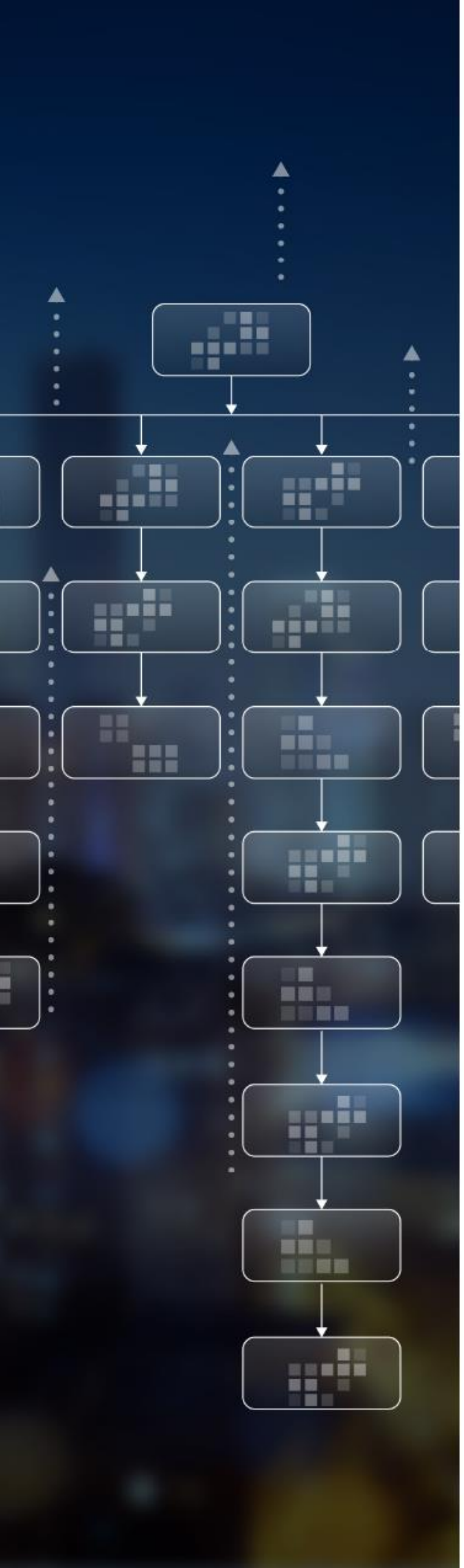

ESG strategy and management: Complete guide for businesses

June 2023

TechTarget

In this guide:

This ESG strategy and management guide explains what ESG involves and how it can benefit companies. You'll also find guidance on creating an ESG strategy and measuring a company's performance on ESG issues, plus information on frameworks for ESG reporting and software that can help manage ESG initiatives. Throughout the guide, hyperlinks point to related articles that cover those topics and others in more depth.

In this guide:

ESG strategy and management: Complete guide for businesses

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For companies of all sizes, environmental, social and governance issues have become key business considerations. Corporate ESG policies and practices are closely watched by investors, employees, customers, government officials and other stakeholders. That makes an effective ESG strategy underpinned by strong management processes increasingly important to long-term business success.

ESG isn't a new phenomenon. The history of ESG investing, in which investors use ESG criteria to help evaluate companies, dates back to 2004 to 2006. In those three years, the term *ESG* was popularized, a legal framework for factoring ESG information into investment decisions was outlined, and a set of six ESG investing principles that's still used today was published -- all efforts driven by the United Nations. ESG investing's roots go even deeper to the socially responsible investing practices that started to take shape in the 1960s and 1970s and expanded over the next two decades. But ESG initiatives in companies have been thrust into the spotlight in recent years because of increasing pressure -- from both inside and outside organizations -- to improve environmental sustainability and act in socially responsible ways.

Studies show that most large companies have ESG programs. In a report published in October 2022, consulting firm KPMG said its research found that 96% of the world's 250 largest companies by revenue report publicly on ESG or sustainability matters. Similarly, Governance & Accountability Institute Inc., an ESG consultancy, said in a November 2022 report that 96% of the companies in the S&P 500 and 81% of the ones in the Russell 1000 Index published sustainability reports in 2021.

