

ESG Report

in 8 Steps

denxpert



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1. Introduction

“Society is demanding that companies, both public and private, serve a social purpose. To prosper over time, every company must not only deliver financial performance, but also show how it makes a positive contribution to society. Companies must benefit all of their stakeholders, including shareholders, employees, customers, and the communities in which they operate.”

Excerpt from letter to CEOs from Larry Fink, BlackRock chairman and CEO.

For a cleaner, more secure and more sustainable world, it is essential for every company to recognize the importance of **Environmental, Social and Governance (ESG)** risks, and to manage them appropriately in line with business objectives.

ESG is a still-dynamically developing framework that serves to help evaluate the sustainable operations and long-term flexibility of companies. Corporate financial partners are increasingly demanding sound corporate strategies and programs for sustainability.

A strong ESG program will stand its ground in the long run, responding to investor needs and societal change, whether the focus is on understanding key areas, setting goals, designing schedules, introducing metrics or tracking progress.

But what exactly is ESG, how does it relate to sustainability, why is important and for whom? How should a company approach the 'ESG question', and how does it fit with the existing framework of the company's business operations, the size of the company and the expectations of its stakeholders? This e-book seeks to find answers to these questions.

2.

What is meant by ESG?

ESG has three pillars: Environment, Social and Governance. Together, these three aspects form a framework that is used to help evaluate a company's performance in terms of long-term sustainability and well-being. For many investors, it is not enough to address only two of the above aspects and ignore the third. Instead, they are looking for carefully planned, forward-thinking programs in all three areas.





Environment

Here, environment includes issues related to carbon dioxide and other pollutant emissions, disposal procedures, resource efficiency, waste management, biodiversity, and relationships with environmental regulators.

Investors are particularly interested in issues related to environmental responsibility. An excellent environmental program is a representation of the company's commitment and ability to minimize its environmental impact.



Social

The social pillar is concerned with how the company manages its relationships with its employees, customers, suppliers, partners, and local communities. This includes, but is not limited to, how employees are treated, benefits, and diversity.

It is important for a company to have a defined social 'policy', a set of social values, and a demonstration of how these are (or are not) put into practice. Human rights issues, procurement processes, customer service, consumer protection and the company's impact on local communities are also criteria to consider.



