conjunction with the competitive environmental issues discussed above, initiatives that create a disproportionately high burden on listed companies compared with private companies may influence a company's decision to list.

Scope of subject matter: 'Materiality' of sustainability issues

Stock exchanges and regulators should consider explicitly including sustainability issues in their definitions of material information and make these part of companies' requirements to determine and disclose material business risks. Several international organisations have now developed guidance on how to conduct a materiality analysis, for example, the Carbon Disclosure Standards Board, Global Reporting Initiative, International Accounting Standards Board, International Integrated Reporting Council and International Organisation for Standardisation. This approach will encourage companies to think actively, and on an ongoing basis about how sustainability issues affect their business and to define the thresholds that deem an issue material.

In certain contexts, stock exchanges and/or regulators may consider providing minimum requirements for disclosure or examples of information that companies should consider reporting. This could relate to specific sectors or to issues of local imperative.

Suggestions to Optimise Policy Outcomes

Promote responsible investment practices

Responsible investment refers to the efforts of investors to incorporate sustainability issues into investment decisions and to actively engage with investee companies to encourage improved sustainability practices. Stock exchanges and regulators should consider promoting responsible investment practices among investors as a means of creating further demand for high-quality sustainability reporting.

Consider making reference to international standards

Reporting on sustainability performance in accordance with international standards and guidelines provides a consistent and comparable approach to sustainability issues. Consistency and comparability add value to sustainability disclosures for investors and other stakeholders. The benefits of a harmonised approach among companies worldwide have long been evident in financial reporting, as reflected in the efforts of policymakers to work towards the convergence of international financial reporting standards. With a view to promoting a harmonised approach stock exchanges and regulators should consider requiring companies to report on sustainability issues in accordance with an international reporting framework. In Sweden, for example, all state-owned enterprises are required to produce a sustainability report using Global Reporting Initiative guidelines.

Use multi-stakeholder consultation

A multi-stakeholder dialogue can identify priorities and challenges from a range of perspectives to assist stock exchanges and regulators in the design and implementation of a sustainability reporting initiative. Optimum buy-in can be created by consulting with key stakeholders throughout the development process as opposed to once a specific approach has been decided: i.e. stakeholders should be involved in the design of the initiative, not merely its approval.

Provide sustainability guidance in local contexts

Sustainability guidance developed by a stock exchange or regulator to complement existing international standards can reflect sustainability imperatives that are globally aligned but locally relevant. Guidance does not need be prescriptive or exhaustive, but can lay a foundation for embedding sustainability and improving transparency. Information that helps link multiple international standards and provides guidance on how such standards can be applied is particularly useful.

Provide incentives for disclosure

Stock exchanges and/or regulators can provide a range of incentives to increase the rate of company uptake of sustainability disclosure initiatives. For mandatory reporting rules, stock exchanges and regulators could review the sanctions they already have in place for non-compliance with listing rules and corporate reporting regulations, particularly those related to non-financial reporting, such as corporate governance issues. To promote compliance, it can be a useful exercise to conduct periodic reviews of the corporate reporting of random samples of companies, or samples of the largest firms.

Promote accessible and timely disclosure

Sustainability information, as with other forms of corporate reporting, should be made publicly available to all current and potential future investors. At present, several countries including Brazil, France, India, Norway and Pakistan, encourage companies in

their jurisdiction to publish a sustainability report on their websites. Regulators or stock exchanges may also plan to set up a central web database that provides a comprehensive and searchable inventory of company sustainability reporting.

Encourage third-party assurance

Stock exchanges and/or regulators may wish to consider creating a requirement to have sustainability data assured by an independent party or defining the legal accountability for the accuracy of such data. Sustainability information supported by an assurance statement from third parties is considered more credible and reliable by many investors. Furthermore, companies that have gone through an assurance process are more likely to increase the quality of their existing data management systems, leading to higher quality sustainability reports.

Conclusions and Key Recommendations

Over past few years an international sustainability trend is emerging wherein stock exchanges and regulators in several countries are introducing new sustainability reporting initiatives. Still, due to significant variation in market conditions and regulatory structures across nations, the decision to develop appropriate sustainability reporting initiatives become quite complex. This paper recognises that there is no "one-size-fits-all" approach to sustainability reporting, and instead offers a roadmap to policy makers and exchanges for designing their approach to introduce such initiatives.

As a starting point, the paper suggests that those designing policy should consider the capacity of companies to report on sustainability issues, and should focus on the disclosure of information that is material to investors and other stakeholders. Among other recommendations, it suggests focusing on enterprises with the greatest sustainability impacts, while introducing more appropriate requirements for smaller companies that do not put an undue burden on their capacity. It also recommends carefully considering the burden placed on listed versus private companies, to avoid discouraging private companies from listing or listed companies from delisting. Stock exchanges and regulators should also consider including sustainability issues in their definitions of the material information that listed companies must disclose.

The paper also compares the choice between mandatory and voluntary disclosure frameworks. It observes that, although companies are more likely to report information if mandated to, well-designed voluntary approaches can also be an effective option. Even if the intention is to introduce a mandatory disclosure rule, beginning with a voluntary regime first can be an important practical step to allow companies to develop the necessary capacity. The paper also suggests adopting a 'comply or explain' framework, allowing companies to elect not to disclose, provided they give their reasons.

In conclusion, while the paper recognises the steady emergence a 'new mainstream' among policy makers, regulators and exchanges, the sustainability challenges the world faces remain enormous. Further progress by exchanges and their regulators on implementation of sustainability initiatives is particularly important given the wider sustainable development context, and the expected introduction of the UN Sustainable Development Goals in 2015.

About UN's Sustainable Stock Exchanges (SSE) Initiative

As a UN-led initiative the Sustainable Stock Exchanges (SSE) initiative was launched by UN Secretary-General Ban Ki-moon 2009. The SSE is aimed to provide a peer-to-peer learning platform for exploring how exchanges can work together with investors, regulators, and companies to enhance corporate transparency, and ultimately performance, on ESG (environmental, social and corporate governance) issues and encourage responsible long-term approaches to investment. The secretariat of SSE is co-organised by the UNCTAD, the UN Global Compact, the UNEP Finance Initiative and the UN supported Principles for Responsible Investments (PRI).

Stock exchanges around the world continue to join the SSE initiative as Partner Exchanges to work on the sustainability measures, to share experiences, overcome common challenges and engage with key capital market stakeholders. Since 2012, when the SSE first started inviting the exchanges, its membership has tripled from its original five members to sixteen. At the time of press, more than 17,000 companies, with approximately USD 36 trillion in market capitalisation, are listed on SSE Partner Exchanges, which represents over half of the current global market capitalisation.

** This article mainly draws from the researches carried out in *Sustainable Stock Exchanges Report: A Report on Progress,* and *Best practice guidance for policymakers and stock exchanges on sustainability reporting initiatives*[15].

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4 Sustainability Context in Measurement and Reporting: Making Metrics Meaningful

By Bill Baue, Poonam Madan and Mark McElroy

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"Sustainability requires contextualisation within thresholds. That's what sustainability is all about."— Allen White, Co-Founder & Inaugural CEO, Global Reporting Initiative[1]

Introduction

The term corporate sustainability is inherently normative—baked into it is a desirable and objectively definable goal needing achievement. This inclusion of a 'goal line' carries profound implications in practice, as the sustainability of an organisation is no longer assured for business (and human society as a whole). Indeed, only when the viability of a system is in question, does the word sustainability become relevant. So the applicability of the term corporate sustainability is rising precisely because the ability of our current business (and social) systems to survive and thrive is, quite literally, at risk.

Perhaps ironically, organisations are so successful at achieving their goals of wealth creation and product/service provision that they are depleting the very resources they rely upon, and destabilising the balance needed for self-perpetuation. In order to continue achieving these goals, business needs to layer in an additional set of goals: namely, respecting the limits of our world's ecological systems and fortifying the foundations of our collective social systems. Only by operating within what Johan Rockström and Kate Raworth call "a safe and just operating space for humanity" can business continue to create healthy prosperity.[2]

Background

In 2013, the term sustainability celebrated its 300th birthday—Hans Carl von Carlowitz coined the concept (*Nachhaltigkeit* in German) in his 1713 treatise on sustainable forestry yields, *Sylvicultura Oeconomica* ("We must aim for a continuous, resilient, and sustainable use" of forests, he wrote).[3] In recent decades, this notion gained traction in corporate thinking, spurred by the 1987 fusing of the concepts 'sustainability' and 'development' in the watershed Brundtland Report: "Sustainable development is development that meets the needs of the present without compromising the ability of future generations to meet their own needs."[4]

In the realm of corporate reporting, the Global Reporting Initiative (GRI) enshrined this concept when it introduced the term 'Sustainability Context' as a core Principle in the second generation of its Sustainability Reporting Guidelines (also known as G2) in 2002:

"The reporting organisation should seek to place its performance in the larger context of ecological, social, or other limits or constraints," GRI stated in defining the new Principle. "This will involve discussing the performance of the organisation in the context of the limits and demands placed on economic, environmental or social resources at a macro-level." [5]

Significantly, GRI established this principle within the framework of capital theory, which is predicated on preserving stocks and flows of vital resources at levels sufficient to support human wellbeing and prosperity. [6]

"[S]ustainability reporting draw[s] significant meaning from the larger context of how performance at the organisational level affects economic, environmental, and social capital formation and depletion at a local, regional, or global level... [S]imply reporting on the trend in individual performance (or the efficiency of the organisation) leaves open the question of an organisation's contribution to the total amount of these different types of capital. [P]lacing performance information in the broader biophysical, social, and economic context lies at the heart of sustainability reporting and is one of the key differentiators between this type of reporting and financial reporting..."[7]

G2's definition ended with the acknowledgment that the "understanding of how best to link organisational performance with macro-level concerns will continue to evolve."[8] Such evolution has indeed unfolded over the past decade, in both theory and practice, with significant caveats.

On the theory front, Center for Sustainable Organizations (CSO) Executive Director Mark McElroy conceptualised Context-Based Sustainability (CBS) as a framework for operationalising GRI's Sustainability Context Principle.[9] The implementation of CBS at the company level hinges in particular on the application of two interrelated concepts:

- **Thresholds** that demarcate the carrying capacities of vital capital resources and which therefore should be represented in the measurement of sustainability performance[10] and
- **Allocations** that apportion to companies their fair shares of vital capital resources and/or the burden to produce and maintain them at levels that are sufficient for stakeholder wellbeing.

