ESG Third Report for Konrad Adenauer Foundation 2023-2024

United Kingdom and South Africa: ESG principles and Disclosures

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Overviews

Building on the success of the *Interdisciplinary Journal of Economics and Business Law* (IJEBL) ESG Special Report published in Volume 10 (2021), the tenth anniversary volume of IJEBL and featured in the much - viewed Business Day Dialogue of 9 November 2021 also supported by KAS, and the Second ESG Report published in IJEBL Volume 11 published in November 2022 we assess the Third Phase of the future of ESG success by looking at the current definition of ESG and how success is based on the strength of disclosures to integrate ESG principles.

We concentrate on an extended analysis of ESG practice in the UK's City of London and South Africa's Johannesburg Stock Exchange (JSE) featured in the first Report and carry on from the analysis in the Second Report showing that ESG has widened in its remit and has developed a variety of strategies to progress ESG becoming embedded and an integral part of daily company policy and action. ESG has moved away from a marketing and public relations perspective that were often exaggerated to actual reflection as to what can be realistically be achieved mainly in this phase through a high standard of disclosure. The war in Ukraine and the severe effects of the energy crisis has caused asset managers and companies to reflect as to what they can realistically deliver. Regulators are becoming more aware as well of the difference between greenwashing and genuine adherence to ESG principles. Regulators are also becoming stricter, banishing companies from ratings and ESG

compliant lists for not practicing all three components of ESG. There is a recognition that all three components of ESG are interlinked. The most important progress at this stage is that there is an overall movement towards realisation, especially in the City of London, Europe, and in the JSE that in the near future, non-compliant companies will be ostracised from the world economy.

Redefining ESG and moving forward

ESG implementation has been affected both positively and negatively by the war in Ukraine and Russian denial of gas supplies to Europe. In both the UK and South Africa there have voices calling for backing away from renewables, enlightened social policies and tighter governance in companies that pension funds choose to invest in. Fossil fuel companies are arguing that they cannot move towards net zero because the urgent need is for immediate use of oil and gas to replace restricted gas supplies from Russia. In the UK, the current government has given way to those who say it is time to dispense with the drive for renewables and the push towards net zero with management asset funds disagreeing along with shareholders. In South Africa there are those in the government and some companies who argue that more coal is needed as there is a constant shortage of energy and moving to renewables immediately is not a viable option.

Yet, on the positive side, renewables have been an overwhelming success in the UK with net zero well in sight. In fact, under the last government, renewable companies have made massive profits and the largest most productive wind turbine site in Europe resides off the Yorkshire coast and produces pollutant free large amounts of energy and provides jobs for the local population. There is a push for inland wind turbine sites. Clean energy investment has grown by 12% a year since 2020, in part due to the rise of public and private support for sustainable finance, especially in wealthy countries such as the UK. Renewable energy, new grids, and energy storage account for more than 80% of total power sector investment. The IEA **1** (International Energy Agency) estimates spending on solar, batteries and EVs is now growing at a rate consistent with reaching global net zero emissions by 2050. A recent report by the IEA found more people are now employed in clean energy (which it defined as

including renewable energy, electric vehicles (EVs), energy efficiency measures and nuclear power) than the fossil fuel industry. One problem, however, is that clean energy jobs are not as well paid, in part because they are less likely to be unionised. But the argument that there are no jobs in clean energy has dissipated.

It is the success of renewable energy companies in the UK that were granted legacy contracts meaning they can keep all the profits that has led to higher energy prices. Fossil fuel companies are facing anger from the population who allege they are racketeering making huge profits which they are not investing in renewables nor are they showing any concern for the planet and net zero goals. Large asset management companies who hold pension funds are increasingly wary of investor backlash if they turn to fossil fuel investment. Regulators and rating agencies are striking companies off their lists who claim to implement ESG principles while supporting the fossil fuels industry. In South Africa there are those in the government and elsewhere who are backing the support from Germany, Switzerland, the US, and elsewhere to abolish coal fired plants and turn to solar and wind.

Pertinent issue analysis

We will analyse this conflict in approach and how the emphasis is moving towards implementation of the environmental, social and governance in equal measures.

We will also discuss how the war in Ukraine has been a wake- up call to countries trying to implement ESG that over reliance on one country's fossil fuels such as oil and gas is very dangerous and that all renewable options must be pursued and advanced as quickly as possible.

Asset managers are realising that the pressures on them to adopt ESG principles have not lessened; only genuine ESG principles are being demanded rather than exaggerated public relations claims and posturing without substance. This is positive as asset managers and companies are reflecting seriously on how they can implement ESG principles in real terms without hyperbole and with straightforward disclosures.

