

ESG 101

A Pocket Guide
To ESG
& What It Means
For Your Company



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What ESG is (& what it isn't)

Your company, like every company, impacts and is impacted by the environment.

It operates within a wider society.

It requires governance.

ESG is a philosophy which recognises that your customers, employees, regulators and investors are increasingly looking beyond your company's financial achievements to its performance on environmental, social and governance issues.

Based on your performance on these issues, conclusions are drawn about the value of your products, the quality of your management, your exposure to risks and ability to grasp opportunities, your chances of long-term success, and your attractiveness as an investment.

You may already be addressing environmental, social and governance issues with your philanthropy and corporate social responsibility.

In fact, Trinidad and Tobago companies are among the world's most generous, giving 2-4 percent of their profits to good causes.

Your philanthropy and CSR, however, are cash-flow-negative and not appreciated by many investors.

ESG, on the other hand, treats ‘doing good’ and ‘good business practice’ as the foundation for new lines or models of business.

ESG helps your company identify its strengths and weaknesses, which makes it better at leveraging opportunities and at mitigating business and reputational risks.

ESG provides opportunities for partnership and progressive improvement.

ESG demands quantifiable returns, making you more attractive to investors.

In this way, ESG = Doing Good + Making Profit.

**Why you should
embrace ESG**

ESG's rise is driven by increased societal concern over the negative impacts of companies.

This, in turn, is leading to new laws and taxes to deter unsustainable business models.

For example, stricter regulations are coming to help Trinidad and Tobago reduce its greenhouse gas emissions by 15 percent by 2030, so the country can meet its commitments under the Paris Agreement.

Still, most of the companies that have embraced ESG say they did it for business opportunities, competitive advantages, and to safeguard their long-term success (Figure 1).

For instance, ESG is understanding that when you continue to rely on energy-hungry equipment, or on increasingly scarce and expensive resources, you drain cash that could be invested elsewhere, and you put the continuity of your business at risk.

ESG is knowing that, while improving your operations can be costly, delaying change is more expensive in the long run.

ESG is providing the assurance that your company poses no significant social or environmental threats, is resilient to risks, and is sufficiently agile and strategic to exploit new opportunities.

ESG-aligned companies enjoy improved credit ratings and are more attractive to investors.

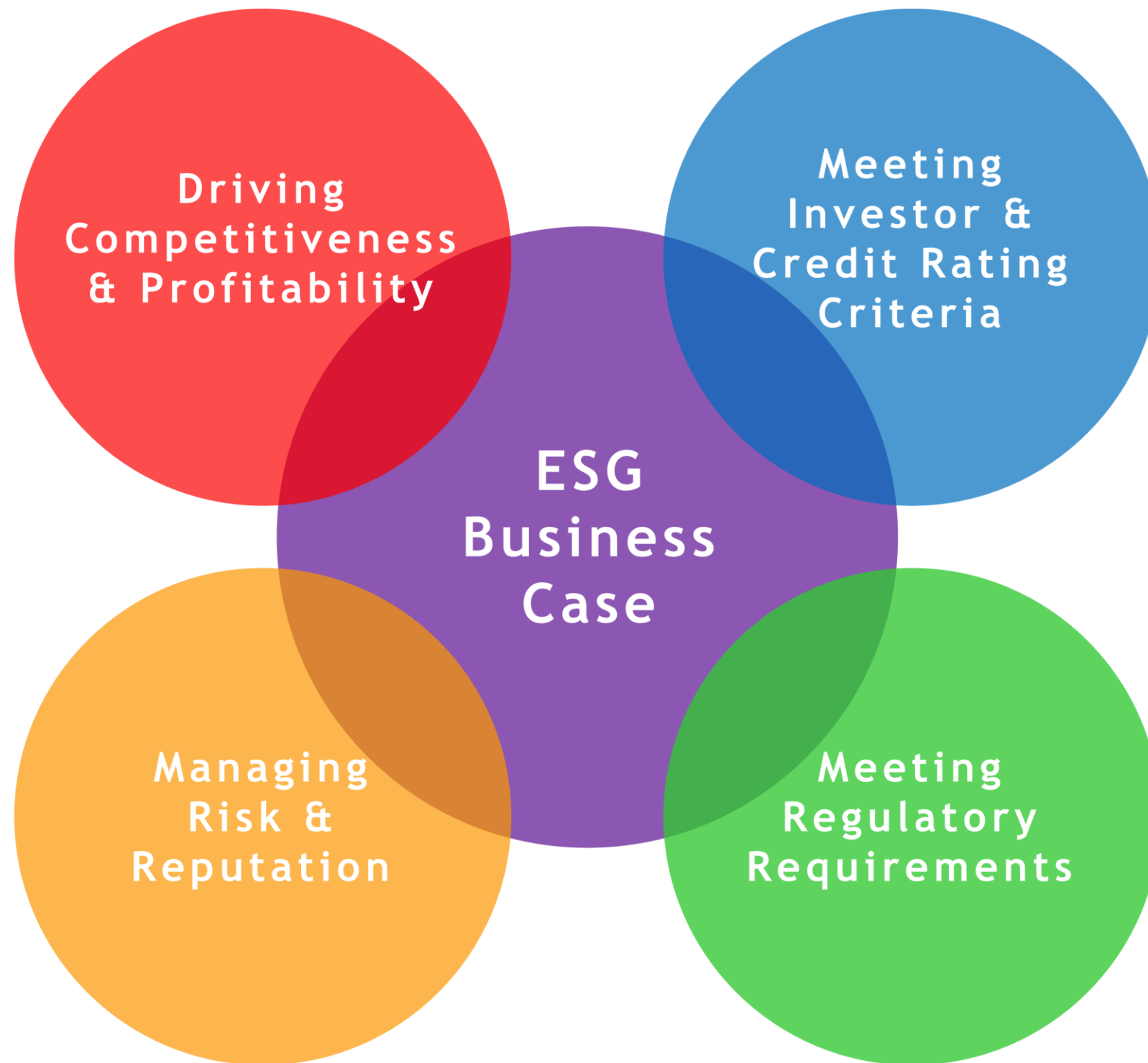
Indeed, ESG-driven investments topped USD 41 trillion in 2020, equivalent to 10 percent of worldwide assets, and are expected to reach USD 53 trillion by 2025.