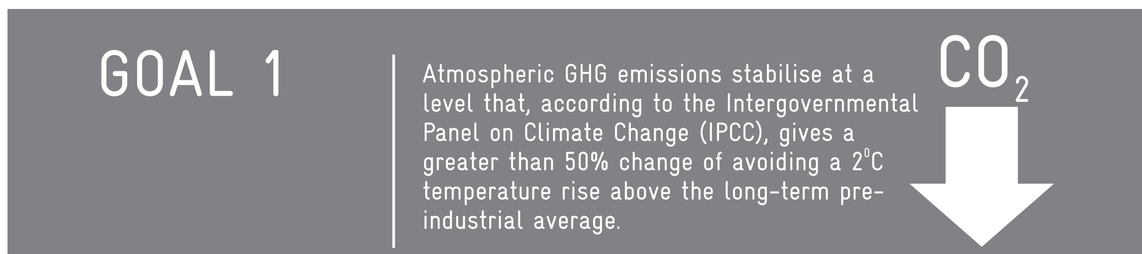
On the practice front, the Sustainability Context Principle has been applied most widely to greenhouse gas (GHG) emissions in the context of science-based carbon budgets:

- **Ben & Jerry's** (a US-based subsidiary of Unilever) helped pioneer the Global Warming Social Footprint method (created by CSO) launched in its 2007 Social & Environmental Assessment Report[11]
- **BT** Chief Sustainability Officer Chris Tuppen developed the Climate Stabilising Intensity (CSI) Targets method in partnership with *Limits to Growth* co-author Jørgen Randers—who published this greenhouse gas emissions per unit of value added (GEVA) method in an academic journal[12]
- **Autodesk** adapted CSI to build out its own C-FACT (Corporate Finance Approach to Climate-Stabilising Targets) metric, which it made freely available[13]
- **EMC** took advantage of this accessibility, and modified the methodology to make it even more aggressive[14]
- **Mars**' "Sustainable in a Generation" programme set science-based targets for GHGs (as well as water and waste)[15] and
- **Ford** extended a science-based carbon target to its products, which represent the lion's share of its carbon footprint across its value chain.[16]

"We have calculated that, to achieve these goals between now and 2030, capital equal to 2 per cent of the South African gross domestic product (GDP) will have to be invested and lent differently into the economy annually. Our 'fair share' of this equates to our market share of debt provision in the economy."

Goal 1, for example, calls for setting "a science-based carbon budget for South Africa for the period 2015-2029":

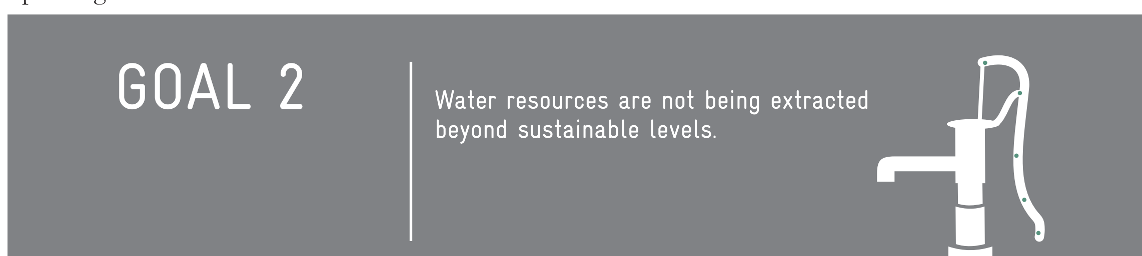
- A science-based carbon budget (which the Intergovernmental Panel on Climate Change set at 1,009 Gt of CO2 emissions between 2012 and 2099 for a 66 per cent chance of staying below 2°C) represents a planetary *threshold.*
- Nedbank calculates South Africa's allocation as 1.5 per cent of this global budget, making it "possible to plot a credible emissions trajectory for South Africa for the remainder of the century and to calculate the corresponding carbon budget up to 2030."
- Nedbank further decomposes this allocation to the company level, enabling "a succession of five-year carbon budgets [to] be developed from which Nedbank will calculate what the total emissions of its lending book should be in every five-year period."



An example relevant to financial institutions in the developing world is that of **Nedbank** in South Africa. Nedbank is advancing context-based sustainability (CBS) reporting through its Fair *Share 2030* initiative, which sets eight sustainability goals across the Triple Bottom Line of environmental, social, economic issues that need to be met to "make a thriving South Africa happen."[17] Nedbank integrates both key elements of CBS, tying its goals to external thresholds in the broader context it operates within, and setting allocations for its fair share proportion of operating within these boundaries:

Similarly, Goal 2 sets the context-based condition that "water resources are not being extracted beyond sustainable levels," and proposes targets that "ecological water requirements are maintained in catchment areas" and "groundwater is not extracted beyond the rate that it is replenished."

On the social and economic legs of the Triple Bottom Line's stool, Goal 3 steps in the direction of



a context-based approach by calling for South Africa's labour force to be"employed at percentages comparable to other countries." This goal contextualises itself in relation to other nations' employment rates, which may or may not be sustainable; taking final steps toward full contextualisation requires comparison to thresholds for sustainable rates of employment, and then applying Nedbank's proportionate responsibility for supporting the achievement of such employment rates.

GOAL 3

South Africa's labour force is employed at percentages comparable with other countries.

Exceptions, Not the Norm Yet

However, these examples represent exceptions to the broader dynamic of near-universal absence of Sustainability Context in company reporting. In a published 2014 dialogue, GRI Co-Founder and inaugural CEO Allen White explained the reasoning behind establishing the Sustainability Context principle in 2002, and candidly assessed the current state of play:

"As head of GRI at that point, I felt very strongly that an initiative that purports to be a sustainability initiative could not simply frame its work along the lines of, shall we say, incremental performance assessment. That is, companies that were improving each year in regard to water management, energy management, living wages and occupational health and safety should be recognised in the evolving GRI framework. *But incrementalism alone, at the end of the day, was insufficient to be faithful to a sustainability reporting framework*," said White. "ESG *does not, by nature, carry a true sustainability gene*."(Emphasis added)

"We would have to take a further step and include a principle that would call for assessing…performance against...limits, thresholds, and norms that are externally defined, not simply defined by peer group comparison or internal targets and goals," White continued "*Sustainability requires contextualisation within thresholds. That's what sustainability is all about*." (Emphasis added)

"In the best of worlds, reporting would have evolved to supply...Context-based disclosures. *But this is not the case*," White concluded. "*[T]o this day in the reporting world, as you well know, Sustainability Context is incipient, uneven, and occasional*." (Emphasis added)[18]

Given that Sustainability Context is one of GRI's first-order principles (along with Materiality, Stakeholder Inclusiveness, and Completeness), why do GRI-based reports fall so short in applying it?[19] In the lead-up to the 2013 issuance of G4 (the fourth generation of GRI Sustainability Reporting Guidelines), a group of 66 thought leaders and practitioners in the Sustainability Context Group (SCG—a global community of practice network advocating for understanding and uptake of Sustainability Context) submitted a public comment calling on GRI to rectify this problem:

"Although GRI's Guidelines currently do advocate for the inclusion of Sustainability Context in organisational reports, they fail to provide specific guidance for how to do so. Because of this lack of guidance, very few GRI-based sustainability reports have ever actually included such context—and yet without it, there can be no true or authentic sustainability reporting, in our opinion."[20]

Upon its release in May 2013, G4 did not add such guidance, prompting strongly worded responses.[21] Over the next year-and-a-half, SCG's Co-Founders engaged with the GRI Board and senior executives to jointly conduct research that confirmed the insufficiency of current guidelines. However, at an October 2014 meeting between SCG and GRI, the incoming GRI CEO suggested it is up to the broader community to advance this kind of innovation in practice.

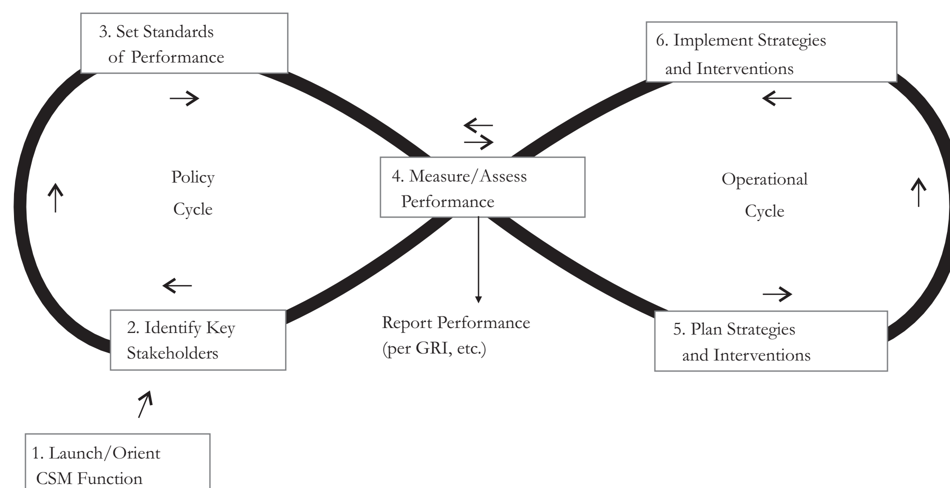
Corporate Sustainability Management and Context-Based Metrics

As earlier noted, the first and most comprehensive implementation of the Sustainability Context Principle in practice was developed by Mark McElroy

and is known as Context-Based Sustainability, or CBS. Unlike other approaches, CBS measures, manages and reports the performance of organisations relative to real social, economic and ecological thresholds in the world. For example, water use is measured relative to renewable limits in watersheds; greenhouse gas emissions relative to constraints in the climate system; solid wastes relative to zero-waste targets; etc.

In practice, CBS takes the form of a six-step methodology known as the Corporate Sustainability Management (CSM) Cycle (see Figure 1). In broad strokes, the CSM Cycle follows the logic of a gap analysis, whereby (1) context-based targets are defined, (2) actual performance relative to the achievement of such targets (i.e., gaps) is revealed, and (3) wherever gaps are found, management interventions are made to help close them. The process repeats itself endlessly, as new standards and new gaps can appear at any time, not to mention new strategies for how best to address them.

