THE PENNSYLVANIA STATE UNIVERSITY
SCHREYER HONORS COLLEGE

DEPARTMENT OF ACCOUNTING

An Evaluation of Challenges in Reporting for Environmental Social and Governance Criteria

Alexander Palmer
SPRING 2022

A thesis
submitted in partial fulfillment
of the requirements
for a baccalaureate degree
In Accounting
with honors in Accounting

Reviewed and approved* by the following:

Samuel B. Bonsall IV
Associate Professor of Accounting
Thesis Supervisor and Honors Advisor

Schalyn Sohn
Assistant Teaching Professor of Accounting
Faculty Reader

* Electronic approvals are on file.

ABSTRACT

This thesis researches the problems that currently exist with the environmental, social and governance (ESG) reporting frameworks and ways in which these frameworks can improve to provide comprehensive information for investors to utilize. There are hundreds of frameworks being utilized as companies look to provide information on their ESG actions. These frameworks each have their own niches as some focus specifically on environmental, or social issues, while others look to provide comprehensive ESG information.

I began by researching major problems that the major reporting frameworks face. These include the Global Reporting Index (GRI), Carbon Disclosure Project (CDP), Sustainability Accounting Standards Board (SASB), and International Sustainability Standards Board (ISSB), and continued by providing details on the problems that have been occurring across all reporting frameworks. In addition, I conducted interviews with professionals in venture capital and private equity firms who specialize in ESG investing, and in these interviews, they provided context to the problems in the accessing of ESG information. The respondents highlighted issues they have faced with companies lacking the resources and knowledge on how to report and improvements which would improve reporting including standardization across industries and reporting requirements for all companies to allow for more informed investment decisions.

With the development of these frameworks there is significant room for growth; however, with improved ESG frameworks investors will be able to make informed decisions while promoting sustainability, social progress, and good governance.

TABLE OF CONTENTS

LIST OF FIGURES

ACKNOWLEDGEMENTS

The first and foremost thanks is to Samuel Bonsall for his help throughout the Thesis Writing process. He has been a strong supporter of every idea I have had and helped pushed me towards where I needed to go all while being a strong supporter in helping with connections and leading me as I wrote this thesis.

I would further like to thank Schalyn Sohn for being my Thesis Reader. She hopped on in the role of Thesis Reader in my last semester in the MAcc Program and I owe her many thanks for taking on this role last minute and being able to be a support seeing my thesis to completion.

I would also like to thank the amazing friends and supporters I have had along the way as I wrote this thesis. My time at Penn State has been an unforgettable and flawless experience that I would not have traded the world for, and it is all due to the amazing friends I have made along the way. They continued to push me to stick around and keep accomplishing the world and I am unbelievably grateful for their support as they pushed me from a freshman student who was still deciding what I wanted to do in life, to the confident masters graduate I am now. I could not have done it without them.

Finally, I would like to thank my Family for their unimaginable support throughout my entire life and especially in my time at Penn State. They truly are the only reason I am where I am now and could not have done it without their support all along the way. Thank you so much Mom, Dad, and Nick!

Chapter 1

Background on Accounting Standards

FASB, IFRS and ESG

With the growth of environmental, social, and governance (ESG) prioritization across the world there has come an equal-sided increase in the standardization of reporting as multiple groups and standards board's look to provide further ESG information to investors. This is all being done with the goal of allowing investors to make more informed decisions on both positive and negative ESG actions that companies have been making. Simultaneously this looks to promote companies making positive actions towards increasing the sustainability, social wellness, and good governance across the company. With this goal, there has been an increase in problems that these investors have faced in being able to collect and have access to accurate and comprehensive information.

One of the primary goals of accounting standards is to provide comprehensive standardized financial statements that are free of material misstatement. These statements are made for the public to be able to rely on and utilize this information for their investment making decisions. With the growth of ESG, the Financial Accounting Standards Boards (FASB), which creates accounting standards for the United States financial system, and the International Financial Reporting Standards (IFRS), which creates accounting standards for the international financial system, have not created standards which directly provide information on companies ESG actions. The FASB and IFRS's lack of standardization has created a void in comprehensive ESG information which has been filled by countless reporting standards. The number of reporting standards has created confusion amongst consumers, companies, and investors as there is no comprehensive way to report on information and no comprehensive reporting standard to follow.

This problem has been further exacerbated by the difference in evaluations across currently existing ESG Reporting standards as a study by Florian Berg, Julian Koelbel, and Roberto Rigobon (2019) out of the MIT Sloan School of Management shows. In their study they found that "correlations between the ratings range from 0.38 to 0.71, based on ESG ratings from six different raters." This leads to many significant problems for investors where they are unable to properly evaluate the companies which they are looking to invest in and unable to make correctly informed investment decisions. This confusion can further lead to a reduction in investment by companies into ESG initiatives if they are not being properly understood and evaluated based on their ESG Actions. In order to get proper information for investors to make investment decisions there is a strong need for standardization which allows for both comparability of information and ease of decision making.

Current Accounting Standards

Currently, within Generally Accepted Accounting Principles (GAAP) there is no standardization that provides direct information about the ESG activities on companies reported financial statements. Specifically, the standards only "requires an entity to consider changes in its business and operating environment when those changes have a material direct or indirect effect on the financial statements and notes thereto" (FASB, 2021). This paper highlights a few key points which show how the current accounting standards do not prioritize the reporting of

ESG information. Specifically, a detriment to the increase in reporting of ESG information is the fact that “[f]inancial accounting standards are not intended to drive behavior in any way, including benefitting one industry or business model over another or spurring businesses to take certain actions.” Standardization of information on ESG actions would go against this mentality as it would promote businesses to take a further role in creating positive ESG actions.

