



INSTITUTE OF DIRECTORS  
IN IRELAND



# **The Sustainable Finance/ESG Agenda: What Do Directors Need to Know?**

with Laura Heuston, Director and Co-Founder,  
SustainabilityWorks

IoD Ireland Briefings Series: Sponsored by Accenture



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# Agenda

1. Stepping back: the big picture
2. Why business is embracing sustainability
3. The sustainable finance agenda
4. EU sustainable finance policy & the Taxonomy
5. SFDR
6. The TCFD
7. So what do directors need to know?
8. Q&A

# The big picture

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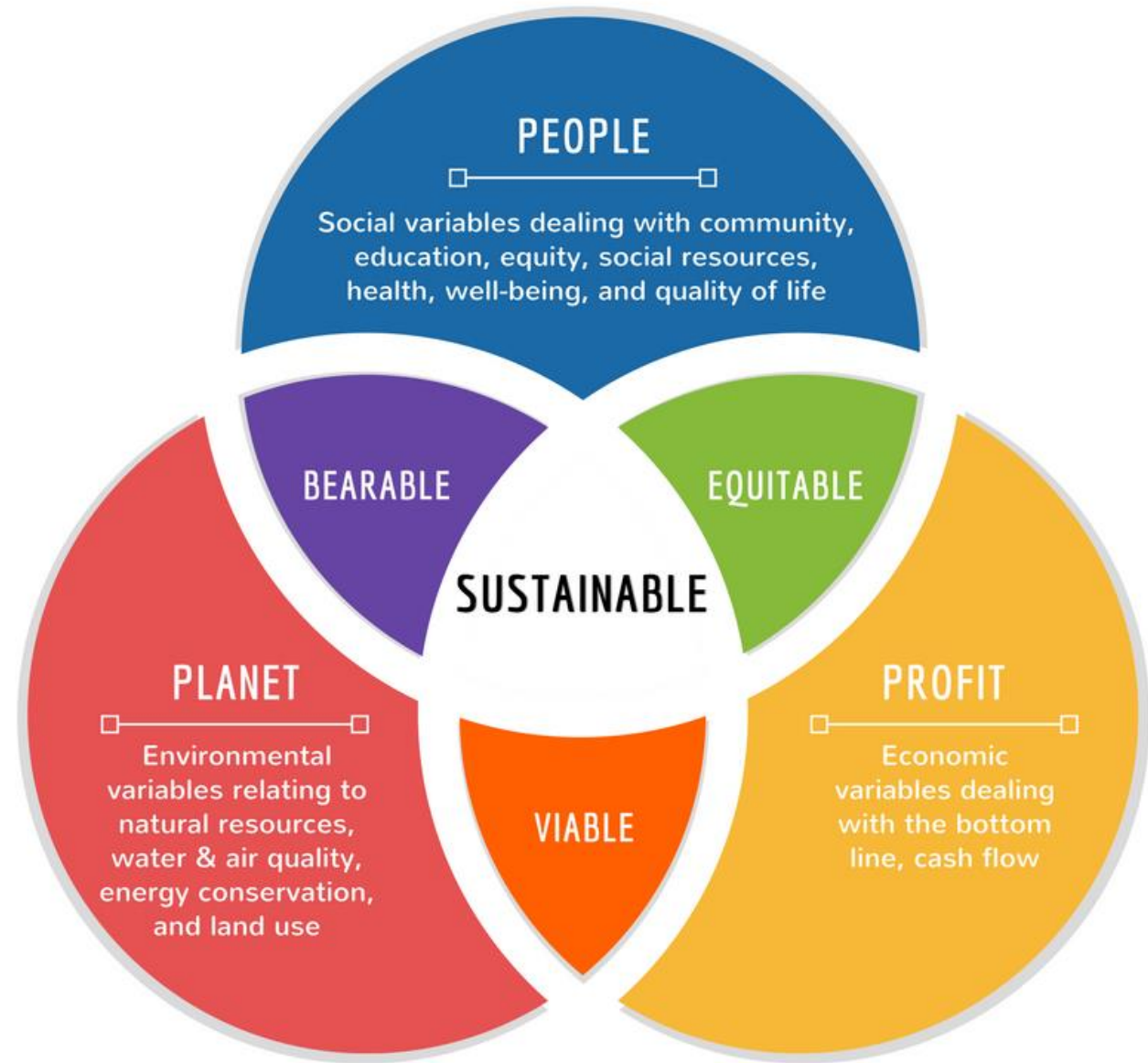
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# Defining Sustainability

Sustainable  
*Adjective*

Able to continue  
over a period of  
time

Cambridge Dictionary



# Drivers of the global sustainability agenda

Population growth

Use of natural resources

Waste (including carbon)

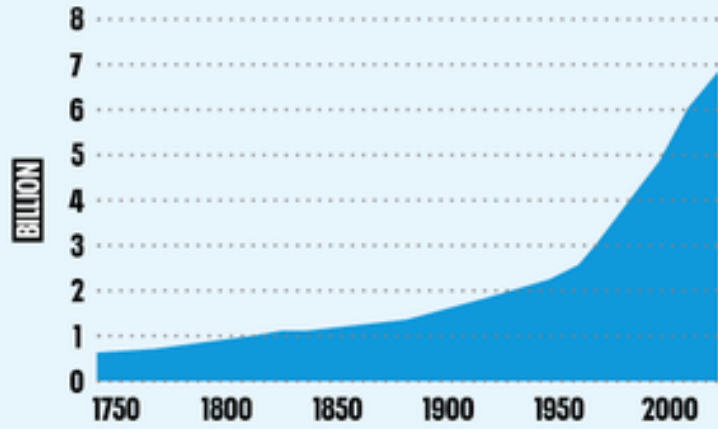
Benefits of economic progress not equally distributed – leading to social challenges

Negative “externalities” not factored into economic models & systems

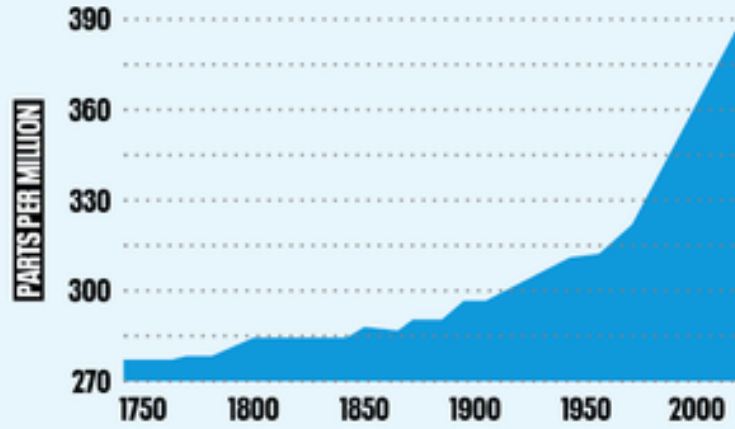
Increased policy interventions as a result