Figure 1—The CSM Cycle



Source: McElroy and Van Engelian, 2012

Each of the six steps in the CSM Cycle is described below:

1. Launch/orient CSM function

The first step calls for a formal embrace of CBS. This is not for the faint of heart, since the adoption of CBS can, for some, be seen as a very real threat to the sanctity of shareholder primacy, or to the view that profit maximisation should be pursued above all else. Indeed, in its purest form, CBS calls for performance that is socially and environmentally sustainable, as well as economically sustainable. In other words, CBS explicitly accounts for, measures, and balances trade-offs between social, environmental, and economic performance.

The challenge here is to make trade-offs that are fair and equitable, and which do not disproportionately or persistently favour one stakeholder group or dimension of performance (e.g., economic) over all others. For this to happen, CBS must be formally endorsed by its board and management at the highest levels of an organisation, including its CFO, too, whose historical commitment to the primacy of financial performance may no longer be appropriate or helpful to the long-term sustainability of the organisation.

2. Identify key stakeholders

CBS is fundamentally about managing impacts on vital capitals so as to not put the sufficiency of such capitals or the wellbeing of those who depend on those capitals at risk. Thus, in CBS, sustainability management equates to capital impact management with the wellbeing of stakeholders in mind. Therefore, stakeholders must be clearly identified. In CBS, we define stakeholders as anyone to whom a duty or obligation is owed to manage one's impacts on vital capitals in ways that can affect their wellbeing. Such duties and obligations can come about in two ways: as a result of actual impacts on vital capitals that need to be sustained, or due to contracts and/or agreements around management of vital capitals.

3. Set Sustainability standards of performance

Once an individual or group has been accorded stakeholder status, associated sustainability standards of performance must be defined for normative impacts on the carrying capacities of vital capitals upon which those stakeholders rely for their well

being. In other words, where a duty or obligation exists to have, not have or manage one's impacts on vital capitals in some way, the duty or obligation itself is quantitatively expressed in terms of the carrying capacity of the corresponding capital(s)—or, actually, in the inverted sense of the term.

By "inverted sense," we mean to say that whereas the term carrying capacity is usually used to express the size of a population an environment can support, in CBS we specify an environment (or capital) size a population is entitled to, or must, have in order to ensure its well being. This in turn is predicated on either how much of a fixed environment (e.g., natural capital) already exists and must be shared in a fair and proportionate way, or how much a non-fixed or anthropogenic environment (i.e., human, social, constructed or economic capital) must be created and maintained in a similarly fair and proportionate way.

> For a business not to engage in discretionary philanthropy is not unsustainable; for it to over-consume water while putting the wellbeing of others who rely on the same resources at risk, however, is

In the case of natural capital, we are all entitled to no more than our own fair and proportionate shares of what is available; in the case of the other capitals, we are expected to help produce and maintain no less than our fair and proportionate shares of what ought to be made available. Sustainability standards of performance are thereby expressed in the form of quantitative allocations, either of resources available (natural capital) or resources that can be made available or continually produced (the other capitals). Allocations can therefore also be thought of as either shares of available resources or burden shares of the responsibility to produce and maintain them. In the case of water consumption vis-à-vis duties owed to local communities, such standards might be expressed in terms of not-to-exceed levels of consumption (i.e., in gallons or litres per year); in the case of economic performance vis-à-vis obligations owed to shareholders, standards might be expressed in terms of minimum returns on equity capital (i.e., in terms of a percentage of financial capital provided).

It is also important to understand that in CBS we are not talking about philanthropy or discretionary contributions of any kind by businesses to society. CBS is strictly about performance relative to duties and obligations that are morally, ethically and—in that sense, at least—enforcedly owed to stakeholders to manage impacts on vital capitals in ways that can affect their well being. Sustainability performance is about performance relative to non-discretionary standards—duties and obligations, which if disregarded or overlooked, can put vital resources and human well being at risk. Here it should be clear that no business is responsible for all of the world's problems, nor should any one, therefore, be expected to address them as if they are. Rather, a business can only be held accountable for performance relative to the duties or obligations it actually has. For a business not to engage in discretionary philanthropy is not unsustainable; for it to over-consume water while putting the well being of others who rely on the same resources at risk, however, is.

4. Measure and assess sustainability performance

Having identified (1) stakeholders, (2) the context-based duties and obligations owed to them, and (3) the corresponding capital-based sustainability standards of performance, the CSM cycle continues by applying all of that to the measurement of performance. Context-based metrics take the form of quotients in which the sustainability standards of performance identified in step 3 of the cycle are positioned as denominators, and actual measures of performance are positioned as numerators.

A context-based water metric will typically indicate Actual Water Consumption/Normative Water Consumption. The denominator would be expressed in terms of, say, the maximum amount of water a manufacturing facility can use in a year, which in turn would have been calculated based on the size and shape of the watershed it is in, the amount of precipitation it receives each year, the number of other users located in the same place, etc.

For impacts on natural capitals such as water, the CBS scoring convention is that all scores of < 1.0 signify sustainable activity and all scores of > 1.0 signify the opposite. For impacts on human, social and constructed capitals, the scoring convention is reversed, since they are anthropogenic—humans produce them. Thus, the applicable norms are expressed in terms of minimums, not maximums; sustainability in this case is about continuously producing capitals at levels that are at least minimally sufficient to meet basic needs. The scoring convention of the other capitals is therefore as follows: > 1.0 signifies sustainable activity; < 1.0 signifies the opposite.

Here it should be clear, we hope, that CBS is firmly grounded in a capital- and context-based theory of performance. When applied to performance in all of

its dimensions, therefore (i.e., in a full Triple Bottom Line fashion), economic performance, too, is determined from a sustainability perspective. After all, economic performance is a function of what an organisation's impacts on capital are, the only difference being that the types of capital involved are financial and economic.

The CBS approach described herein has recently undergone a fairly significant evolution into a full-fledged integrated measurement and reporting system known as the Multi Capital Scorecard™ (MCS).[22] The MCS is the world's first and only capital- and context-based integrated measurement and reporting system.

> Consider Context a kind of reality check of business models that continue to create positive value, but which may or may not be doing so within a safe and just operating space

Thus, unlike prior iterations of CBS, the MCS now fully incorporates economic performance with duties for financial returns to shareholders taken account of, and also provides a completely new set of standardized reporting formats. The MCS is available on an open-source basis for end-user applications.

4a. Report performance

For organisations interested in making external disclosures of their performance, the results of measurements taken in step 4 of the CSM Cycle can also be reported in step 4. Context-based reporting, however, is still rare in practice despite the fact that the Global Reporting Initiative (GRI) has been calling for it for well over a decade now. The same is true for capital-based reporting, notwithstanding the fact that sustainability performance is clearly about impacts on vital capitals above all else.

Still, for organisations that take sustainability seriously and who therefore choose to measure, manage and report their performance in capital- and context-based ways, there is no better way to do so, we believe, than to embrace CBS and to disclose performance, when it comes to reporting, in a context-based fashion. Those that do can legitimately lay claim to fully adhering to the Sustainability Context Principle in GRI's Guidelines, and now also to the capital-based Framework for integrated reporting put forward by the International Integrated Reporting Council (IIRC) as a standard in late 2013.

5. Plan strategies and interventions

Once gaps, if any, have been found between an organisation's actual impacts on vital capitals and the corresponding standards for such impacts defined in step 3 of the Cycle, management strategies and interventions intended to close them must be devised. Other than calling for such strategies and interventions to close gaps, CBS is largely agnostic on the question of which ones to use and how. There are no preconceived notions here. This is the management side of CSM, the door to which for creativity and innovation should always be open. What CBS contributes to the mix is the idea that performance must be judged relative to the carrying capacities of vital capitals and that there are sustainability thresholds involved. Whether or not a strategy or intervention is successful should be held to this criterion, no more no less.

6. Implement strategies and interventions

The 6th and final step of the CSM Cycle is the implementation of strategies and interventions devised in step 5. This may be the longest running step and also the least predictable one. Most important is the fact that it is by definition the step intended to close gaps, if any, in the sustainability performance of organisations. It is therefore crucial that it be followed by a return to step 4 in order to determine whether or not the actions taken have, in fact, had their intended effects.

It should be clear, then, that steps 4, 5 and 6 of the CSM Cycle comprise a loop that can be thought of as the Operational Cycle, the day-to-day operations of the Corporate Sustainability Management function. We reveal gaps; take steps to close them; and then measure again to see how well we did. Steps 1, 2 and 3, by contrast, comprise what we call the Policy Cycle, which largely sets the stage for the performance measurement, management and reporting. On a periodic basis, organisations should take care to revisit policy decisions, as the makeup of stakeholders and the duties and obligations owed to them are liable to change.

Drivers and Challenges

The business case for employing Sustainability Context flips the traditional equation on its head—while most business initiatives must justify their return on investment, CBS turns the tables by holding businesses accountable to sustainability standards and thresholds for what their social and environmental impacts would have to be in order to be sustainable. Consider Context a kind of reality check of business models that continue to create

positive value, but which may or may not be doing so within a safe and just operating space.

Emerging standards are steering markets in this direction, best articulated in the IIRC Value Creation Background Paper:

"Ultimately value is to be interpreted by reference to thresholds and parameters established through stakeholder engagement and evidence about the carrying capacity and limits of resources on which stakeholders and companies rely for wellbeing and profit, as well as evidence about societal expectations... *The challenges will be to reach agreement at corporate, national and international level on what those thresholds and limits are, how the resources within those limits should be allocated, and what action is needed to keep activity within those limits so that value can continue to be created over time*"(Emphasis added).[23]

In other words, IIRC is calling for mechanisms to determine thresholds and allocations that can be applied market-wide, relieving the burden of individual companies having to conduct the research necessary to make such determinations, and thereby "levelling the playing field" through consistent and standardised mechanisms.