Regional emphasis

UK/City of London – We wish to build on this from the original report as £2.6 trillion is now being invested in UK pension schemes mainly through the City of London. Two-thirds of UK savers now wish for their savings to account for the environment and

make profit. There is increasing demand especially now after COP 26 to make pension investments greener by using them to support companies that mitigate climate change. COP 28 will be held this year 2023 in Dubai and the outcomes will need to be explored.

The UK government appears to be sending mixed messages with the Prime Minister confirming a new oil and gas development named Rosebank, off the Shetland Islands which will begin drilling for oil and gas in the very near future.

UK Defence Industry

In relation to defence spending and investment, Grant Shapps the UK Minister for defence stated that ESG is excluding the defence industry from access to debt and equity capital. Kroll, the City of London Consultancy firm released data showing that debt issuance linked to ESG metrics is becoming more common and found that listed companies with strong ESG scores outperformed rivals for annual returns. Shapps stated that because of such divestment, the cost of procurement is rising and diverting taxpayers' money away from other defence spending and public services. He further argued that he will have to work with defence industries and the City of London to secure greater access to investment for industries linked to the UK's national security. He believes ESG ratings need to use a methodology that takes fairer account of important role of defence industries. What this means is unclear as Shapps also stated that there is no contradiction between ESG principles and the defence industrial sector. He mentioned the nuclear deterrent stating that the important values within ESG should not undermine capabilities being developed to preserve security and peace.

When Shapps statement was read out in the House of Lords by Baroness Goldie the defence minister and Tory peer, he emphasised that investors must be free to choose what to invest in, but it needs to be fact based. Therefore, ESG should be clearer in its methodology and quickly correct errors when they are pointed out if they are errors indeed.

Carla Nunes from Kroll noted that increased ESG regulation in relation to ratings will bring some uniformity. **2**

Therefore, in the UK while ESG is praised by some government ministers such

as Shapps because there is great support for ESG principles by a majority of UK companies large and small, the government seems to have its own ideas of how ESG should be defined. This contradiction can only be solved when a standard method of disclosure is developed which we are assessing in this Third Report which will lead eventually to standardised ESG methods of measurement, and a universal shared understanding.

The British energy thinktank Ember found a record northern summer of solar generation which meant the continent (Europe) was able to avoid spending €29bn on gas. Across the EU's 27 countries, renewable energy provided 35% of electricity, compared to 16% from coal. In 2022, there has been a record lowering of carbon intensity because of a 12% increase record growth in in the global mix of solar and wind derived energy. The electricity sector is the world's largest carbon emitter responsible for over a third of the world's energy related emissions in 2021 of which almost a third was from gas and three quarters from coal production. It is in a transition period and holds potential to rapidly reduce carbon emissions globally. **3**

This is why the transition in South Africa from dependence on coal and the move to renewables is essential for both the health of the climate and the economy. This transition impacts ESG scorecards and ratings for companies listed on the JSE. The second half of this Third Report looks at the transition to ESG principles on the JSE and in pension/asset fund management.

Republic of South Africa - There is a good deal more research to be done in this area with South Africa, since COP 26, being heavily invested in from the UK, EU, US, Germany, and France to move away from coal-fired dilapidated power stations to renewable energy such as solar. The Cop26 climate summit in Glasgow, when South Africa signed a partnership with Germany, the UK, the US, and the EU promised $US8.5bn of global capital over the next three-to-five years as the country restructures its coal-dependent energy system. In this Third ESG Report we plan to assess the latest progress of this commitment taking place in 2023.

South Africa has 2500 hours of sun compared to only 1500 for the UK for example, so solar panel installation is beginning in earnest with ESG financial investment from pension funds. There are also many training programmes being instituted in South Africa to train former coal fired power station workers and new recruits in all aspects of renewable energy.

There is and will be much more material to research on developments of

pension fund capital investments both within South Africa and between the UK, EU, US, Germany, Switzerland, France and South Africa for ESG implementation, especially for environmental but also for social and governance purposes.

USA – The largest economy in the world with the current Administration of President Joe Biden being completely in support of climate change mitigation with the Inflation Reduction Act (IRA) having been passed with substantive measures to mitigate climate change must be alluded to in this Third ESG Report. No ESG study could be complete without including the USA. The USA is also home to the world's largest pension funds with, as explained below, intense regulation by the SEC increasing in recent years.

Clean energy investment has grown by 12% a year since 2020, in part due to the rise of public and private support for sustainable finance, especially in wealthy countries such as the US. Renewable energy, new grids, and energy storage account for more than 80% of total power sector investment. The IEA estimates spending on solar, batteries and EVs is now growing at a rate consistent with reaching global net zero emissions by 2050. **4**

Analysis has found the Inflation Reduction Act (IRA) could propel the US to a 43% cut in emissions by 2030 compared with 2005 levels – a big leap from where it was otherwise headed. If the US political system holds together, it should put the national target of a 50% cut this decade, and there are bigger cuts beyond this, within reach.