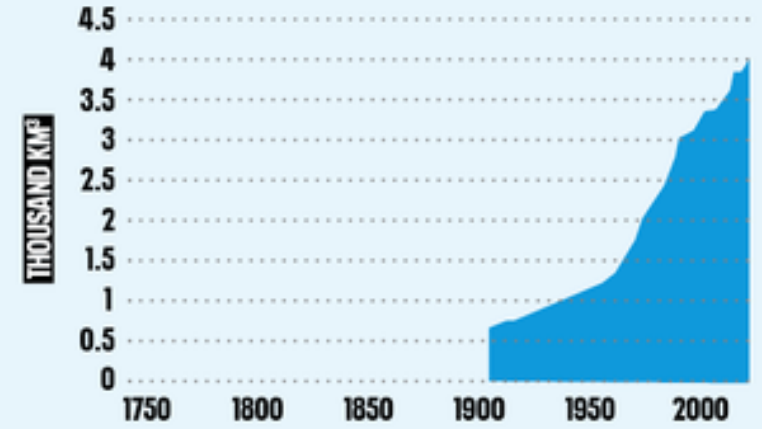
### WORLD POPULATION



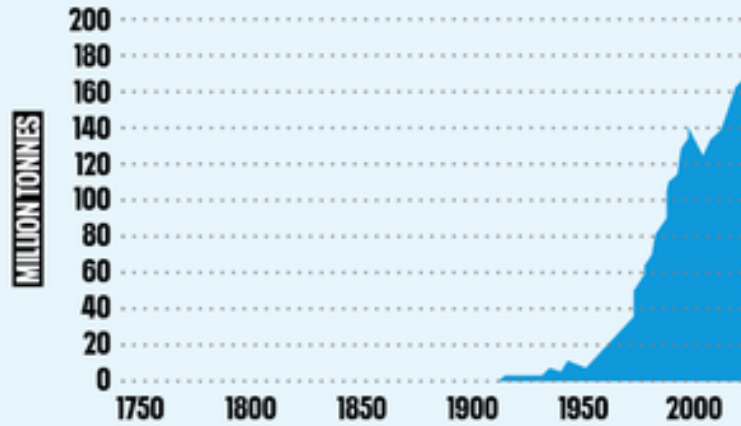
### CARBON DIOXIDE (CO<sub>2</sub>)



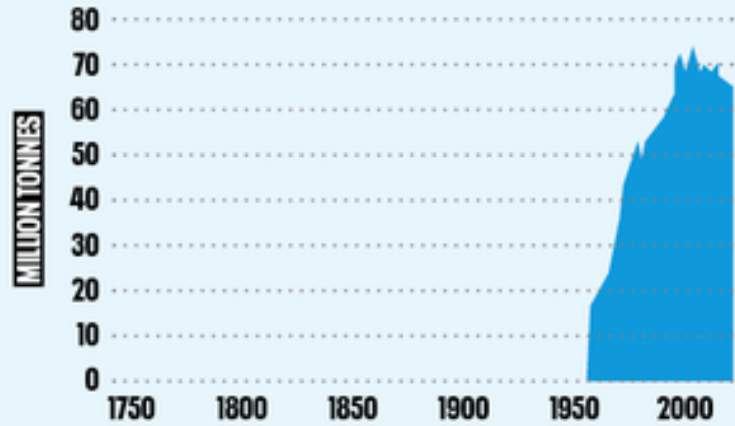
### FRESHWATER USE



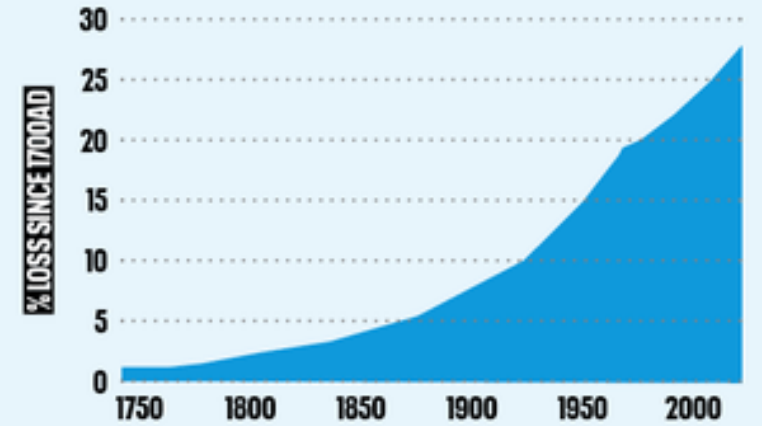
### FERTILIZER CONSUMPTION



### MARINE FISH CAPTURE



### TROPICAL FOREST LOSS



# Global Sustainability Challenges...

Interlinked with economic stability

Top national government agendas

No one country can solve

International political consensus vital

Climate Change

Natural resource depletion

Biodiversity

Pollution

Modern slavery

Inequality

Deforestation

Urbanisation

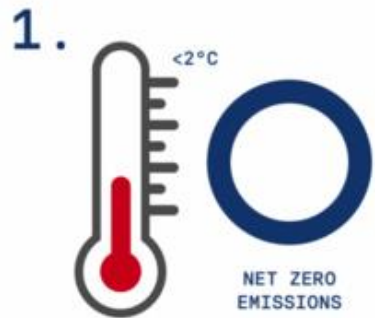
Pandemics

# The Global Policy Response in 2015...

## THE GLOBAL GOALS For Sustainable Development



## PARIS CLIMATE AGREEMENT



Limit the avg. global temperature increase to  $< 2^{\circ}$  centigrade + achieve net zero emissions by mid-century



Enhance resilience and adaptation to climate impacts certain to occur



Align financial flows in the world with these objectives



# Why business is embracing sustainability

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Business is embracing sustainability  
*‘for profit, purpose and survival’*

Leading Sustainably, Bridges & Eubank, 2021

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“Sustainability is the single biggest business **opportunity** of the 21st century, and will be the next source of competitive advantage.”

H. Lee Scott, CEO of Wal-Mart

“The **next 1,000 unicorns** won't be more search engines or social media companies, but rather ones that **help the world decarbonize and make the energy transition affordable** for all consumers.”

Larry Fink, CEO Blackrock, Jan 2022

“Firms that align their business models to the transition to a net zero world will be **rewarded handsomely**. Those that fail to adapt will cease to exist.”

Mark Carney, Former Governor of the Bank of England

# Benefits for Businesses

Of embracing sustainability

Lower cost of capital

Improved corporate financial performance

Enhance brand and increase competitive advantage

Customer loyalty

Improve risk management

Foster innovation

Attract, engage & retain employees

# Corporate Sustainability Issues

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## Environmental

- Materials
- Energy use
- GHG emissions
- Water use
- Waste
- Biodiversity
- Pollution (e.g. air)



## Social

- Human rights
- Labour rights
- Health and Safety
- Diversity & Inclusion
- Training & development
- Responsible sourcing
- Community engagement
- Product safety
- Customer safety & welfare
- Access & affordability
- Responsible marketing / advertising / labelling



## Economic

- Livelihoods & jobs
- Procurement spend
- Legal Compliance
- Business ethics
- Data protection / privacy
- Tax transparency
- Risk (incl. climate risk)

All underpinned by Corporate Governance

# The Financial Lens: ESG

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# Corporate Sustainability v ESG

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Two sides of the same coin...