While there are times in which ESG actions can factor into the statements of a company, these are considered in the context of the actual functioning of the business and are not emphasized for investors to use as a tool for investment-making decisions. As the FASB (2021) claims “an entity may consider certain ESG matters as an input to an accounting analysis; for example, a material decline in demand during the reporting period may be a consideration when estimating future cash flows used in a long-lived asset or goodwill impairment analysis. Lastly, risks and opportunities related to ESG matters may have an unfavorable, favorable, or neutral effect on financial statements”; however, the company’s actions are not explicitly rated and judged for investment making purposes. The general purpose is to provide information about the current financial health of companies and the only time where ESG is considered is when it is going to affect the accounting analysis. This fails to provide information on a large section of ESG as the FASB expects more than just financial reporting to be used in the investment making decision process.

This is followed up with the same process by the IFRS (2021) where they have decided on the separation of IFRS Accounting Standards and IFRS Sustainability disclosures. Specifically, at the Climate Change Conference of the Parties 26 they announced the creation of the International Sustainability Standards Board (ISSB). The ISSB goal is to create a “global baseline of sustainability disclosure standards” which is important as it shows that in the accounting field across both the United States and internationally, the way in which ESG reporting is moving forward is going to be done separately from GAAP and IFRS. This separation has allowed for multiple reporting systems to find a foothold in the ESG reporting world, with each having its own areas in which it increases information for invests and drawbacks to the information it provides.

Chapter 2

Reporting Standards Outside of Accounting

Due to the current reporting information where GAAP and IFRS have decided against including standardized ESG information in financial reporting, there have been many reporting systems which have been created to help by providing standardized information on companies' ESG actions with the goal of allowing more accessible ESG information for investors to make decisions on. This lack of a central reporting system and over 600 different scores, ratings, and other analyses has created a lack of harmonization as stated by the Green Business Bureau (2021).

This is the key problem currently with the reporting of ESG Information as with the major financial reporting standards in GAAP and IFRS failing to create a centralized standardization investors have had to look for unstandardized and unaudited information to utilize. With a wide variety of ratings being produced there are consequences to the promotion of ESG activities. As the Organization for Economic Co-operation and Development (OECD) reported (2020) "inconsistent disclosure requirements mean[s] that both institutional investors and corporates cannot properly communicate on their ESG-related decisions, strategies and performance criteria, with beneficiaries and shareholders. This in turn makes it hard for such beneficiaries to assess how their savings are used, and for companies to attract financing at a competitive cost that fully considers ESG factors." When there are differences in ESG ratings as is currently seen across the major reporting standards, investors have difficulty in making informed investing decisions based on ESG actions. Steves (2021) reported on a survey which found "almost half (45%) of valuation experts believe a lack of a standardized and recognized measurement system is the biggest threat to effective environmental, social and governance

(ESG) disclosures for businesses." With investors being unable to make decisions based on ESG actions this will further reduce the incentive for company leaders to make positive ESG decisions and thus reduce the number of positive actions being made for the environment, social issues, and good governance.

There have been significant steps towards standardization across the major ESG Reporting systems. The Global Reporting initiative (GRI), Carbon Disclosure Project (CDP), Sustainability Accounting Standards Board (SASB), Climate Disclosure Standards Board (CDSB), and International Integrated Reporting Council (IIRC) came together to release the Statement of Intent to Work Together Towards Comprehensive Corporate Reporting (2020). In this statement they highlighted their vision to reduce confusion and achieve "global legitimacy for sustainability disclosure frameworks and standards, as a part of a comprehensive corporate reporting system." They are looking towards comprehensive corporate reporting with each major reporting standard having its own part in providing ESG information. From here it is important to understand the progress each standard and where they are faltering in their reporting.

Global Reporting Initiative (GRI)

The Global Reporting initiative is an all-encompassing standard which provides recommendations on how to report on information regarding companies' actions both in the economy and in sustainability. As the Governance and Accountability Institute reports, the GRI is currently the most widely adopted reporting standard across the fortune 500 companies with over 51% of ESG reporting companies using the GRI (2019). This is compared to the next leading standards being the SASB which only 14% of S&P 500 companies used in 2019. The

Global Reporting Initiative is issued by the Global Sustainability Standards Boards (GSSB) and is broken into 3 key sections universal standards, sector standards, and topic standards as showcased by the following graphic provided by the GRI (2021). Specifically, each standard provides detailed breakdowns on each major topic that needs to be disclosed and detailed information under each category.

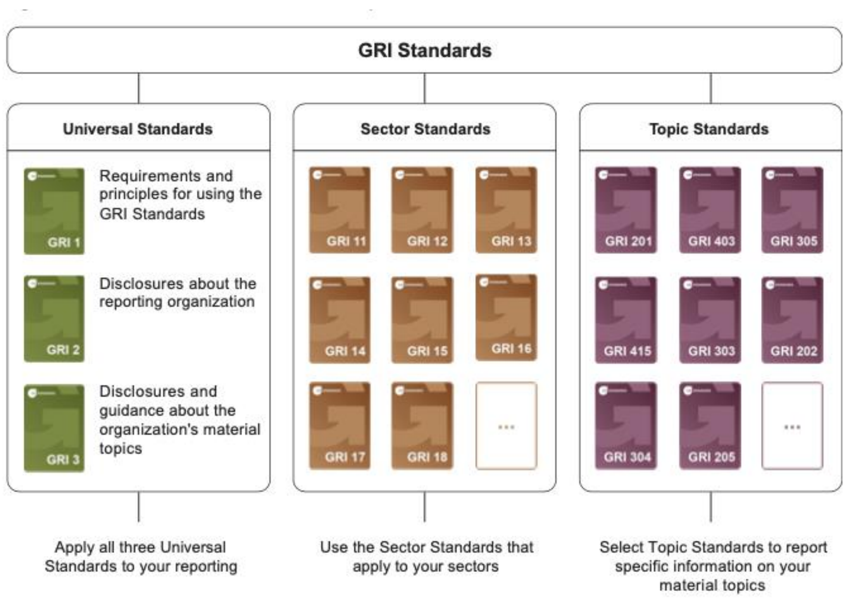

Figure 1. GRI Reporting Standards Breakdown

These issues focus on disclosing information that is best for the public interest. For example, in the oil and gas sector they provide specific details on reporting for both sector specific details in their greenhouse gas emissions, but also sector nonspecific issues like occupational health and safety and non-discrimination and equal opportunity initiatives.