The recent US law underlines that penalising fossil fuel industries by pricing carbon is, while not dead, out of fashion. The IRA is mostly about investment – $US370bn of it – to help clean solutions usurp the outmoded, unclean models. Much of it will be available only to goods manufactured in the US. Experts say in addition to cutting local pollution, this could also increase competition and lower costs on international markets.

The cost of green energy like wind and solar has been falling for decades in real terms in the UK, EU, USA and now is beginning to fall in South Africa.

As climate change events are multiplying causing drought, flooding, social discontent, and poor governance, ESG is being taken more seriously in most quarters and we will explain how this is happening and progressing, moving on to expand on the first and second ESG Reports and to include the social and governance aspects of ESG.

Defining ESG

ESG is continuing to be re-defined and expanding in its scope. (This is explored more fully in the second half of this Third Report). In my estimation, if ESG was defined as Eating, Socialising and Gourmandising adherence and adoption would be nearly 100% yesterday! However, Environment, Social and Governance goals are more demanding and require now high standards of disclosure which mitigates against greenwashing and facile public relations exercises. There is near universal agreement and in the City of London that those who do not adopt ESG principles will be left behind and excluded from asset fund manager/pension funds lists. Such exclusion will come from trustees, pension fund managers and shareholders alike. The seriousness of increasing commitment to ESG integration throughout company organisations can be seen in all business sectors.

Marine insurance and Shipping

A noteworthy example was West's P&I Club launch and release of its inaugural ESG & Sustainability Report during London International Shipping Week in September 2023. This leader in marine insurance deeply rooted in the City of London is committed to green shipping and healthy oceans. This is the Club's first ESG report and one that focusses on disclosures of ESG initiatives outlining in detail in this extensive report initiatives by integrating, for example, into company practice goals found in the United Nations' Sustainability Development Goals (UN SDGs). Actions include instituting policies that support the environment, social issues, and governance issues. The ESG actions include supporting seafarers mental and physical wellbeing, moving forward gender diversity, and initiating training programmes for West employees. The new ESG programmes include training on new fuels and technologies to support West's decarbonisation transition and how to protect the marine environment. Other actions by West to deeply imbed ESG principles through action include creating a dedicated ESG Committee and dedicated ESG Department. In addition, West has established its operational carbon footprint by commissioning carbon emission reports on all offices and taking a zero - tolerance stance on greenwashing. The Club contributes to ESG investment funds, is a member of the Marine Anti-Corruption Network and promotes ethical business throughout its workforce. Details of this ESG commitment report and disclosures may be read as

West ESG & Sustainability Report 2023: Navigating the New Reality (westpandi.tutl.co). The ESG committee section has quotations from committee members who are all linked at a high level to sections of West, as to why they are so willing to support ESG. **5**

Shipping and marine related industries such as insurance and pension funds tend to have a high rate of compliance with ESG principles and to continuously improve their ratings. So much so that two shipowners, Connecticut - based Eagle Bulk Shipping and New York's International Seaways have had BlackRock Asset Management increase their stakes in the companies since their last reporting as shown in public filings. Both shipping companies have featured in the five top places of analyst Michael Webber's annual ESG scorecard. This is despite the fact, that both shipping companies have been involved in bulk cargoes including crude oil and coal respectively. BlackRock, a high - profile supporter of ESG that uses these principles to shape its investments has also a pragmatic understanding of transitioning industries that do not happen overnight. **6**

Different paths to disclosure

There are broadly a variety of different ways that ESG implementation can be accelerated and support essential disclosure. The second half of this report will explain them in relation to the South African JSE and listed companies. In this half we look at 3 strategies taken by most companies in the City of London.

> *Narrow the definition and concentrate on achieving that to a high standard and learning how to tackle the other aspects of ESG with net zero efforts as a template for other aspects of ESG. In a piece in Forbes this strategy for building effective disclosures is suggested in relation to the environmental focussing on net zero.*

While the scope of net zero is relatively narrow compared to broad concepts like ESG, it is one of the most urgent and impactful efforts that an organisation can address. An example of the urgency is that NASA scientists predicted that global temperatures are on target to increase between 4.8 to 5 Fareinheit **7** by the year 2100. As already occurring this degree of global warming will be a catastrophe for the global economy and the well-being of billions of people. The Forbes piece suggests that

despite its narrow focus there are several simple steps that most organisations can begin right away moving towards net zero.

1. Start with A Carbon Footprint Assessment and Create Goals

It is essential for all businesses to have a thorough understanding of how much carbon and greenhouse gases their organisation produces from both direct and indirect sources for which a professional sustainability expert can assist by recording and guide a company under scrutiny by a process of recording and calculating the carbon footprint.