## Sustainability

Companies managing the sustainability / ESG risks and opportunities relevant for their business, and reporting on their progress



## ESG

Financial sector scrutinising companies' performance on sustainability / ESG issues to inform their decision-making

# ESG is just Data (or a list of issues)

There is no such thing as:- An ESG stock

- An ESG company

- An ESG economic activity

And “ESG investing” covers a really broad spectrum



# Climate is at the core of ESG

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“Shifts in our climate bring potentially profound implications for insurers, financial stability & the economy”.

“Need better information to allow investors take a view”.

“The right information allows sceptics and evangelists alike to back their convictions with their capital.”



Mark Carney, Former Governor of the Bank of England, 2015 Speech

# Who is driving the Sustainable finance agenda?

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# What is Sustainable Finance?

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## A Process?

Refers to the **process** of taking due account of environmental and social considerations when making investment decisions, leading to increased investment in longer-term and sustainable activities

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## A Source of Finance?

Is **finance** to support economic growth while reducing pressures on the environment and taking into account social and governance aspects.

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## Disclosures?

Sustainable finance also encompasses **transparency when it comes to risks** related to ESG factors that may have an impact on the financial system, and the mitigation of such risks through the appropriate governance of financial and corporate

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EU Commission Definition (2018)

# Driving the sustainable finance agenda

All of these stakeholders are driving the agenda

Overlapping reasons for each

Financial materiality of sustainability-related risks, challenges, opportunities and trends

Financial stability

Climate-related financial risk at the core



**Institutional Investors**



**Governments**



**Financial Regulators**



# Institutional investors

Correlation between ESG and financial performance

Other studies show correlation with stock market performance

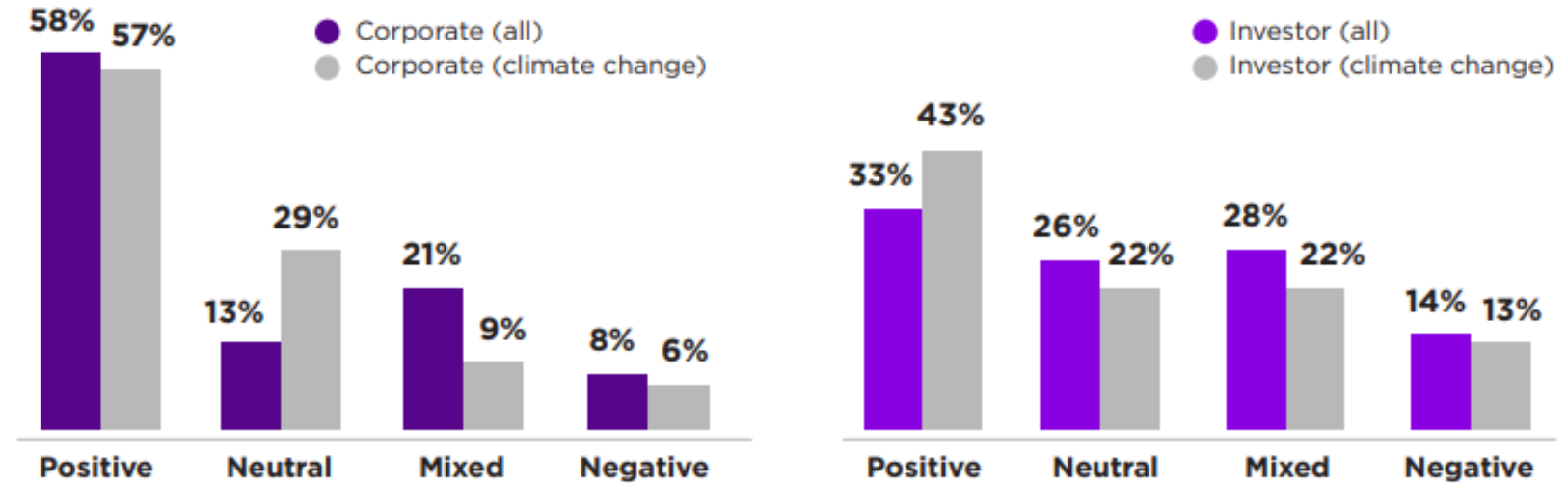
And – high profile controversies relating to ESG issues hitting market value and bottom line

Managing for a low carbon future does improve financial performance

Focus on the material issues for sector

Climate-related financial risk unhedgeable

**Figure 1.** Positive and/or neutral results for investing in sustainability dominate. Very few studies found a negative correlation between ESG and financial performance (based on 245 studies published between 2016 and 2020).



ESG and Financial Performance: uncovering the relationship by aggregating evidence from 1000 plus studies published between 2015 – 2020  
NYU Stern Center for Sustainable Business and Rockefeller Asset Management



# Governments

Why?

Need private capital to deliver on policy objectives relating to climate and sustainability

Systemic financial risk from climate change

Securing sustainable economic growth

## What can and are they doing?

- Ensure transparency and disclosure – by financial sector and real economy -> SFDR & CSRD
- Can define green to tackle greenwashing -> EU Taxonomy
- Develop standards and labels/certifications -> EU Green Bond label
- Can get sustainability on the agenda of investors/banks/insurance companies
- Can “nudge” the financial regulators to consider ESG and climate risks
- Can consider where put own money (EIB, EIF, InvestEurope etc)



# Financial Regulators

Concerned about climate-related financial risks...