Over 60 stock exchanges worldwide already issue ESG disclosure requirements to listed companies.

The Trinidad and Tobago Securities and Exchange Commission intends to join them.

- ❖ Helps firms outperform industry peers
- ❖ Allows new markets to be tapped and existing markets to be expanded
- ❖ Enhances efficiencies, reducing costs
- ❖ Boosts consumer preference
- ❖ Drives innovation

- ❖ Enhances risk oversight
- ❖ Reduces the risk & cost of noncompliance
- ❖ Boosts companies' reputations & brands
- ❖ Helps companies attract & retain quality workers
- ❖ Connects employees with their work, which improves productivity



- ❖ Improves access to finance & preferred partner status
- ❖ Attracts ESG investors, the fastest-growing sector in investing
- ❖ Leads to greater returns on investment & higher stock prices
- ❖ Delivers better credit ratings

- ❖ Reduces regulatory pressure & the risk of adverse government action, affording greater strategic freedom
- ❖ Eases approvals & licences to operate
- ❖ Helps companies meet evolving compliance, reporting & listing requirements

Figure 1. How good ESG performance benefits companies.

What ESG involves

There are multiple ESG frameworks, but they all have the same underlying structure.

To illustrate the basic structure of all ESG frameworks, this Guide uses the FTSE Russell framework, developed by the Financial Times Stock Exchange 100 Index.

There are three ESG pillars: environment, social, and governance.

Each pillar is divided into several business-relevant issues (Figure 2).

The FTSE Russell framework divides the environment pillar into five issues, the social pillar into five issues, and the governance pillar into four issues—for a total of 14 issues (Table 1).

Other ESG frameworks may have more or fewer issues, within each ESG pillar or overall.

Each issue is relevant to all companies, but some issues will be more relevant to businesses within a given industry than to others.

Understanding that every ESG issue is multifaceted, ESG frameworks list the aspects of each issue that they consider important.