What allows for GRI's success is their principles which are accuracy, balance, clarity, comparability, completeness, sustainability context, timelessness, and verifiability. They use these principals to guide their actions to ensure that reports utilizing the GRI standards are high quality. These allow companies of any size to have detailed guidance on how to report on their own actions, so the problem of reporting is not amplified by a lack of guidance. While they hope for high quality standards, they are not verified by the GRI and are instead self-reported. This does allow organizations to provide inaccurate or incomplete information. This freedom specifically reduces one of the major goals of reporting which is comparability between companies and accuracy of data. This also allows them to attempt to paint the best picture of themselves in the reporting and thus reduces the verifiability of GRI Statements. The GRI currently has the scope and detail for widespread adoption, with the main drawback being that reporting is optional and the data is not always comprehensively reported.

Carbon Disclosure Project (CDP)

The Carbon Disclosure Project is a major evaluation metric which is providing information and ratings based on companies' sustainability activities, which focuses on comparability between companies. Formed in 2000 the CDP has been able to provide significant information about companies ESG actions and been a resource for investors to make informed decisions about the ESG actions of public companies. There are over 13,000 companies reporting on the CDP which is significant in comparison to many other standards. What allows the CDP success is the comparability between companies. Because the CDP only provides rations on climate change, forest protection, and water security, it is easy to compare the actions of companies on these major issues. These companies are also given a score from A to F which allows for direct ratings comparisons between companies, and thus allows investors to make more informed decisions on these issues.

The CDP is not without drawbacks including its limited scope and opt in strategy. While there are standards which are currently in the works like the ISSB and GRI which are comprehensive ESG reporting standards, the CDP provides information exclusively on sustainability issues. With its limited scope, it does not provide the full picture of actions that a company is doing and while it allows ease of decision making, it has reduced information in comparison to other standards. This is further worsened by the problem that all current standards face which is that companies must opt in to report using the CDP. As there is currently no major legislative requirement requiring companies to provide information to the CDP, only a small subset of all public and private companies have provided sustainability information with the CDP.

Sustainability Accounting Standards Board (SASB)

The SASB differentiates itself from the other major ESG reporting standards due to its focus on information that effecting revenues expense, valuation of assets/liabilities, cash flows, or cost of capital as reported in the shared vision between the CDP, CDSB, GRI, IIRC, and SASB. This focus allows the SASB to provide improved information to investors which has the goal of promoting investment in companies based on their ESG actions. With information provided being focused on investors, this allows companies to see more direct financial benefit from their investment into environmental issues, implementation of good social policies, and promotion of good governance. As with the GRI standards, there are specific standards created for each sector to allow for more detailed and specialized reporting on issues each industry faces. Within each industry the SASB is also focused on five key sections to report on: environmental, social capital, human capital, business model and innovation, and leadership and governance. In each sector they focus on certain metrics that are considered material to the sector. Then when evaluating companies, they focus on these metrics to provide the highest detail in their reporting systems. For example, in the E-commerce sector they focus on energy management, customer privacy, data security, employee engagement and DEI, and product design and lifestyle management. This focus provides the most important details to each sector while ignoring immaterial issues.

While being a part of the Statement of Intent to Work Together Towards Comprehensive Corporate Reporting (2020), as previously mentioned the SASB's niche is to focus on financially material ESG factors and ensure that those are accurately reported to provide further ESG information for investors to make decisions upon. The SASB provides less detail to investors than the GRI but allows for a clearer analysis of the most important details to each sector. The largest problem to the SASB at the current moment is scope. Where the GRI had 51% of the reporting fortune 500 companies utilizing its standards, SASB lagged with 14% of reporting fortune 500 companies (Governance and Accountability Institute, 2019). The SASB is also not without critics. Professor Carol Adams from Durham University Business School critiqued the SASB saying the SASB doesn't "provide information on management approach, governance oversight and incorporation of sustainable development issues into strategy in the way that the GRI standards do" (Bouvier, 2022). This focus on only sector specific issues reduces the amount of information reported and provides less detail compared to other ESG reporting frameworks.

To increase the number of companies using the SASB framework, the SASB is combining with the ISSB in June of 2022. As reported by SASB in their SASB Standards and the new International Sustainability Standards Board report they are consolidating as "Capital markets need evidence-based, consistent, comparable disclosure to deliver long-term value to shareholders, while also helping to secure the future of our people and our planet" (SASB, 2022).

With the SASB and ISSB consolidating, they are looking to reduce the complex reporting standards and due to the significant support the IFRS has had in its creation of the ISSB. From here it is important as well to understand the support the ISSB has from preexisting ESG reporting groups.

International Sustainability Standards Board (ISSB)

As previously mentioned, one of the newest forming ESG Reporting standards comes with the ISSB. What is important to consider is the fact that the ISSB is still in its formation process; however, it has the backing of important players in the financial reporting realm which provides the ISSB with the potential to provide wide ranging regulation and improved information for investors across the world.

As described by Maurer (2021), the ISSB's first set of standards are expected to come in the second half of 2022 and are expected to follow in the same manner of the International Accounting Standards Board (IASB) which creates IFRS. While jurisdictions would have their own say in whether to utilize ISSB, with the widespread choice to adopt IFRS it will still provide countries with a baseline ESG reporting system to adopt which can then be further expanded upon by countries internal legislation requiring further. Across the world there are "144 jurisdictions (87 per cent of the profiles) that require IFRS for all or most domestic publicly accountable entities (listed companies and financial institutions) in their capital markets" as the IFRS (2018) reported. The widespread adoption of IFRS this provides strong credibility to the standards set by the ISSB. With this credibility there is a large market of potential adopters allowing for a further standardization of reporting on ESG. What is most compelling about the adoption of the ISSB is the ease of adoption and widespread impact that the standard has.