Impacting stability of the global financial system

Individual financial institution safety & soundness

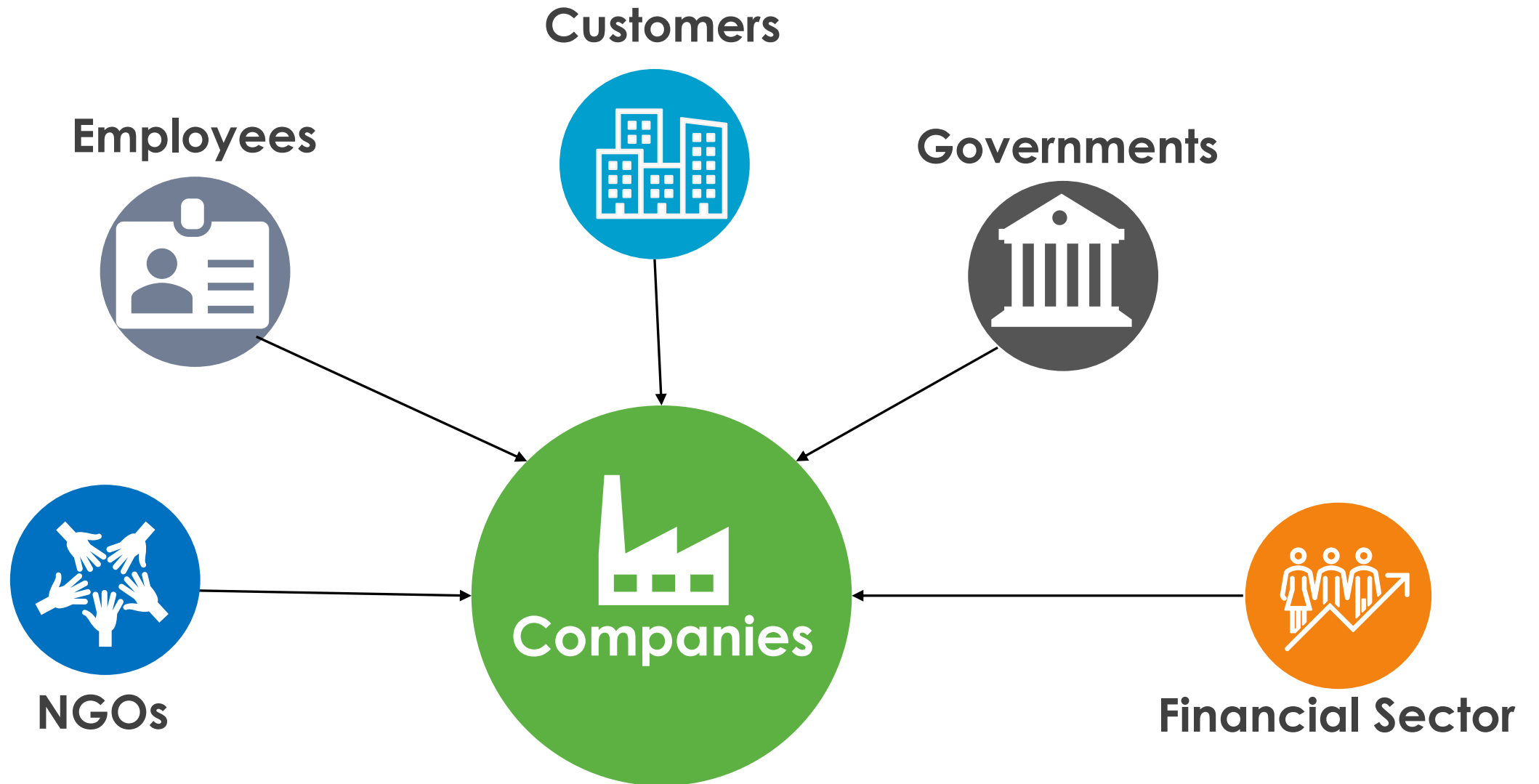
Consumer/investor protection re greenwashing

Very focussed on climate risk initially but can see that broadening out to ESG

## What can they and are they doing?

- Use supervisory review to understand ESG risk exposure and firm's sustainability strategy
- Identify concentrations of ESG risks - climate stress testing
- Tackle greenwashing – ensure consistency and transparency
- Consider data gaps on exposures
- Green supporting factor for lending
- Gatekeeper role – to ensure regulated entities have right expertise

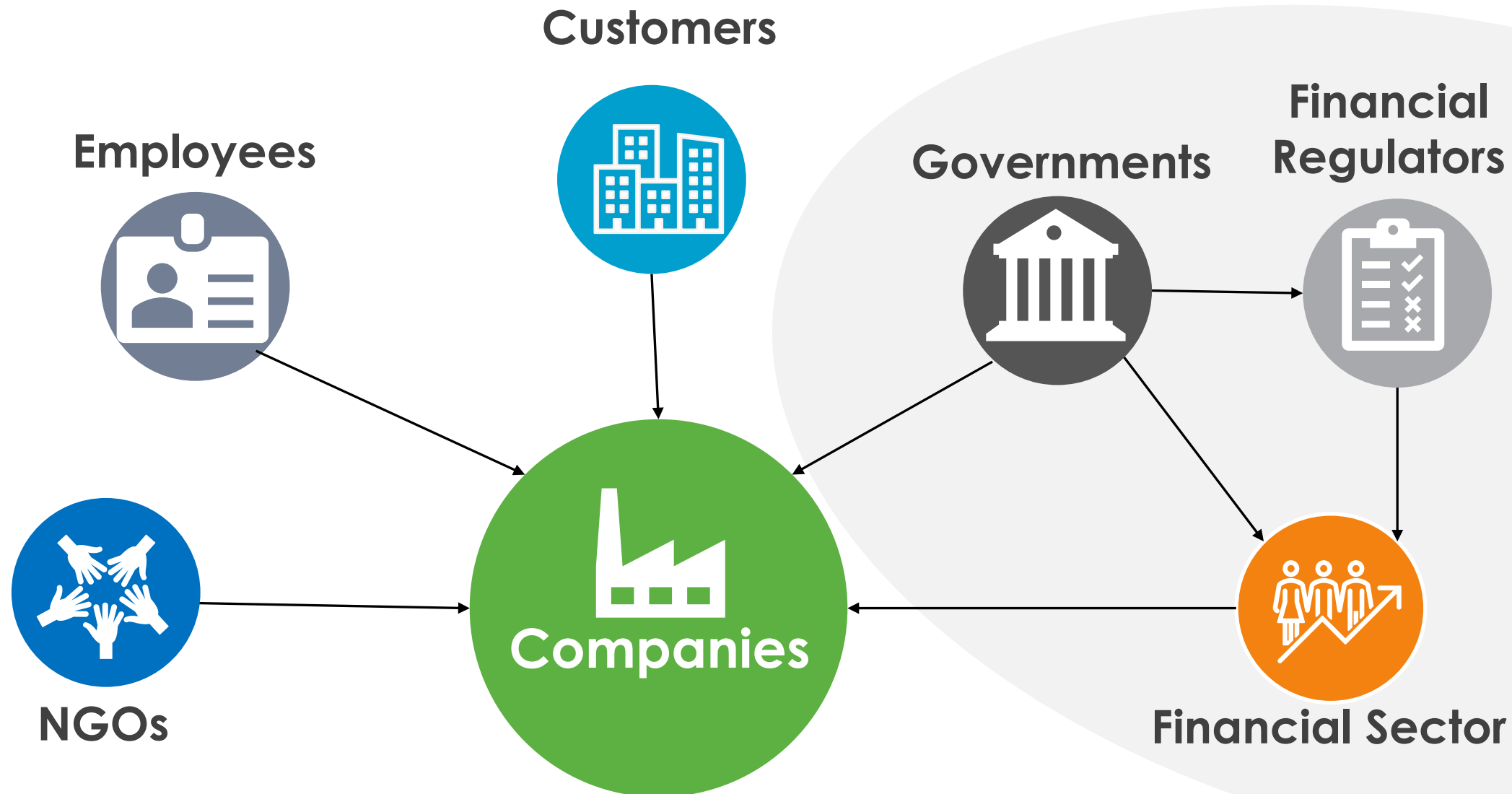
# Increasing pressure from multiple stakeholders





# Sustainable Finance Policy & Regulation

*The political trojan horse*



# The EU sustainable finance agenda

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# EU SUSTAINABILITY POLICIES