But many ESG efforts aren't fully formed, and some companies have yet to get started. In a 2022 survey of IT professionals involved in technology purchasing decisions that was conducted by TechTarget's Enterprise Strategy Group division, only 30% of the 400 respondents said their organization's ESG program was mature. Another 41% said their company had partially implemented ESG initiatives, while 29% said nothing was in place at that point.

THE 3 PILLARS OF ESG

ESG focuses on various issues related to environmental, social and corporate governance practices. An ESG program documents a company's impact on the environment and on different stakeholders as well as its approach to governance; it also assesses potential business risks and opportunities in each of the three areas. Here's a breakdown of the key ESG factors to consider as part of corporate initiatives:

- **Environmental.** Examples of environmental factors include energy consumption; water usage; greenhouse gas emissions and overall carbon footprint; waste management; air and water pollution; deforestation; biodiversity loss; and adaptation to climate change.
- **Social.** The social factors of ESG involve a company's treatment of employees, supply chain workers, customers, community members and other groups of people. Examples include fair pay and living wages; diversity, equity and inclusion (DEI) programs; workplace health and safety; fair treatment of customers and suppliers; responsible sourcing; oversight of supply chain partners; community engagement; charitable donations; and social advocacy.
- **Governance.** This involves the internal management practices, policies and controls that govern how a company operates. Examples include the composition of senior management and the board of directors; executive compensation; financial transparency; regulatory compliance; risk management; data privacy policies; ethical business practices; and rules on corruption, bribery, conflicts of interest and political lobbying.

ESG is closely related to business sustainability and corporate social responsibility (CSR), two other concepts that look beyond standard profit-and-loss calculations. But there are clear differences between the three concepts. Business sustainability focuses more broadly on positioning a company for ongoing success through responsible management practices and business strategies, while CSR is a self-regulating approach to taking actions that have societal benefits. By comparison, ESG is a formalized strategy that includes measurable goals and processes for tracking, managing and reporting on them.

In this guide:

HOW CAN ESG INITIATIVES BENEFIT BUSINESSES?

From a general standpoint, ESG programs can contribute to business sustainability efforts and ensure that there's a commitment to -- and accountability for -- responsible and ethical practices in companies. Those things can pay long-term dividends, but there are also more immediate reasons for companies to invest in ESG strategies. The following are [five specific business benefits of ESG initiatives]:

1. **Competitive advantages over business rivals.** Companies with successful ESG programs can improve their market position and brand strength compared with competitors.
2. **More attractive to ESG-focused investors.** ESG investing has become a significant part of capital markets. In a report published in December 2022, the US SIF Foundation said $8.4 trillion in assets were being managed in the U.S. using ESG and sustainable investment approaches, amounting to 12.6% of all investment assets under professional management in the country.
3. **Better financial performance.** ESG initiatives can help improve a company's overall financial performance by reducing energy bills, operating costs and other expenses -- in addition to potentially driving higher sales.
4. **Increased customer loyalty.** Companies that adhere to ESG principles can more easily attract and retain customers who apply ESG considerations in buying decisions. For example, in the Enterprise Strategy Group survey, 70% of the respondents said they think their company would pay more than a 5% price premium for products from IT vendors with strong ESG practices.
5. **More sustainable and adaptable business operations.** It's also easier for companies with well-managed ESG strategies to adapt to changes in regulatory and legal requirements, as well as the effects of climate change, depletion of natural resources and other environmental issues.

In addition, ESG initiatives can increase employee engagement, make it easier to hire and retain workers, reduce business risks and improve the standing of companies in the communities where they have operations.

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HOW TO CREATE AN ESG STRATEGY

Companies should look to incorporate various ESG trends, practices and ideas into their plans. Some examples include reducing greenhouse gas emissions, creating more responsible and sustainable supply chains, implementing climate adaptation measures and adopting a circular economy model, which aims to reuse product components and materials instead of throwing them away or recycling them.

