Preparing for Climate Reporting Requirements

A Roadmap to ESG Compliance

Across the globe, climate regulations are fast approaching, and organizations are facing a series of burning questions:

"Are we prepared to share scenarios of how our operations will adapt to climate factors — including physical, legal, market and economic changes?"

"Is our company prepared to make disclosures on Scope 1, Scope 2 and, if necessary, Scope 3 impact?"

"Are we ready to do all of this in a timeline of months, rather than years?"

In March 2022, the U.S. Securities and Exchange Commission (SEC) put forward plans to require publicly traded businesses to outline the climate risks their operations bring about. Similarly, companies in the European Union must comply with increasing environmental, social and governance (ESG) obligations, with the EU Taxonomy Regulation applying from January 1, 2022. In the Asia Pacific region, the need to keep pace with peers, combined with a growing reputational risk, has led to dramatic growth in ESG reporting over the past half-decade.

What's more, across all regions, the vast majority of upcoming climate disclosures will be mandatory, not voluntary; they will likely cover both qualitative and quantitative information; and they are only a few of the sweeping changes on the horizon.

Combined with an ever-increasing investor and stakeholder focus on ESG, such developments could spell trouble for those organizations still relying on legacy systems and outdated processes for climate tracking and reporting. But specialized ESG reporting technology can offer a way forward. With the right solution in place, organizations can benefit in a number of ways — from tracking progress against ESG standards and frameworks to automatically updating compliance dashboards when new regulations arise. When it comes to scaling and maturing your ESG program, technology can integrate with your existing systems and grow with you.

Aligning SEC and ESG

With the recent SEC climate proposals dominating ESG headlines, and with those proposals likely to become requirements sooner rather than later, listed companies in the U.S. should ensure that any ESG technology solution they are evaluating can assist with the following tasks, at a minimum:

- Outlining and documenting Scope 1, 2 and 3 emissions
- Automatically updating compliance dashboards, reflecting new regulations as they arise
- Monitoring third parties
- Aggregating and collecting climate-impact data, with data sets updated automatically in real time
- Filing accurate, up-to-date statements and reports (on greenhouse gas emissions or net-zero plans, for example), and automatically generating auditable disclosures

Climate Urgency Is Increasing in All Areas of Business

As the focus on climate grows, it can be expected to permeate businesses at multiple levels. No matter the size of the organization, the industry in which it operates or the region in which it is based, companies must now dedicate time and energy to a full understanding of emerging frameworks — and they must get a firm grasp on how to track their Scope 1, Scope 2 and, where necessary, Scope 3 emissions, as well as reporting on reductions in greenhouse gas emissions or the progress of their net-zero plan.

To put it simply, audit-ready ESG metrics are fast moving from nice-to-haves to must-haves.

New disclosure regulations will require data, processes and technology that most organizations still don't have in place. Firms shouldn't wait until disclosures become an obligation to establish these systems; by then, it will be too late. The best way to prepare for new disclosure requirements is to start building an ESG reporting infrastructure now.

At a minimum, organizations should be tracking:

- The climate impact of their business operations, such as the energy use of their buildings and the carbon footprint of their business travel
- The climate impact of third parties and their supply chains

But why the sudden urgency to digitally transform climate reporting? It stems, in large part, from legacy systems simply not being up to the task.

Legacy Systems and Processes Can’t Keep Up with the Demands of Climate Reporting

Many climate-reporting systems used by organizations today are homegrown, several years old and highly specialized, making it difficult to add in new features and functionality as reporting demands evolve. Furthermore, few of these tools are capable of linking climate data to all of the areas in which it will have an impact. For many, this information exists in separate and disconnected systems. Coupled with outdated, often time-consuming and manual processes, this causes many organizations to find themselves ill-equipped to keep up with the rapid pace of change.

> “The importance of centralizing your climate data can’t be overstated — the core benefit being able to “collect once, reuse many times.” Demands from regulators will continue to grow and change, and shareholders and investors already have their own differing demands, which further complicates matters. Overloading high-value staff with the collection, aggregation and calculation of climate data for multiple frameworks using traditional workflow systems or spreadsheets is riskier and more error-prone than ever before. Only a purpose-built data collection tool built for the evolving nature of climate reporting will suffice.”