## CLIMATE AND ENERGY

- 2030 Climate and Energy Framework
- Energy Union Package
- EU Strategy on Adaptation to Climate Change



## ENVIRONMENT

- Natural Capital Management
  - Air
  - Water
  - Land
  - Biodiversity
- Circular Economy



## INVESTMENT AND GROWTH

- Investment Plan for Europe (Fund for Strategic Investment (EFSI); InvestEU; EU cohesion policy funds)
- External investment plan
- Horizon 2020

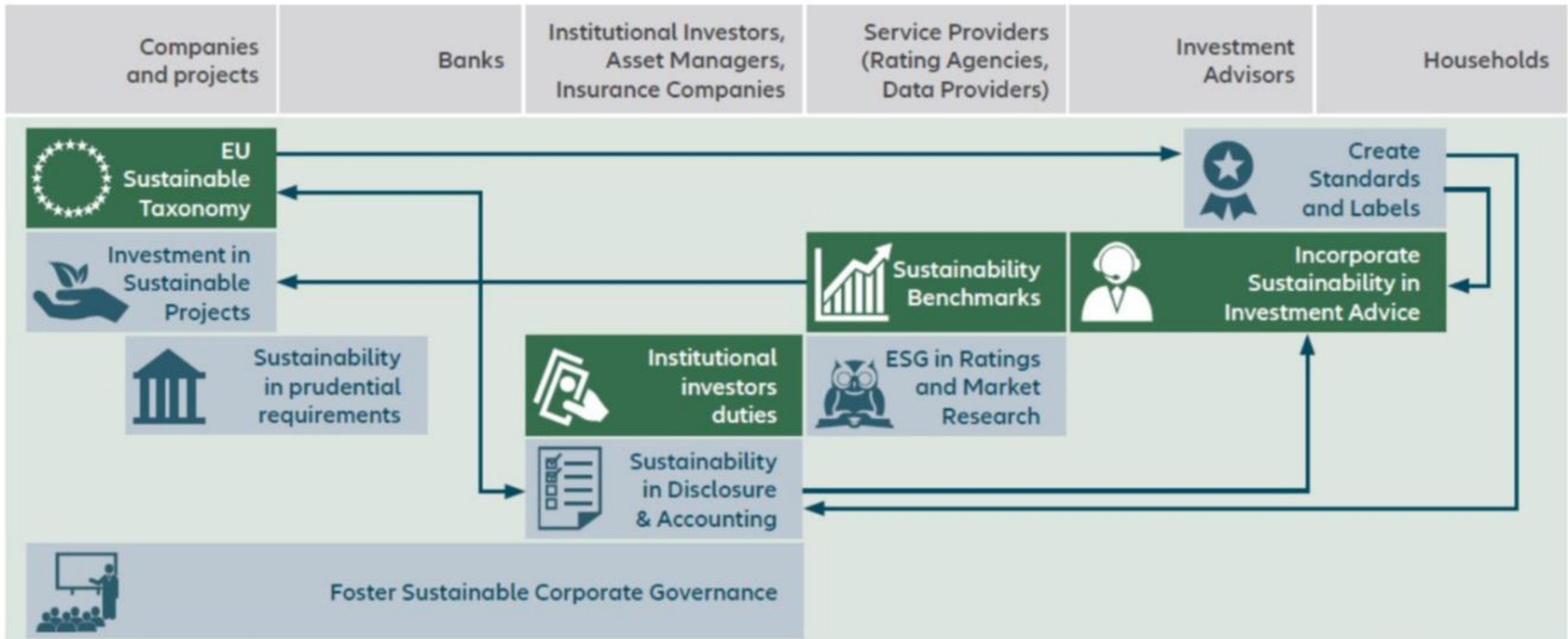


## SUSTAINABLE FINANCE

- Sustainable Finance within the Capital Markets Union

- Long-term strategy to reach carbon neutrality by 2050
- EU Environmental Action Plan

# 10 Pillars of EU Sustainable Finance Action Plan



# The EU Taxonomy

The backbone of the EU sustainable finance policy agenda

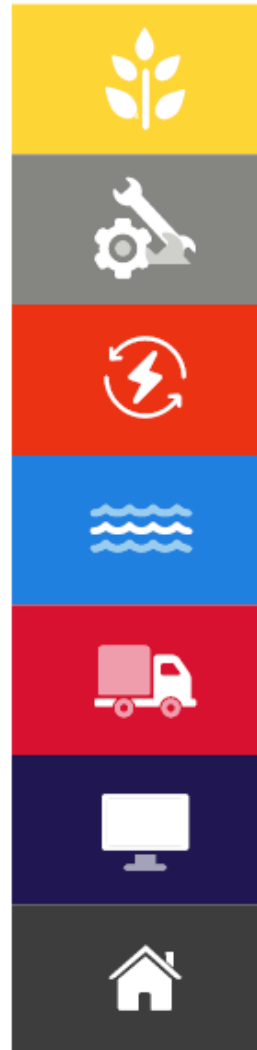
A dictionary of what a green economic activity is

Defines green not brown/neutral

Scientific/technical language

Does not tell anyone what to invest in/lend to

Has been very controversial



**Agriculture and forestry**

**Manufacturing**

**Electricity, gas, steam and air conditioning supply**

**Water sewerage waste and remediation**

**Transport**

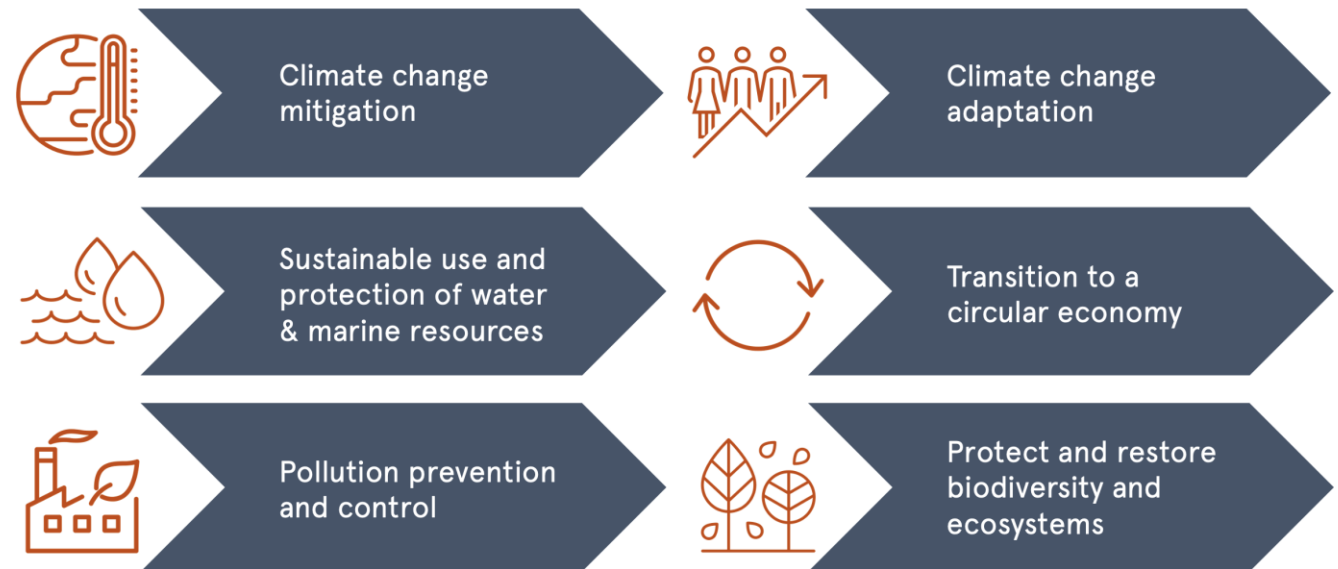
**Information and communication technologies (ICT)**