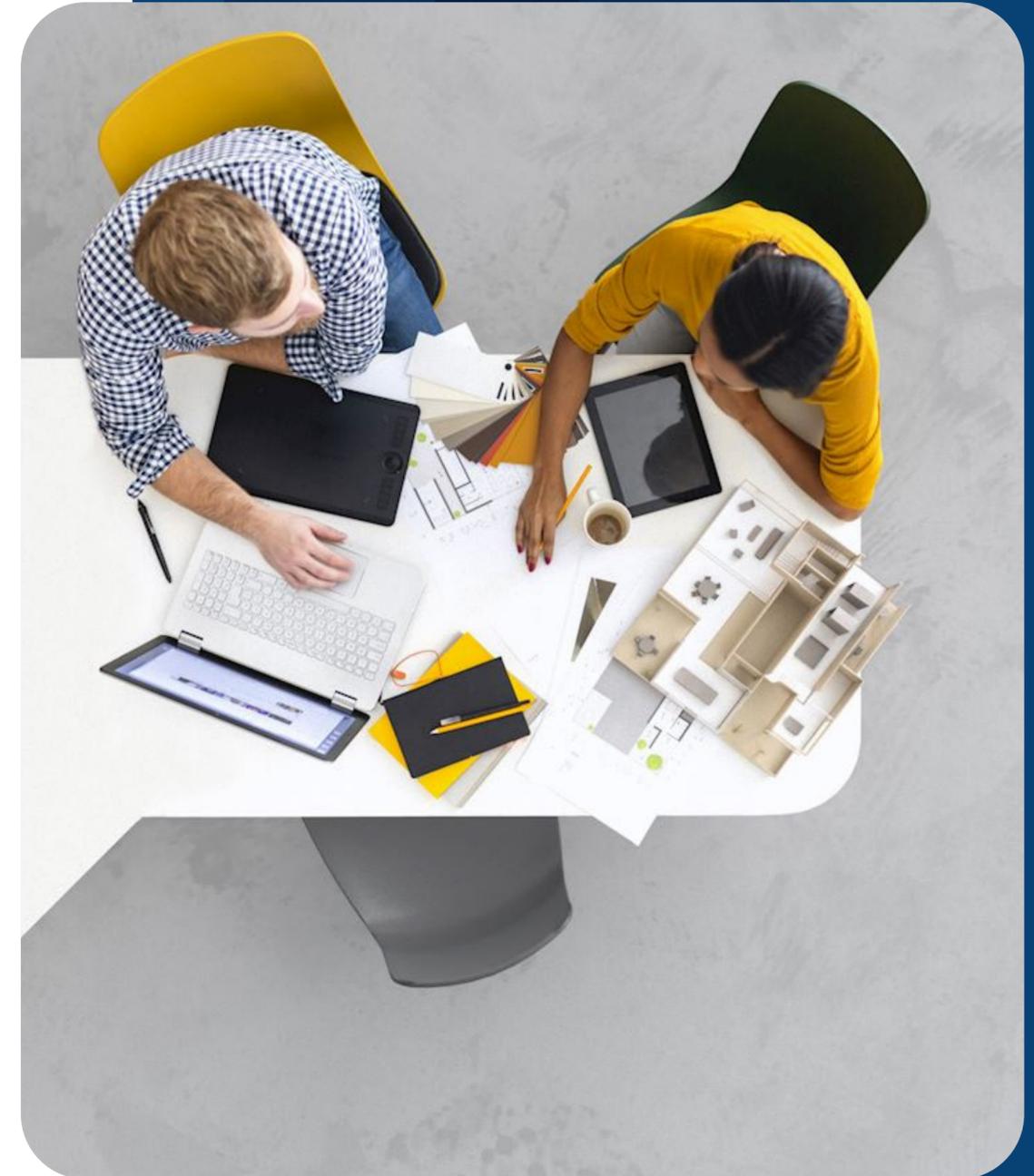
2.3

Governance

This pillar includes the extent to which management integrates sustainability considerations into corporate governance processes. Examples include cooperation with stakeholders (shareholders, investors, employees, partners, etc.), incentives, executive remuneration, and key indicators of success from a sustainability perspective. At the same time, attention must also be paid to corruption cases, conflicts of interest, transparent operations and the leadership hierarchy.

While two decades ago such a framework would have been classified as a special interest, today it is a basic expectation. Buyers want to avoid the risk of an unpleasant surprise after completing an acquisition.

ESG helps bring relevant (non-financial) business risks and liabilities to the surface so that customers can make more informed decisions while also supporting sustainable investments.



3.

Why is ESG so important?

An increasing number of correlations have been identified of cases where adverse environmental and social impacts have affected previously successful business activities, even while complying with applicable legislation.

We see such connections in relation to **global climate change**: over the decades, **greenhouse gases** were emitted over the decades while the consequences were ignored. Today, this is a global problem. Now that climate change has been scientifically proven, we need to devote huge resources to making our daily lives carbon neutral and adapting to climate change. This is especially true for large companies whose business is based on the use of fossil fuels.

Similarly, inadequate treatment of **plastic waste** has become a factor that influences opportunities for the next generation. We now know that plastics break down into small particles in the environment and can be detected throughout the food chain. Today, we also see the packaging materials of global brands drifting in rivers and seas, something which also reflects poorly on the brand manufacturer.

Depletion of raw materials: whether it is water or the raw materials needed to produce food or batteries, some resources are limited, or in some cases global climate change is reducing access. It is often as a result of productive activity that an important resource becomes limited for local communities. These factors can significantly affect the predictability and efficiency of production, the length of the supply chain, or even the reputation of the company.

Especially at the beginning of global value chains, the **inadequate working conditions** or poor income conditions of those working in extraction and manufacturing plants are equally important issues in terms of a company or brand's reputation.

Consumers are becoming increasingly sensitive to the above consequences. The costs of environmental and social damage are borne and paid by local communities, governments or, if there is a global impact, by everyone. In addition to portraying the perpetrators of any issues in a bad light, social burdens can also have repercussions on the way a company operates in the form of restrictions, inaccessible natural and human resources, and declining purchasing power.

In other words, it is partly a question of **social responsibility**, but also of **business risk**. There are material, moral and/or reputational risks that may result in significant losses to the value of companies as a result of environmental damage or scandal. In addition, these problems can, of course, be seen as a new opportunity, as companies that respond to sustainability issues thoughtfully and in a timely manner can earn an advantage over their competitors or gain new markets by transforming their products or business models.

As a result, in addition to economic performance, sustainability performance is also playing an increasingly important role in assessing the value, prospects and confidence of companies. This means that companies are under increasing pressure to disclose their sustainability information, often referred to as non-financial information, together with – and with a similar weight and consistency to – financial data.



The risks and opportunities for sustainability are not easy to see: complex, interdisciplinary knowledge is required. As a result, in order to interpret its sustainability performance, a company requires:



**Uniform,
standardized
methods**



**Scientific
validity**



Precise data



**Easy-to-understand
information**

For this reason, ESG provides a framework for interpreting non-financial data, making the risks of environmental and social impacts visible and understandable to investors and also decision-makers who are less familiar with technical, scientific and social issues.

It is therefore understandable that there is a great deal of interest in ESG, as increasingly stringent investment strategies in the field of sustainability favor companies with ever-lower risk ratings, which in turn makes it easier for these companies to raise funds. A number of green loan programs already exist to finance sustainable activities. The essence of these programs is that companies with a good ESG rating can obtain credit at a lower cost to develop their activities.

In other words, in addition to the financial results of a business, there is an increasing market expectation that companies, beyond financial reports, should also report on the environmental and social impacts that accompany their activities.

