Meeting Minutes for the APPG on Environmental, Social, and Governance

Topic: Defining impact from the perspective of ESG directors across various sectors
Date: Wednesday, 24 November, 10.30am (Hybrid)

Chair
Alexander Stafford MP (APPG on ESG Chairman), (Chairman)

Parliamentary Attendees
Andrew Selous MP (Vice Chair of the APPG on ESG), (AS)
Baroness Northover (Member of the APPG on ESG)

Attendees
Neil Acres, Global Head of Government and Regulatory Affairs at MSCI Inc, Joseph Butler, Finance and Project Development Analyst at EDF Energy, Hannah Cool, Director of Environmental, Social and Governance and the Programme Lead for ESG at KPMG UK, Robbie Epsom, EMEA Head of ESG at CBRE Global Investors, Ciaran Hamill, ESG Specialist at Severn Trent, Devid Melhuish, Chief Development and Sustainability Officer at The Gym Group, Poppy Price, Energy and Natural Resources Strategic Communications Consultant at FTI Consulting, Diana Rose, ESG Research Director at insig AI, Nicola Stopps, CEO of Simply Sustainable, Caroline Turnbull-Hall, Director Corporate Affairs, Regulation and Legal Issues at PwC, Robert Walker, External Affairs Officer at Pension Protection Fund, Cornelia Woschek, Head of Sustainability at The Gym Group.

The meeting starts at 10:30 am.

The Chairman thanked all attendees for joining the APPG on ESG's third meeting of 2021.

Chairman: Obviously, this meeting seeks to find the impact of ESG from the perspective of ESG directors, like yourselves, across a range of businesses and industries. We are not looking at impact in isolation but as a collaborative exploration. These meetings are a vital component about how we can feed into the Government process and have them listen to sector experts. ESG needs to work for businesses, and this is the first APPG meeting since the conclusion of COP26 and there were some encouraging noises coming from the Chancellor - this financial dimension was a success of COP26, and it was good to see governments working with business leaders to realise the potential of ESG practice in the drive towards net zero and other climate goals.

What is 'impact'? How do we define it, and what does it mean? 'Impact' is a buzzword, and we are seeing more and more people becoming 'impact investors' - but each person seems to have a different definition of it.

Contribution: Impact and materiality are intimately linked. We look for what is impactful from a company's perspective in terms of what is meaningful and what is material. For example, if you have an advertising company that reduces its water waste and consumption then this is a positive, but an irrelevant step for them. If you have a bottling company doing the same, then this is very impactful. Therefore sector-by-sector analysis is important. We look at their key material issues by sector and then delve into how they can be rated appropriately.

Contribution: Impact is usually spoken about how challenging it is to measure. From a sustainability point of view, with materiality and additionality, if a company was not doing what they were doing, what would be the status quo versus the outcomes of their performance? It is hard to quantify, so there is much to be said regarding sharing examples of best practice across businesses.

Chairman: How do we ensure companies report on and talk about the things they have a relevant impact on? Last time we spoke on modern slavery and how businesses were fearful of raising their head above the parapet on such a reputationally damaging issue.

Contribution: For my company, we have a relatively easy way to measure our impact. My company specialises in making people fit and healthy. My definition of impact would be generated by our members getting fit. Directly through exercise, my company is helping to reduce pressure on the NHS, reduce GP visits, and increase customer and community satisfaction and happiness. There is a link between regular exercise and motivational achievements, and regular exercise and lower crime rates - this research was found by Sheffield Hallam University. It creates a pound note value against the benefit to society from all aspects of the benefits of being healthy. We demonstrated a figure of £1.8 billion contributions to society since 2016 through our gyms and members (that's £3 million per site). We can say our facilities provide impact at a low cost.

Chairman: That is an interesting case study of how to quantify your company's outputs. Do you now use this as a marketing tool when opening new gyms or getting permission with local authorities?

Contribution: We don't shout about it enough. We've had talks with Sports England to open channels to local authorities. Of course, they can be competitors to us by providing their own gyms. We can say we generate more social value than local authority-operated gyms. Local authorities need to acknowledge that the private sector can deliver social value.

Chairman: This is a great case study to use. When talking about ESG, we often talk about the E, but when talking about the social value it shows how ESG can help businesses and individuals themselves. We are aiming at putting together a report of case studies from your companies so if you have any contributions then please send them to our secretariat team.