By having a quantifiable starting point, businesses can set science-based goals that align with their business objectives. For example, businesses that operate large fleets of vehicles may want to focus on reducing their fossil fuel consumption while a tech company may need to consider the energy usage of their server farms. It is essential for these goals to be spread across the organisation so that both employees and other stakeholders can support and become an active part of the initiatives.

2. Investing in Energy Efficiency and Renewable Energy

Energy efficiency and renewable energy are key components of a successful net-zero strategy. Companies can naturally opt to replace aging equipment with better, more sustainable versions over time or can aggressively pursue a full replacement of high-energy assets. Even simple changes like using energy-efficient light bulbs, or adjusting thermostats can help.

Since fossil fuels generate significant amounts of carbon dioxide compared to green alternatives, focusing on renewable energy can drastically reduce a company’s carbon footprint. It is probably not possible to eliminate 100% of greenhouse gas emissions, so the remaining balance can be offset by purchasing carbon credits that go toward reducing greenhouse gas emissions elsewhere but must be done through highly reputable organisations.

3. Monitor Progress and Expand to Other Environmental Causes

Measuring your organisation's performance toward net zero is essential to ensure that you are making progress and focusing on the right solutions. Establishing key

performance indicators **8** is a great way to have a benchmark to measure and report on emission reduction projects. Periodically, revisiting your initial assessment can serve to better understand what additional opportunities exist to further reduce your carbon footprint.Net zero is relatively straightforward, making it the perfect starting point for other eco-friendly goals and objectives. Once established it is a good way to leverage the same strategy toward other environmentally friendly initiatives such as clean water reduction, waste elimination in the manufacturing facilities or making the supply chain more sustainable and not the weak link in the eco-system. Net zero is an excellent first step toward building a trustworthy and reputable brand that is both profitable and makes a positive impact on the world. **9**

Another narrow approach, for example to advance better understanding of a particular sector such as ICT which can be a powerful machine learning tool to assess power consumption for companies trying to provide metrics for ESG ratings. Kepler or Kubernetes-based Efficient Power Level Exporter is a project founded by Red Hat's emerging technologies group. It had early on assistance from Intel and IBM. It operates by capturing power use metrics across a broad range of platforms that focus on reporting, reduction, and regression so companies can understand their energy consumption when disclosing their carbon footprint for example for ESG ratings purposes**. 10** As discussed in the second half of this report, at present there are so many variations of metric assessments for ESG, especially in a narrow focus approach, the need for standardising results is greater than ever to produce high standard disclosure.

Medium disclosures that involve peer review such as B Corp disclosure strategies in the City of London and specific problems of SMEs.

BCorp approach

BCorp is a ratings Agency that works with companies to try and improve their score card by encouraging thorough assessments which can take up to six months. It encourages senior managers to document evidence of all ESG aspects.

BCorp which means 'Benefit for all' is one of the most popular ways in the City of London and the UK, to obtain Certified B Corporation status by BLab which benefits all stakeholders. It is a non-profit organisation that offers a rigorous assessment process that measures most of ESG performance to a high standard. This means

achieving a high environmental and social performance of a B Impact Assessment of 80 or above and passing the BCorp risk review. Multinational Corporations must also meet their baseline requirements.

There is a legal requirement for changing their governance structures to benefit all stakeholders and not just shareholders and to achieve benefit corporation status if within the companies' jurisdiction.

Transparency is achieved as companies' ratings by BCorp as measured by BCorp standards are publicly available on the BLab website. BCorp certification is a rigorous process which is outlined on their website, through receiving accreditation from BLab (a non-profit organisation). BCorp requires a re-certification every three years or after change of ownership or a public offering. Some of the benefits listed by BCorp is valuable additional capacity that greater employee retention results in, higher levels of innovation, greater community engagement, increased robust governance structures and a high scorecard for ESG principles.

There are a number of medium size companies that are BCorp accredited including Innocent Drinks (juices and smoothies), The Body Shop (cosmetics and personal care), Jamie Oliver Group (restaurants, products and media), Ella's Kitchen (plant- based food) and Sipsmith (gin).

Anton Collela, CEO of Moore Global Ltd, noted in his support of ESG;

"The new disruption in the market place will be the businesses that embrace a renewed and profound humanity." **11**

Another development in promoting ESG disclosure strategies is specialist insurance provider Beaszley. They have established an ESG Consortium. In January 2022 with capacity moving fully to syndicate 5623 from January 2024 once they receive regulatory approval. The Consortium offers valuable additional capacity to businesses with high ESG scores according to Bob Quane, chief underwriting officer.