Factors affecting operation

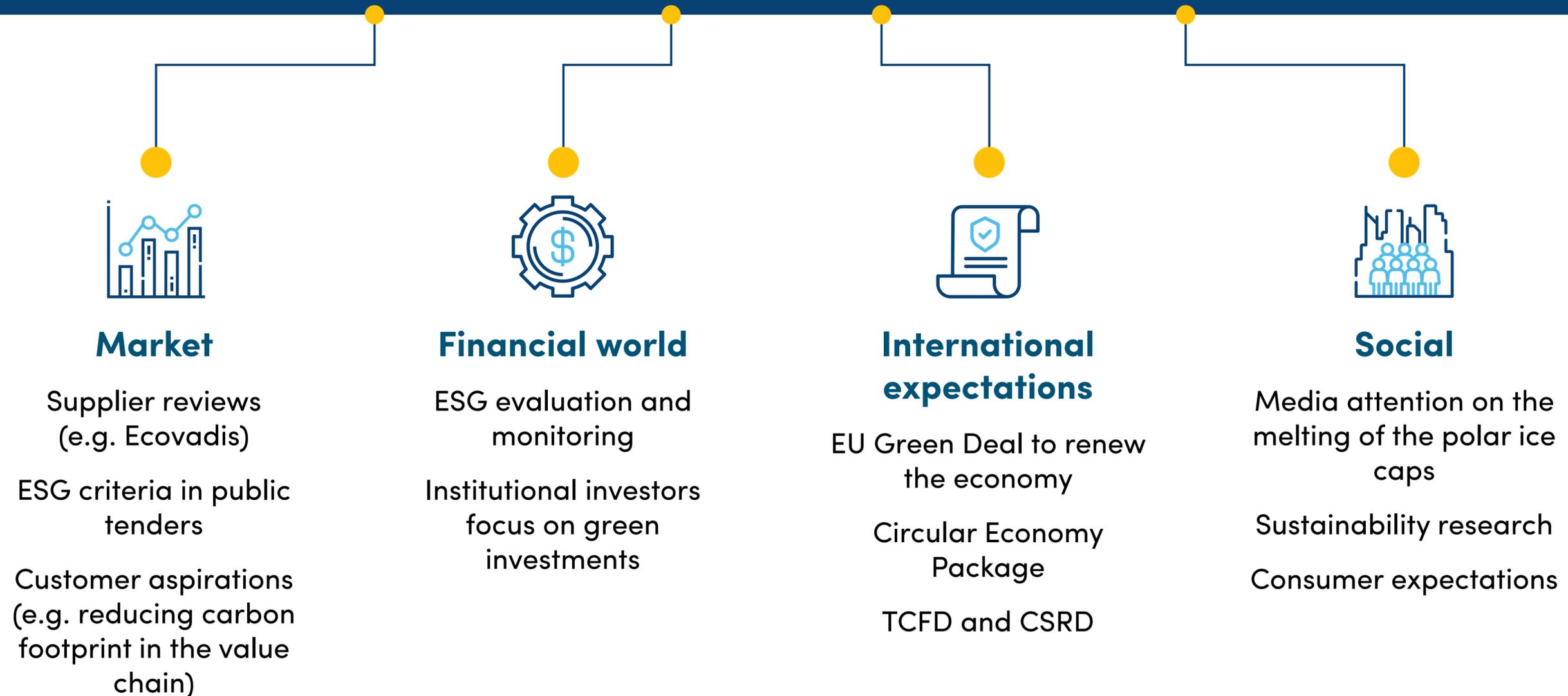


Figure 1: System of market and social expectations for companies

4.

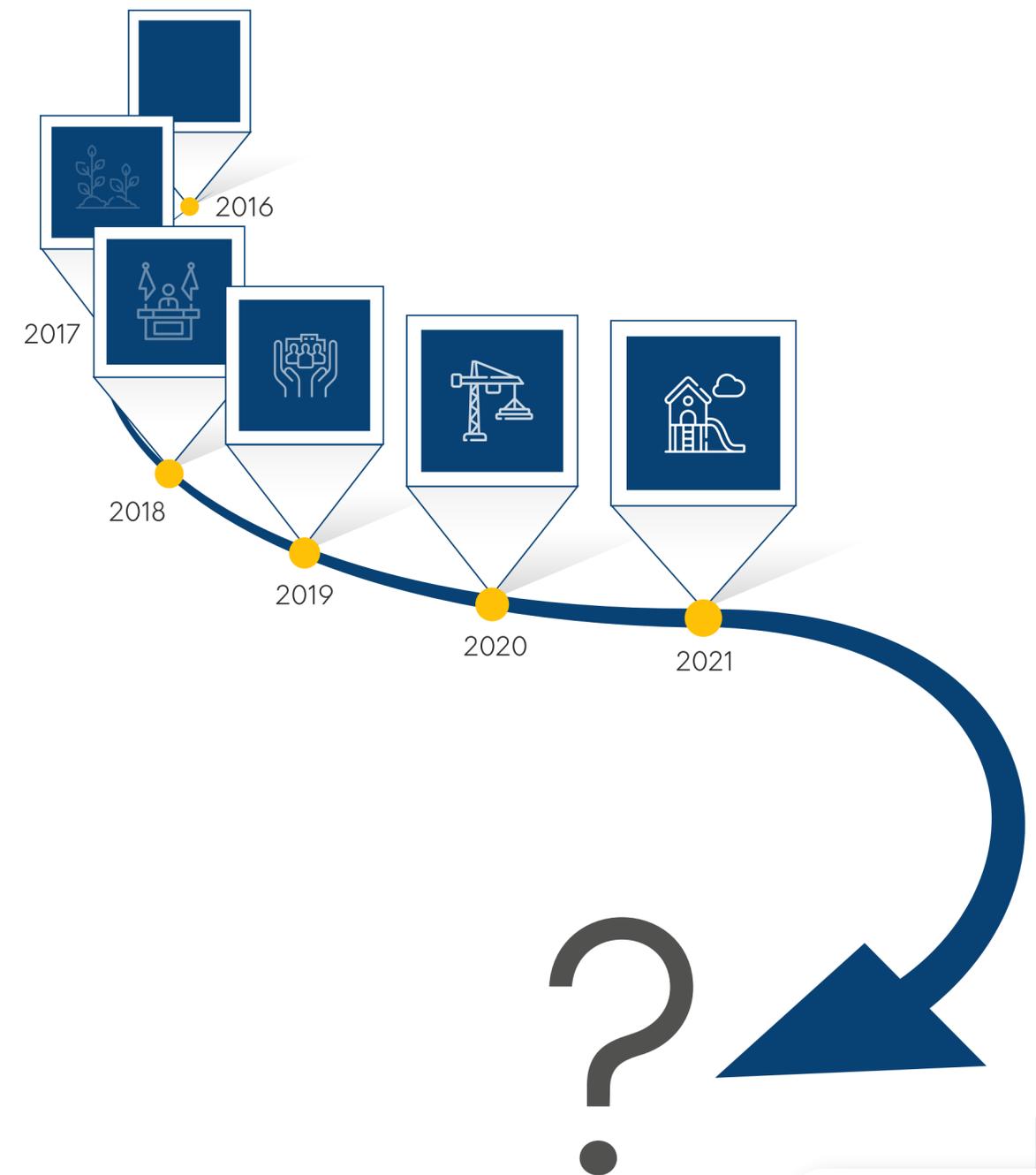
CSR, Sustainability and ESG reports – features and differences

