ESG and Finance

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Why finance and ESG?

The majority (86%) of ASX200 companies now report annually on material ESG – environmental, social and governance – risks and opportunities[1]. From climate change and sustainability to governance structures and workplace diversity, the ESG focus has moved beyond minimal reporting obligations to be action-focused and a key differentiator for many larger organisations.

Recent changes in the Australian regulatory environment, coupled with greater requirements in many overseas markets and institutional investor interest, mean there is a growing focus for more Australian companies to better report, track and demonstrate progress in addressing identified ESG risks.

The finance function is integral to the ESG discussion, due to the roles of finance in sourcing, costing and allocating capital, risk management and longer-term strategic planning.

Commercial implications for CFOs and finance professionals

In planning and managing the business, ESG-related commercial considerations for CFOs typically include climate change, sustainability and energy supply. Key finance-led impacts focus on the cost of capital, capital allocation, risk, strategic planning, procurement and supply chain.

> A listed entity should disclose whether it has any material exposure to economic, environmental and social sustainability risks and, if it does, how it manages or intends to manage those risks.
>
> ASX Corporate Governance Council Principles & Recommendations (4th Edition). 2019

There is growing investor interest in improved transparency on ESG issues, influencing changes in reporting frameworks. This is generally driven by investors' desire for an improved ability to assess investment risk and to seek ethical and sustainable investments. Additionally, in some industries, the competitive landscape is further shifting due to changes in risk profiles, consumer preferences and/or regulatory changes in overseas markets.

The Human Element

From a human resource perspective, attracting and retaining good talent will continue to be a challenge in coming years. Strong ESG credentials can be a compelling point of difference in the employment market.

Working for organisations with aligned values may be motivating and engaging for many of your staff, with a growing preference among quality candidates to work in organisations that display a strong purpose and values, and transparent approaches to ESG.

> **As leaders, CFO's have no right or option not to lead on ESG and climate change.**
>
> Stephen Moir

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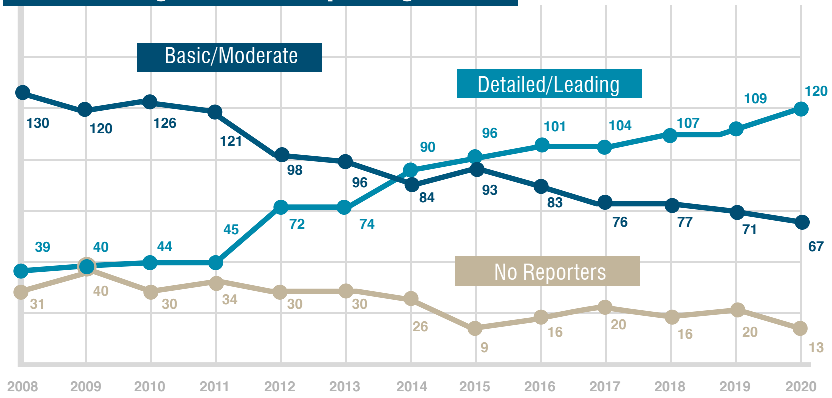
Leading on ESG

The use of an integrated or sustainability report framework is common as is, where relevant, referencing the recommendations of the Financial Stability Board's Task Force on Climate-related Financial Disclosures (TCFD).

In 2021, the Australian Council of Superannuation Investors (ACSI) highlighted improvements in reporting of ESG, with a growing number of ASX200 companies whose reporting was classified as 'detailed or leading'.

ASX200 long-term ESG reporting trends



[1]Source: Australian Council of Superannuation Investors

There is also greater use of selected UN Sustainability Development Goals in reporting, with best practice seen as demonstrating transparency, 'substantive change' and documenting progress on a journey to addressing identified issues.

There is an underlying expectation that thorough auditing will uncover issues, rather than demonstrate excellence across all measures, which may be seen as 'greenwashing'.

ESG Checklist

Leading organisations will consider the following in their ESG strategies and reporting.

Environmental

- Sustainability reporting, adherence to relevant environmental laws, environmental impact management including direct and indirect carbon emissions (Scope 1,2 and 3)
- Water management
- Safety such as incident reporting, safety breaches and fines
- Energy consumption, use of renewables and waste management.
- Environmental criteria may also include deforestation, pollution of air or water, impact on climate change and raw material sourcing.

Social (human capital management)

- Review and audit of work health and safety performance
- Gender equity including gender representation at senior levels and addressing the gender pay gap
- Diversity and inclusion across the entire organisation
- Anti-discrimination
- Board and senior staff remuneration and link to company performance
- Supply chain audit and management (incorporating Modern Slavery Act 2019 reporting).

Governance

- Frameworks, policies and incentives in place to ensure best practice and performance by the company
- Review of corporate conduct and related stakeholder risks due to unethical behaviour
- Risks to brand reputation and brand value
- Specific sector-relevant disclosures such as anti-money laundering or resource extraction impacts.

Reporting will usually include risk to disruption of business and measures taken to reduce climate impact.

Moir Group regularly runs discussion groups and webinars on ESG topics, as part of our support for finance professionals throughout their careers. Don't miss out on our next event by signing up to our events alerts on our website.

[1]ESG Reporting Trends: A detailed assessment of ESG reporting in ASX200 companies. May 2021. Australian Council of Superannuation Investors.