Beazley will also be offering additional capacity to European and US clients.**12**

SME companies need to take medium disclosures approach

SME companies have difficulty in taking a narrow approach and broad strategy in pursuing a successful disclosure strategy because of their size. They cannot afford to hire narrow focus machine learning metrics companies such as Keppel mentioned above or to move to new more climate friendly headquarters and set up extensive training programmes like West P&I Club also mentioned above. SME company budgets are often so constrained they cannot afford an internal individual quality control person for their company to further ESG compliance and integration.

In the City of London, the Chartered Insurance Institute (CII) has recently published a new guide to help small and medium-sized brokers develop and integrate ESG strategies and progress high standard disclosures.

The 2022/23 CII Broking Community New Generation group, carried out the research which assessed how ESG strategies are being implemented by SME companies. They also looked at how these ESG strategies may be adopted by other SME brokers to strengthen their sustainability, accountability and performance.

The group's research showed that the majority of larger brokers already have an individual or committee(s) within their organisation that is responsible for assessing ESG strategy implementation, while this was not the case for SMEs.

The understanding of ESG targets was found to be inconsistent across the workforce, while both more senior staff and larger companies were far more likely to have a deeper understanding of their companies' targets than those in entry or intermediate level roles or at SME brokerages.

In SME brokerages, about 25% of entry level employees felt confident in their understanding of ESG targets, while more than a third of those surveyed had no understanding. Overall, only 32% of those at small brokers understood the ESG targets at their companies. **13**

Therefore, with such low rates of disclosures among SME companies, standardised methods need to be developed in addition to low cost training programmes, perhaps using machine learning that can raise the awareness of company employees which will assist in raising employee awareness of ESG targets and how to achieve them to allow for lucid and accurate disclosures of a high standard.

A broader approach and global reporting

Globally, the bulk of the ESG data available to investors historically has been derived from voluntary cooperation, from companies either answering survey questionnaires or publishing sustainability reports based on one or more of dozens of frameworks and reporting standards created by various non-profit organisations active in environmental and social causes. Voluntary disclosure of ESG information over the past 30 years has seen globally the development of several key reporting standards and frameworks noted in this Third Report. Voluntary cooperation as a strategy for disclosures to determine ESG ratings has been now deemed necessary across the globe, very early on in the City of London and more recently in South Africa's JSE.
The demand for enhanced ESG disclosure has become intense as globally, overall ESG investing has become massive, especially for larger companies of economy of scale and in the pension sectors. ESG investing has grown as much as tenfold in the last decade. Morningstar, Inc. has estimated that total assets in ESG designated funds had amounted to more than US$3.9 trillion by the end of September 2021. The development of ESG investing has been accompanied by exponential growth in the amount and types of data available for ESG investors to consider. ESG disclosures of public companies have increased to roughly 90% of the Fortune Global 500 having set carbon emission targets, up from 30% in 2009.

In the nineties, the development of the Global Reporting Initiative as a standard reporting framework for corporate social responsibility disclosures was a major step in promoting reporting focused on both ESG issues internal to a company and its external impacts on outside communities and the planet.

The European Commission, in 2014, adopted a financial directive that required certain large companies such as pension funds to disclose relevant information on how they manage and operate social and environmental challenges. This directive was intended to assist investors and other stakeholders evaluate the non-financial performance of large companies, and encourage such companies to develop a responsible approach to business. It was an early call for ESG disclosure for large public-interest companies and required information related to environmental and social matters, treatment of employees, human rights, anticorruption, and board diversity.

The Task Force on Climate-Related Financial Disclosure (TCFD) which was created in 2017 by the G20's Financial Stability Board, has been widely adopted globally and recommends disclosure concerning climate related governance,

strategies, and risks to a company presented by climate change.

Supplementing the directive, in 2019 the European Commission published new climate reporting guidelines for companies that integrate the TCFD's recommendations. To address shortcomings in the Non-Financial Reporting Directive, the European Parliament initiated a new Corporate Sustainability Reporting Directive on 10 November 2022.

The United States has been a good deal slower than Europe in regulating ESG disclosures and more piecemeal in relation to such large companies. Since 2020, disclosures focussed on long-standing financial, risk, and litigation of public companies in relation to environmental issues and, material aspects of a company's human capital management, largely following the US SEC (Securities and Exchange Commission) issued guidance that was established in 2010. After this juncture there were few mandatory requirements and only limited regulatory guidance for disclosure on sustainability issues by public companies listed or based in the United States.

After finding that this guidance was insufficient, on 21 March 2022, the SEC proposed new rules to require companies filing mandatory reports and securities registration statements with the SEC to provide detailed information about their handling of climate related risks and opportunities. This included climate-related governance, strategies, risk management, metrics, and goals based on the TCFD framework mentioned above. These proposed rules also require companies to measure and disclose greenhouse gas (GHG) emissions in accordance with the GHG Protocol methodology, the most widely known but non-binding voluntarily used international standard for calculating GHG emissions. **14**

The SEC proposal noted that several jurisdictions have already adopted disclosure requirements in accordance with the TCFD's recommendations, including Brazil, the European Union, Hong Kong, Japan, New Zealand, Singapore, Switzerland, and the United Kingdom.