These concepts emerge in parallel, often as synonyms for each other, although there are significant differences to the expert eye. It is not only difficult for company directors to navigate the growing number of requirements, but also for experts in the field.

4.1 CSR

At the same time, **CSR (Corporate Social Responsibility) reports** provide details on the company's related programs, and have some specific features:

- They are retrospective – they present the grants and programs of the recent period. If they do look ahead, CSR reports only do so in the short term and in general
- No indicators, or key performance indicators (KPIs) – programs are not driven by KPIs and are not linked to 'results'
- They do not include long-term goals, strategic goals (e.g. climate change program for 2030 or 2050)
- They do not necessarily reflect the main environmental and social impacts of the company
- CSR is not value chain-based, it is more about forming opinions than about reducing impact
- The main goal is to increase the image, build (local) relationships, and improve the perception of the company in the eyes of employees (employer branding)

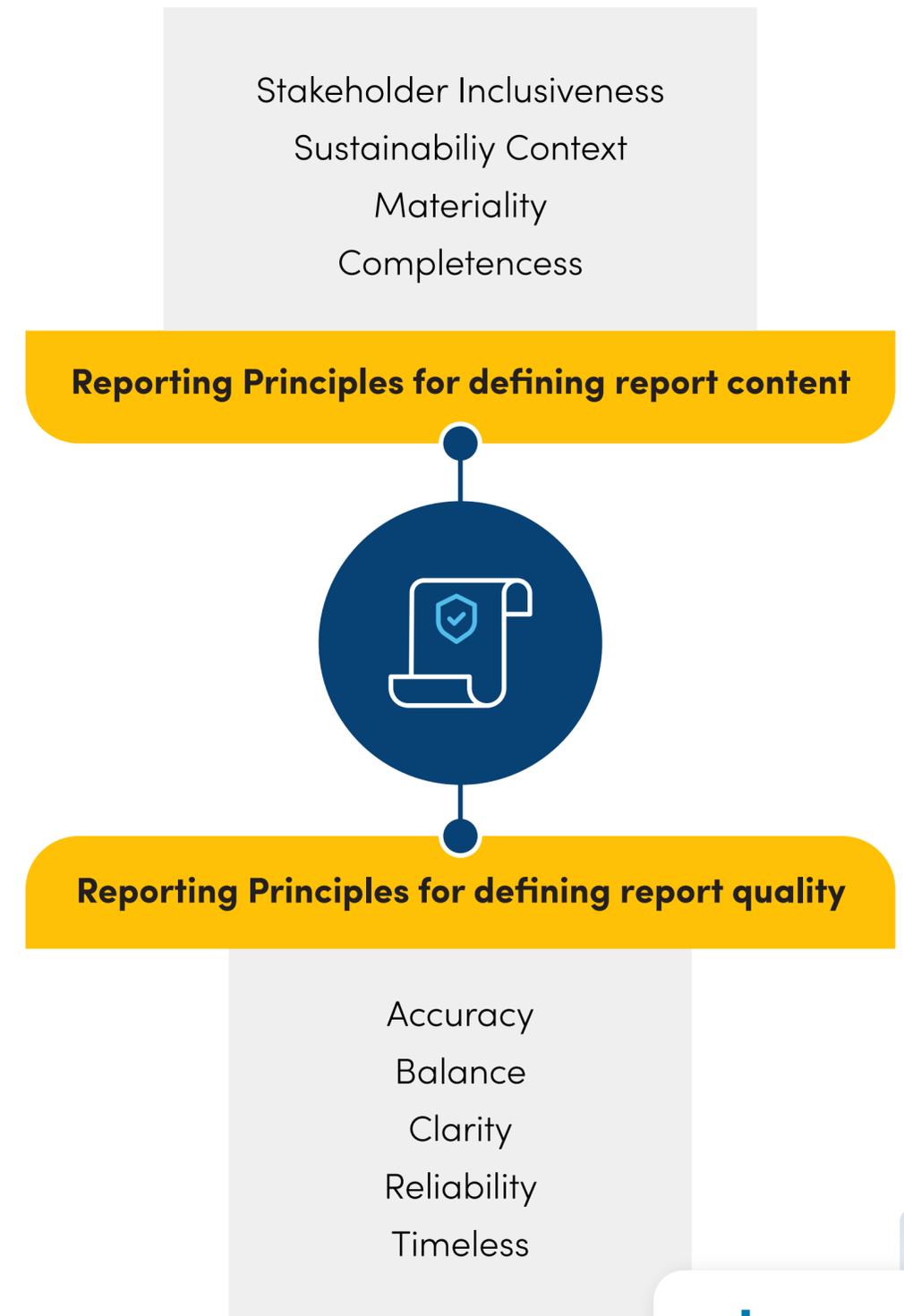


4.2 Sustainability

Sustainability reports, although similar to CSR reports, differ in key respects:

- A sustainability report is a forward-looking statement defined by international standards and expectations (e.g., the Global Reporting Initiative – GRI). This standard ensures that the report is about what is important to stakeholders about the company's operations, and not just what the company wants to emphasize its results in
- It focuses on standard-defined performance indicators and metrics
- In addition to the direct effects of the activity, it also affects the sustainability issues that appear in the entire value chain of the given activity
- It formulates goals and commitments
- Basis of the report:
 - 1) Stakeholder consultation (on what is expected)
 - 2) Materiality assessment (what is important, relevant to the stakeholders, the natural, social environment and the company). 'Double materiality' is a new concept that also takes into account the financial impact of a given case on a company

Figure 2: Sustainability reporting guidelines



4.3 ESG

ESG is a **system of risk-based evaluation criteria** that makes the company's sustainability performance and risk interpretable for the financial and investing world. At the end of the process, the company is provided with a rating similar to a credit rating. Such a classification creates a clear and unambiguous decision for investors – according to their investment policy, they can decide whether or not to invest in a particular company.

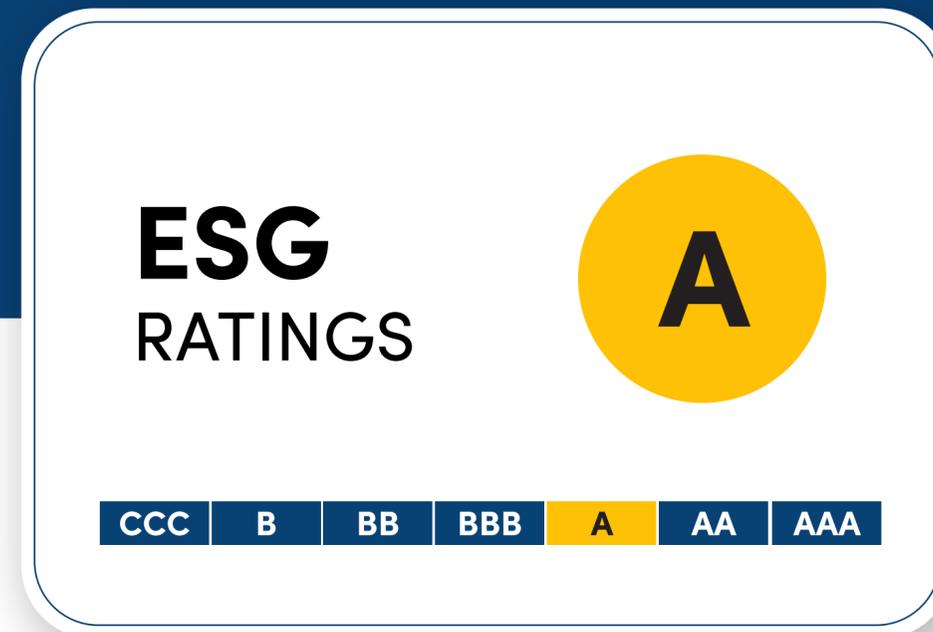


Figure 3: ESG Rating example

5.

Is reporting required?

ESGs of some large global companies are evaluated regularly and automatically. Smaller companies need to request the evaluation. An ESG rating is particularly recommended if a company wants to appear in the capital markets, for example – if it wants to go public or is looking for institutional investors.

The situation is different when it comes to the sustainability (non-financial) report on which the ESG assessment is based. Issuing sustainability reports is a long-standing, voluntary option for companies. In recent years, international guidelines, and later standards (e.g. GRI Standards), have been published to improve and standardize the quality of reports. Current processes point to a standardization of reporting standards.

In order to achieve Europe's sustainability goals, it is essential that companies provide better data on their sustainability risks and their impact on people and the environment.

All of this can help strengthen the relationship between companies and society, as well as provide an opportunity for businesses, investors, civil society and other stakeholders to improve the way information on sustainability is communicated and used.

The issuance of a sustainability report is therefore not mandatory, but it is recommended to inform stakeholders on the subject, regardless of the regulations. Several regulations currently in force for the publication of ESG data and the issuance of a sustainability report apply to certain large companies.

- 1** Under the **Non-Financial Reporting Directive (NFRD)**, since 2018, listed companies, credit institutions, investment firms and insurers have been required to report their ESG data and sustainability performance above a certain size.
- 2** **Sustainable Finance Disclosure Regulation (SFDR)**. The Sustainable Finance Disclosure Regulation imposes ESG disclosure obligations on asset managers and other financial market participants from 2022 onwards.
- 3** For financial stakeholders, the **EU Taxonomy** makes clear exactly what criteria certain activities can be considered sustainable. The Taxonomy criteria system appears in both NFRD and SFDR reports to identify the sustainability of activities.
- 4** In the near future, as a result of stronger EU incentives, the NFRD will be replaced by the **Corporate Sustainability Reporting Directive (CSRD)**, which is expected to extend reporting to small and medium-sized enterprises based on a standardized reporting standard.

5.1 Who is affected by CSRD?

The CSRD will replace the current Reporting Directive (NFRD) after 2024. Under the current version of the CSRD under preparation, significantly more companies in the EU will have to report their non-financial data on their sustainability performance than before (NFRD).