With such considerations in mind, here are eight steps to take in developing and implementing an ESG strategy:

1. **Get input from internal and external stakeholders.** Consult with board members and business executives about ESG issues that are important to the business, and talk to various other stakeholders -- employees, institutional investors, customers, suppliers, community leaders -- about ones that matter to them.
2. **Assess the materiality of different ESG issues.** Use the input you've gathered to identify the issues that are most important to both the business and stakeholders, as well as the issues that are less important to either party or to both. The individual elements of the ESG strategy can then be prioritized based on that assessment.
3. **Establish a baseline on ESG performance.** Document current performance levels, policies, practices and statistics on the ESG factors that will be addressed as part of the strategy. Doing so provides a starting point for future comparisons to evaluate the progress of ESG efforts.

4. **Define measurable goals for ESG initiatives.** This involves setting objectives and performance targets for the ESG strategy as a whole and the various pieces of it. Some of these goals might include desired improvements on KPIs, while others might call for maintaining current performance levels and practices that already meet requirements.
5. **Create a deployment roadmap.** Next, build out a detailed implementation plan for the ESG program with project timelines, milestones and responsibilities.
6. **Choose the reporting standards and frameworks to use.** As covered in more detail below, numerous ESG reporting options are available to companies. Many businesses use more than one to meet different reporting and disclosure requirements. Choosing the right framework or combination of them is a key part of developing a successful ESG strategy.
7. **Collect, analyze and report on ESG data.** Once the ESG program is operational, processes are needed to collect and analyze data on the relevant KPIs and then to prepare reports for stakeholders. Full reports typically are done on an annual basis, but internal progress updates for the board and senior management are more frequent.
8. **Review and revise the strategy as needed.** ESG requirements can change as business needs, stakeholder concerns and regulatory mandates evolve. An ESG strategy should be reassessed regularly to make sure it's still effective and to identify required updates -- including weak spots that need to be optimized.

ESG AUDITS AND MATERIALITY ASSESSMENTS

The second step in the list above is formally known as an ESG materiality assessment. Such assessments apply the financial accounting concept of materiality to ESG issues and extend it to what's called *double materiality*. That considers not only how material -- or important -- different ESG factors are to a company's business operations, but also their materiality to different groups of stakeholders.

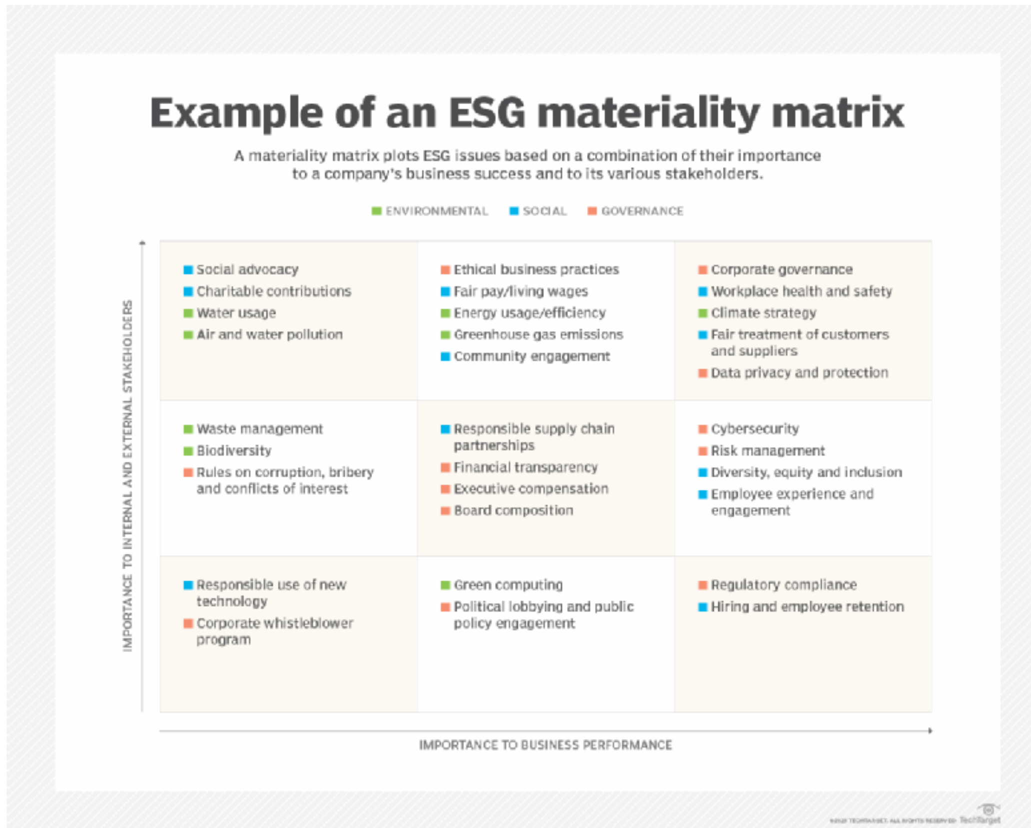
Combining that materiality information provides a blueprint for ESG strategies, which can be visualized by creating a materiality matrix. It plots different ESG issues in a grid along x- and y-axes that represent their importance to the business and stakeholders, thus depicting the issues from least to most important.