The US Securities and Exchange Commission (SEC) is expected to adopt final rules requiring mandatory and binding detailed disclosures by companies of climate-related risks and opportunities by the end of 2023. The recently-formed International Sustainability Standards Board (ISSB) (see second half of this Third Report for further details), adopted two new reporting standards in June 2023; one on climate-related risks, and a second on a variety of sustainability related information.**15** Irrespective of how much harmonisation there will be between these and other ESG disclosure

standards, it is without doubt that mandatory, standardised sustainability reporting by corporations will increase significantly worldwide over the next few years.

Greenwashing

The Financial Conduct Authority (FCA) in the City of London in 2022 began to tighten rules to ban greenwashing. The FCA Director, Sacha Sardan has stated that greenwashing misleads consumers and erodes trust in all ESG products as the great growth in the amount of investment products are being marketed as green. In fact, the market for UK based responsible investment funds grew by 64% in 2021to reach £79 billion.

The FCA's rules have changed for ESG sustainable investment which investment managers must justify to the city regulator by demonstrating that they meet the criteria for the following three categories;

One, is that products which have a sustainable focus are required to invest in assets already deemed to be sustainable such as renewable energy. Second, sustainable improver products must invest assets in transitional companies that have clear goals set to transition for example, to green energy. Third, sustainable impact products that can be invested in must be developing new sustainable products rather than just buying existing companies, for example a company developing a new way to capture thermal energy.

The Director for investment and capital markets at the Investment Association, Galina Dimitrova, noted that a new labelling system is very important to guide investors at all levels to a much better understanding of what they are genuinely investing in and how the categories meet ESG, green principles.**16**

The SEC also has proposed anti-greenwashing rules applicable to investment firms. These provide that only funds with a particular ESG purpose would be allowed to label themselves as such. The new rules would also require mandatory disclosures for ESG-focused funds to enable third parties to confirm if a supposedly ESG-focused fund is implementing its stated investment purpose.

Like the SFDR, these new rules would create three categories of ESG funds;

1. Integration Funds, which would be required to disclose how ESG factors are incorporated into their investment process, in addition to any non-ESG factors

2. ESG-Focused Funds, which identify ESG factors as a major or main consideration and are therefore, required to make a more detailed disclosure
3. Impact Funds, which seek to achieve a specific ESG impact and are required to disclose precisely how the fund measures progress towards its stated objectives.

The categorisation of ESG funds on a standardised basis under new European and US funds regulations can be expected to significantly mitigate the problem of inconsistent terminology and nomenclature as to what constitutes and what may not be categorised as an ESG investment. This will potentially serve to facilitate more accurate conclusions on the financial performance of various ESG investment disclosure strategies which provide regulators with accurate measurements on which to base ratings.

In November 2021, the International Financial Reporting Standards (IRFS) Foundation—which administers the IFRS financial accounting standards that are used in most jurisdictions other than the
United States—announced the formation of the ISSB to develop a comprehensive global baseline of sustainability disclosure standards. The ISSB will sit alongside the IRFS International Accounting Standards Board, and it can be expected that jurisdictions that require financial reporting based on IFRS standards will also require sustainability reporting under ISSB standards. As mentioned in the second half of the Third Report, there is a rapidly accelerating consolidation into the ISSB of the most internationally significant existing global sustainability disclosure frameworks and standards, including those of the SASB.**17**

In 2022, the Financial Conduct Authority decided to introduce three different labels for green funds to facilitate accurate and clear disclosure. They introduced a general anti-greenwashing duty that will require fund managers to provide evidence that they have done what they said. FCA's market research found that four out of five adults want their savings to both do good and offer a return.

Taken together, this consolidation of the ESG disclosure ecosystem, the continued enhancement and standardisation of ESG data, and the analyses it promises to yield, should enable market participants to more precisely evaluate when ESG factors are relevant to the creation of long-term value, which in turn can facilitate more confident ESG investment decisions.