– Adrian Fleming, ESG Senior Commercial Director, Diligent

To understand why such inflexibility and disconnection are a problem, and why a new approach is necessary, it's helpful to look at the Task Force on Climate-Related Financial Disclosures (TCFD).

TCFD standards for climate reporting are increasingly popular worldwide and represent a new approach. Indeed, both the SEC's recent proposals and the G7 measures hew closely to TCFD recommendations, and many governments worldwide are already adopting this framework, including New Zealand, Switzerland, the U.K., China, Australia and Hong Kong. Moreover, TCFD recommendations go beyond metrics and targets to encompass governance, strategy and risk management.

Investors are requesting data of similar scope and detail as well. Whereas previously a few statistics related to energy savings and recycling may have satisfied questions about sustainability, now investors want a more holistic view of how climate links to corporate strategy and risk, with rigorous detail and tangible progress linked to promises.

Do all company operations meet Sustainable Finance Disclosure Regulation (SFDR) guidelines? Is your net-zero plan on track to meet its targets? Have shifts in return-to-work commutes and leasing arrangements altered the company's climate impact?

To answer questions like these confidently, organizations need to be able to close the data gaps between what they say they're doing and what they're actually doing when it comes to climate. They need to connect the dots between climate and business strategy. They must be able to adapt swiftly to a growing volume of disclosure demands and reporting requirements — while maintaining accuracy, productivity and efficiency.

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Additionally, successful climate reporting relies on a joined-up approach that is often neglected when organizations choose not to adapt their existing, siloed legacy processes. From haphazard document management to poor communication to a lack of oversight over third parties in the supply chain, the challenges that arise from an outdated approach to collecting and collating information can severely hinder the agility, speed and thoroughness that is needed for meaningful climate reporting.

> "You're going to need to be reporting on this for years to come, and reporting at an even more detailed level."
>
> – Matt DiGuiseppe, Former Vice President of Research and ESG, Diligent

As we've established, the vast majority of legacy systems and the processes that often go alongside them weren't built or designed for such work. But dedicated ESG reporting technology can be the difference between an organization simply treading water and one tackling ESG requirements head-on and thriving as a result.

With change not just around the corner but, in many ways, already here, let's take an in-depth look at how technology can help organizations to prepare for — and rise to — the ESG reporting challenges they face.

Where Legacy Systems Fall Short

Climate reporting requires a flexible, forward-looking system capable of handling a diverse array of requirements. Legacy systems fall short in a number of ways:

- They are often cumbersome and slow and are unable to interact with other systems or keep up with new ways of working
- They are often siloed, with different functionalities residing in different areas of the system
- They often don't have the functionality to keep abreast of the latest news and regulations, and don't provide insight into how peers and competitors are performing
- They fail to keep pace with the growing volume of disclosure demands and reporting requirements
- They can be expensive and time-consuming to run, diverting valuable organizational resources away from more important matters

Four Key Steps to Remaining Compliant with Climate Impact Regulations

1. Strengthen the CIO-Board Relationship

A fully realized ESG technology solution enables organizations to approach ESG with confidence. Whether it's reporting, managing data or simply ensuring that there's a futureproof system in place, ESG technology represents a marked step up from older systems and processes. But what capabilities should organizations look for — and why are they so important?

It goes without saying that accurate reporting is not possible without good data management. Data-rich organizations operate more efficiently, more decisively and with greater foresight than their peers — and this is particularly important when it comes to ESG.

The ESG data you collect will ultimately power the organization's tracking, reporting and collaboration, so it's vital to identify the right mix of internal and external data sources.

To assess your ESG data needs, start with the ESG goals you've laid out as an organization, as well as the frameworks you've selected. As you identify the data you'll need, take time to determine where it will be sourced — whether it is internal or external. Robust external data sets can be purchased from proxy advisory or consulting firms — or even from companies like Diligent, who specialize in governance data and peer group modeling.

Given the evolving nature of ESG regulations and a rapidly changing world, make sure that your chosen solution keeps your data relevant and timely. Ideally, your data sets — whether drawing from internal departments or external markets — should update automatically in real time.

Relying on old data not only limits the visibility of your ESG performance, but it serves as a warning to investors and stakeholders that your organization is not taking its ESG responsibilities seriously.

Become committing to any ESG solution, take the following actions:

- Learn from your peers and competitors. Take the time to analyze their ESG processes and disclosures. Monitor the news. Keep abreast of regulatory change.