In addition to helping companies prioritize ESG plans, materiality assessments can aid in creating a business case for initiatives and deciding what performance measurements to track. To be accurate, though, an assessment must begin with a comprehensive stakeholder engagement process to gather information on relevant ESG issues as well as related risks, opportunities and goals.

Later in an ESG program, ESG audits are another important step to take. They involve internal or third-party audits to verify that ESG data, performance metrics and reports are accurate and comply with accepted standards. That process is commonly referred to as *ESG assurance*, which can take two forms: limited assurance that involves less scrutiny and verification by the auditor, and higher-level reasonable assurance that results in an auditor affirming that the ESG information is materially correct.

In this guide:

An ESG audit is similar in nature to a financial audit. As a result, best practices in preparing for an audit include implementing appropriate controls on ESG data collection and reporting, establishing board oversight of the reported information and conducting an audit readiness assessment beforehand.



In this guide:

EXAMPLES OF ESG INITIATIVES ACROSS AN ORGANIZATION

An ESG strategy typically includes separate initiatives in different departments and operations throughout a company. Here are some examples of what that can involve:

- **IT.** In the IT department, data centers are at the heart of green computing efforts because of the high amounts of energy consumed in them. To help increase energy efficiency and reduce carbon emissions, green best practices in data centers include consolidating servers and storage devices; replacing old technologies with newer equipment that uses less energy; using AI and machine learning tools to create power usage effectiveness models and autonomously manage HVAC functions; and redesigning facilities to take advantage of hot and cold aisle configurations and energy-efficient doors, windows and lighting.
- **HR.** The HR department plays the lead role in ESG initiatives related to employees. This can include managing DEI programs aimed at increasing the representation of different groups of people in the workforce and ensuring that all employees are treated equally. Employee experience and engagement efforts, fair pay practices, and health and well-being initiatives -- mental health support and flexible work schedules, for example -- also fall under HR.
- **Supply chain.** As part of ESG programs, supply chain managers are in charge of responsible sourcing initiatives that take environmental and social factors into consideration on purchases of materials and finished products. They're often also tasked with overseeing supply chain partners on labor practices, efforts to reduce greenhouse gas emissions and other sustainability measures.