**Buildings**

# How does it work?



## The six environmental objectives of the EU Taxonomy



# New buildings



Make a substantial contribution to one of the 6 environmental objectives:

1. Climate mitigation

# Technical Criteria to be met

Energy Performance

The Primary Energy Demand is at least 10% lower than national Nearly Zero Energy Building (NZEB) requirements, certified using an as-built Energy Performance Certificate.

Air tightness and thermal integrity

Large buildings (>5,000m<sup>2</sup>), must undergo testing for air-tightness and thermal integrity to ensure design objectives met, and any deviation in the levels of performance set at the design stage or defects in the building envelope are disclosed to investors and clients

Global Warming Potential

Large buildings (>5,000m<sup>2</sup>), life-cycle Global Warming Potential of the building, calculated for each stage in the life cycle & disclosed to investors/clients on demand

# New buildings



Do no significant harm (DNSH) to the other environmental objectives

# DNSH Criteria

## Climate Adaptation

Assess and reduce material physical climate risks through a robust climate risk and vulnerability assessment

## Water

Requirements re efficiency of water appliances

## Circular economy

Requirements around waste and preparation for reuse, recycling and other material recovery

## Pollution prevention

Requirements around use of dangerous materials and emissions of volatile organic compounds. Ensure site isn't contaminated. Measures to reduce noise, dust, pollutants during construction/maintenance

## Biodiversity

No building in protected natural areas or land of recognised high biodiversity value



# New buildings



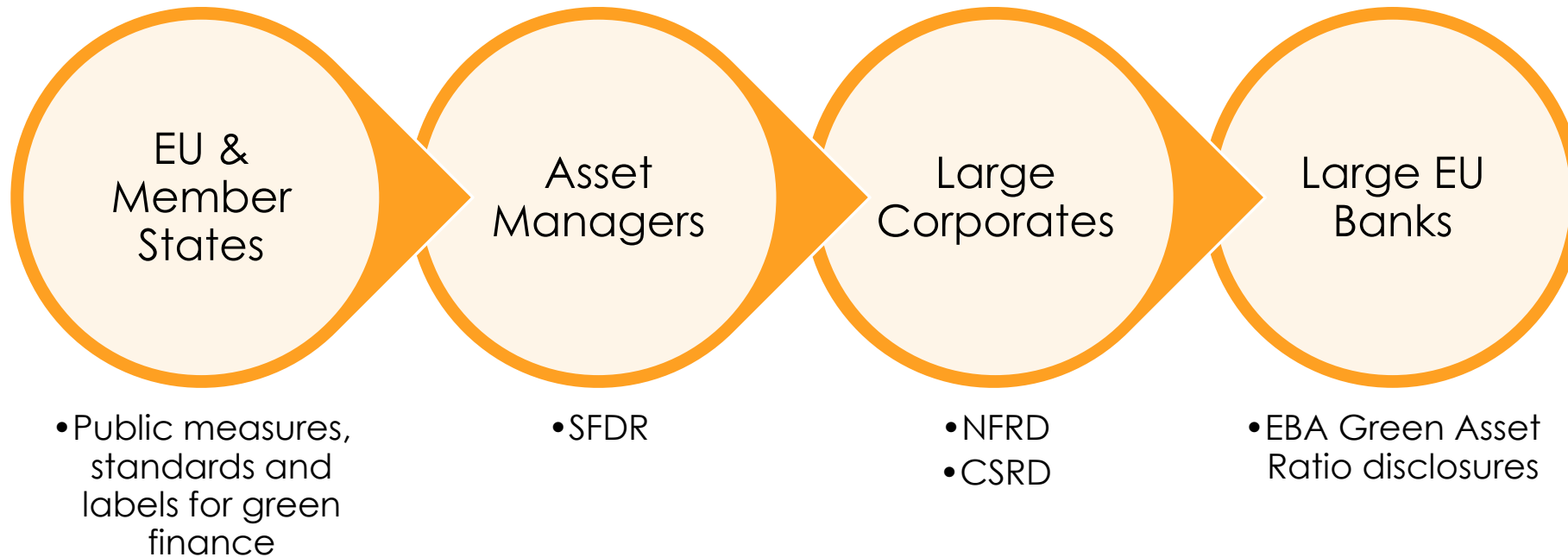
# Minimum Social Safeguards

Policies and procedure in place aligned with:

- OECD Guidelines on Multinational Enterprises
- UN Guiding Principles on Business and Human Rights
- The International Labour Organisation (“ILO”) declaration on Fundamental Rights and Principles at Work
- The International Bill of Human Rights

# Who must use it?

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For private sector: just disclosure requirements

What is SFDR and why was it introduced?

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# Sustainable Finance Disclosure Regulation (SFDR)

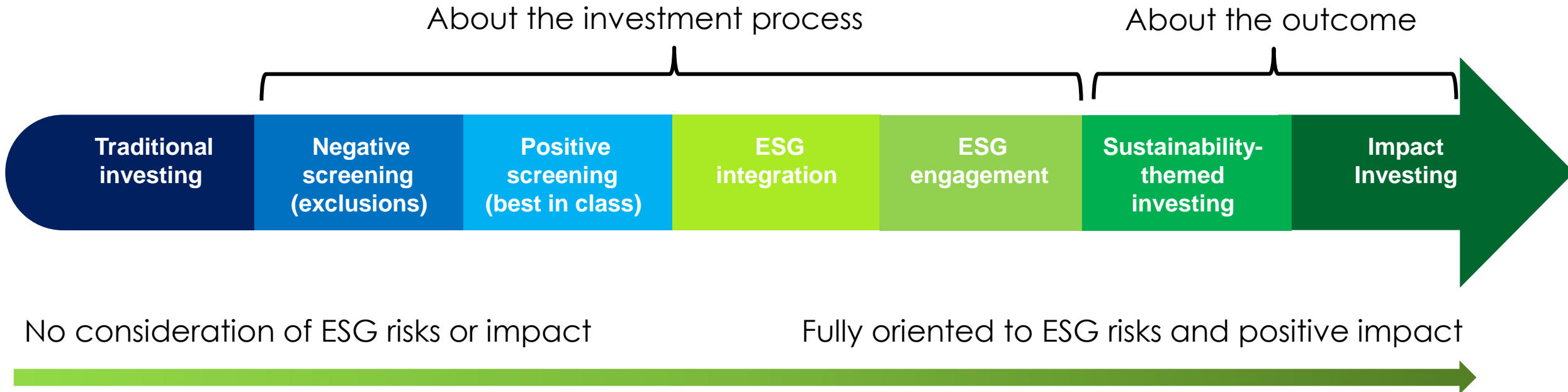
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What is it?	A new set of disclosure requirements applicable to financial market participants, financial advisors and financial products.
What is it not?	It is not a product label. No-one has certified that the disclosures are correct. However the disclosures will be subject to financial regulator supervision. Likely that labels will be developed that are based on the criteria
Why introduced?	Increase transparency in the investments sector in relation to sustainability (tackle greenwashing) Harmonise disclosure requirements and facilitate comparability across products.
What is the link to the EU Taxonomy?	The definition of an environmental objective in SFDR is not linked to the Taxonomy. However must disclose alignment of investments with the Taxonomy.