With the formation of the ISSB there is also support from existing ESG reporting groups which are consolidating. As previously mentioned, the SASB is one of the major reporting groups joining the ISSB to produce an all-encompassing reporting standard. In their statement about their consolidation, the SASB showed their expectation, “We anticipate that the ISSB’s standards will be adopted worldwide, through a combination of regulatory and market support.” (2022). The Climate Disclosure Standards Board (CDSB) is also consolidating with the ISSB to provide investor focused sustainability disclosure information. As the ISSB (2022) reported in its announcement “CDSB technical guidance will form part of the evidence base as the ISSB develops its IFRS Sustainability Disclosure Standards.” The ISSB is utilizing different existing reporting standards to condense reporting information and develop their own comprehensive reporting system.

While the ISSB is poised to have success in its implementation and use across the globe it is important to ensure that the information provided is being utilized to make environmental, social, and governance improvements. As Bouvier of the IPE reported on critics “the ISSB’s approach to sustainability reporting risks serving the interests of large asset managers and not those of wider society” (2022). As the ISSB is continuing to develop there are major considerations which need to be handled to ensure that it is both effective for investors in their decision-making process as well as effective in promoting positive ESG actions.

Other Developments in the Climate Reporting World

These reporting systems are developing as there are significant developments occurring across the ESG investing sector. While there has been significant progress, certain investing communities have been overstating their sustainable investing actions. Specifically, Kowsmann et al. (2021) reported on the fact that Deutsche Bank's "$1 trillion asset manager overstated its sustainable-investing efforts." With the increase in ESG investing and ESG reporting there has been an equal growth in the asset managers focusing on sustainable investing. This has provided incentives for overstatement of sustainable actions only possible due to the lack of ESG reporting standards. This had led to the SEC to consider "whether to require fund managers to disclose the criteria and data they use to apply labels such as green, low-carbon or sustainable." As Kiernan reported (2021). With the SEC considering requiring fund managers to report what sources are used for evaluating sustainable criteria are used, standardization of verifiable ESG data is important for fund managers and investors to have access to.

With the wide variety of reporting standards, investors, and business both find it difficult to make judgements on the information available. This is further exacerbated by hundreds to thousands of details about a company which can be evaluated. This leads to, as the Wartzman and Tang (2021) reported, "various components and subcomponents of ESG are often rolled up into a single metric." Wrapping up scores into a single metric leads back to the problem of not providing enough detail, and the line between too much and too little information must be balanced as reporting standards develop. This is compounded by the lack of standardization of scores. As Tariq Fancy (2021) the former chief investment officer for sustainable investing at Blackrock discussed "The scores vary from provider and provider and lack clear industry standards. And yet, these ratings give the impression to quantify the impact these funds are meant to create. That's a myth." While there are clear developments focused on the growth of reporting on ESG, professional investors focused on sustainability believe there need to be significant improvements. With improvement, investors will one day be able to not only invest in companies based on their ESG information, but also have the ability to trust that the information they are utilizing is accurate.

Chapter 3

Research Design

To help provide a better context to the problems that investors are currently facing when looking to invest in companies based on their ESG actions, I conducted interviews with ESG investing professionals to better understand the extent to the problems that they have been facing when looking to invest in companies based on their ESG actions. While there are some information problems which are clear on paper, what is further important is the real-world challenges that investors are facing when looking to make their decisions, and how these experiences have shaped where they have looked for information.

Research Question

As previously described, each of the current reporting frameworks has its own significant areas of expertise and its own drawbacks. To enhance our understanding of these problems I conducted qualitative interviews with experts in ESG reporting—primarily with private equity and venture capital firms, which have been the most important users of this information to date. My goals were to use the interviews as a vehicle to understand what problems investors are facing with respect to access to ESG information, what reporting frameworks are helping this problem, and how these investors would like to resolve this problem.

Participants

I conducted nine interviews which ranged from 15 to 30 minutes on Zoom which would provide further context to problems that the major ESG reporting systems had. I aimed to probe which data was accessible to investors, what data was most comprehensive, and what the drawbacks of the reporting methods were. The respondents had a wide variety of backgrounds:

- A partner at a VC fund investing in climate technology
- A VP leading their companies climate tech fund and investment efforts
- A principal in a company focused on energy technology investments
- A partner in a middle market private capital investment firm
- A senior analyst and director of ESG at an asset management firm with a commitment to ESG and sustainability
- An investment manager running the ESG investing for their firm
- Two directors at a firm focused on investing in real assets that address global challenges related to environmental and climate issues

I initiated the interview process through initial connections and contacts which were fostered through both Penn State Schreyer Honors College and Smeal College of Business alumni. The Penn State and Schreyer Alumni helped connect me with people with whom they have worked during their careers. In addition, I made some connections through the Smeal Center for the Business of Sustainability. As claimed on the Center for the Business of Sustainability's website "The center is oriented toward the business problems of scaling up technological solutions, promoting and strategically deploying new products and services, and devising a regulatory framework that fosters sustainability." Each of the groups to which I reached out helped me identify professionals who had investing experience and a focus on ESG and would be potentially able to identify and discuss problems that they have faced.