Initiatives that assess and establish threshold- and allocation-setting methods are emerging, thereby advancing context-based consciousness and action across the marketplace. For example, a consortium of top non-governmental organisations (CDP, WRI, WWF, and UNGC) collaborated to launch the *Science-Based Targetsinitiative* in 2014 to create guidance for companies to set science-based targets for GHG reductions. The overarching initiative assesses existing methodologies, such as those from CSO, BT, and Autodesk, while also devising a sector-based methodology that allocates emissions reductions according to physical attributes per sector (e.g., by units of production).[24]

This initiative builds on earlier work such as the CDP-WWF-McKinsey *3% Solution* report, which ties carbon reduction to profit opportunities and the Climate Counts *Carbon Score* report, which documents decoupling of carbon contraction from financial growth.[25] These reports point to the economic and financial implications of what former GRI COO Ralph Thurm calls the "Sustainability Context Gap,"[26] highlighting the systemic risks of a widening gap as well as the market opportunities for companies that proactively close the gap across their value chains. Capital markets are starting to recognise company-level implications of global ecological thresholds, too.[27]

Investors are starting to call for reporting that links company-level impacts to the broader context across all areas of impact (carbon and beyond). Investors surveyed in the Ceres-led Investor Initiative for Sustainable Exchanges (IISE) for its Listing Standards Proposal expressed a significant desire for "a more explicit connection between company activities and sustainability impacts to the broader marketplace (externalities and systemic risk)."

However, companies are generally not providing this connection in their reporting—nor even in their strategic and operational planning. In his 2014 book *The Big Pivot*, Andrew Winston called for "Big, Science-Based Goals," a need underlined by research for the related PivotGoals.com website that found less than 10 per cent of the 1,621 sustainability goals surveyed (amongst Fortune 200 companies) to be "science-equivalent," and "only a few specifically science-based."[28]

Why this disconnect? In large part, because the traditional drivers of practice—for example, ratings, frameworks, and standards—aren't driving practice in this (arguably necessary) direction.

This may change in the future, as the Global Initiative for Sustainability Ratings (GISR)—which takes a multiple capitals approach—includes Sustainability Context as one of its 12 Principles, explicitly calling on raters to embed Context into their ratings.[29]

A handful of emerging initiatives and frameworks specifically take Context-Based approaches. The Future-Fit Business Benchmark, the ThriveAbility Foundation, and the MultiCapital Scorecard (earlier mentioned) are creating frameworks to assess business-level impacts through a context-based lens for back-casting from a truly sustainable and flourishing future to identify current systems conditions that respect the global ecological thresholds documented by the Planetary Boundaries research from the Stockholm Resilience Centre (SRC), the Thresholds Database from the Resilience Alliance, the Global Footprint Network, the UNEP GEO-5 reports, among others.[30] The World Business Council for Sustainable Development (WBCSD) is partnering with SRC to embed the Planetary Boundaries in its Action 2020 and Vision 2050 initiatives, but it acknowledges challenges around translating the science on thresholds into company-level allocations and business-ready applications.[31]

Role of Research

As most companies have not yet even mastered the ability to fully measure and report their own

sustainability data, contextualisation could be a tough proposition in the absence of adequate standards and tools.

In the case of some performance aspects, such as liveable wages, as the responsibility belongs exclusively to an organisation and it would be easy to find estimates of wages needed to be in order to be sustainable across geographies, the organisation' sperformance can more easily be assessed in the context of such standards. However, in case of others, especially environmental impacts, for example water use, the responsibility for ensuring the health and viability of the resources involved is a shared one. The responsibility needs to be allocated to the individual parties involved in a fair and proportionate way.

> What we seek is research and development around what these should be for organisational impacts in different social and environmental areas of concern

McElroy and Baue[32] devised a context-based water metric that starts by quantifying the volume of available renewable supplies in a watershed using data from a number of scientific sources. We use Geographical Information System (GIS) tools to do this. After allowing for loss of water due to non-human functions, we can allocate the remaining supplies to human use. We have been using two ways of doing this. The first way is to allocate available renewable supplies on a per capita basis according to the population size of a watershed. We then allocate a share of available renewable supplies to the organisation according to its per capita equivalent size relative to the size of the watershed population in which it is embedded.

The second way to handle allocations in cases like water is to do so on an economic basis (McElroy, 2012a[33]). In that case, the mechanism we use is "contribution to GDP", going through the same initial steps as the per capita method (i.e., we account for environmental loss, make assignments to non-human functions, etc.), but handle the final step differently. First, we allocate to the general population on the basis of generally accepted norms for what a sufficient daily supply of water is per person; we then allocate the remaining balance, if any, to entities that contribute to GDP. The allocations assigned to individual organisations, then, are made according to the proportionate size of their contributions to GDP.

The challenge is that virtually no concerted research or coordination has been done to establish the norms, standards, or thresholds that are so important to CBS. What we seek is research and development around what these should be for organisational impacts in different social and environmental areas of concern. We need sufficiently researched, developed, and vetted standards of performance that have at least survived criticism better than their competitors, and which can be used as credible starting points for organisations interested in applying context-based sustainability. This research agenda may fit well within the academic community, particularly in the area of social and environmental accounting. In some cases, this will consist of specific guidance, such as updated tables of liveable wage standards for different parts of the world. In other cases, it will consist of procedural guidance for how to establish local standards that are utterly non-universal, but which should still be determined according to a standardised or common method.

Likewise, the question of allocation methods stands to benefit from academic research and development. For example, the existing economic-based allocation methodology relies on GDP measures to determine proportionate shares, but it may be possible that some of the alternatives to GDP (as indicators of human well-being) are just as usable, and even preferable, in allocating rights and responsibilities in ways that are more closely aligned with true value creation—such as the Genuine Progress Indicator (GPI) (Costanza, 2009).

Relevance for India: Need for a supporting data-enabled environment

In India, an increasing number of companies is publishing sustainability reports. The quality of disclosure, however, has unsurprisingly not allowed for performance comparability, which is a challenge, both temporally and across peers and competitors. Under the broader-based GRI reporting standard, companies tend to adopt a discretionary approach, with many selecting boundaries and reporting on indicators based more on convenience than materiality. At the same time, there are several voluntary initiatives with a number of companies supporting the cause of better measurability in areas such as carbon and water.

One important step was Holcim's Indian subsidiary Ambuja Cements publishing the first social and environmental P&L (profit and loss) analysis[34] in 2014 using KPMG's True Value methodology. This approach is puts a price on externalities, which are the impacts of an organisation's activities in the

world expressed in terms of positive and negative valuations. Given that this is mainly about expression of non-financial impacts in monetised terms, it relates to the goal of assessing such impacts relative to their effects on shareholder value—economic capital. While this is a welcome step towards measuring the triple bottom line, CBS goes further by assessing how such impacts compare to organisation-specific sustainability standards of performance[a].

Another relevant development is the voluntary India GHG programme launched in 2013 by WRI in collaboration with The Energy and Resources Institute (TERI) and Confederation of Indian Industry (CII). More than 20 Indian companies joined as founding members of this platform, which is focused on developing an internationally consistent and locally relevant GHG measurement and accounting framework based on the GHG Protocol. Significantly, at the global level, WRI is collaborating with CDP for supporting the next steps for the GHG Protocol to develop guidance on science-based GHG reduction targets. The programme's India ambit includes data analytics and benchmarking.

The 2014 assessment[35] by the Carbon Disclosure Project (CDP) and Accenture based on responses from 59 companies among top 200 Indian companies by market capitalisation, shows that Indian companies have embarked upon their journey towards a low carbon economy. The report finds that 50 per cent of the reporting firms have demonstrated it is possible to decouple business growth from carbon emissions. It further highlights that

"More than 90 per cent of the companies state that climate change opportunities are driven by change in regulation. The Perform, Achieve and Trade (PAT) scheme[b], based on market mechanisms, has had a catalysing impact on the companies. However, a more robust and enabling regulatory environment will be required to accelerate the transition to a low-carbon economy[36]."

The India Water Tool[37] launched in 2013 is another voluntary initiative. This is a WBCSD country customisation of the Global Water Tool, developed by a working group of 14 companies[39] based in India. The tool is aimed to help companies see which sites should be high priority for detailed analysis for developing water risk-management plans in such locations. CBS would require further work to allocate water resources to individual facilities as a basis for measuring if they are using water sustainably. Already-existing context-based water tools, such as the Corporate Water Gauge, may be appropriate for this[39].

Data for the India Water Tool was collated with help from the Central Groundwater Board of India and Ramsar Convention on Wetlands. However, as the initiative acknowledges:

"Ground water data gives only a partial understanding of the water situation at each site, however, given the high dependence on ground water by users in India, it is a useful proxy to assess water risks... Future versions will include additional data sets including rainfall, surface water and water scarcity *as they are made available*." (Emphasis added)

Over the past few years, Indian policymakers and regulators have sought to encourage companies to consider sustainability as a core business approach through normative and mandatory instruments.

The 2011 National Voluntary Guidelines on Social, Environmental and Economic Responsibilities of Business (NVGs) issued by the Union Ministry of Corporate Affairs (MCA) form a comprehensive set of nine principles, associated indicators and core elements of responsible conduct and offer guidance on implementing the NVGs through leadership, integration, engagement and reporting. The Securities and Exchange Board of India (SEBI) requires the top 100 listed companies to include Business Responsibility Reporting (BRR) within their annual

[a] In the P&L approach, a company monetises the value of its impacts on society, the economy or the environment, without necessarily taking sustainability standards of performance into account. In the CBS approach, an organisation first determines what its social, economic and environmental impacts must be in order to be sustainable and then measures and assesses its impacts in those terms accordingly; very often without monetising them at all. Such normative impacts may include the fulfilment of duties or obligations owed to communities in order to compensate for the adverse impacts of a company's operations where appropriate. It is evident that even the new CSR law in India setting a spending norm of 2 per cent of profits may increase social spending in the country per se, but may or may not fully satisfy duties or obligations owed to communities. The latter must first be defined in non-monetary terms, after which the sufficiency of monetary contributions of organisations to communities can be better assessed.

[b] The PAT scheme was one of the measures associated with India's National Action Plan on Climate Change (NAPCC), which is, in turn, related to the country's target of reducing its emissions intensity by 20-25 per cent by 2020 from a 2005 baseline. PAT involves tradable energy saving certificates (ESCerts)—to enhance energy efficiency in 'designated consumers' that are large energy-intensive industries and facilities.

reports in a format derived from NVGs. An analysis of the first round of BRRs indicates, on average, room for improvement in disclosure and work is underway to build capacities for eliciting better quality data. Sector-specific guidelines are also being developed. The Institute for Cost Accountants of India (ICAI) has also initiated a project to assess how it can apply IIRC's framework of integrated reporting to Indian companies.

