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ESG Reports and Ratings: What They Are, Why They Matter

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Editor's Note: Betty Moy Huber is Counsel and Michael Comstock is an associate at Davis Polk & Wardwell LLP. This post is based on a Davis Polk publication by Ms. Huber and Mr. Comstock.

Most international and domestic public (and many private) companies are being evaluated and rated on their environmental, social and governance (ESG) performance by various third party providers of reports and ratings. Institutional investors, asset managers, financial institutions and other stakeholders are increasingly relying on these reports and ratings to assess and measure company ESG performance over time and as compared to peers. This assessment and measurement often forms the basis of informal and shareholder proposal-related investor engagement with companies on ESG matters. Report and ratings methodology, scope and coverage, however, vary greatly among providers. Many providers encourage input and engagement with their subject companies to improve or sometimes correct data. There are currently numerous ESG data providers, a summary of each of which is beyond the scope of this post, but some well-known third party ESG report and ratings providers include: (i) Bloomberg ESG Data Service; (ii) Corporate Knights Global 100; (iii) DowJones Sustainability Index (DJSI); (iv) Institutional Shareholder Services (ISS); (v) MSCI ESG Research; (vi) RepRisk; (vii) Sustainalytics Company ESG Reports; and (viii) Thomson Reuters ESG Research Data. This post provides an overview and analysis of these providers. [1]

This post also provides information on the ESG ETFs and portfolios offered by the following asset managers, which are based in part on these ESG reports and ratings: (i) BlackRock; (ii) The Vanguard Group; (iii) State Street Global Advisors (SSGA); (iv) BNY Mellon Investment Management; (v) PIMCO; (vi) Fidelity Investments; (vii) J.P. Morgan Asset Management; (viii) Wellington Management Group LLP and (ix) Prudential Financial.

Bloomberg ESG Data Service

Overview

In 2009 Bloomberg acquired New Energy Finance, which provides information regarding renewable energy and the carbon market, and subsequently launched Bloomberg ESG Data Service. Bloomberg collects ESG data for over 10,000 publicly-listed companies globally. ESG data is integrated into Bloomberg Equities and Intelligence Services. Bloomberg ESG Disclosure Scores rate companies annually based on their disclosure of quantitative and policy-related ESG data.

Market Cap Coverage: Mid Cap (more than \$2 billion) to Large Cap (more than \$10 billion).

Rating Scale and Methodology

Rating Scale: Out of 100. Bloomberg also provides scores from third party rating agencies (RobecoSam, [2] Sustainalytics, [3] ISS Quality Score, [4] and CDP Climate Disclosure Score [5]) and an overview of a company from an ESG perspective both historically and relative to peers.

Methodology: Bloomberg evaluates companies on an annual basis, collecting public ESG information disclosed by companies through corporate social responsibility (CSR) or sustainability reports, annual reports and websites, and other public sources, as well as through company direct contact. This data is checked and standardized. Bloomberg ESG data covers 120 environmental, social and governance indicators including: carbon emissions, climate change

effect, pollution, waste disposal, renewable energy, resource depletion, supply chain, political contributions, discrimination, diversity, community relations, human rights, cumulative voting, executive compensation, shareholders' rights, takeover defense, staggered boards, and independent directors. Bloomberg ESG rating will penalize companies for "missing data."

Reputation and Usage

In 2016, Bloomberg had over 12,200 ESG customers, providing ESG data to mainstream investors worldwide.

II. Corporate Knights Global 100

Overview

Corporate Knights, a Toronto-based company, publishes an annual index of the Global 100 most sustainable corporations in the world in their Corporate Knights magazine. The Corporate Knights magazine is the world's largest circulating magazine focused on sustainability and responsible business.

Rating Scale and Methodology

Rating Scale: Out of 100 and ranked against other companies in the same industry group. Updated annually.

Market Cap Coverage: All companies that have a market capitalization in excess of \$2 billion.

Methodology: Ranking is based on publicly disclosed data and is released annually in January. All industries and geographies are considered and 14 key performance indicators are analyzed, covering supplier performance and resource, employee and financial management. Companies are scored only on relevant performance indicators for their specific industry.

Company Involvement: Companies are invited to participate in a formal data verification process prior to publication of the list.