Overview of Interview Instrument

Once I made initial contact with the participants, I followed up by scheduling interviews based on the participants' availability and sending Zoom links and information about what to expect in the interview. I also included the consent guide (see Appendix A) with the Zoom invitation link. I conducted the interviews on Zoom so they could be recorded and subsequently transcribed to help provide more accurate details about the responses to questions by the participants. During the course of the interview, I asked participants the following questions:

- What specifically brought you to wanting to invest in companies that have high ESG values?
- What problems have you faced when trying to get information about the ESG actions of major companies?
- Is there a specific reporting system which has been able to provide you with more accurate information than other systems?
- What improvements would you make to increase the accessibility of information on the ESG actions of companies?
- Is there anything else you would like to add or that you think is important to understand?

After the conclusion of the interviews, I transcribed the Zoom calls in order to assess any qualitative trends in participants' responses to the interview questions that would reveal important insights about which major reporting systems were more accessible, which provided more accurate information, and what improvements investors are looking to see in order to help enhance their decision-making process and to allow for further analysis of the drawbacks that current investors are face when they attempt to make ESG-based investment decisions.

Chapter 4

Results

The interviews with professional investors provided insights into major trends which have been occurring across the ESG reporting field and provided real world context to problems that have been occurring in accessing information on companies ESG actions.

What specifically brought you to wanting to invest in companies that have high ESG values?

One of the first key points which came out of the interviews is that there has been significant growth within both the investing and reporting on companies based on their ESG activities. Since the participants invest money on behalf of both individual investors and pensions, they have fiduciary duties to those investors. As information about ESG activities has grown significantly, the demand from these investors has forced the participants to consider ESG in every investment they consider.

One participant mentioned that they specifically have experienced a pension fund putting pressure on them stating "we are not going to invest in you if you do not consider ESG in your investment decision making process." Another participant noted that the pension funds "realized private equity firms have been controlling the decisions and thus they could push the private equity firms to make a difference." This push from investors was noted in all interviews and has motivated them to increase the consideration of ESG when investing.

While they were pushed into focusing on ESG, what one participant noted is that investing in companies which value ESG could also be good for business. They brought up that not polluting could reduce the risk of getting fined. They also noted that if you are seen as a bad company for society, your valuation could go down. Another participant mentioned “having diversity in the organization drives diversity of thought” which would allow for the further incentivization of ESG. The main goal of the private equity and venture capital firms is to see high returns for their investors. With some PE and VC firms seeing higher returns for companies which reduce their pollution, and which work to increase diversity, these investors have been incentivized to invest in companies on behalf of their investors. Another participant mentioned that they have not seen ESG providing higher returns. For PE and VC firms who have and have not seen higher returns based on companies positive ESG actions, these investors are still considering ESG in their investment making decision.

What problems have you faced when trying to get information about the ESG actions of major companies?

While there has been pressure to consider the ESG actions of companies in the investment process, each investor had similar problems in doing so. The first of these major problems that they faced is small and startup companies rarely if ever provide information on ESG activities. There are many reasons which have deterred small companies from reporting about ESG activities which is not resolved by many of the previously researched reporting frameworks. Across the interviews every venture capital investor described the problem that small companies and startups do not have readily available ESG information and do not know how to report on it. To combat this lack of information the venture capital firms each decided what information they are looking for related to ESG and in their information gathering process asked the firms specific details that they need. They did not expect startup companies to be utilizing ESG reporting frameworks and had to source the information they needed from each firm.

This problem is heightened by the point which came out in one of the interviews that firms do not have the capital to provide detailed reporting information. One respondent shared their experience that startups "are normally focused on how they will make it to the next week" and thus do not have the resources to report or even know where to start or even what the standards are. While the VC firms may be focused on ESG due diligence, the actual companies in the startup stage do not have the capacity to provide the details needed. To resolve this lack of information, five of the respondents mentioned that they collected data yearly from companies they have invested in which allows them to get their footing and focus on reporting once they have the capacity to do so.

This lack of resources is also exacerbated by the prioritization of reporting by companies. "No one has objections to financial information that follows GAAP, but our investors have told us what [ESG] information we want, and we then forwarded it to the portfolio company, they might not provide the requested information." There is the expectation to provide financial information; however, providing ESG information does not face the same expectation. While there is a growth in the focus on ESG it still lacks the importance and falls to the wayside of both investors and companies. As one respondent stated "People have lots of other things that people need to track and ESG and DEI are not historically impacting their bottom line and are not causing companies to grow in value. What is the motivation to measure these things?" Even while ESG reporting has grown significantly over the past years, there still is a lack of prioritization, and when a company is reporting on their actions to investors, ESG reporting is lagging significantly behind.

The largest problem that has been mentioned and emphasized across every interview is that there is a lack of standardization. One respondent noted “Everyone comes at it from a different place, and everyone has different information that they’re willing to provide.” While there are countless standards out there providing frameworks for ESG reporting there is no central standard that every company utilizes which has forced the venture capital and private equity firms to each create their own standards and expectations on information to collect. There are many different methods of reporting, and each industry faces its own challenges that creates inconsistencies across the market. As one respondent said, each industry has its own pollutants that they are looking to measure and have their own issues. Accordingly, there is no standard which allows for both prioritization on what to report and standardization across the market.

There were also numerous other small issues that investors experienced. One mentioned that there are specific areas within ESG about which companies are less likely to report. For example, they noted that data privacy and security were areas about which companies were less likely to report, while there were issues like diversity where it was easy for companies to evaluate and report on and thus, they were able to find details like that easier. Another noted that companies only worried about quantify their environmental, social, and governance impacts once they were willing to go public and provided less comprehensive information to the VC firms until they were ready to go public.

Is there a specific reporting system which has been able to provide you with more accurate information than other systems?

Across the interviews there were no significant reporting systems that most participants utilized and what was important to understand was that the reporting frameworks that companies utilized came from the venture capital firms requiring companies to report using a framework. When a private equity or venture capital firm is looking to invest there is specific information that they are looking for to make their investing decision. Instead of seeing what information the company has the firms have instead gone to the companies and ask the companies to utilize a specific framework. This helps the VC and PE firms have standardized information that they can use and that they want. As they have done this each firm has had their own framework that they have either joined on as supporters of or have just decided to utilize. Some examples are the GHG protocol, Principles for Responsible Investment (PRI), GRI, SASB, Task Force on Climate-Related Financial Disclosures (TCFD), and the Global Real Estate Sustainability Benchmark (GRESB).