This period of transition is an appropriate time to initiate conversations on context-based sustainability. One of the fundamental issues for this is availability of consistent data, benchmarks and standards in order for carrying capacities and allocations to be estimated.

Clearly ESG disclosure in India is driven to a large extent by regulation by a range of authorities that set norms and mandate reporting on specific metrics such as for water, air emissions, waste, energy and labour. As an annexure to the NVGs, MCA introduced a basic matrix that shows the link between various environmental and social laws prevalent in India vis-à-vis the nine principles of business responsibility. This appears to be the only integrated policy-driven reference tool of its kind in the public domain in India so far. However, as a recent report capturing the ESG disclosure landscape[39] in a similar matrix that maps legislation incentivising disclosure in the country with further details, reflects:

> Since the concept of CBS is equally applicable for social and environmental indicators, it is quite relevant for governments' efforts in encouraging business to disclose and manage its footprint in their countries

"The distinct drawback with reporting to regulators is the distributed formats and physical location of reporting; data aggregation and digitisation stands to improve accessibility to a vast wealth of ESG-related data previously lost in the various mechanisms of the Indian bureaucracy. While work has been done in this area to identify the regulatory overlaps, more substantive efforts are needed to begin building infrastructure linking data at the institutional level (e.g., a web portal solution which facilitates inter-Ministerial ESG data aggregation—mining data from public record compliance reporting)."

With global investor anticipations about India's growth story reviving, the overall sustainability of its development path cannot be over-emphasised. As TN Ninan comments in an editorial[41] on the 2014 Human Development Report of the UNDP:

"Two factors are particularly worrisome, and both relate to the environment. One is that India suffers from natural resource depletion at a rate that equals 4.9 per cent of gross national income-which must be placed against annual GDP growth in the last three years of 5.3 per cent. It does not help that the figure for China is 6.1 per cent, and that the average for Medium category countries is 7.7 per cent. Also a matter of concern is the picture on water. India draws 33.9 per cent of its renewal water resources each year, compared to a Medium category average of 13.9 per cent, and China's figure of 19.5 per cent. It should be clear that growth achieved while doing damage to the environment is not sustainable. If one factors in… that the people who suffer the most on account of environmental damage are the poor, then it should be clear that a growth process that is environmentally harmful is also anti-poor."

Since the concept of CBS is equally applicable for social and environmental indicators, it is quite relevant for governments' efforts in encouraging business to disclose and manage its footprint in their countries. Regulatory requirements that incorporate standards/norms could make a good starting point for assessing specific aspects of a company's sustainability performance.

Easier access to consistent and comparable data sets for social and ecological indicators (that may also be linked to national policy goal-setting) would further create an enabling environment for companies to better assess material issues, create suitable strategies and targets and monitor and report on the same. Governments could support voluntary initiatives that are developing industry/sector benchmarks or tools, including by strengthening policy/regulatory measures to elicit more and better data. For example, the European Commission has sponsored research on environmental sustainability thresholds and indicators that has sought to support EU policy efforts by making practical progress on a few selected key thresholds of interest, identifying and testing ways in which thresholds could be defined in quantitative terms and monitored effectively through indicators.[42] This aligns with efforts mentioned earlier around identifying thresholds; what remains to be done is to translate these thresholds into business-ready applications—specifically, by expressing thresholds in ways that lend themselves to allocation to the company level.

All this calls for a greater role of multi-stakeholder platforms that facilitate and increase engagement among business, research institutions and government agencies for understanding the need for science-based approaches and consistent data sets at local, sub-regional (for example river basins), sectoral and national levels. The new UN Sustainable Development Indicators[43], which are intended to track progress in achievements of related goals at local, national, regional, and global levels, are expected to catalyse better data capture by national statistical systems. The indicators are expected to serve as a tool for countries to devise implementation strategies and allocate resources.

Conclusion and Recommendations

This paper documents that, despite significant delays and roadblocks, Context-Based Sustainability is now mainstreaming, with an arc of inevitability bending in its favour. That said, the rate and scope of adoption still places at risk the vital capital resources at the heart of CBS—and at the heart of business viability. Given that most sustainability challenges are common—shared widely across industries, sectors and economies—it makes sense that solutions will arise best from robust collaboration.

Below are a set of recommendations that flow from the points made above:

- Global multilateral organisations (e.g. UN bodies such as UNEP and UNDP) should collaborate to create a global governance body of scientists, business practitioners, academics, and stakeholders to provide guidance on methodologies for determining ecological and social thresholds, as well as guidance on approaches to allocations, all of which are broadly applicable to the business level.
- Provide support and funding to independent frameworks and raters to develop mechanisms to apply Context-based assessments of corporate sustainability performance based on publicly available data routinely disclosed in sustainability reports.
- Engage with reporting standards/guidance bodies such as GRI, IIRC, SASB, CDP etc. to encourage more explicit integration of Sustainability Context into their frameworks, for example by applying the concept of carrying capacities to multiple capitals-based frameworks.
- Educational institutions, particularly in business and management studies, need to embrace a context-based approach to integrating sustainability into their curricula.
- Similarly, academics and scientists need to continue to produce research on best practices for advancing a context-based approach to sustainability, particularly in business.
- Regulators—such as securities and exchange commissions—need to begin to mandate a context-based approach to sustainability.
- Investors should start developing context-based screens to apply to their portfolios, prioritising investment in companies that operate within the carrying capacities of capitals, based on the investment case that non-compliance with thresholds poses both financial as well as social risk.

All this would help shift business from its current status of unsustainability in terms of its collective environmental and social impacts, to a world where sustainable business is defined not only in terms of financial capital, but also in terms of the other capitals—natural, social, human, and manufactured—to create a truly sustainable world.

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5 Special Section: User tools for ESG performance benchmarking

Introduction

This volume has sought to raise issues regarding how ESG reporting can be a tool as well as a driver for risk assessment, transparency & behaviour change. Reporting companies use one or more reporting standards such as GRI, UNGC, or now in India—the BRR, among several others in practice across the world. This brings into the public domain a substantive amount of ESG performance data from a growing number of reporting companies. However for such data to become meaningful, users ranging from civil society stakeholders to regulators to the investing community should be able to compare companies' performance. This calls for standardised and consistent tools of measurement. Such assessments also help companies understand better where they stand vis-à-vis peers and competitors and eventually can drive companies to improve their performance and set higher goals for themselves.

As Rathi and Miller in their article in this volume say, "An important tool for enhancing the effectiveness of a voluntary sustainability reporting initiative is the creation of a related sustainability index. Such indices typically highlight top performers, allowing public pressure and competiveness between firms to drive disclosure and ultimately performance… In Brazil, for example, the BM&FBOVESPA stock exchange launched its carbon efficient index in 2010 which, within 24 months of its launch, led to a 44 per cent increase in the number of companies that are voluntarily reporting emissions data."

Just as there are a multitude of sustainability-related standards or metrics globally, such as UN PRI (Principles of Responsible Investment), GRI, UN Global Compact, SASB (Sustainability Accounting Standards Board), the Forest Stewardship Council, and the SA8000 standard—there is also a very wide range of benchmarking/rating/ranking tools and indices are available. These include tools covering the full range of sustainability issues as well as specific theme-based ones, such as water, climate and governance. The former includes FTSE4Good, Dow Jones Sustainability Index (DJSI), and Oekem. An example of the latter type is the Carbon Disclosure Project (CDP). Providers of such tools include sustainable investment and research firms, multi-stakeholder groups as well as stock exchanges. Ratings provide unbiased perspectives on how a company is performing in comparison to a historical trajectory and in relation to peers within a specific country and industry sector. A sustainability index also offers objective benchmarks to investors for managing their investment portfolios. Equity fund managers can take advantage of the research embedded in these indices and deploy appropriate strategies to select companies from the investment universe set by them.

Since for users of ratings it can be challenging to decide which rating to depend on, at there are a few global initiatives to address this concern. One is the Rate the Raters research by leading consultancy, SustainAbility with GlobeScan. Their periodic surveys of sustainability experts about key sustainability ratings, rankings and indices show that DJSI, FTSE4Good, oekom corporate ratings and CDP are among the five most credible ratings, where the key drivers of credibility are a positive impact on corporate sustainability performance and a focus on the right issues. Further, the Global Initiative for Sustainability Ratings (GISR), launched in mid-2011, is intended to play the role of an independent, non-commercial body that will accredit sustainability ratings/rankings/indices. GISR is working to build a standard that outlines the core principles, issues, and indicators through a collaborative development process.

India has some participation and awareness of several of these global metrics and ratings including GRI, UN Global Compact and CDP, while DJSI has included a few leading Indian companies such as Mahindra, Wipro and TCS.

India, however, is developing its own set of standards and tools in alignment with the best global practices. SEBI's Business Responsibility Reporting (BRR) is based on the National Voluntary Guidelines on Social, Environmental and Economic Responsibilities of Business (NVGs). The BRR cycle is entering the third year now. Several sustainability expert and stakeholder organisations are analysing data reported through GRI, CDP and BRR formats and sector-based benchmarks are being developed. The BSE (Bombay Stock Exchange) has provided sustainability indices focused on climate issues. An India-focused Business Responsibility index based on the nine principles of the NVGs is being developed by the National Foundation for India (NFI), a national philanthropic organisation based in Delhi. This index will assess the performance of top 100 listed companies across the NVG principles, which cover governance and ethics, well-being of employees, community (including CSR) and consumers, human rights, stakeholder engagement, environmental footprint and policy advocacy/lobbying by businesses. An advisory committee of experts has been constituted for index development, drawing from various similar good practices. The index is expected to further strengthen the debate around business responsibility, encourage transparency in business disclosure and encourage involvement of top leadership in responsible business practices.

This special section highlights some relevant existing tools—India ESG Invest by cKinetics, Sustainable Plus by CII (Confederation of Indian Industries), the BSE CARBONEX and BSE GREENEX.