The three labels that will come into force in about a year's time are the following;

1. Sustainable focus are funds that meet a credible standard of ESG.
2. Sustainable improvers that can deliver measurable improvements in the long - term sustainability profile of assets.
3. Sustainable impact which has a clear objective to produce measurable and positive contributions to sustainable outcomes.**18**

The success of ESG becoming embedded in company organisation some argue rests with activists. Tom Braithwaite for example, notes that PwC carried out a US$12 bn drive by hiring 100,000 new staff to advise companies on delivering sustainable outcomes; many who were derived from the auditing sector. Yet, he argues that it was not these money motivated marketeers that persuaded ExxonMobil to curtail new gas and oil developments. Rather, it was the activist fund Engine No.1 with extraordinary effort that managed to place three experienced and climate aware Directors on the ExxonMobil Board. This caused shares to soar and demonstrated how effective activists can be in changing the mindset of even the biggest supporters of fossil fuel companies.**19**

More heated political debate

In addition to this massive and widespread regulatory momentum to require greater volume, consistency, and reliability of corporate ESG disclosures, there is also increasing regulation designed to mitigate "greenwashing" where the potential social and environmental benefits of a fund's ESG investment strategy have been overstated or even blatantly false.

In addition to greenwashing both ecological and social issues are becoming more acrimonious and politically based according to analysis conducted by Cision. It analysed articles in the traditional media as well as posts on social media such as Twitter, Facebook, Instagram, YouTube, Reddit and Tumblr in English, Spanish, French, German and Italian during the period of January 2020 and June 2023.

A variety of differences were found in the emphasis placed on the key elements of ESG internationally, with most countries focused on social issues, including human rights violations, racism, and LGBTQ rights.

In Germany, for example, during Cision's assessment period, it was found that ecological issues increased by 74% while social issues by 8% and corporate

governance issues by even less at 6%. The ecological topics focus on climate protests, and politics, such as the new climate protection law. A total of 29% of the sentiments across all ESG media scrutinised were negative, characterised by anger, disgust, sadness, or fear. This could be linked to the fact that social media is known to play with emotions and often attracts those who have mental instability or are naïve in the estimation of the author of the first half of this Third ESG Report.

"Companies are becoming more and more transparent due to the increasing ESG reporting requirements, while at the same time being confronted to a somewhat greater extent with accusations of greenwashing. In terms of communications, they should show a clear stance on ESG issues and give specific examples of their progress," said Manuela Schreckenbach, head of insights consulting, DACH at Cision.

In all the languages analysed, the topic of corporate governance is only rarely mentioned in the context of ESG reporting. However, the analysis clearly shows that protests and politics can often determine the ESG agenda.**20**

Supply Chain complications

It is notable that almost half of the world's insourcing countries are viewed at high risk of supply chain ESG violations. The UK, Germany, Portugal, and Italy are all among the list of countries ranked as at high risk from the most severe infractions which include among others, forced labour, child labour, freedom of association and wage-related violations. China has increasingly been rejected as a sourcing market due to its severe record of human rights violations such as using forced/slave labour. Yet, supply chain managers are exploring new insourcing markets, such as Vietnam and, Mexico which may also have their own problems.

These findings are of global assurance specialist, LRQA's, bi-annual *Supply Chain ESG Risk Ratings Report*, which compiles data annually from 20,000 global supplier audits.

The findings also reflect an overall decline in audit transparency on a worldwide basis. Sourcing countries such as Vietnam, Thailand, Indonesia, India, China, and Italy have all become less transparent since the COVID-19 pandemic. Auditors are increasingly becoming unable to access accurate information and make conclusions from site visits. This decline in transparency when compared to pre-pandemic levels

has complicated the ability of many companies to govern higher risk levels, with suppliers in 50 sourcing geographies on average less transparent than in the previous year.

This report has been compiled by LRQA's sustainability division, ELEVATE, which collects information from over 45 million data points derived from in person site visits collated in ELEVATE's data analytics solution, EiQ.

Kevin Franklin, managing director of advisory at ELEVATE, said commenting on the Report's findings: "The current geopolitical, economic and legislative climate has made it increasingly difficult for businesses across the globe to be confident about ESG risk in their supply chains. Even historically lower risk Western markets have started to slip. It is now clear that simply homeshoring or nearshoring manufacturing in countries previously thought to be 'safe' from egregious ESG risks is not enough.

"Systematic and proactive supply chain risk assessment, monitoring and management should be applied in all sourcing locations to avoid negative business impacts and trade disruption. **21**

Recommendations

1. SME companies need to have available to them an organisation that provides' assistance with an affordable training course or measurement programme (non-profit) like BCorp that familiarises employees with ESG principles, how to measure them and integrate them into daily practice to facilitate high standard disclosures. The majority, of companies in the UK are SMEs (about 95%) and companies of this size need to be integrated into the ESG disclosures ratings process. SME companies should not be penalised or left behind in the global requirement of adopting ESG principles.

2. There needs to be more research undertaken to ascertain the extent to which supply chain companies are undermining accurate ESG disclosures and are affecting not only the ratings but standards of often large companies they supply to in relation to integrating and upholding ESG principles.

3. There increasingly needs to be global standardisation of measurement systems so high standards of ESG disclosure can be achieved and understood by all stakeholders.To avoid greenwashing a template like the City of London’s

4. Financial Conduct Authority ‘s three types of investing models could be adopted more widely so investors will know what they are investing in an informed and clear manner.