There have been a few major aspects that have been positive about these frameworks. For example, GRESB "provide asset level data, [where] it includes both sustainable information, but also provide information on the governance components. It allows for apples-to-apples comparison to companies that report with GRESB and has 3rd party verification." The GRESB for example is a framework which specifically is focused on the real estate sector, and thus is the best for the investing that this real estate sector. They also recommend the GRI for a more generalist focus, which is important to consider that each framework has its own benefit.

Some participants have also resorted to creating their own adjustments to the frameworks to ensure that the frameworks are tailor made to what information is looking they are looking for. For some this meant additions to existing frameworks and others it meant using these frameworks as guidance and creating their own criteria for evaluation.

There are also specific issues which companies are able to more easily report on that the participants have noted. For example, one participant said, "Governance is easy to find and is a part of how public companies have to think about their proxy voting and is built into how companies' function." Another participant also said in their own experience diversity and inclusion was easy for them to measure as they are specifically focused on startups. With the small number of employees that these firms have they can easily measure how diverse these firms are.

What improvements would you make to increase the accessibility of information on the ESG actions of companies?

The first and most major improvement that each participant mentioned was that there needs to be standardization in each industry so that companies' actions can be easily understood and compared with their activities. As previously mentioned in the problems that these participants had experienced, one of the most consistent problems that investors were experiencing was that there is a lack of standardization and companies of all shapes and sizes were both unsure on what information they would need to report on and did not have guidance on what information they should report on. Participants noted that it would be helpful for reporting companies by not only giving them outlined steps on how to report but also providing investors with detailed comparable information.

The other main takeaway about how to increase accessibility of ESG information would be with making reporting on certain ESG actions mandatory. While there are specific developments that have been pushing the industry towards mandatory reporting including recent developments where the SEC has been developing requirements for emissions reporting. Verney (2022) with responsible investor reported that all listed companies will be required to "disclose their Scope 1 & 2 emissions – those that arise from their activities and energy use – over the next three fiscal years, rolling out from the largest to the smallest firms.” There is still room to expand this requirement as the SEC as of March 2022 is considering a rule which “requires companies with a market value of $700 million or more to disclose relevant Scope 3 Emissions from the 2024 fiscal year.” While this requirement is set to impose reporting requirements on emissions, what is still missing is reporting on other key areas of sustainability and any consideration of social or governance reporting. This is where interview participants mentioned there needs to be further required disclosures. While there are currently steps being taken to make reporting accessible, there is still significant progress that need to be made to improve the accessibility of ESG information, and it begins by improving the reporting requirements.

Is there anything else you would like to add or that you think is important to understand?

Each participant had their own information which they wanted to add. This included stressing the importance of sustainability and highlighting the growth that ESG has had in their industry over the past 5 to 10 years, with even more growth since COVID began. Each participant has seen ESG grow and develop as they experienced “the wild west” as companies figured out how to be sustainable. As each company that they have worked for has worked to figure out how to keep up with the growth of ESG they noted that ESG is not going away, and investors and companies alike need to understand how to function in these changing times. With rapid change occurring in ESG reporting, it is up to everyone to make the necessary changes. It is up to companies to increase the information they report and to work to improve their sustainability, social policies, and governance. It is up to investors to set expectations about ESG reporting and look to invest in the companies which are making changes for the better. Finally, it is up to the reporting frameworks to guide investors and companies, while improving the access to ESG information across the market.

Chapter 5

Key Takeaways

With the significant developments which have pushed companies to consider their environmental, social, and governmental actions, the financial reporting world has had to tackle how they want to take on this challenge. As the major reporting standards of US GAAP and IFRS have decided to focus only on financial reporting, the major ESG reporting frameworks have the GRI, CDP, SASB, and the ISSB have been looking to increase the information they provide investors.

Each reporting framework has had its own challenges and successes in providing information on businesses actions. The GRI focused on a providing optional comprehensive standards that every company can utilize to guide their ESG reporting. The CDP focused specifically on sustainable reporting while providing comparable ratings for investors to utilize. The SASB focused on ESG reporting while looking to provide investors with just the information which is likely to impact their investment decision. There have been further ESG reporting frameworks forming including the ISSB which looks to create a comprehensive international reporting standard that countries across the world can implement.

Venture Capital and Private Equity investors have also experienced many of the challenges as they look to research on companies' ESG actions. As pressure from their investors has come to consider environmental, social, and governance issues they have been forced to look for ESG information. In this they have experienced a wide variety of accessible ESG information as each company has utilized their own standards and provided their own set of information to investors. With this lack of standardization across the industry, investors have had to either develop their own expectations and require companies to report with their own standards or promote a specific standard that they utilize. With these problems, investors are looking for two key changes in the current system: standardization and mandatory reporting.

As ESG reporting and frameworks continue to develop into the future there are many significant developments which if implemented will allow investors to make informed decisions to support companies which are working towards improving their impact on this planet. Everyone from investors, to reporting companies, to the frameworks have steps they can take to create more informed and educated sustainable investors.

Appendix A

Consent Form for Interview Participants

Consent for Exempt Research
The Pennsylvania State University

Title of Project: *An Evaluation of Challenges in Reporting for Environmental Social and Governance Criteria*

Principal Investigator: *Alexander Palmer*

Address: [redacted]

Telephone Number: [redacted]

Faculty Advisor: Samuel Bonsall

Faculty Advisor Telephone Number: [redacted]

You are being invited to volunteer to participate in a research study. This summary explains information about this research.