AS: I sit on the Advisory Committee on Human Slavery, and a report by Sheffield Hallam University ('In Broad Daylight') found that Uighur slave labour is involved in around 40% of the production of polysilicon cells found in solar panels globally. I wonder how we crack the China issue as they are secretive and drilling down into their supply chain would be near impossible. China is not a free society, and getting clear, transparent answers is not feasible - so what do we do? These solar panels are good for the E, but what about the S? Does anyone know how we could crack this issue?

Chairman: This is exactly the issue with ESG. If you have an impact on the E at the expense of the S, how can we remedy this?

Contribution: I also read that report. Having worked in various sectors with modern slavery challenges, I've learnt it must be tackled at a sector level and acknowledged as a sector issue. The garment industry specifically must. Nike, for example, has acknowledged that modern slavery exists which makes it easy for them to drill down into their supply chain to root it out, rather than in denial or willful ignorance. Pretty much every sector and company have modern slavery in their supply chains, which is horrific. We need to acknowledge that and put processes in place to resolve this. The construction sector is also a big part of this.

Contribution: This is why disclosure is important. Investors and others will then be able to assess the risk of working with a company. As much disclosure as possible is needed, but ultimately companies and investors need to make the decision.

Chairman: This was one result of the last discussion, that we need a TCFD but for things like modern human slavery. We all know it is occurring, but we need a blueprint to help companies know what to do. If all companies need to disclose these details, then at least they will all be on the same footing. Once acceptance happens, change happens, and impact can be reduced.

AS: That is helpful, but China remains a problem. We miss the potential of the combined purchasing power of business globally. China cannot pick off individual sectors in individual countries. Is there mileage in identifying these human rights abuses and penalising China through seeking suppliers elsewhere in the world where there is more supply chain transparency? The global purchasing power of business could change in ways governments can't.

Chairman: That is exactly what we are seeking to do - putting the onus on business.

Contribution: It links to the point on how important the sector is in terms of context. The technology and garment industry both have modern slavery problems and neither want to stick their head above the parapet because they are working against competitors. There needs to be a more collaborative approach. Boycotting is an extreme expression of purchasing power but making shifts as an industry towards deliberate and thoughtful impact-based decisions would be very significant.

Chairman: Obviously, with China, we shouldn't let this blindside us. By focusing on one country, we can ignore other issues. Human rights abuses exist across the world, so more government intervention against China is needed. But we cannot let China distract us from human rights abuses across other countries.

Contribution: Adding to that point on global purchasing power - China has applied to the CPTPP (Comprehensive and Progressive Agreement for Trans-Pacific Partnership). This could be a powerful mechanism for the UK and other like-minded nations to pressure them to clean their act up.

Contribution: Yes, business purchasing power has a huge influence, however, it may underestimate the complexity of the supply chain. Labour will always be exploited, especially so in a rapidly expanding sector. This is not just a business problem, but governments need to take an advisory role in identifying human rights abuses in some supply chains or identifying certain products which have been made through modern slavery.

Chairman: This is a great point. If someone wants to buy solar panels, how do they know where they come from? How do you measure something as complex as a supply chain?

Contribution: We have called for a disclosure of the top 10 suppliers of any company. We currently have no information on this to run models on this to collate the necessary reports on this. Also, investors have a role to play. From an index perspective, we have over 200,000 indexes we run where investors will be able to view with a role to include and exclude various businesses based on supply chain disclosures or controversies. There are tools available to measure the supply chain. It must be a cohesive effort from business, the investment community, and governments to find the right element. Too often people concede it is too difficult to measure.

Chairman: Isn't labelling companies as good and bad quite controversial? Companies trying to get onto the good list will just do what they must do to tick the boxes to get onto that list, so is it hollow impact?

Contribution: This is the challenge. There is now a financial lens on how companies achieve their ESG aims, but it is just one lens. For example, BP took credit for reducing their emissions, but they just changed the boundaries by selling off their petrol chemicals side of the business. There is a lot of financial power in this, and you have different lenses and assessments, so businesses will try and play the game - this doesn't necessarily move the dial. The Harvard Business Review said that if you want to create change through business as a more sustainable society, do we want the financial sector to just tell us what to measure? What we measure is what we manage which is what changes often.