ESG India Invest: A tool for Responsible Investors

With the overall objective of increasing the adoption of responsible finance practices in India, the India Responsible Investment Working Group, under the aegis of the Sustainable Business Leadership Forum, has developed ESG India Invest—a tool to enable Indian companies and investors investing in India to analyse, compare and assess their own and (potential) investees' ESG disclosure, vis-à-vis their competitors and peers across 15 parameters and more than 70 metrics.

The tool simultaneously addresses the problems of data assessment, comparability and actionability for investors, allowing them to answer the following questions:

- How complete and comprehensive is the ESG disclosure of businesses (existing and potential investments) in India?
- Where does a particular company rank vis-à-vis its peers on ESG disclosure in consistently providing satisfactory amount of material ESG information over time?
- What key material indicators are not being addressed by the companies?
- What are the disclosure highlights over the reporting year on ESG related issues?
- What are the outstanding metrics in which the company has been able to meet benchmark levels of material disclosure?

ESG India Invest is a tool to enable Indian companies (and investor analysts) to analyse, compare and assess ESG disclosure.

Metrics compared: 70

Areas covered

- Disclosure and labelling
- Board structure and independence
- Policies, Standards, Codes of Conduct
- Communications and engagement
- Marketing and ethical advertising
- Child and forced labour
- Employees wellness and training
- Customer satisfaction
- Regulatory and legal challenges
- Labour relations and union practices
- Supply chain standards and selection
- Product life cycle use impact
- Biodiversity impact
- Climate change risk
- Energy management
- GHG Emissions and air pollution
- Waste management and effluents
- Community development
- Lobbying and political contributions

Use of Benchmarks to Evaluate Businesses

The tool has been fed with metric wise and parameter wise benchmarks based on disclosure performance of the chosen set of companies. These benchmarks are intended to provide the baseline and act as reference point to enable assessment of the risks and opportunities presented from the ESG disclosure of the companies being evaluated.

ESG Invest: Classifying disclosure into risk and opportunities

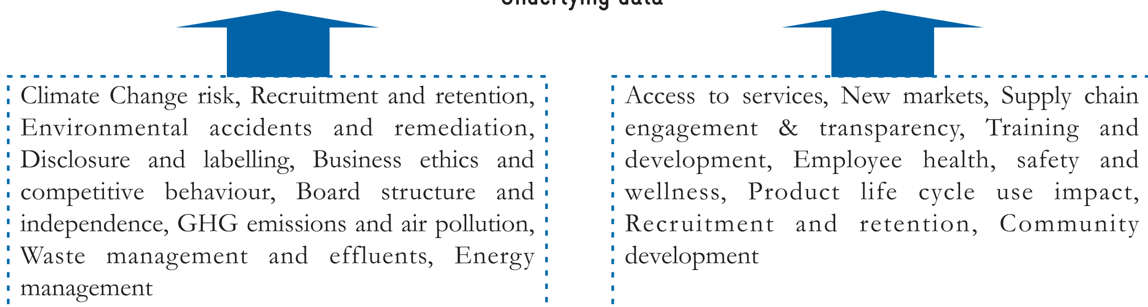
Risks

- Legal Risk
- Reputational Risk
- Operational Risk

Opportunities

- Operational Efficiency
- Product Innovation and Differentiation
- Accessing New Markets
- Building Reputational Capital

Underlying data



Methodology for Developing Benchmarks

Companies in focus include top 100 listed businesses (for whom disclosure is mandatory). The process for formulating sectoral benchmarks includes:

Step 1: Collect ESG information of companies through the following sources:

- Annual company disclosure (annual reports and sustainability reports)
- Collection of news on all ESG issues
- Communication by the company on ESG issues
- Company filings with SEBI

Step 2: Identify the materiality of the different metrics (on which data is collected) for the different sectors

Step 3: Score ESG disclosure based on its quality. The quality of disclosure has been quantified based on the extent to which the information can be used to compare the information.

The ESG benchmarking Scoring metric ranges from 0 (no data provided) to 1.75 (disclosure of benchmarkable data that allows for comparison over earlier period reports)

Scoring the quality of disclosure		
0.25	Disclosure: no data	Some disclosure on the indicator
0.5	Disclosure: absolute data	Disclosure on the indicator with data related to it (e.g. total energy saved)
0.75	Disclosure: relative data	Disclosure of data that helps assess materiality or relevance of the parameter (e.g. percentage of energy saved)
1	Disclosure: absolute data time	Disclosure on the indicator with data related to it (e.g., total water over consumption: years 2007-2010)
1.25	Disclosure: relative data that is benchmarkable	Disclosure of data that helps compare vis a vis benchmarks (e.g. per employee or unit of production—energy intensity of production)
1.5	Disclosure: relative data time	Disclosure of relative data that allows for comparison over earlier period over reports
1.75	Disclosure: relative data time that is benchmarkable	Disclosure of benchmarkable data that allows for comparison over earlier over period reports

Benchmarks for 2013-14

The first version of the ESG India Invest tool contains benchmarks developed from the disclosure of businesses in 2013-14. Figure 1 depicts the benchmarks for the different parameters across sectors.

Once a user of the tool feeds the ESG information available for the company being evaluated, the benchmarks are used to provide the user with information on how the company ranks vis-à-vis its peers, as also the metrics/parameters where information enhancement is needed through further engagement, as shown in the illustrative outputs in Figures 2 and 3.

Figure 1: Benchmarking parameters across sectors

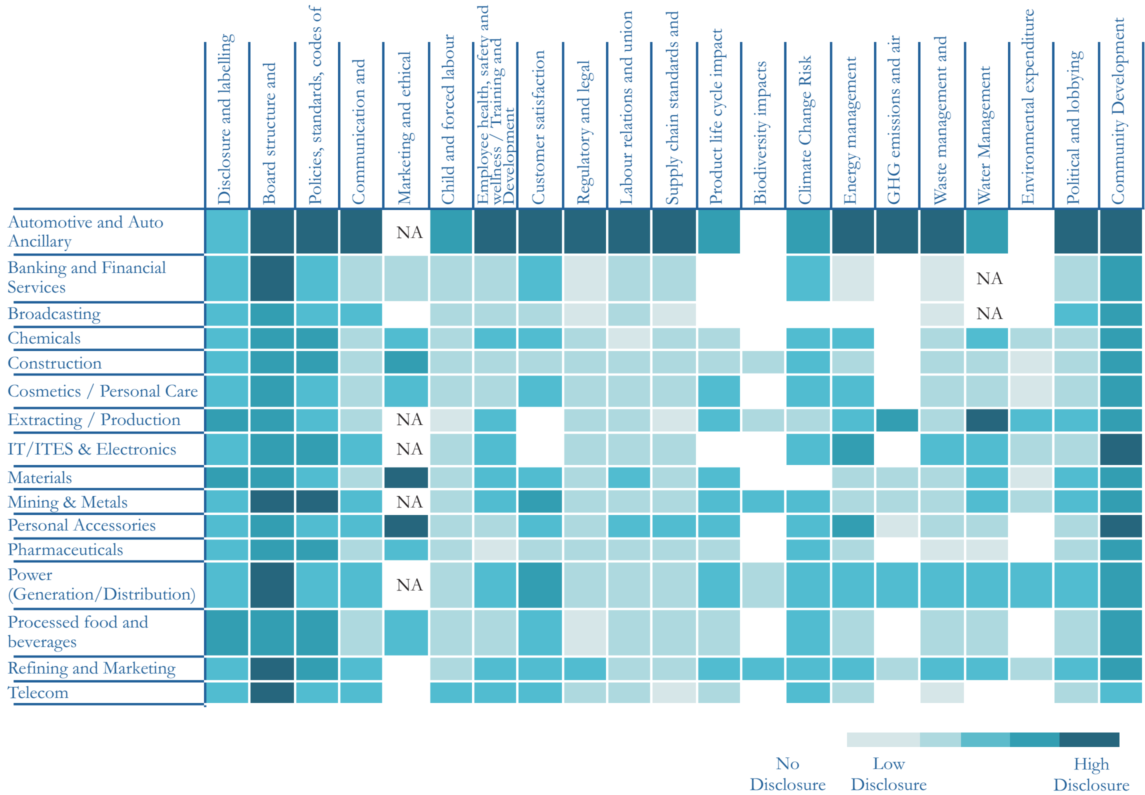
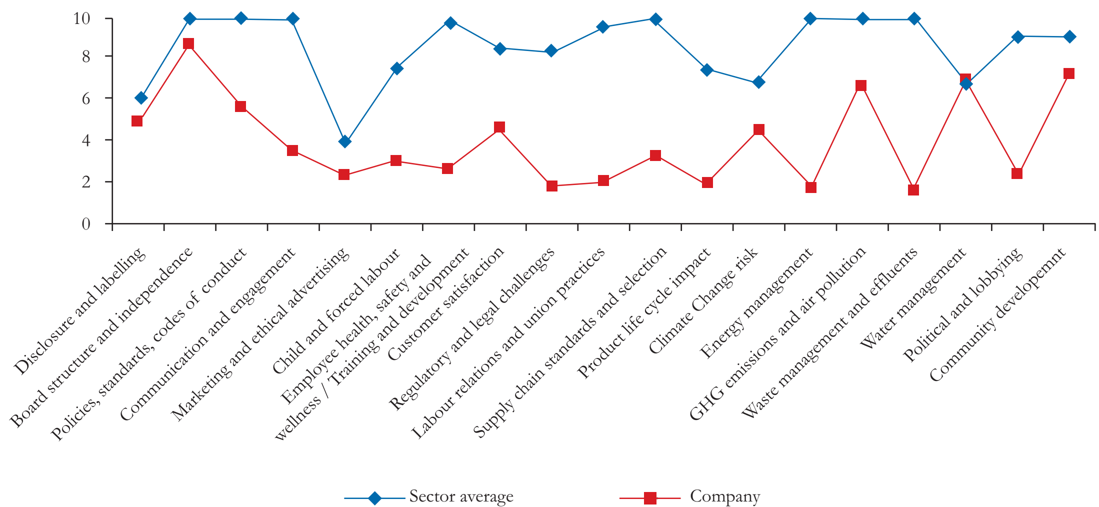