- This research is done through interviews to learn about your experience investing and what challenges you faced when looking to invest in companies which have positive ESG actions. This study will be a 15 to 30 minute interview which will be composed of 5 to 6 questions if time allows. The interview will be conducted by Alexander Palmer. It will be on zoom with the link to be provided once a time has been scheduled. This zoom audio and video will be recorded only to take accurate notes on what you have said and will then be subsequently deleted. Once finished, there will be no need for follow up. You are free to skip any question which you prefer not to answer.
- There is a risk of loss of confidentiality if your information or your identity is obtained by someone other than the investigators, but precautions will be taken to prevent this from happening. The confidentiality of your electronic data created by you or by the researchers will be maintained as required by applicable law and to the degree permitted by the technology used. Absolute confidentiality cannot be guaranteed.
- Efforts will be made to limit the use and sharing of your personal research information to people who have a need to review this information. Reasonable efforts will be made to keep the personal information in your research record private. However, absolute confidentiality cannot be guaranteed.
    - Information will be stored electronically only through the duration of the research and will be deleted following the completion of research.
    - In the event of any publication or presentation resulting from the research, no personally identifiable information will be shared.
    - We will do our best to keep your participation in this research study confidential to the extent permitted by law. However, it is possible that other people may find out about your participation in this research study. For example, the following people/groups may check and copy records about this research.
        - The Office for Human Research Protections in the U. S. Department of Health and Human Services
        - The Institutional Review Board (a committee that reviews and approves research studies) and Penn State's Human Research Protection Program.

If you have questions, complaints, or concerns about the research, you should contact Alexander Palmer at [redacted] or Samuel Bonsall at [redacted]. If you have questions regarding your rights as a research subject or concerns regarding your privacy, you may contact the Human Research Protection Program at 814-865-1775.

Your participation is voluntary, and you may decide to stop at any time. You do not have to answer any questions that you do not want to answer.

Your participation implies your voluntary consent to participate in the research.

BIBLIOGRAPHY

Berg, Florian, et al. "Aggregate Confusion: The Divergence of ESG Ratings." *SSRN*, 20 Aug. 2019, https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3438533.

Bouvier, Stephen. "SASB Delivers Update on ISSB Merger Progress." *IPE*, IPE, 9 Mar. 2022, https://www.ipe.com/news/sasb-delivers-update-on-issb-merger-progress/10058566.article.

Fancy, Tariq. "Tariq Fancy: The Fairytale of Sustainable Investing." *Responsible Investor*, 10 Feb. 2022, https://www.responsible-investor.com/tariq-fancy-the-fairytale-of-sustainable-investing/.

"FASB Staff Educational Paper - FASB Home." *FASB*, 19 Mar. 2021, https://www.fasb.org/cs/BlobServer?blobkey=id&blobnocache=true&blobwhere=1175836268408&blobheader=application%2Fpdf&blobheadername2=Content-Length&blobheadername1=Content-Disposition&blobheadervalue2=333644&blobheadervalue1=filename%3DFASB_Staff_ESG_Educational_Paper_FINAL.pdf&blobcol=urldata&blobtable=MungoBlobs.

Global Reporting initiative. "The Global Standards for Sustainability Reporting." *GRI - Standards*, 2021, https://www.globalreporting.org/standards/.

Governance and Accountability Institute. "65% Of the Russell 1000® Index Published Sustainability Reports in 2019." *2020 Russell 1000 Flash Report*, 2020, https://www.ga-institute.com/research-reports/flash-reports/2020-sp-500-flash-report.html.

Green Business Bureau. "ESG Reporting: Standards, Frameworks, Challenges and Benefits." *Green Business Bureau*, 3 Dec. 2021, https://greenbusinessbureau.com/topics/sustainability-benefits-topics/esg-reporting-standards-frameworks-challenges-and-benefits/.

GRI, et al. *Statement of Intent to Work Together towards Comprehensive ...* Sept. 2020, https://29kjwb3armds2g3gi4lq2sx1-wpengine.netdna-ssl.com/wp-content/uploads/Statement-of-Intent-to-Work-Together-Towards-Comprehensive-Corporate-Reporting.pdf?_hsenc=p2ANqtz-8YvirxZ02vOFBBs4TVWm4LTtO-F48b1lJXB1QVjSPZDst8jmUlvCGgd7my104uQHiPvJP4.

IFRS Advisory Council. *AP4: Update on International Sustainability Standards Board*. 10 Nov. 2021, https://www.ifrs.org/content/dam/ifrs/meetings/2021/november/advisory-council/ap4-update-on-international-sustainability-standards-board.pdf.

IFRS. "Climate Disclosure Standards Board." *IFRS*, 2022, https://www.ifrs.org/sustainability/climate-disclosure-standards-board/.

IFRS. “IFRS-Analysing the Use of IFRS Standards.” *IFRS*, 25 Apr. 2018, https://www.ifrs.org/use-around-the-world/use-of-ifrs-standards-by-jurisdiction/#analysis-of-the-166-profiles.

Kiernan, Paul. “SEC Considers Asking Funds for Criteria Used to Tout Sustainability.” *The Wall Street Journal*, Dow Jones & Company, 1 Sept. 2021, https://www.wsj.com/articles/sec-considers-asking-funds-for-criteria-used-to-tout-sustainability-11630513822?mod=article_inline.

Kowsmann, Patricia, et al. “WSJ News Exclusive | U.S. Authorities Probing Deutsche Bank's DWS over Sustainability Claims.” *The Wall Street Journal*, Dow Jones & Company, 25 Aug. 2021, https://www.wsj.com/articles/u-s-authorities-probing-deutsche-banks-dws-over-sustainability-claims-11629923018?mod=Searchresults_pos9&page=3.

Maurer, Mark. “Global Accounting Organization Launches Climate-Disclosure Rule Maker.” *The Wall Street Journal*, Dow Jones & Company, 3 Nov. 2021, https://www.wsj.com/articles/global-accounting-organization-launches-climate-disclosure-rule-maker-11635936301.