The CSRD applies to all large companies and all organizations with securities listed on EU regulated markets, with the exception of micro-enterprises.*

It is not just large companies that need to publish their sustainability reports. According to the EU proposal, listed small and medium-sized enterprises may also be affected by the regulation, though they will be subject to simpler rules than large companies.

** Large company: According to the Accounting Directive, companies that exceed the thresholds of at least two of the following three criteria: a) balance sheet total: EUR 20 million, b) net sales: EUR 40 million, c) average number of employees during the financial year: 250. Subsidiaries: Under the proposed new regulation, subsidiaries will be exempted from reporting if the required information is included in the consolidated accounts of the parent company. From 2023, exempted subsidiaries will also have to publish the financial statements of the parent company reporting at group level and refer to the exemption in their own financial statements.*



Figure 4:

Which companies are covered by the CSRD?

From 2017 until the introduction of CSRD:

Non Financial Reporting Directive (NFRD)

Companies of public interest (listed on the stock exchange) employing more than 500 people, as well as banks and insurance companies.

Approximately 11,700 companies in the EU

Gradually after 2024:

Corporate Sustainability Reporting Directive (CSRD)

All large corporations and all listed companies (excluding micro-corporations).

Approximately 49,000 companies in the EU

Note: The overview here is based on the CSRD proposal published by the European Commission and the related standards proposal. The proposal does not constitute a definitive directive, the conclusions of which may change until final regulation. This article was last modified on 08/04/2022.

5.2

5.2. How can I prepare for CSRD compliance?

Different approaches can be used to prepare the reports, depending on whether a company is preparing to write its first sustainability report, it has previously communicated its non-financial performance, or whether it is expected to be affected by CSRD expectations.

If the company is expected to be covered by the CSRD, it is a good idea to perform a gap analysis that shows the current status of compliance. The next step is to plan how the deficiencies can be remedied so that the report is fully compliant with the CSRD by the deadline.

The final version of the unified reporting standard to facilitate CSRD compliance is expected in October 2022. In the meantime, the first steps can be taken based on the information available. A double materiality analysis needs to be carried out, stakeholders need to be mapped out, channels need to be developed through which you can learn about sustainability issues that are important to stakeholders, and corporate governance structures and data collection methods, etc. also need to be developed. Some companies may have other reporting obligations in addition to the CSRD, all of which need to be known, and a timetable should be put in place for the company to meet all of these deadlines.

Complying with the EU Corporate Sustainability Reporting Directive (CSRD)

The first steps to take in 2022.



Companies that have previously reported their non-financial performance are preferred, especially if their reports have been prepared in accordance with the requirements of an international standard. However, it is also essential for these companies to review their reporting practices in the light of anticipated new expectations.

Figure 5: Steps to prepare for CSRD compliance

6.

How can I get an ESG rating?

Any business that wants to raise capital will most likely need an ESG valuation, be it a manufacturing company, a service company or a country. In order for a company to receive an ESG assessment, you need to contact an ESG assessment body. There are a number of such organizations, the most significant of which are MSCI, Sustainalytics and S&P Global.

These organizations carry out evaluations based on the company's publicly available performance indicators, although their methods may differ, which means the outcome of the evaluation may be different. Some carry out work based on sustainability and financial reports issued by the company or even a review of the website; others send questionnaires and data requests to complete. It is up to investors to decide which evaluation to take into account.



6.1 How can I get a good ESG rating?

Adherence to the following principles is essential if you want to achieve a positive ESG assessment:

- Management commitment, integration of sustainability aspects into corporate governance, decision-making and risk analysis
- Application of standards in the design and maintenance of corporate sustainability processes
- Focusing on materiality and repeating the materiality survey on a regular basis
- Involvement of stakeholders (in the form of a systematic and continuous program)
- Consideration of the entire value chain
- Developing and digitizing the sustainability data collection process
- Measuring sustainability performance
- Setting objectives using data calculated in a standard way
- Aligning financial perspectives with sustainability objectives
- Third party certifications based on relevant international standards
- Transparency: publication of sustainability information and data

The quality of an ESG assessment is fundamentally affected by two factors: how realistic the reported data are and what the outcome of the company's sustainability efforts is. An accurate, realistic assessment, based on honest and transparent reporting, reduces the risk that investors may be late in discovering something that may affect their decisions. This is aided by different reporting standards, e.g. the **Global Reporting Initiative (GRI)** or the **Sustainability Accounting Standards Board (SASB)**, which frame ESG topics and their key indicators.

The most important concepts and steps required for ESG evaluation are detailed in the sections below.

A

Stakeholder involvement

Stakeholders in a company are the stakeholders with whom the company interacts, be they individuals, other companies, investors, government actors, NGOs, or local communities, etc. In order to develop a fully fledged ESG strategy, the company needs to map its stakeholders, i.e. assess its relationship with stakeholders, especially in terms of sustainability. The evaluation should answer the following questions:

- What is the purpose of our relationships with our stakeholders?
- How can we assess the expectations and problems of our stakeholder groups and what ESG topics they think we should focus on?
- Who needs to be informed about who and when?
- How, in what and when do we involve them?
- How can we use stakeholder knowledge to create added value for everyone who plays a role in the life of the company?

With the involvement of stakeholders, the company is ready to assess ESG topics relevant to it.



B

Materiality analysis

Materiality analysis is the cornerstone of ESG strategy and ensures that all companies strive for sustainability with maximum efficiency. Without proper evaluation, a company can make ad-hoc decisions without consensus and specific goals.