Figure 2: Illustrative Output 1: Comparison vis-à-vis sector and peers



Information on outstanding metrics where more information is needed

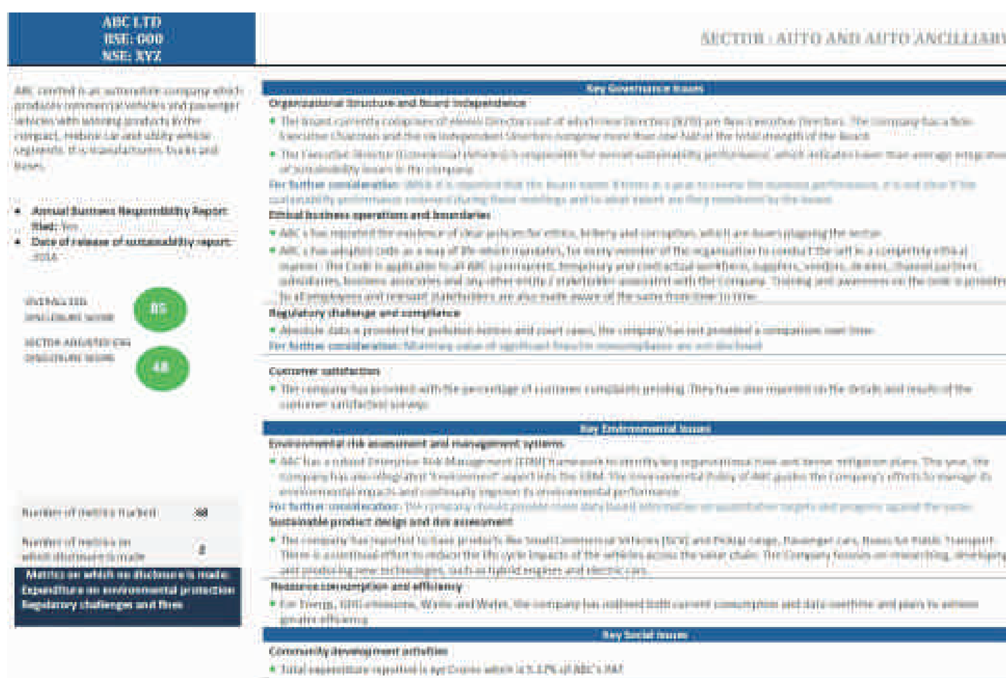
The India Responsible Working Group has also used the benchmarks to compare and contrast the disclosure of top 100 listed businesses to identify how they rank versus their peers and what parameters should investors be engaging with businesses on. The information is captured in the report *ESG Score of India Inc: 2014*[1].

- What are the key material indicators (currently not being addressed by the company in question) the investor should look to address in their engagement with their businesses?

Roadmap

The working group is developing ESG Benchmarking tool version 2.0 with enhancements based on user needs. The new version is being designed to indicate

Figure 3: Illustrative Output 2



Application of the tool

Businesses can use the tool to evaluate how their ESG actions are seen by investors and the public. It also offers them a comparison of their disclosure relative to their peer group. For businesses developing their strategy for investor relations and stakeholder engagement the tool (updated annually) can give them a direction.

Investors have been viewing ESG disclosure for identifying risks as well as a proxy for management quality. ESG Invest is meant to enable investors to increase integration of ESG indicators into their decision making processes. Two key take-away points from the tool are:

- Where does a particular company rank vis-à-vis its peers in providing satisfactory amount of information on material ESG information (which has an implication on risks and opportunities) which is consistent over time?

quantified impacts. This is now possible, given the increase in ESG disclosures by Indian companies with data that can be benchmarked and possibly mapped with financial performance. Over 2015, the group plans to host investor analyst discussions to provide feedback into the enhancements required. The aim is to better understand risk, revenue and expense impact. Monetising environmental, social and governance impacts of a business can help assess its true value.

The latest version of the India-ESG Invest Tool can be accessed at http://www.ckinetics.com/ESG/India_ESG_Invest 2014v12.xlsm

More information is at http://SBLF.Sustainability Outlook.in/about-the-forum/sustainability-disclosure-and-reporting

[1] ESG Score of India Inc: 2014 can be accessed at http://www.ckinetics.com/ESG/Annual%20ESG%20Benchmarking%20report%202014.pdf

Sustainable Plus

Sustainable Plus has been developed by leading industry association, the Confederation of Indian Industries, CII. It is a corporate sustainability label that acts as a brand identity tool for companies to communicate that they are sustainable, responsible and well-governed. The label, launched in 2012, is an innovation of CII-ITC Centre of Excellence for Sustainable Development[2]. This recognition product was conceptualised at a time when the thrust on sustainability reporting and disclosures had been increasing but there was a lack of effective communication tool for companies to link sustainability to their brand. As an initiative of a business association that is juxtaposed between the industry, government and civil society to charter change, Sustainable Plus is a tool for business to engage with consumers and investors and communicate about its sustainability performance. It is also a potential driver for improving sustainable performance of its members and enabling them to become more competitive.

Annually, the top five companies across 20 sectors (as per BSE market capitalisation) are selected to be analysed voluntarily by CII. Hence, Sustainable Plus provides readily available information about sustainability performance of 100 companies with a combined market capitalisation of USD 800 billion or INR 51.2 trillion. Several companies including ITC, Mahindra and Mahindra, Maruti Suzuki, Siemens, Tata Chemicals, Tata Power and Wipro are already using Sustainable Plus on their websites and reports to communicate their sustainability performance.

Methodology

Around 450 ESG indicators are used to assess a company and different weightages are assigned to these indicators based on whether they are general or industry-specific across environment, social and governance dimensions. Their weights add up to a score out of 100 which correspond to three different levels i.e. Sustainable Plus Platinum, Sustainable Plus Gold, and Sustainable Plus Bronze.

The ESG indicators used for the analysis have been developed by CII after scanning several global indicators, principles and external standards in this space and selecting the most appropriate ones depending on their materiality for respective sectors. The label also integrates GRI and CDP indicators[3].

Some of the key aspects that the indicators cover are: Corporate governance; business ethics; risk management; tax strategy; transparency and disclosure; employee development; stakeholder engagement; human rights; health & safety; corporate social responsibility; supply chain; product responsibility; biodiversity; and environmental management.

Innovation, responsiveness of the company to risks and its future plans are also considered to project the risk outlook. The scoring is based not just on disclosures but also on performance. Hence while some indicators assess enabling factors such as policies in place across specific ESG aspects, they are also assessed on results achieved through such policies.

The analysis is done through an online tool which also has a public interface to create transparency wherein consumers, investors and other stakeholders can access readily available information pertaining to sustainability performance of the companies across the following sectors:

- Agriculture
- Capital Goods
- Chemical and Petrochemical
- Consumer Durables
- Diversified
- Finance
- FMCG
- Healthcare
- Housing related
- Information Technology
- Media and Publishing
- Metal, Metal Products and Mining
- Miscellaneous
- Oil and Gas
- Power
- Telecom
- Textile
- Tourism
- Transport Equipment
- Transport Services

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[2] CESD has been a Network Supporter for UN Principles for Responsible Investment since 2014.

[3] GRI and CDP are partners in integrating their indicators with the indicators for Sustainable Plus.

Evaluation process

- A communication is sent to selected company CEOs and relevant sustainability contact persons at the beginning of the process
- After this, analysts who are trained experts in this field analyse publicly available information based on the ESG indicators
- They also analyse media information in order that relevant questions can be asked to the companies and linkages drawn to ESG aspects. The media scan forms an essential part of the exercise wherein key issues are highlighted to the company, giving them an opportunity to communicate how they are addressing them, and their response to such issues.
- Responses to the gaps in publicly available information along with questions pertaining to media analysis are then requested from the company
- After the company responds, the information received is reviewed and incorporated in the analysis in order to derive an overall score and thereafter the apprporiate label is assigned
- The label and a summary report on their ESG performance is shared with the companies
- Labels of all 100 companies are disclosed in public domain.

Key Features of the label

- The labelling process is focused on enabling companies to understand their ESG risks, gauge their sustainability performance vis a vis others in their own and other sectors and take action and foster innovation to tackle external exigencies
- Most labels around the world are product-based labels whereas Sustainable Plus assesses the entire company as it is a 'corporate sustainability' label.
- The label gives third party credibility to sustainability initiatives of companies and rewards them with a label that they can use for communicating their sustainability through brand differentiation factors for easy recognition by consumers.
- Robust quality controls are under documentation this year.
- Most of the factors used by Rate the Raters[4] to assess the robustness of rating methodologies are embedded in the label as highlighted above.

[4] Rate the Raters is a project of SustainAbility which aims to understand the universe of sustainability ratings and improve the quality and transparency of such ratings. Sourced from: http://www.sustainability.com/projects/rate-the-raters

S&P BSE CARBONEX

Climate change is expected to have differential impacts on the profit potential of firms listed in India's equity indexes. BSE CARBONEX has been created as a response to identified needs of investors to develop sophisticated approaches to portfolio management that incorporate climate change risk and opportunity. BSE CARBONEX incorporates forward looking criteria that assess the potential future consequences of climate change and economic responses to it. Companies that understand the risks and opportunities, and position themselves well in relation to them, will deliver higher long run returns than those which fail to adapt. As past history and current positioning may not be a reliable guide to future relative performance, the index criteria include and emphasise future risks, opportunities and commitments.

About CARBONEX[5]

The index is based on the S&P BSE 100, with the constituent weights modified in accordance with the companies' relative carbon performance as measured by the level of their greenhouse gas (GHG) emissions and carbon policies. BSE CARBONEX is 'industry neutral'. Overall industry values remain the same as the underlying index but individual constituents may be over or under weighted based on their performance in the assessment process relative to the S&P BSE 100 index. Companies are 'tilted' against their industry level peers, so that broadly comparable companies are being compared with each other. Companies in an industry that achieve the strongest assessment scores are favoured (over-weighted) at the expense of those producing poor results—the latter get under-weighted. Constituents' weights are modified in accordance with the companies' relative carbon performance as measured by the level of their greenhouse gas (GHG) emissions and carbon policies.