Reputation and Usage

- The Corporate Knights magazine reaches 380,000 of the world's most influential business and political decision-makers.
- Out of the top 10 corporations listed on the 2017 Global 100, 4 out of 10 companies had published a press release regarding this listing. [6]
- Corporate Knights Global 100 data is available on both Bloomberg and Reuters.

III. Dow Jones Sustainability Index (DJSI)

Overview

Launched in 1999, DJSI was the first global index to track sustainability-driven public companies based on RobecoSAM's ESG analysis. S&P Dow Jones Indices has partnered with RobecoSAM for publication and calculation of ESG indices. DJSI is broken down into: DJSI World (tracking the world's leading companies), DJSI Regions and DJSI Country.

Market Cap Coverage: Small Cap (less than \$2 billion) to Large Cap (more than \$10 billion).

Rating Scale and Methodology

Rating Scale: Out of 100 and ranked against other companies in their industry. Updated annually.

Methodology:

DJSI World: This index represents the top 10% of the largest 2500 companies across 60 industries in the S&P Global BMI (Broad Market Index). [7] Scores are derived from RobecoSAM's annual Corporate Sustainability Assessment (CSA) whereby 2,500 publicly traded companies are invited to participate in the CSA for possible inclusion in the DJSI World. An industry-specific questionnaire is sent to the participants covering relevant economic, environmental, and

social factors. There are generally 80-120 questions in a questionnaire. DJSI World covers 100 ESG issues. An annual questionnaire is sent in early April and CSA results are announced in early September.

Questions cover economic, environmental, and social governance topics such as: Corporate governance, risk and crisis management, codes of business conduct, customer relationship management, policy influence, brand management, tax strategy, information security & cybersecurity, privacy protection, environmental reporting, environmental policy & management systems, and operational eco-efficiency.

DJSI North America: This index represents the top 20% of the largest 600 North American companies in the S&P Global BMI. Scores are derived from RobecoSAM's annual Corporate Sustainability Assessment.

DJSI Europe: This index represents the top 20% of the largest 600 European companies in the S&P Global BMI. Scores are derived from RobecoSAM's annual Corporate Sustainability Assessment.

DJSI Asia Pacific: This index represents the top 20% of the largest 600 companies in the Asia Pacific region in the S&P Global BMI. Scores are derived from RobecoSAM's annual Corporate Sustainability Assessment.

DJSI United States: This index represents the top 20% of the largest 600 U.S. companies in the DowJones Sustainability North America Index (see above).

Company Involvement: Companies are provided with feedback to help them improve and enhance their score and performance.

Reputation and Usage

- Partnered with RobecoSAM.
- Out of 10 Industry Group Leaders listed on the 2016 DJSI, all 10 companies published a press release regarding this listing. [8]
- Dow Jones Sustainability Indices are published on RobecoSAM's website and are publicly available.

IV. ISS

Overview

ISS provides a suite of ESG solutions to enable institutional investors to develop and integrate responsible investment policies and practices into their investment decisions, to inform company engagements and to execute upon these policies through end-to-end voting. In 2015, ISS acquired Ethix SRI Advisors and formed a strategic partnership with RepRisk [9] allowing ISS to further expand the ESG and socially responsible investing (SRI) research it provides. ISS's solutions also include climate change data and analytics from its recent acquisition of Climate Neutral Investments. ISS's ISS QualityScore provides in-depth research on corporate governance on over 5,600 publicly-traded companies globally.

Rating Scale and Methodology [10]

1. ISS Quality Score

Rating Scale: 1st to 10th decile (overall score and score for each pillar described below). 1st decile indicates relatively higher quality governance practices and relatively lower governance risk while a score in the 10th decile indicates relatively higher governance risk. Updated on an ongoing basis.

Methodology: ISS analyzes over 200 factors, divided into four pillars: board structure, compensation/remuneration, shareholder rights, and audit & risk oversight. Depending on the governance standards in each region, the ISS voting policy, and the impact on governance practices, a specific weight will be placed on each factor.

Specific factors include: for board structure (board and board committee composition, board practices, board policies, related party transactions and board controversies), for compensation/remuneration (pay for performance, non-performance based pay, use of equity, equity risk mitigation, non-executive pay, communications and disclosure, termination and controversies), for shareholder rights (one-share one-vote, takeover defenses and meeting and voting related issues) and for audit and risk oversight (external auditor and audit and accounting controversies). [11]