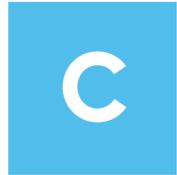
Depending on the activities of a company, you cannot focus on all ESG issues with the same amount of effort. Materiality analysis identifies the key ESG issues that are most relevant to the company and the options for action depending on the business background. Materiality analysis has now been expanded to take into account not only the internal, business (financial) effects of the company, but also its effects on its natural and social environment. This is known as double materiality.

Materiality analysis and its results are unique to each company, as sustainability priorities depend on, among other things, the company's industry, activities, natural and social environment, management, and other stakeholders.

As a result of a good materiality analysis, the company should have:

- A materiality matrix that shows the relative importance of ESG topics that are important to the company and its stakeholders
- An insight into the situation of its industry and its competitors
- Guidance on the proper reporting of material items
- A method of prioritizing the next steps

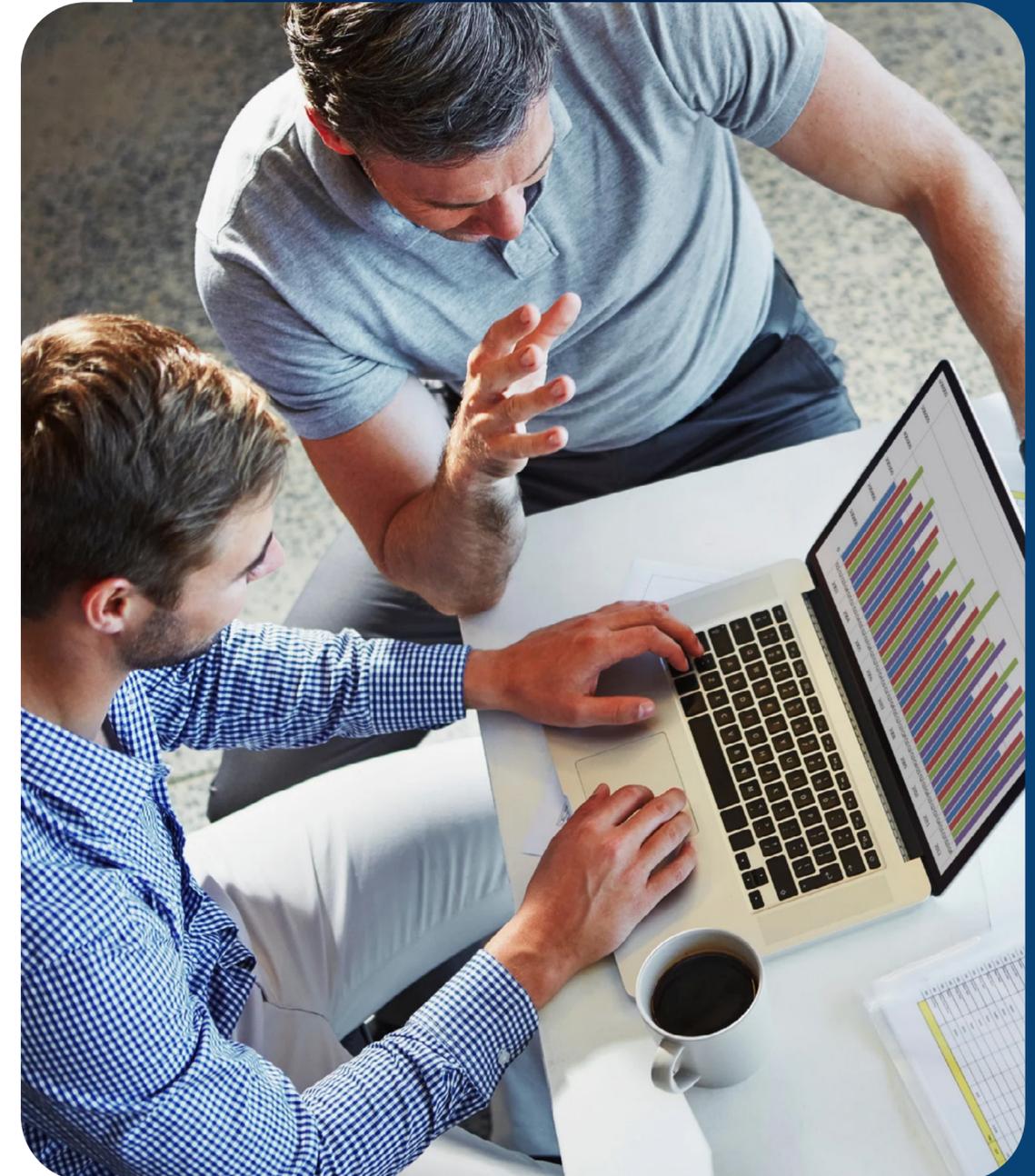
A qualitative materiality analysis supports and validates the company's communicated ESG priorities.



Performance indicators

Key Performance Indicators (KPIs) are needed to assess a company's key sustainability issues. In part, these data provide the basis for ESG assessments. Reporting standards provide guidance on the possible range of KPIs, but it is essential to develop a metric system that:

- Best expresses the company's sustainability performance
- Applies to the period covered by the report
- Covers all areas of sustainability deemed relevant
- Based on metrics that can be produced with as little effort as possible
- Is determined by standard methods
- Is certified or certifiable by a third party
- Can be produced regularly in the long run.



Example for a good ESG rating:

Climate change is one of the most important sustainability issues, with a carbon footprint as a key measure. The carbon footprint is now a basic requirement for ESG companies.