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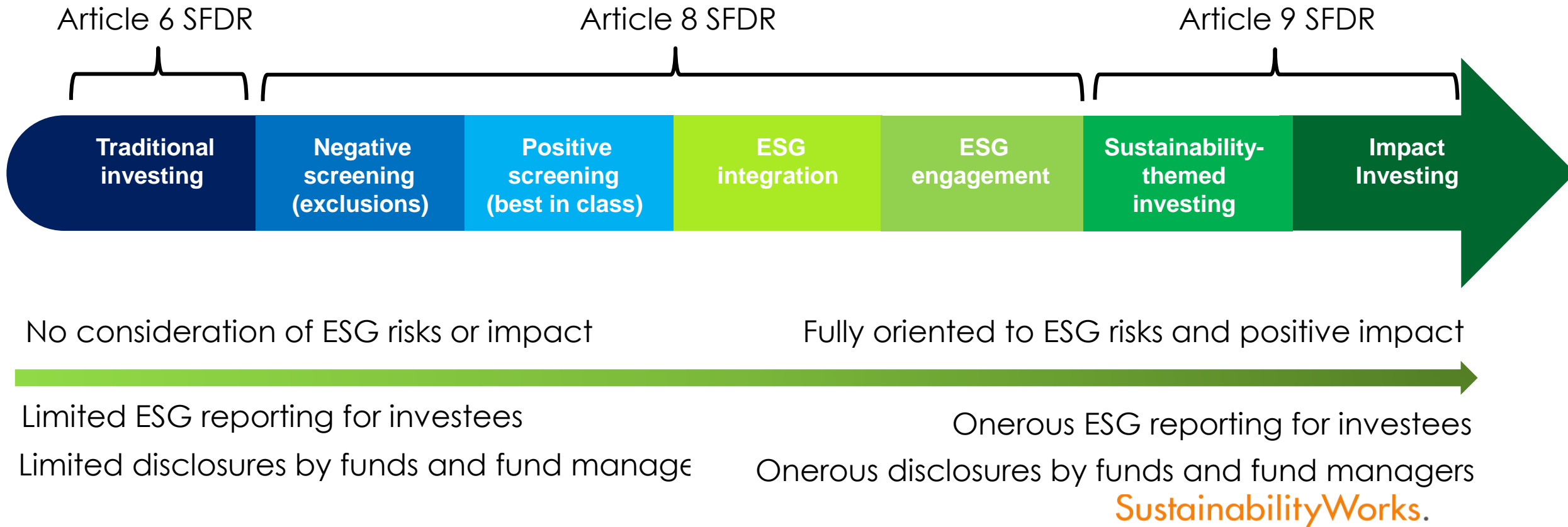
# ESG investing is a broad spectrum...

*“Responsible investment is a strategy and practice to incorporate ESG factors in investment decisions and active ownership – to better manage risk and generate sustainable, long-term returns.” UN PRI*



# Linking ESG investing approaches and SFDR

But remember... the Sustainable Finance Disclosure Regulation (SFDR) is simply that... about disclosures... It is not prescribing any investor or asset manager to invest in anything in particular but simply to disclose what they are doing



# The financial regulators are coming

**Deutsche Bank raided by authorities over ESG 'greenwashing' claims: 'We've found evidence that that could support allegations of prospectus fraud'**

**Morningstar culls 27% of European sustainable funds after fresh review**

**Asset managers told to clean up greenwashing and net zero claims**

Financial regulators clamp down on companies misleading investors by overstating the greenness of their funds

ENERGY

**The SEC Is Fed Up With ESG Greenwashing**

**SEC Fines BNY Mellon Over ESG Claims**

Regulator is boosting its scrutiny of funds as market grows

# Task Force on Climate Related Financial Disclosures

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# TCFD is gold standard for climate disclosures



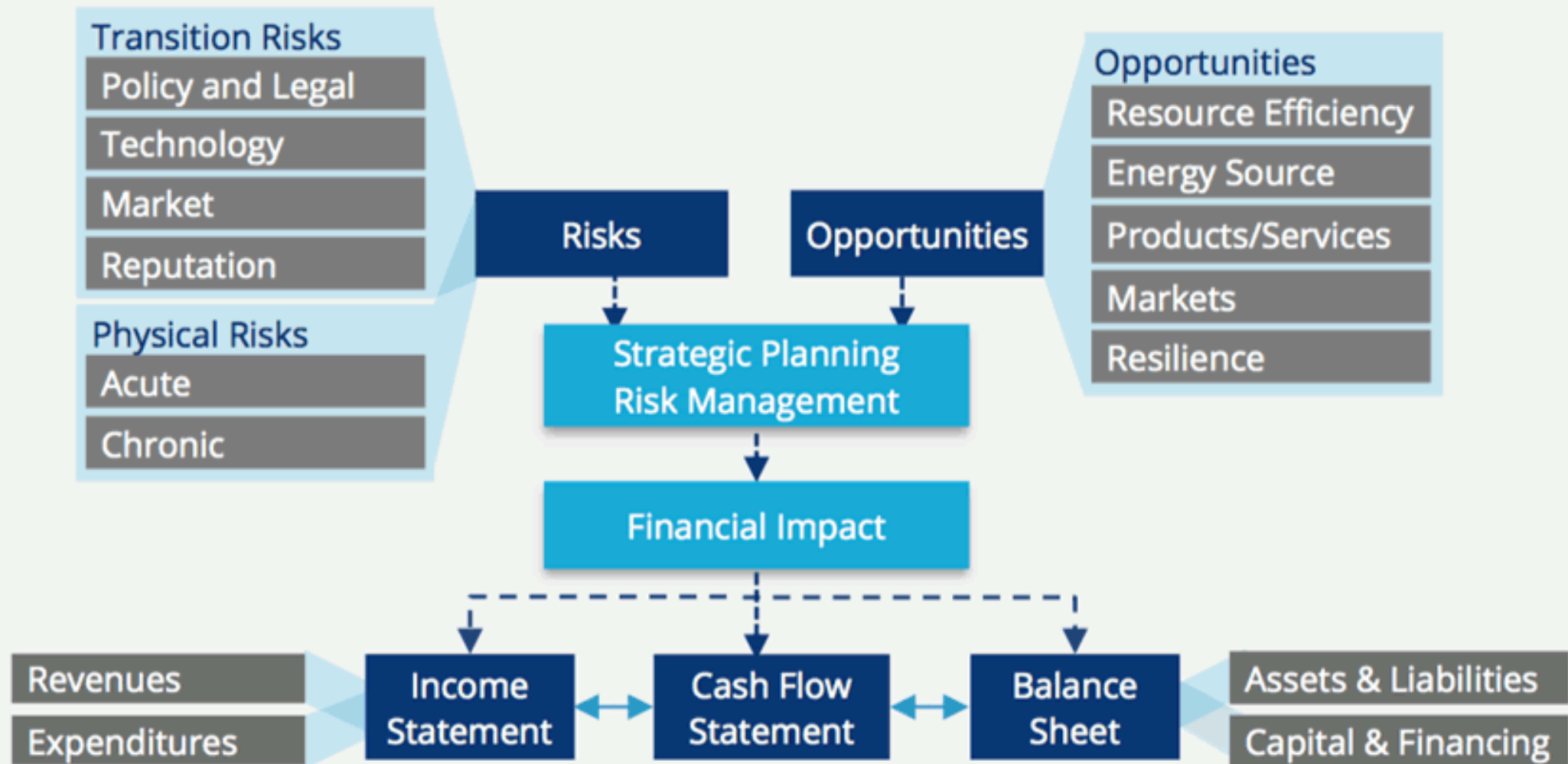
Governance	Strategy	Risk Management	Metrics and Targets
Disclose the company's governance around climate-related risks and opportunities.	Disclose the actual and potential impacts of climate-related risks and opportunities on the company's businesses, strategy, and financial planning where such information is material.	Disclose how the company identifies, assesses, and manages climate-related risks.	Disclose the metrics and targets used to assess and manage relevant climate-related risks and opportunities where such information is material.