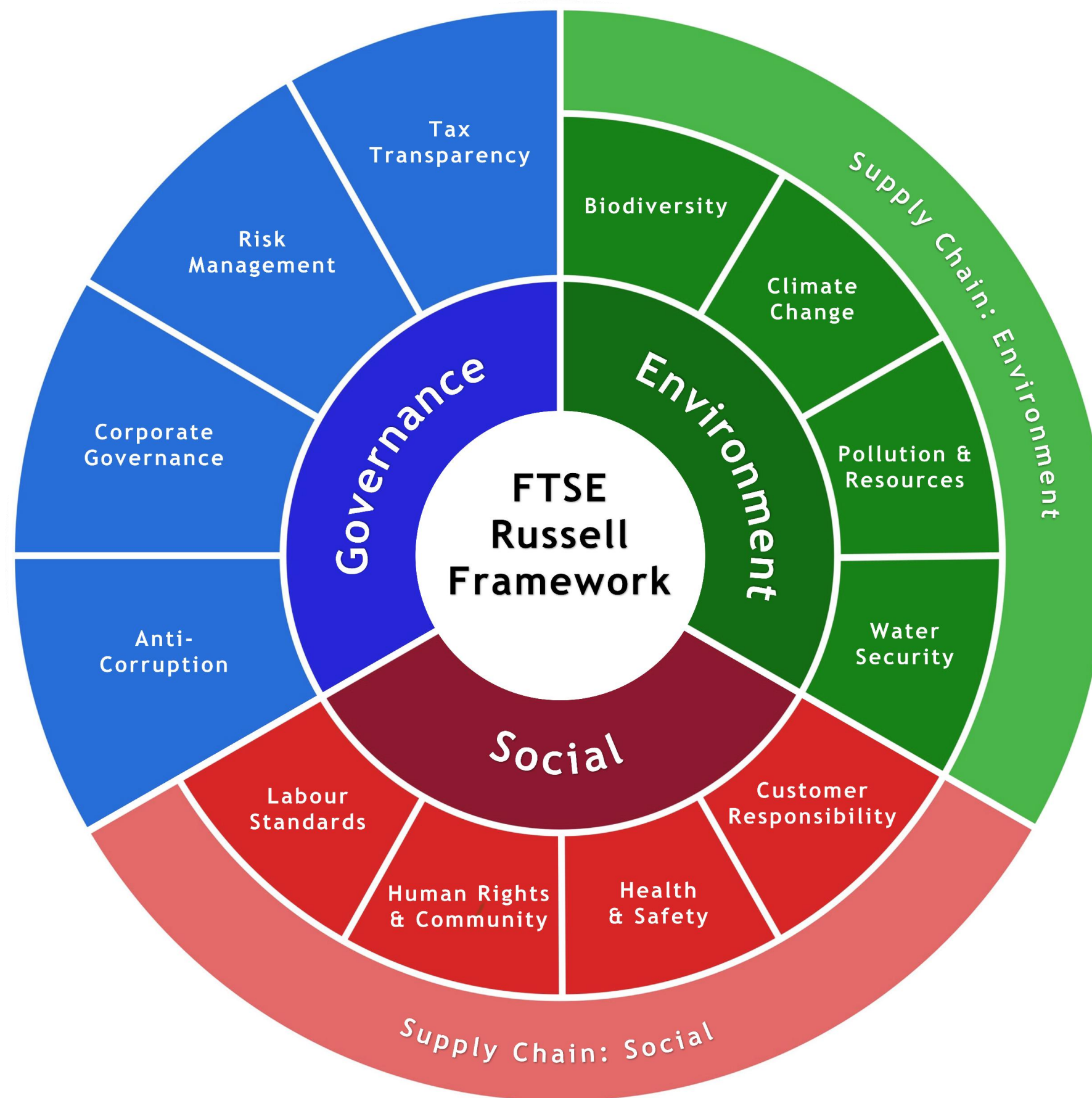


Figure 2. The FTSE Russell framework's pillars and issues.

Table 1. FTSE Russell issue meanings.

Environment Issues

Biodiversity

All businesses disrupt natural habitats & ecosystem services (e.g., watersheds)

Climate Change

All businesses are responsible for some greenhouse gas emissions

Pollution & Resources

All businesses contribute to pollution or use resources at unsustainable rates

Water Security

All businesses use, pollute or redirect water

Supply Chain: Environment

Every company should consider how components of its supply chain perform on the four environmental issues above

Social Issues

Labour Standards

Companies should respect the rights of those who provide work & services

Human Rights & Community Indicators

Companies should respect human rights & strive to improve the quality of life where they operate

Customer Responsibility

Companies should provide safe products & deliver on promises

Health & Safety

Firms should ensure working conditions are safe & minimise stress

Supply Chain: Social

Every company should consider how components of its supply chain perform on the four social issues above

Governance Issues

Tax Transparency

Companies should disclose tax payments & prepare for taxes that deter unsustainability

Risk Management

Companies should identify & manage risks

Corporate Governance

Companies should have mechanisms by which they pursue objectives

Anti-Corruption

Companies can be perpetrators or victims of corruption

These aspects are chosen because experts believe that, by addressing them, a company will create the greatest and most-timely benefits, not just for the issue, but also for business (Table 2).

For example, in the FTSE Russell framework, the ‘Climate Change’ issue has aspects that include ‘greenhouse gas emissions’ and ‘energy consumption and efficiency’.

A company’s performance on a particular issue is determined by how well it performs on the issue’s aspects.

Its performance on a particular pillar will be determined by how well it performs on that pillar’s issues.

And the company’s performance across the three pillars will determine the business’s overall ESG status.

Many Trinidad and Tobago companies are already doing well in ESG’s governance pillar, and have environmental and social initiatives in place that provide a sound foundation on which a robust ESG standing can be built.

Many companies, though, have not been framing their actions and accomplishments in ESG terms, or they have not sufficiently applied the ESG philosophy to their business strategies, policies and processes.

However, the good news is that most Trinidad and Tobago companies will not be starting from scratch.

Table 2. ESG aspects that are found in most frameworks.

| ENVIRONMENT | SOCIAL | GOVERNANCE |
|--|--|--|
| <ul style="list-style-type: none">❖ Greenhouse gas emissions❖ Energy consumption & efficiency❖ Reliance on fossil fuels❖ Water, air and soil pollutants❖ Water consumption, recycling & management❖ Waste production & management (solid, liquid, hazardous)❖ Consumption of non-renewable resources❖ Impact on habitats & ecosystem services❖ Research & innovation in environmentally-friendly products & services❖ Supply & value chain issues❖ Susceptibility to climate change's physical impacts (e.g., floods, wildfires) | <ul style="list-style-type: none">❖ Labour relations❖ Workforce freedom of association❖ Child labour❖ Forced & compulsory labour❖ Trafficking in human beings❖ Workplace health & safety❖ Discrimination, diversity & equal opportunity❖ Human rights adherence❖ Supply & value chain issues❖ Investment in communities❖ Customer health & safety❖ Customer rights, including rights to value for money & information❖ Customer data security❖ Responsible marketing & advertising❖ Whistleblower protection | <ul style="list-style-type: none">❖ Governance mechanisms with roles & responsibilities for directors❖ Codes of conduct established & enforced❖ Respect for laws, regulations & legal obligations❖ Accountability & internal controls (e.g., audits)❖ Transparency & disclosure mechanisms❖ Disclosure of executive pay & its comparison with worker pay❖ Board diversity❖ Independence of directors & conflicts of interest❖ Tax strategy & planning❖ Fraud, bribery & corruption controls❖ Stakeholder engagement mechanisms❖ Protection of shareholder & investor rights |

Who should take the lead

Company directors should accept that their fiduciary duties under the Companies Act extend beyond financial matters, and that their mandate to seek the best interest of their business also includes environmental, social and governance issues.