- Determine your corporate carbon footprint, i.e., baseline emissions data for the entire value chain (Scope 1, 2, and 3) according to the GHG Protocol (Greenhouse Gas Protocol)
- Set science-based targets in line with the Paris Agreement (1.5 °C but well below average temperature rise below 2 °C) (SBTi)
- Plan for the 'decarbonisation' of your company to achieve the above emissions reduction target, which you will then incorporate into your strategy and financial plans
- Consider the feasibility of a net zero strategy
- Plan to compensate for your emissions
- Enable your organization to determine your carbon footprint on an annual basis
- Also certify the standard calculation with a third party

The development of a company can be clearly demonstrated if there is a base year to which it can be compared. Once the company has clarified the key issues, it needs to assess the current situation: what programs are working, what metrics it has, and what commitments it has made in the past.

Due to the diversity of sustainability issues within the company, the areas of HR, environmental protection, finance, procurement, logistics and energy, among others, may be involved. Once the current state of the company has been clarified, its aims regarding ESG and the company's ability to achieve its goals can be better assessed.



7. Successful ESG report in 8 steps

Disclosure of sustainability information requires careful preparation in a wide range of areas of the company's operations.

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Preparations

1

Examine your organization's readiness to publish sustainability information: If you haven't already issued a sustainability report, assess what is needed to run the process in-house.

2

Examine what non-financial disclosure obligations you will have to meet (NFRD, CSRD) and what disclosure standards and guidelines you will need to consider (GRI, SASB, etc.).

Main steps

- 1** Assess your value chain and identify sustainability impacts along it.
- 2** Identify the company's stakeholders and clarify their expectations and requirements.
- 3** Evaluate the relevance of sustainability issues with stakeholders using a dual materiality approach.
- 4** Define performance indicators (KPIs) for key sustainability issues. Define the base year to which you will compare progress in the future.
- 5** Establish a data collection system to manage KPIs. Like financial data, there will be a need for ongoing management and monitoring of sustainability data. Provide an appropriate software solution for this.
- 6** Set goals and approve them at board level. Set clear, science-based, realistic and ambitious environmental goals.
- 7** Publish a voluntary sustainability report. If the company and the report are sufficiently mature, certify it with a third party.
- 8** Based on the KPIs and programs presented in this report, contact the most appropriate ESG assessment organization for your company to obtain the best rating.

Figure 6:

Suggested ESG preparation steps

Step 1

Assess your value chain and identify sustainability impacts along it.



Step 2

Identify the company's stakeholders and clarify their expectations and requirements.



Step 3

Evaluate the relevance of sustainability issues with stakeholders using a dual materiality approach.



Step 4

Define performance indicators (KPIs) for key sustainability issues. Define the base year to which you will compare progress in the future.



Step 5

Establish a data collection system to manage KPIs. Like financial data, there will be a need for ongoing management and monitoring of sustainability data. Provide an appropriate software solution for this.



Step 6

Set goals and approve them at board level. Set clear, science-based, realistic and ambitious environmental goals.



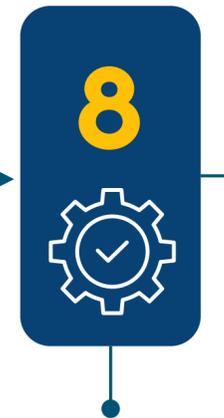
Step 7

Publish a voluntary sustainability report. If the company and the report are sufficiently mature, certify it with a third party.



Step 8

Based on the KPIs and programs presented in this report, contact the most appropriate ESG assessment organization for your company to obtain the best rating.



denxpert ESG solution

Denxpert helps corporates align their business vision with ESG requirements through intuitive compliance, report-driven data collecting, and 15+years of experience.



Let our expert team set you up for ESG success

Our team of experts will bring order to chaos by offering step-by-step guidance throughout your ESG journey.



Manage all of your ESG operations in one place

With our intuitive ESG management software, compliance, data collection, and reporting will become effortless.



Stay competitive by sustainable growth

Denxpert helps find your competitive edge through balancing profit, environment, and society.

Trusted by teams at over 500 of the world's leading organizations



Authors



Robert Szucs-Winkler

Experienced Environmental Health Safety Specialist with a demonstrated history of working in the environmental services industry. Strong information technology professional skilled in Sustainable Development, ISO 14001, Environmental Issues, Environmental Compliance, and Agile Methodologies. He is an advocate for data driven environmental protection. Currently he is the CEO of denxpert EHS&S software Ltd. and leader of the Inogen Alliance Digitalisation Workgroup.



Csaba Csiszko

Experienced safety and sustainability expert with global leadership roles. Work experience in different geographies, implementing projects and systems in all continents and in different cultures. Leading safety, environmental and sustainability global functions. Work experience in manufacturing and commercial organizations in leadership roles. Several internal and external recognitions, speaker in global events. Currently leading the sustainability department of the consulting company denkstatt Hungary.



About denxpert

Denxpert is an EHS management consulting and software as a service provider with over 15 years of experience in the Environment, Health & Safety and Sustainability field. Our focus is to provide organizations a one-stop-shop that enables swift and hassle-free management of applicable EHS legislation, obligations, and optimized processes. Denxpert streamlined EHS for over 300 organizations around the globe thanks to our solution – in development since 2006 –, and the international network of experts we collaborate with.

With our international ESG partner [denkstatt](#), we provide tailored consulting services for all sustainability challenges.

denxpert EHS&S software Kft.

Phone: +36 1 239 1206

Email: office@denxpert.hu

Customer support: szabo.andras@denxpert.hu

Technical support: papp.zsolt@denxpert.hu

Executive support: szucs-winkler.robert@denxpert.hu

www.denxpertsolutions.com