Contribution: I attended COP26, so at some point I would like to discuss that later. On modern slavery, the key thing with supply chains is life-cycle assessment. This is a powerful tool as it's not just about environmental impact up and down the supply chain, but social too. Environmental Product Declarations are on the cards with the construction sector - this is great as it will mandate EPD (a document communicating the life cycle impact of these construction products). We are moving to a stage where every product will have an EPD. This is important as the complexity of sustainability is that you can fix one problem and inadvertently shift it to a different stage in the life-cycle or a different impact, or even change it from an environmental impact to a social impact. Lifecycle assessments give us the opportunity to look at products within the bigger picture - from avocados to solar panels. Technology is coming to help prove the reliability through blockchain, and there is a big place for blockchain-type technology to add credibility to that discussion. This should be at a consumer and business level. Businesses can transcend borders in ways politics cannot. Apple and Google are almost East India-style companies and operate at scales of some countries. If we can empower them to be transparent in regard to value chains, then they can start making decisions to avoid these risks as they do not want to be associated with value chain issues such as modern slavery. On impact, we need to be careful. There are two things regarding sustainability: One is 'fixing current problems' and tackling things like greenhouse gas emissions. The other is 'impact' which is going beyond and leaving things in a better place than we found them, like biodiversity. Businesses should aim to integrate ESG across all their products, which means getting to net zero by 2050, doing all the ESG basics like rooting out slavery in the supply chain, but must go beyond these minimum expectations. Many companies in finance have impact funds, and when you have one of these it is about picking a specific topic and going beyond what is expected. Net positive gas emissions? That is an option.

Chairman: You mentioned blockchain, I'm still unconvinced as I don't really understand its relevance. On impact, which is a great definition - going further than the basics. What do we mean by 'going further'?

Contribution: That's the trick. I think there's a place for academia here. We've mentioned studies, and I think impact can often target outcomes and topics. There is a need to incorporate a depth of academic rigour to substantiate company claims of impact.

Contribution: If they are encouraged to make their disclosures public there'll be that discipline that kicks in. Open disclosure should be encouraged. You also need to consider third party review of reports.

Chairman: Apparently, 88% of impact investors that report their investments meet or exceed their expectations and return 6.4%, compared to 7.4% for non-impact funders. Firstly, should we do more to encourage impact funding, secondly, if we are getting a 6.4% return investing, do we still see an uphill battle and how can we persuade others to do impact investing?

Contribution: At the risk of lowering the quality of the debate, I have a simple description of sustainability: do less harm, do more good stuff. Doing more good stuff is really the 'impact' aspect of this.

Chairman: When talking about fossil fuel companies, are they just selling off assets or reducing what they do? They are still doing harm to the environment. How do you fit energy companies into this mix when talking about impact? When talking about net positive, can a fossil fuel company ever be impact invested in?

Contribution: It goes back to materiality and context of the society we are in. We are in a climate crisis, so materially a fossil fuel company, climate change, adaptation, resilience, and impact will be number 1, 100% the material issue - so it would be difficult to invest in them under an investment positive benefit to society. There is a danger that we focus on fossil fuel companies as a purely negative force. We need to be careful to not push, large responsible companies to sell off smaller parts of the business to smaller, less-responsible companies, whereas there is an element of supporting them through that transition.

Chairman: I believe there needs to be a place at the table for fossil fuel companies - they fear their clout and money. They can achieve a lot with this money.

Contribution: It is an uncomfortable truth, but we are at a stage now where they are essential to that transition and have the influence to invest in transformative technologies. Impact investing will be a combination of value and pragmatism.

Contribution: I wholeheartedly agree with the previous impact of 'impact'. From an impact definition perspective tying it to broad brush ESG commitments and defining that as a company-wide impact plan is important. Yes, there are baseline commitments and future environmental and social value commitments we should build in. I understand the argument over how we realign our profits and value creation metrics to focus on those community and environmental commitments, but the only way this is possible is aligning with a simple, consistent framework used across sectors and businesses. More and more businesses are aligning to the Rewired Earth approach, or UN SDGs - so how do we align your ESG reporting framework to your real-world impact? I would also add that the reporting process for businesses is aligned to legacy financial reporting done on a quarterly or annual basis. Does this work for impact investment and aligning those decision-making criteria? My company is moving to a more live reporting structure whereby we will update sustainability metrics on a monthly basis to make sure our decision-making criteria are current and in the moment.