In the way that they approach their company's finances, directors should make ESG a fundamental component of their companies' strategies, decision making, activities and relationships.

A company's board and executives should thus establish and drive the business's ESG agenda.

The board and executives should have oversight of the company's identification of, response to, and reporting on ESG issues which can harm or benefit the business.

A company should ensure that at least some of its directors have the ESG expertise needed to respond to the business's ESG risks and to capitalise on ESG opportunities in the marketplace.

ESG oversight responsibilities can be undertaken by the full board, or they can be delegated to one or more committees that report to the board.

When committees are involved, they can be already-established ones—like the audit committee or the health and safety committee—which then have ESG issues added to their mandate.

However, this approach might lead to ESG being treated as an afterthought, and not as a highly strategic and integral aspect of the business that merits significant attention.

Ideally, a company should have a standalone, cross-functional ‘ESG committee’, comprised of senior members of key business committees (Figure 3).

This will allow ESG issues that may otherwise be siloed in the business’s departments to be considered holistically.

Many of the aspects that will be used to assess your company’s performance on an ESG issue entail demonstrating that your board has adequate oversight mechanisms and related policies in place.



Figure 3. ESG governance structure with a standalone, cross-functional ESG committee.

Where to start

A company must first identify its stakeholders.

These are the individuals or organisations that have an interest in the company's decisions or activities, or whose power can affect the chances of success of the business's decisions and activities.

While they are generally external parties, such as community groups and civil society organisations, a company also has internal stakeholders that include its employees and shareholders.

The company should map its stakeholders to identify which of them are simultaneously high-interest and high-power (Figure 4).

In close consultation with these key stakeholders, the company should determine the ESG issues and aspects that are most 'material' to its business.

An issue or aspect is material if it can have a major impact on the company's finances, operations, reputation, compliance with laws and regulations, and relationships with stakeholders.

Material issues and aspects with positive impacts are opportunities, while those with potentially negative impacts are risks.

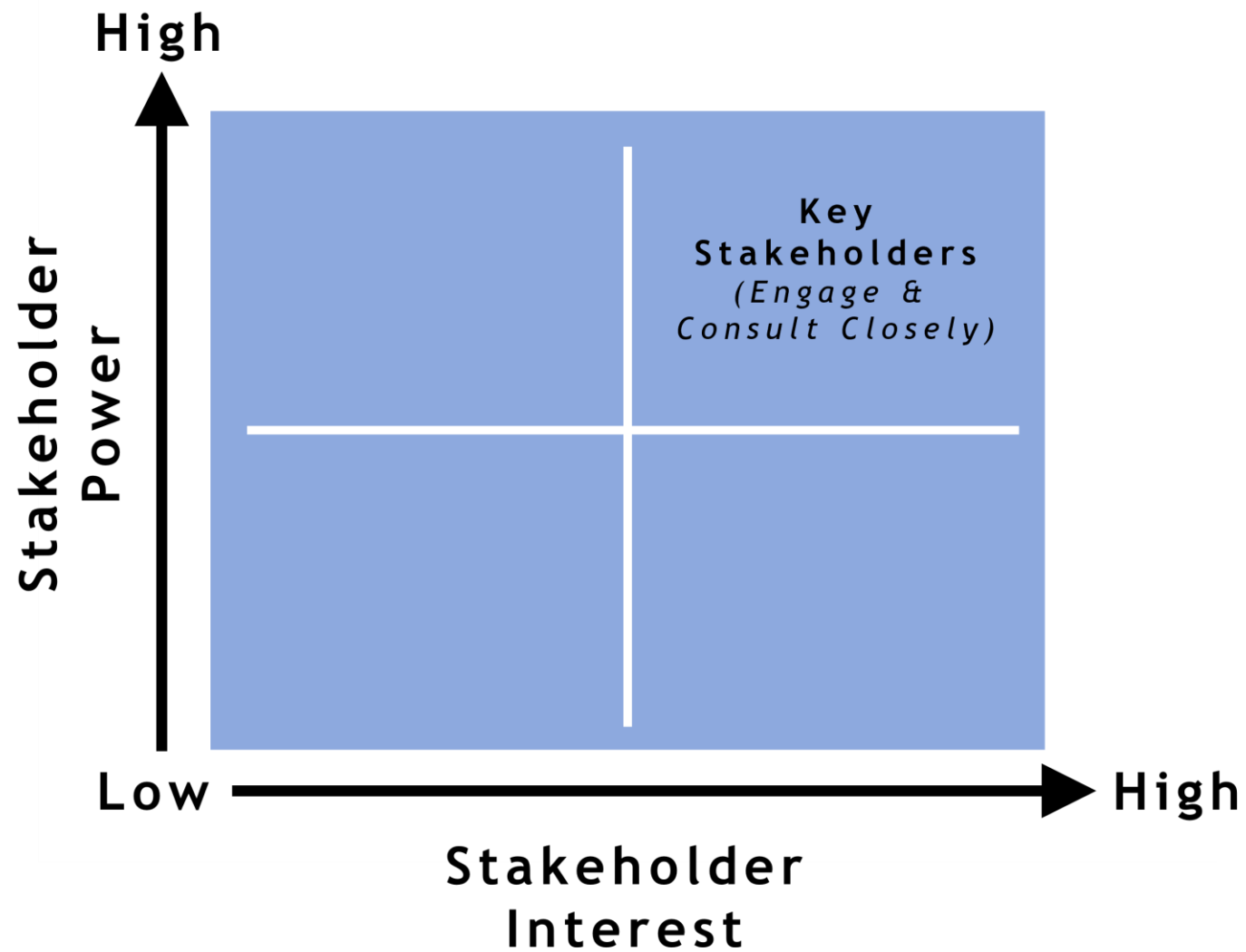


Figure 4. Stakeholder map with top-right quadrant isolating key stakeholders.