- Involve all relevant business units in any discussion around data. Make sure that all those involved in monitoring and reporting on ESG are aligned on KPIs and are working within the same ecosystem.

- Memorialize your data aggregation and collection processes and keep track of where inbound requests for ESG information are coming from.

2. Embrace Automation

Climate reporting demands are in a constant cycle of evolution. For organizations mired with cumbersome legacy systems, keeping track of those demands can feel like an impossible task. But adopting a solution that utilizes robotic process automation (RPA) can make the task much easier, simpler and far less time-consuming.

RPA automates time-intensive and repetitive tasks, running data access, reporting and remediation tasks from end to end. Moreover, it is able to integrate across disparate departments and systems, bringing old and new together so organizations can leverage their legacy technology rather than adding on more systems or rebuilding their infrastructure from scratch. From gathering, preparing and analyzing information to monitoring and reporting on data, RPA streamlines what were previously manually driven information-gathering processes into something much more seamless and much less prone to error. It is a tool that brings the right data to the right people at the right time.

Climate issues, now more so than ever, can impact operations at many levels. Before evaluating and selecting any RPA technology solutions, make sure to take the following steps:

- Build a list of time-consuming, repetitive tasks in your climate-related operations. One place to start is with the spreadsheets teams use on a daily or weekly basis.
- Calculate how much time staff currently spend manually collecting and analyzing data — and troubleshooting issues — in these areas.
- Consider the accuracy of your climate reporting, both internal and external. Where are you least confident that teams are collecting the most up-to-date, relevant data?
- Identify your biggest pain points in climate-related data collection and analysis. Deadlines? Document versioning issues?
- Map the problem areas above against the goals of individual teams and the entire organization.

3. Monitor and Report

Are your ESG initiatives meeting expectations, deadlines and commitments? Is data being consistently disclosed across stakeholders and frameworks? An automated ESG solution can help boards and executives keep their fingers on the pulse of activities and progress — and spot red flags before they escalate into bigger issues.

A dashboard, particularly a customizable one with real-time data, can give your organization visibility into KPIs, metrics and commitments. Automated monitoring can help ESG teams sift through mountains of information in a fraction of the time.

When telling your ESG story, it's important to remember that no organization needs to start from scratch. ESG is a broad umbrella: Take inventory of the impactful activities your organization is already doing as a starting point.

As regulations continue to evolve, organizations must also make sure that their ESG reports are meeting expectations, deadlines and commitments. Look for a technology solution that can automatically generate auditable disclosures from your ESG data and dashboards. In the months and years ahead, it will be increasingly important to make sure that all changes and values are tracked for a robust audit trail. The ability to prepopulate ESG assessments with existing data not only makes the process more efficient, but easier to refer to when needed.

Before committing to any ESG solution, ensure that:

- ☐ The ESG technology platform you choose makes reporting seamless, with reporting and data collection capabilities located under one roof.
- ☐ The platform can aid you in communicating your ESG progress in a compelling way, helping to ensure stakeholders get the message. Ensure key talking points extend across proxy materials, sustainability reports and your conversations with investors.

4. Enable Adaptability and Scalability

As months and years pass, regulations and reporting frameworks will evolve. In tandem, the operational and disclosure needs of your organization will also increase. Whereas legacy systems — cumbersome and segregated – are ill-equipped to deal with such change, an automated ESG operating system can grow with you, easily integrating with existing systems and evolving with your organization.

Given the complexities and variability of ESG tracking, monitoring, reporting and compliance, a solution that doesn’t need reconfiguring and recalibrating is crucial. Different industries use different ESG frameworks and have differing stakeholder expectations. Laws and regulatory requirements vary across jurisdictions and each organization has its own people, processes and practices for managing ESG issues.

A good ESG solution must enable them to act quickly and easily, now and in the future. Boards must be able to tailor features to their specific roles, regulatory environments and reporting requirements.

Ultimately, any solution needs to accommodate an organization wherever it stands in its ESG journey — and evolve as the organization’s needs evolve. Before committing to any ESG solution, ensure that it can:

- Easily track shifting investor and stakeholder expectations.
- Work with your current level of ESG maturity and grow as you do.
- Help map ESG data to your internal objectives.

Prepare Today for Tomorrow's Disclosure Requirements

A mature ESG program with the right components in place will pave the way toward seamless compliance with future disclosure requirements.

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