Chairman: Going back to frameworks, I am interested in your comment on reporting structures. With technology now, you can report live. But is consistent reporting dangerous and a ‘pat on the back’ exercise?

Contribution: Consistent reporting is a huge exercise for clients and companies. FTSE 50 companies will be able to do it, but even large companies don’t have the necessary tools to do it on an annual basis. It should be monthly, but this is just not possible for many companies. It takes time to collect data and the financial year often ends with a report with incomplete data. What is the benefit of reports with out-of-date metrics?

Chairman: If you are looking at companies just in the UK, that’s fine, but global companies will take ages to collect data. Thank you, Andrew Selous MP, for joining us, I can see you have had to leave, but you ask whether the Church of England’s ESG team can join this APPG - of course, get them to drop us a line.

Contribution: As information comes in, it should be assessed. If you have a governance disaster, it happens overnight, you don’t wait till the end of the year to decide, so why should it be treated differently to E or S. Information that comes in should be assessed as and when it comes in. The data is currently coming in without context or qualitative overlay.

Contribution: If it is material and you are a public company your competitors would expect you to tell them what is going on. Do not tell people about a problem after it's fixed.

Contribution: I think it's exacerbated by social media. You cannot escape the never-sleeping court of public opinion. Companies should do their best to mitigate the fallout.

Contribution: I wonder whether it’s worth discussing the EU taxonomy and the UK’s recently launched equivalent. If we think in terms of impact, then maybe we shouldn’t fight against this anymore as it seems to be picked up legislatively in terms of whether it affects your scope. We have investors asking about whether portfolios are taxonomy aligned. I wonder whether that threshold that the technical screening criteria gives us a good point to draw the line on where what a company should be doing ends. If we see impact as an additionality, taxonomy gives us a good point at which we can say we’ve gone beyond that. If you develop a new asset, it must be a net zero energy asset +10% - this is taxonomy aligned. If we go net zero +30%, then we are going way more than the markets agreed. All sectors have these KPIs emerging through the technical screening criteria. I look forward to the publishing of the social criteria which will give us similar criteria and thresholds on the social side. This is where the market is moving. Is that worth utilising and adopting formally? That would be dynamic.

Contribution: I agree. From a client perspective being EU taxonomy aligned and understanding the UK-specific implications is something we are strongly with our clients on. Making sure we are aligned from a drill-down taxonomy perspective whilst equally elevating that aligns to those with metrics. There’s an intersection to do that - it’s the operationalising and how to build it into your business, which is where taxonomy comes in.

Chairman: On that point, it’s always worth thinking about real world examples. M&S on Oxford Street are demolishing the building to build net zero flats. But that has 39,000 tonnes of embedded carbon in the building that may take seventeen years to cancel out, negating the benefits. Could the building be retrofitted? We need to be careful to avoid throwing the baby out with the bathwater.

Contribution: This is where you need to ask companies for qualitative descriptions behind the decision they’ve made. If retrofitting wasn’t a sustainable option, then they need to prove that.

Contribution: The basic concept of sustainability is you need to think about things in context. The size of the company, its power, the size of the issue, your impact on the issue is all relevant. For large employers in areas of deprivation, how you operate is more significant than it would be in other areas, so qualitative and quantitative information is very important for context.

Chairman: How can we encourage more people and organisations to take up impact investing? Is there anything Westminster and Whitehall can do to help?

Contribution: The work by BEIS and the DWP is important because the trustees need protection and backing to explain to investors or pension funds why they didn’t focus only on the procurement methods rather than the fiduciary methods. It’s not quite clear yet, but I would look to expand on that.

Chairman: It is important to get government backing so it isn’t just about fiduciary responsibility but the wider context that needs to be focused on. Is there a tension between impact investment and ESG in terms of one diluting the conversation, or do they go hand in glove?

Contribution: I think they send the same market signal that there is interest and financial benefit in operating as a sustainable and responsible business and by being a benefit to society and the environment. If that plays out as impact investing, or stronger regulatory requirements on ESG disclosures, then it is all part of the same ecosystem of impact. In terms of how to encourage impact investment, our company’s expansion into Amsterdam introduced us to impact economy programmes there that support and encourage companies.