Using a materiality matrix, the company can isolate the material ESG opportunities and risks that are simultaneously of very high importance to key stakeholders and of very great impact to business success (Figure 5).

Strategically focusing on these few very-high-priority material issues and their aspects is more likely to yield results and boost a company's competitive advantage.

Trying to deal with more can result in spreading yourself too thin and diminishing returns.

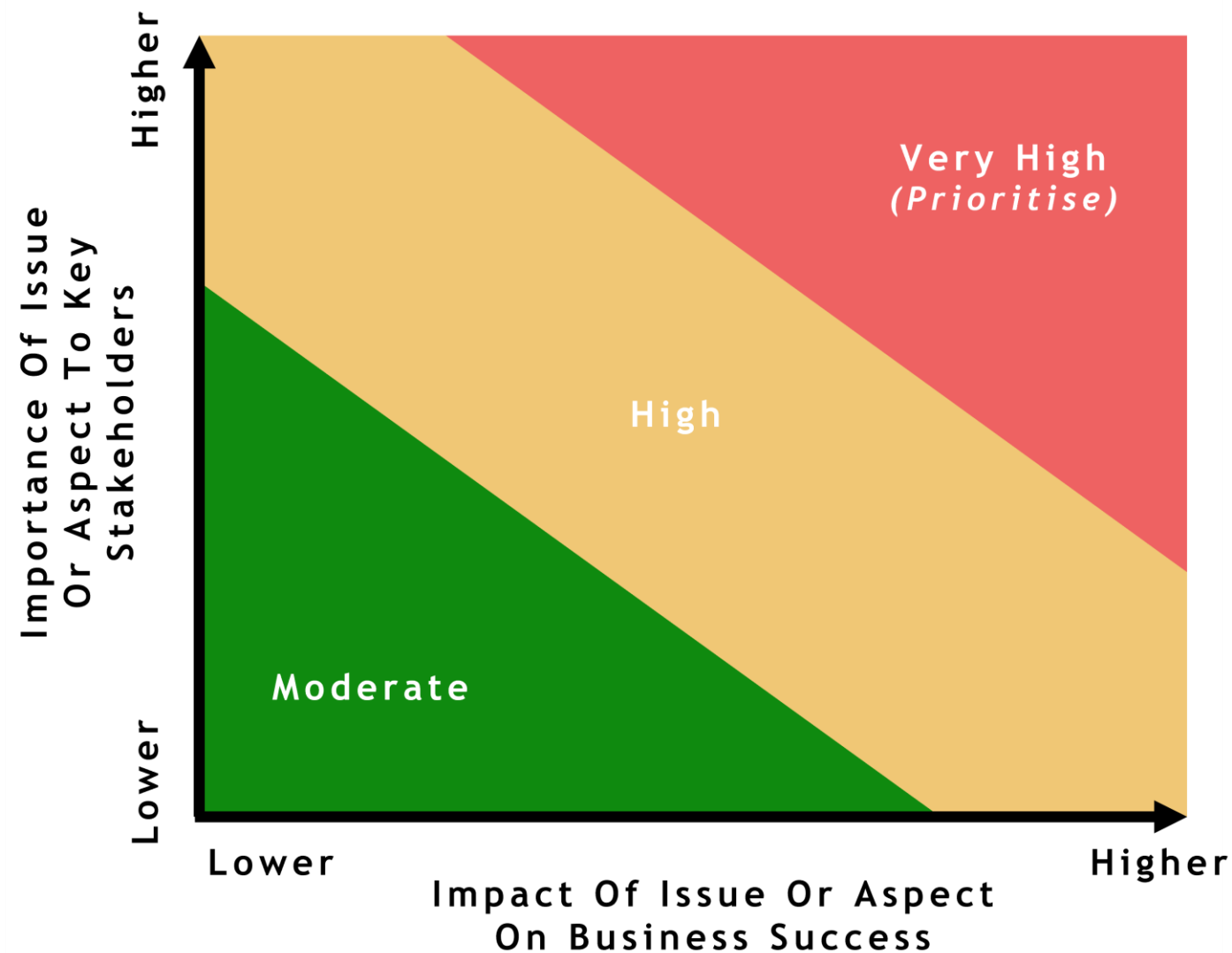


Figure 5. Materiality matrix that can be used to prioritise ESG issues and aspects.

Knowing its priority ESG issues and aspects, a company should develop and implement an ESG strategy through which it will capitalise on opportunities and respond to risks, ideally covering a ten-year period.

An ESG strategy will state the company's ESG ambitions, objectives and targets (Figure 6).