- **Marketing.** The marketing department is responsible for ESG marketing efforts that highlight a company's ESG initiatives, goals and progress on meeting those goals. Done properly, ESG marketing can help increase brand recognition, customer loyalty and, ultimately, revenue. But it needs to be honest about ESG plans and practices. If not, a company could face a backlash, including charges of greenwashing -- making false, unsubstantiated or exaggerated claims about environmental actions.
- **Finance.** The CFO is directly responsible for financial transparency and accounting integrity initiatives as part of the governance aspect of ESG. The finance department also has a hand in considering and funding ESG initiatives in other parts of the organization as a result of its control of budgeting, financial planning, cash flows and other financial functions.
- **Legal.** Development of corporate policies on ethical business practices and rules that prohibit actions such as bribery and corruption are commonly led by the legal department.

WHO SHOULD OVERSEE AND MANAGE ESG PROGRAMS?

Oversight of ESG programs often begins at the board level or in the C-suite, with the CEO, COO or executive committee as a whole taking the management lead. Some companies have now added a chief sustainability officer or a chief ESG officer to lead their corporate programs. This role also might be referred to as the vice president of sustainability or ESG in other cases.

Companies might also have a chief diversity officer who oversees DEI programs, generally in collaboration with the HR department. Otherwise, individual ESG initiatives are typically managed by department heads, such as the CFO, the chief marketing officer, the general counsel and the CIO. The latter has a particularly big role to play in driving environmental sustainability efforts because of IT's high energy consumption and the proliferation of e-waste as systems and devices are replaced. In addition, the CIO must ensure that IT systems and tools are deployed as needed to support ESG efforts.

HOW TO MEASURE ESG PERFORMANCE AND PROGRESS

Performance is measured through various ESG metrics, which are KPIs that can be both quantitative and qualitative in nature. Some examples of quantitative metrics include the following:

- Greenhouse gas emissions.
- Energy and water usage.
- Amount of waste generated.
- Compensation data.
- Employee turnover rates.
- Charitable contributions.
- Workforce and board diversity.

In this guide:

Examples of qualitative metrics, on the other hand, include labor practices, community engagement, codes of conduct and policies on business ethics.

ESG metrics are the key content in the reports that companies file on the status and progress of their initiatives. Metrics also help executives manage ESG-related risks and can be used by organizations to measure themselves against the triple bottom line. The TBL is a sustainability-focused management concept and framework that treats the social and environmental impact of companies and the economic value they create as bottom-line categories. It was designed to encourage business leaders to think more deeply about how their company operates instead of focusing only on financial performance.

KEY TERMS TO KNOW

Read our glossary of sustainability and ESG terms that business and IT leaders should know to help set a foundation for developing an ESG strategy.

TOP ESG REPORTING FRAMEWORKS

Reporting frameworks and standards provide a structured approach for publicly disclosing information about a company's ESG strategy and initiatives. They help businesses demonstrate their commitment to ESG practices and sustainable growth, while also creating transparency and accountability and giving stakeholders a detailed view of ESG programs. In

In this guide:

addition, ESG rating agencies use submitted reports and other data to issue ESG scores to companies, either as a number or a letter rating that investors and other stakeholders can use in evaluating an organization.

The following list outlines some of the prominent ESG reporting frameworks:

- **IFRS Sustainability Disclosure Standards.** These are new standards covering disclosures of sustainability-related financial information and information about climate-related risks and opportunities. The International Sustainability Standards Board (ISSB), which was created in 2021 by the International Financial Reporting Standards (IFRS) Foundation, is developing the standards and plans to release the first version of them in mid-2023.
- **SASB Standards.** Released in 2018 by the now-defunct Sustainability Accounting Standards Board (SASB), they provide specifications on disclosures of financially material sustainability information that are tailored for 77 industries. The SASB Standards were consolidated into the IFRS Foundation in 2022 and will be replaced by the IFRS standards, although the ISSB is building on them to create the new ones.
- **CDSB Framework.** This framework enables ESG reporting to be included in annual reports and 10-K filings. But, like the SASB Standards, it will soon be replaced by the IFRS standards. The Climate Disclosure Standards Board (CDSB), which developed it, was also absorbed by the IFRS Foundation in 2022, and no further work is being done on the CDSB Framework.
- **GRI Standards.** Developed by the Global Reporting Initiative (GRI), they include sets of universal, sector-specific and topic-based standards for sustainability reporting on economic, environmental and social factors. GRI published the first version as

In this guide:

guidelines in 2000 and made several updates before formally releasing the GRI Standards in 2016.