Chairman: Going back to impact investing, what does this mean to you?

Contribution: We are keen to attract other investors into our business. I think the introduction of impact, as opposed to sustainability funds, is an interesting area that needs definition with some translation between financial institutions and businesses. We do see ourselves as leading our sector and we add social value and want to distinguish ourselves by pushing this achievement. Most of our buildings are repurposed, and we seek to tackle more areas in a positive way that adds value.

Contribution: We are a relatively small company and spend a lot of time and effort and we want everything we do to be reported - but this can be difficult as many frameworks out there do not fit our model. Overrating or underrating certain issues may occur, and it is really tough to engage with the number of regulations out there. We need a simplified framework to make ESG reporting more inclusive and more broadly available for smaller companies.

Chairman: That is a great contribution. Is working with small companies worth doing?

Contribution: Certainly. Although we may not have exposure to all the smaller companies out there. We have a reporting framework that we invite companies to participate in, but we also try to adapt this for smaller businesses. There is a need to engage with smaller businesses when it comes to disclosure.

Chairman: Reporting frameworks certainly aren't working for everyone and engagement with them is needed.

Contribution: This is a great discussion. For my company, we are running a large infrastructure project with several angles to consider. We need to raise £20 billion in equities and debts and cannot do this without impact investors. I agree with the previous definition of impact, and we are absolutely looking at going above and beyond for this specific project - by kickstarting the hydrogen economy perhaps. We have looked at engaging with ESG rating agencies, and they have broadly similar themes and if you can position your company in a way to get the right data then you can largely plug into these rating agencies and get a similar outcome.

Chairman: I'd like to briefly circle back to how impact translates to materiality in reporting.

Contribution: Impact reporting relates to impact on the company. When looking at frameworks, GRI or WEF disclosures, I think overall that if you follow these, you will disclose just 60% of your true impact. So much of that is unique to your business. Just following frameworks may not capture all the data needed. You need to provide a minimal level of what you should include in the disclosure and then more principles to report and reflect your true impact. For example, you see an increase of women at board levels and in leadership teams - this is disclosed and measured, but the outcome should be how the range of opinions and perspectives has changed due to this. This isn't reported.

Contribution: I agree. From a double materiality point of view, social, financial, and environmental impact is key. There is always space for tools designed by the government, like DEFRA's biodiversity net gain, which are useful for reporting. Perhaps we can have a toolkit to measure social value.

Contribution: SFDR has three definitions, but Articles 8 and 9 are really the ones which matter. Article 8 covers funds to promote ESG as part of what they do, and Article 9 is those that effectively have something from the ESG role in the objective of the fund. Broadly, this means that most impact funds sit in Article 9 and provide a nice framework to decide where they sit. To have an impact you must have a focus and often this is on a specific topic on which you can go above and beyond on impacting. Impact is great, but it isn't an excuse to let other ESG criteria slip. SFDR is a useful framework.

Contribution: As I mentioned earlier, I attended COP26 and came away feeling positive. The media and activists played the role of the opposition and provided a reality check. However, I thought the key thing COP26 did was see the attendance of the ‘real economy’. Businesses and individuals, from CEOs, tech executives were speaking to governments which is vital in the possibility of change. This was also the first COP which looked to speak to consumers. Sky News had a daily climate show which broadcast COP26 live, the BBC had extensive coverage. Most people are aware it happened which has shifted things dramatically. People are understanding the issues. Whilst in some areas COP26 fell short (‘phasing down coal’ rather than ‘phasing out coal’), the pact brought 200 countries together to agree on a way forward and this is a strong signal to businesses. All agreed a way forward from adaptation, net zero, to loss and damage, and businesses are looking to get ahead of policy on this front. Such a leadership role for business means that they won’t be looking at policy goals of 2050 but will look to reach the same goals by 2040. This is a massive step forward that can only be looked at with optimism.

Chairman: This is an upbeat summary of the summit. I agree that it was positive and business attendance was an undeniable benefit. If you have any case studies you would like to add, please send this to the secretariat team as we are looking at putting together a report after this. I look forward to seeing you all at the next meeting.

Meeting ends at 12.00pm.