It will provide the action plan the company will use to achieve those ambitions, objectives and targets.

It will guide the company's decision-making, including on the information that is disclosed, the products and services that are developed and delivered, capital allocations and investments, the appetite for and response to risks, resourcing and supply chain issues, hiring and remunerations, marketing, partner choice and stakeholder engagement, and other areas of the business.

By stating the company's ESG objectives and targets, the strategy also makes the business's ESG performance easier to monitor, manage and report.

Implementing the ESG strategy will require an overarching ESG policy for the company, and/or policies that address specific ESG issues and aspects.

A policy outlines the company's position on what is acceptable and unacceptable for the given subject, and provides instructions that direct the company's approach to the subject.

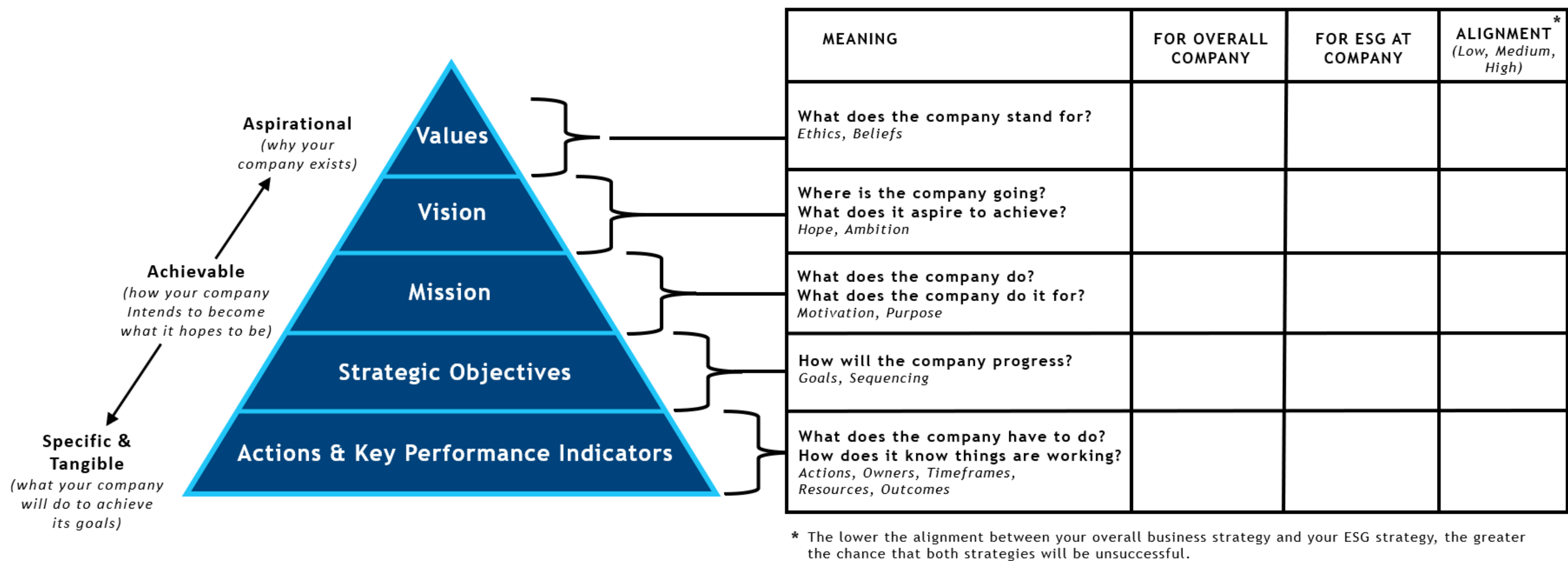


Figure 6. ‘Strategy Pyramid’ tool to help a firm develop an ESG strategy that is aligned with its overall strategy.

Policies are implemented via procedures.

A procedure explains the specific action plan, with step-by-step instructions, for carrying out a policy.

Procedures tells employees when and how they should deal with a situation.

Knowing the company's ESG policies and procedures, employees and representatives will understand how to approach their work without the need for trial-and-error or micromanagement.

ESG policies and procedures help companies comply with regulations, industry-based and other standards, and stakeholder expectations—which, in turn, assure quality control and resilience to risks.

Developing and implementing ESG strategies, policies and procedures might seem burdensome.

However, almost every company may find that parts of its existing corporate strategy, and some of its policies and procedures, can already be categorised under ESG's broad banners.

Again, most of you will not be starting from scratch.

How To Measure & Report Performance

You need to measure your company's progress toward the objectives of its ESG strategy because, as the saying goes, "If you can't measure it, you can't manage it."

Determine your indicators and metrics

An indicator is something you can measure to tell you about your progress towards an intended result, or to let you know when the intended result has been achieved.

Once you have chosen an ESG framework, look to the aspects that are listed for each ESG issue to see the indicators for that issue.

In the FTSE Russell framework, for instance, the aspects "greenhouse gas emissions" and "energy consumption and efficiency" are indicators for the "Climate Change" issue.

The FTSE Russell framework, with its 213 aspects, thus has 213 indicators to be measured—which may seem a daunting task.

You do not have to measure them all, though.

Instead, you should focus on measuring aspects of the ESG issues that your materiality assessment identified as high-priority opportunities and risks.