S&P Dow Jones Indices has partnered with RobecoSAM[6], a specialist in sustainability investing to provide the Carbon Performance Scores and Industry Tilt Factors. Carbon Performance Scores of Indian companies are calculated by RobecoSAM in the framework of the annual Corporate Sustainability Assessment (CSA)[7] of companies from around the world. Companies in each of the underlying broad market indices are asked to respond to an extensive industry-specific CSA questionnaire. Not all companies choose to respond to the CSA questionnaire. For all companies in the underlying benchmarks that do not respond to the questionnaires, RobecoSAM completes the CSA questionnaire, to the extent possible, based on publically available information only, in order to ensure that certain minimum representativeness requirements are met.

Index Eligibility and Construction[8]

Constituent Weights: Each stock in the index is weighted based on its carbon adjusted float market capitalisation, which is calculated based on the Carbon Performance Scores provided by RobecoSAM.

Stock weight calculations consist of two steps as follows:

1. Carbon Re-Weighting Factors

Carbon Re-Weighting Factors are calculated for all stocks in the S&P BSE 100 using the current year's Industry Tilt Factors and Carbon Performance Scores provided by Robeco SAM. New Carbon Performance Scores are calculated annually in March and are based on the annual CSA figures released in the previous year.

Theme	Weight in the Carbon Performance Score
Strategy & Governance	40%
Reporting & Disclosures	30%
Performance & Achievement	20%
Ecosystem Action	10%

Each of the themes includes between three and ten specific carbon-related indicators. If a company does not have a Carbon Performance Score, its Carbon Re-Weighting Factor is assumed to be 1. Industry Tilt Factors are provided by RobecoSAM and calculated to represent each industry's relative exposure to carbon-related risks and opportunities. They are calculated based on the weights of the carbon-related questions in each overall industry-specific CSA questionnaire. In the course of the CSA process, companies are assigned to one of the 59 industries defined by RobecoSAM. For this, the Global Industry

[5] http://www.bseindia.com/downloads/about/abindices/file/methodology-sp-bse-carbonex.pdf
[6] Founded in 1995, RobecoSAM is headquartered in Zurich and employs approximately 100 staff.
[7] The first CSA was undertaken in 1999, with the launch of the original family of the Dow Jones Sustainability Indices
[8] http://www.bseindia.com/downloads/about/abindices/file/methodology-sp-bse-carbonex.pdf

Classification System (GICS[9]®) is the starting point. At the industry group and sector levels, the RobecoSAM Industries match the standard GICS® classifications. However, some non-standard aggregations are made at the industry level. Companies in industries with greater exposure to carbon-related risks and opportunities receive a higher Industry Tilt Factor and therefore, a higher weight restatement compared to companies in other industries belonging to the same sector.

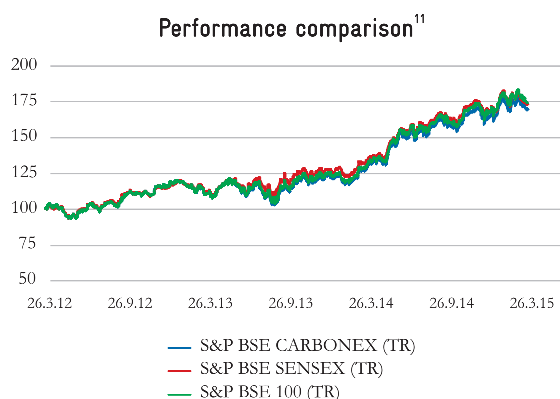
2. Carbon Adjusted Float Weights

Once the Carbon Re-Weighting Factors are determined, the float weights of the stocks are tilted based on their Carbon Re-Weighting Factors. After the float weight tilting, the overall sector exposure is again realigned with that of S&P BSE 100 to arrive at the Carbon Adjusted Float Weight of each constituent stock in the index.

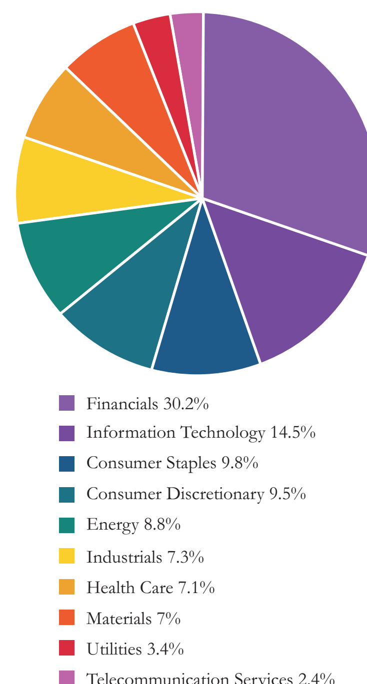
Companies in industries with greater exposure to carbon-related risks and opportunities receive a higher Industry Tilt Factor and therefore, a higher weight restatement compared to companies in other industries belonging to the same sector. After the float weight tilting, the overall sector exposure is again realigned with that of S&P BSE 100 to arrive at the Carbon Adjusted Float Weight of each constituent stock in the index. Stock weights are adjusted at each semi-annual rebalancing to reflect each constituent's Carbon Adjusted Float Weight.

Number of Constituents	100
Launch Date	Nov 30, 2012
Constituent Total Market Cap (Rs Million) as of March 24, 2015[10]	
Maximum Market Capitalisation	5,080,059.00
Minimum Market Capitalisation	41,921.35
Mean Market Capitalisation	704,547.07
Median Market Capitalisation	364,095.66

Performance comparison[11]



Sector composition



Based on GICS Sectors (As on March 24, 2015): The weightings for each sector of the index are rounded to the nearest tenth of a percent; therefore, the aggregate weights for the index may not equal 100 per cent

Top 10 Constituents by Index Weight

Company	Sector (As of March 24, 2015)
HDFC Bank Ltd	Financials
Infosys Ltd	Information Technology
ITC Ltd	Consumer Staples
ICICI Bank Ltd	Financials
Larsen & Toubro Ltd	Industrials
Housing Development Finance Corp	Financials
Reliance Industries Ltd	Energy
Tata Consultancy Services Ltd	Information Technology
State Bank of India	Financials
Tata Motors Ltd	Consumer Discretionary

[9] For more information about GICS®, please refer to the Global Industry Classification Standard (GICS®) Methodology available at www.spdji.com.

[10] http://us.spindices.com/indices/equity/sp-bse-carbonex

[11] http://www.asiaindex.co.in/indices/equity/sp-bse-carbonex

BSE GREENEX

The S&P BSE GREENEX includes the top 25 'green' companies in the S&P BSE 100 with energy efficient practices.

The index was co-developed by BSE Ltd. with gTrade Carbon Ex Ratings Services Private Limited and Indian Institute of Management, Ahmedabad. GREENEX is a step in creating a market based response mechanism in India, whereby both businesses and investors can rely upon purely quantitative and objective performance based signals, to assess "carbon performance". The index is calculated using a modified market-cap-weighted methodology. The maximum weight for each constituent is capped at 6 per cent at each rebalancing.

Number of Constituents	25
Launch Date	Feb 22, 2012
Constituent Total Market Cap (Rs Million) as of March 24, 2015	
Maximum Market Capitalisation	2,612,038.20
Minimum Market Capitalisation	111,981.14
Mean Market Capitalisation	1,010,544.99
Median Market Capitalisation	741,304.36

Index construction

Greenhouse gas (GHG) emission numbers are provided by gTrade Carbon Ex Rating Services Private Limited for the eligible universe (S&P BSE 100). The carbon emissions offset is subject to a maximum limit of two-thirds of the company's total emission. The GHG emission numbers (C), average three month float market capitalisation (M) & average three-month value traded (T), are scaled from 0 to 100 within the sector. Points are assigned to the above mentioned parameters from 1-50 within the sector.

- For C: For 0-2, 1 is assigned; for 2-4, 2 is assigned, etc.
- For M & T: For 0-2, 50 is assigned; for 2-4, 49 is assigned, etc.

The composite point for a company is arrived by taking the summation of the points multiplied by their respective weights, where C is weighted 50%, M is weighted 40%, and T is weighted 10%. Companies are ranked on the basis of composite points. The top 25 companies are selected for the base composition. Constituents are reviewed semi-annually.

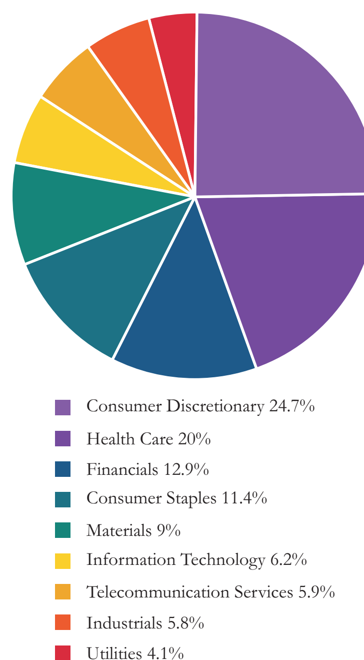
Review and rebalancing

- Mandatory Exclusions: If the existing constituent ranks beyond 35 by final rank, the company is excluded.
- Mandatory Inclusions: If a non-constituent ranks within 15, the company is included.

During rebalancing, companies for which BSE is not able to obtain GHG emission numbers are excluded from the universe. If a company is removed from the S&P BSE 100, it is also removed from the S&P BSE GREENEX Index simultaneously.

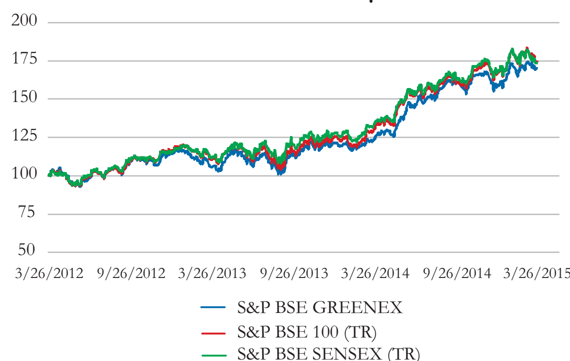
The Index has been back-tested from 1st October, 2008 (Base Date) with the base index value of 1000. It is rebalanced on a bi-annual basis i.e. end of March and September quarters. The September quarter review is based on the fresh set of carbon emission numbers and the March quarter review is based on the existing carbon emission numbers but latest financial data.

Sector composition



Based on GICS Sectors (As on March 24, 2015): The weightings for each sector of the index are rounded to the nearest tenth of a percent; therefore, the aggregate weights for the index may not equal 100 per cent

Performance comparison



Notes

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