- **CDP.** Founded in 2000 as the Carbon Disclosure Project and now known just by its acronym, CDP runs a system for disclosing information on business risks and opportunities related to climate change, water security and deforestation. Companies fill out questionnaires on those topics, and CDP gives them letter-grade scores that can be viewed by stakeholders.
- **Task Force on Climate-related Financial Disclosures.** Typically referred to as the TCFD, the 31-member task force was set up by the Financial Stability Board in 2015. Two years later, it released a set of 11 recommendations on the information that companies should disclose about financial risks related to climate change.
- **United Nations Global Compact.** Launched in 2000, the UN Global Compact is a corporate sustainability initiative that aims to align business strategies and operations with 10 principles on human rights, labor practices, the environment and anti-corruption practices. Participating companies file an annual report on their adherence to the principles.
- **Workforce Disclosure Initiative.** The WDI, which was created in 2016, offers a CDP-like reporting platform focused on workforce practices and management. Companies fill out an online survey on workplace health and safety, employee well-being policies and other topics to receive a disclosure scorecard from the WDI.

Reporting has primarily been voluntary thus far, but ESG disclosure mandates are expanding -- at least in the European Union. The EU's Corporate Sustainability Reporting Directive (CSRD) went into force in January 2023. In stages starting in 2025, the CSRD eventually [will require] approximately 50,000 companies to file annual reports on business risks and opportunities related to social and environmental issues and how their operations impact both people and the environment. That's more than four times the number of companies required to report under an earlier directive approved in 2014.

The CSRD could apply to some EU subsidiaries of U.S. companies or to the parent companies themselves if they meet criteria included in the directive. In the U.S., meanwhile, the Securities and Exchange Commission proposed a more limited rule on climate risk disclosures for publicly traded companies in 2022. The rule has yet to be finalized, though.

CONVERGENCE OF ESG AND GREEN IT

In addition to green computing practices in data centers, ESG strategies are converging with other approaches for making the use of technology in companies greener. That includes green IT, a broader concept that encompasses the efforts to make data centers more energy-efficient along with initiatives such as green storage, green networking and green software development.

Another aspect is green cloud, which involves the steps that cloud platform vendors are taking to improve energy efficiency and reduce carbon footprints in their data centers. AWS, Google and Microsoft have all made commitments to increased sustainability and energy efficiency, with various goals on using renewable energy and becoming carbon neutral or negative. The growing number of IoT devices is also leading to an increased focus on how to address sustainability concerns and meet ESG goals in IoT deployments.

ESG TOOLS AND TECHNOLOGY

Software that can help companies manage ESG initiatives is available from various IT vendors. That includes IBM and major business applications vendors, such as Microsoft, SAP, Salesforce and smaller rival IFS. More specialized providers also sell ESG and sustainability management software, which typically provides a broad set of features for data collection, reporting, analysis and carbon accounting, among other tasks.

For example, these tools can be used to measure greenhouse gas emissions in both a company's own operations and across supply chains using the Greenhouse Gas Protocol's scope 1, 2 and 3 categories as a basis. Key ESG reporting frameworks that are commonly supported include CDP, the GRI Standards, the SASB Standards and the TCFD recommendations. The software can also be used to conduct ESG materiality assessments, track metrics and, in some cases, support DEI programs and other social ESG initiatives.

In a February 2022 report on sustainability management tools, Forrester Research said the following product features were among the criteria it used to evaluate products for the report:

- Support for materiality assessments.
- Carbon calculation and accounting.
- Data management functionality.
- Performance monitoring, benchmarking and auditing.
- Sustainability reporting and risk disclosure.
- Climate action strategy development and tracking.
- Sustainability intelligence dashboards.

CONTINUED READING

5 ESG benefits for businesses

8 top ESG reporting frameworks explained and compared

18 sustainability management software providers to consider