For every indicator, there should be at least one metric that provides a system for measuring that indicator.

For example, a metric for the indicator "greenhouse gas emissions" could be "tonnes of carbon dioxide equivalents emitted."

While ESG frameworks list the aspects you can use as indicators, they acknowledge the different contexts of companies, and allow businesses to decide on metrics that are within their capacities.

Set your targets

A target is a time-bound goal for a given indicator and its metric.

It is usually expressed relative to some initial, or baseline, value for the metric.

For example, a target for "greenhouse gas emissions" could be "15 percent reduction in tonnes of carbon dioxide equivalents emitted within five years."

Your targets will help you demonstrate progress when things are going right, and provide early warning signals when things are going wrong.

Your targets also give everyone in your business a clear sense of what they should be aiming for.

Report on your progress

A company can report ESG information by adding distinct sections on ESG issues to its annual report.

Or a company can report ESG information via regular, standalone ESG reports that deal exclusively with ESG issues.

The ideal is for a company to create what is called an integrated report, which intermingles ESG information with the other information that is typically required in an annual report.

With an integrated report, ESG information is presented as inseparable from and integral to the information that the company's stakeholders and investors demand from a company's reporting, such as its finances.

This affords investors and other stakeholders a more holistic insight into the business's performance.

Integrating ESG information into a company's reporting can make reports longer and more complex.

A solution would be to summarise ESG information in the report's body, and provide added detail and more technical material in appendices or on the company's website.

How ESG ratings work

With your ESG reporting, and documents to verify your ESG performance, you can pursue an ESG rating from an ESG ratings agency, such as FTSE Russell.

As with credit ratings, ESG ratings agencies score companies on identified benchmarks, and assign grades (e.g., from AAA to CCC) that relate the companies' performance to that of their industry peers.

Retaining an agency to audit your ESG reporting and issue an ESG rating can improve your market access, licenses to operate, and attractiveness to ESG investors—the fastest growing segment of the global investing community.

It can, however, be expensive and you should understand the process before moving forward.

Your chosen ESG rating agency will list the ESG issues it considers important, the aspects that it will use as performance indicators on each issue, and its benchmark of good performance for each aspect.

The ratings agency will score your company's performance on and exposure to each issue.

With FTSE Russell, your performance score on each issue can be between zero (no disclosure) to five (best practice).

Your exposure score on each issue can be between zero (no exposure) to three (high exposure).

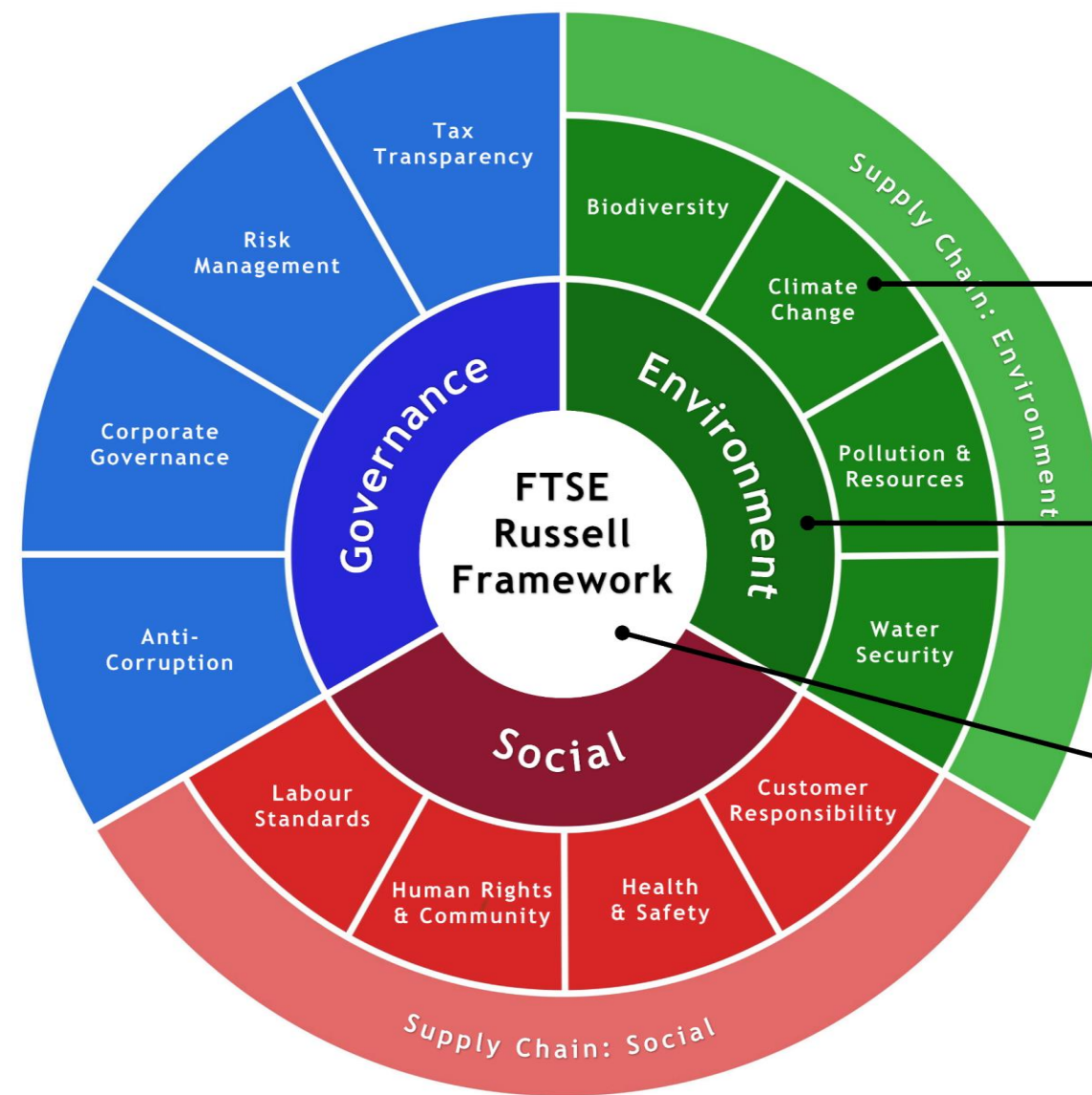
Your issue scores within a given ESG pillar are then inserted into the agency's rating model, which will generate a performance score and an exposure score for the pillar.