OECD. “More Efforts Needed from Governments, Regulators and Business to Unlock Full Potential of Sustainable Finance.” *OECD*, 29 Sept. 2020, https://www.oecd.org/newsroom/more-efforts-needed-from-governments-regulators-and-business-to-unlock-full-potential-of-sustainable-finance.htm.

SASB. “SASB Standards and the New International Sustainability Standards Board .” *SASB.org*, 2022, https://www.sasb.org/wp-content/uploads/2022/03/SASBStandardsandIFRSF-030222.pdf.

Smeal Center for the Business of Sustainability. “Center Vision, Mission, and Goals.” *Smeal College of Business- Center for the Business of Sustainability*, 2020, https://www.smeal.psu.edu/sustainability/about-us/vision-mission-and-definitions.

Steves, Rick. “Lack of Standardization Is Biggest Threat to ESG ...” *Finance Feeds*, 6 July 2021, https://financefeeds.com/lack-of-standardization-is-biggest-threat-to-esg-disclosures-research/.

Verney, Paul. “SEC Commissioners Propose Rule Requiring Large US Companies to Disclose 'Material' Scope 3 Emissions.” *Responsible Investor*, 22 Mar. 2022, https://www.responsible-investor.com/sec-commissioners-pass-rule-requiring-large-us-companies-to-disclose-material-scope-3-emissions/?utm_source=newsletter-daily&utm_medium=email&utm_campaign=ri-daily-bronze&utm_content=21-03-2022.

Wartzman, Rick, and Kelly Tang. “When It Comes to ESG, Companies Often Find It Hard to Stand Out.” *The Wall Street Journal*, Dow Jones & Company, 30 July 2021, https://www.wsj.com/articles/esg-companies-try-standing-out-11627592724?mod=Searchresults_pos14&page=3.

ACADEMIC VITA

Alexander E. Palmer

EDUCATION

The Pennsylvania State University | Schreyer Honor College — **University Park, PA**
Master of Accounting Program (MAcc) | Minor in International Business — Class of Spring 2022
College of Liberal Arts | Minor in German
University of Freiburg — **Freiburg, Germany**
Study Abroad Student — *Feb. 2019 - July 2019*

WORK AND INTERNATIONAL EXPERIENCE

KPMG — **New York, NY**
Advisory | Strategy Intern — *June 2021 - Aug. 2021*

- Created and edited client-facing deliverables in a $3.1 billion carveout as a member of the Separation Management Office, while coordinating between the HR, real estate, IT, finance and accounting, and legal entity groups
- Helped visualize census data in order to support the HR transition process, allowing the buyer to understand the seats needed to be filled for day 1 operation planning
- Dissected contracts in the separation process by searching for problems that will cause delays and identifying key information and steps to solve these separation delays

Rotteck Gymnasium — **Freiburg, Germany**
English Language Teacher | Smeal Campus Ambassador — *April 2019 - July 2019*

- Lead 5 lectures weekly to German students ranging from sixth to eleventh grade while providing first-hand exposure to the American culture and English language, and tailoring the curriculums to the different levels and understanding of the English language
- Collaborated with teachers in the Rotteck Gymnasium to improve their curriculum, better represent the American culture and provide an informative English education for students

LEADERSHIP AND ACTIVITIES

Penn State Dance MaraTHON — **University Park, PA**
THON Entertainment | Head of Timeline — *April 2021 – March 2022*

- Coordinated the logistics of the THON Weekend Timeline with the leaders of all 16 committees to ensure that the 46-hour dance marathon will run successfully
- Oversaw the timing and feasibility of every pre-THON event including the THON 5k, 100 days till THON Celebration, THON Involvement fair, and Family Carnival
- Worked as the diversity, equity, and inclusion chair for the entertainment committee where I worked on accessibility improvements including the inclusion of the first sign language translator for THON and closed caption for the livestream

THON Entertainment | Crowd Entertainment — *April 2020 – April 2021*

- Developed 3 hours of large-scale content, including both prerecorded and live events, to engage and ensure the wellness of the crowd during the THON Weekend Livestream
- Supported, inspired, and led 21 committee members in 2-hour weekly meetings as we developed and expanded Crowd Entertainment activities in a COVID safe virtual format
- Lead a weekly Crowd Focus Group of 43 Entertainment Committee members and 15 Entertainment Captains where we developed innovative ideas for Technology, Shared Crowd Moments, Theme Hours, and Wellness and Family Engagement

THON Supply Logistics Captain | Donor Contact — *September 2019 – March 2020*

- Planned, organized, and ran the Hershey Holiday Toy Drive by rallying the Penn State, THON, and Alumni communities to donate over $10,000 worth of toys to Penn State Children's Hospital in Hershey

Schreyer Honors College First Year Orientation — **University Park, PA**
Communications Team Leader — *Jan. 2018 – Jan 2020*

- Coordinated with the Schreyer Honors College faculty to communicate the events of Honors College Orientation and create the 40-page script of the events during the three-day orientation for the 55 mentors to follow
- Trained incoming mentors on the values of the Schreyer Honors College to have them lead groups of incoming freshmen

Scholar Advancement Team — **University Park, PA**
Schreyer Honors College Ambassador — *May 2018 – May 2021*

- Selected to provide insight to prospective students on life at the Schreyer Honors College through bi-weekly information session and tours of the Schreyer Honors College

HONORS SKILLS AND INTERESTS

Honors: Schreyer Honors College Academic Excellence Scholarship, Fred H. Shaefer Scholar Scholars Program
Skills: Working towards proficiency in Microsoft Office (Excel, PowerPoint, and Word), Working towards fluency in German
Interests: Biking, Penn State Football, Philadelphia Sports, Photography, Running, Travel (U.S and abroad)