Task force on Climate-related Financial Disclosures, Oct 2021

# TCFD: a strategic tool for corporates

Figure 1

## Climate-Related Risks, Opportunities, and Financial Impact



So what do directors need to know?

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# So what do directors need to know?

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As with sustainability, sustainable finance is not going away – this is about financial risk & opportunity

This is not woke-ism ... but is being drawn into the political arena/culture wars in the US

ESG is just data (or a list of issues!)

Climate risk & opportunity is at the heart of all ESG discussions

COVID and the War have increased the focus on the S of ESG

As well as countries and companies, financial sector also setting Net Zero goals and targets for portfolios

Good performance on ESG issues is increasingly about access to capital and the cost of that capital

Investor, policymaker and regulatory focus is moving from the investment process to the investment outcome/impact

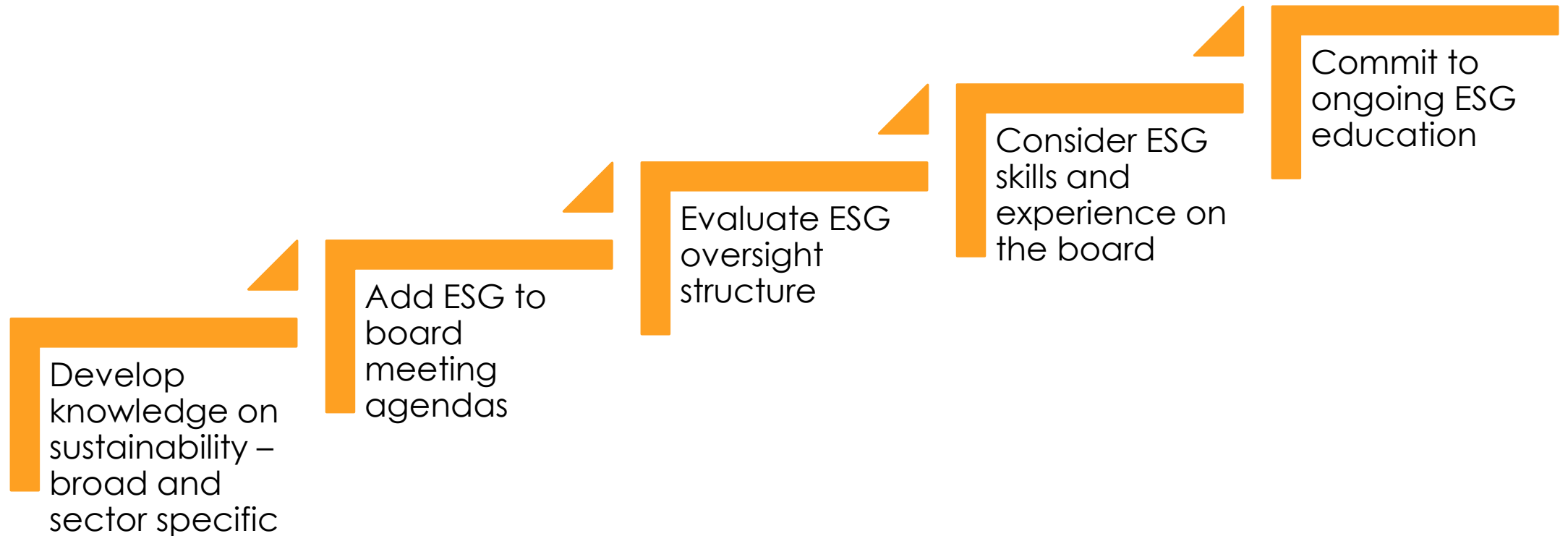
Green taxonomies are expected to steer capital towards green

Financial regulators are increasingly focused on climate risk and greenwashing

Increasing ESG disclosure compliance burden – SFDR, TCFD, new NFRD, CDP– both mandatory and voluntary and on both the real economy corporates and the financial sector

# Immediate next steps as a director

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# 10-Step Roadmap for the Board



## Board Leadership

1. Proactively engage with external stakeholders about sustainability
2. Embed sustainability into all discussions with the CEO and executive team



## Board Culture

3. Establish a purpose-driven culture that looks at issues through a sustainability lens
4. Educate directors on sustainability



## Purpose, Strategy, and Risk Alignment Leadership

5. Apply a sustainability lens to corporate strategy decision-making
6. Set goals and establish clear metrics for tracking progress towards them



## Structure and Process

7. Structure the board to engage meaningfully on sustainability matters
8. Change compensation models to account for sustainability targets



## People and Composition

9. Make sustainability a factor when hiring directors
10. Make sustainability a factor when hiring CEOs

# Q&A

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Laura Heuston, Co-Founder

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# About SustainabilityWorks

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**Aideen O'Hora**



**Laura Heuston**



**Karen Deignan**

**A consultancy on a mission to accelerate Ireland's shift to a sustainable future.**

**Experts in sustainability strategy, finance, policy, innovation, communications and reporting.**

**We make sustainability simple. We make it actionable. We make it work.**





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