Recognising that some issues are more relevant to certain industries, as well as in particular geographic locations, the agency's model will assign weightings to your performance and exposure score for each issue based on your industry and location.

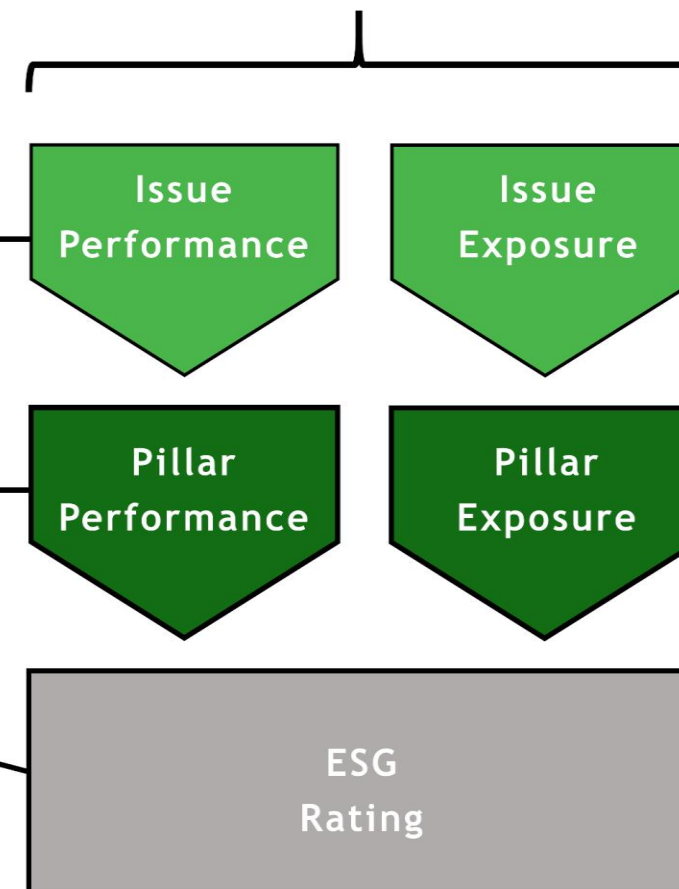
Similarly, the relevance of each pillar to a company depends on the industry and location in which the business operates.

Thus, the rating scheme will assign weightings to your performance score and exposure score for each pillar.

Finally, the model will aggregate your weighted pillar scores to yield your overall ESG rating (Figure 7).

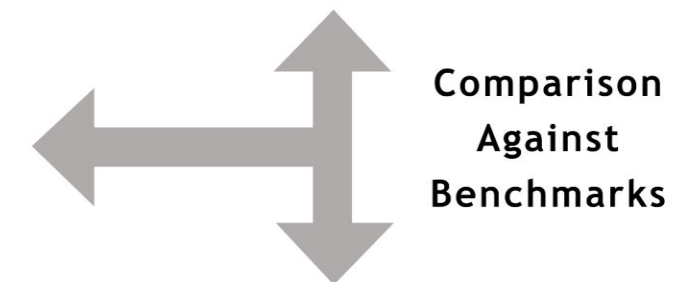


Modelling



Evaluation Of ESG Self-Assessment Reports & Supporting Documents

| Exposure | |
|----------|---------------|
| 3 | High |
| 2 | Medium |
| 1 | Low |
| 0 | Negligible/NA |



| Performance | |
|-------------|---------------|
| 5 | Leading |
| 4 | |
| 3 | Good practice |
| 2 | |
| 1 | |
| 0 | No disclosure |

Figure 7. FTSE Russell's process for determining a company's ESG rating.

What to remember

This Guide's five key messages:

1. Understand the business case for ESG and back it up with board oversight.
2. Identify and focus on ESG issues that are most materially important to the business and its stakeholders.
3. Develop goal-driven strategies to leverage ESG opportunities and respond to ESG risks.
4. Set ESG targets and develop a system to track progress.
5. Report annually on your ESG performance, targeting key audiences (e.g., ESG ratings agencies, investors).

Where to get help

For support and more information, including a more comprehensive ESG guide and toolkit, contact AMCHAM T&T at trade@amchamtt.com.