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More from: David Cifrino, McDermott Will & Emery
David A. Cifrino is Counsel at McDermott Will & Emery LLP. This post is based on his MWE memorandum. Related research from the Program on Corporate Governance includes The Illusory Promise of Stakeholder Governance (discussed on the Forum here) by Lucian A. Bebchuk and Roberto Tallarita; For Whom Corporate Leaders Bargain (discussed on the Forum here) by Lucian Bebchuk, Kobi Kastiel, Roberto Tallarita and Stakeholder Capitalism in the Time of COVID (discussed on the Forum here) both by Lucian Bebchuk, Kobi Kastiel, Roberto Tallarita; Restoration: The Role Stakeholder Governance Must Play in Recreating a Fair and Sustainable American Economy—A Reply to Professor Rock (discussed on the Forum here) by Leo E. Strine, Jr.; and Corporate Purpose and Corporate Competition (discussed on the Forum here) by Mark J. Roe.
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ESG Disclosures: Overview and South Africa

ESG disclosures in South Africa are recommended by the Johannesburg Stock Exchange (JSE) (JSE Metrics, 2023). While it has been possible to give a technical overview of ESG since 1994, this falls outside the scope of this report (King I Report, 1994, pp. 1 with reference to the community, environment etcetera). Nevertheless, in brief, in 1994 the King I Report on Good Corporate Governance clearly stated that good corporate governance practices include consideration of the environment, community and state. These terms closely correspond to the acronym ESG: reference to the environment is self-explanatory, but community refers to social relations, with reference to a United Nations mandate, a state should in principle adhere to the international instruments of that organisation (Dugard, 2020, pp.89-90). The King II Report, meanwhile, refers to the importance of the United Nations Global Compact, which the Paris Stock Exchange also deems relevant to the CAC 40 ESG Index (King II Report, 2009, pp.23; CAC 40 ESG Index, 2021).

In 2016, the JSE played an important role in the development of ESG metrics and contributed to the development of the World Federation of Exchanges (WFE) ESG metrics which have been available since 2018 (WFE ESG Metrics, 2018, foreword). Subsequently, the New York Stock Exchange has made reference to the WFE ESG metrics with regards to its listed companies (NY Stock Exchange, 2023). These metrics

are uncomplicated, referring only to baseline ESG indicators (approximately 30 in total) that may guide listed companies in completing their sustainability reports. These baseline WFE ESG metrics can, to some extent, be identified in the JSE ESG metrics that have been further developed since 2022. The JSE metrics contain approximately 60 indicators/factors compared to the 30 proposed by the WFE. However, the fact that the JSE is informing its listed companies about relevant ESG disclosures is a step in the right direction. It should also be noted that the United Nations' Sustainable Stock Exchanges (SSE) initiative recommends the WFE metrics as baseline indicators for all stock exchanges that are members of the SSE (UNSSE ESG Metrics, 2023). This should assist listed companies to understand the importance of ESG disclosures. The JSE, the NY Stock Exchange, the London Stock Exchange (LSE) and the Paris Stock Exchange are all members of the SSE. Hence, we believe that the SSE will play a greater role in the future in prescribing suitable ESG metrics to its member stock exchanges as a way of establishing uniformity in global ESG reporting.

What is also of interest is that the JSE ESG metrics incorporate the guidelines for ESG reporting published by the Global Reporting Initiative (GRI) and the Sustainable Accounting Standards Board (SASB) (JSE Metrics, 2023). The SASB has merged with the Integrated Reporting Framework (IRF) to create the Value Reporting Foundation (VRF), and since August 2022, the SASB has stated that both the VRF and the SASB will disappear in future and only the International Financial Reporting Standards (IFRS) will be used as the standard for ESG reporting (SASB Standards, 2023). A discussion of these guidelines falls outside the scope of this report, but it should be emphasised that the SASB allows listed companies to incorporate other ESG metrics or frameworks when developing their own ESG metrics for disclosure purposes (SASB Standards, 2023). The JSE metrics also incorporate the GRI and SASB ESG provisions, among others, in their proposed metrics, illustrating the flexibility of the JSE ESG metrics in incorporating other ESG disclosures or frameworks to ensure proper disclosure in companies sustainability reports. This reflects the tendency, as highlighted in the first half of this report, to have 3 disclosure strategies that narrow focus, rely on peers and which are broad as well as multifaceted in nature.

Yet, it should be noted that external companies that rate ESG compliance, for example MSCI, Sustainalytics and Morningstar, use their own ESG metrics (Morningstar, 2023; MSCI, 2023; Sustainalytics, 2023). Hence, these companies can only accurately rate a listed company if it is able to disclose all relevant ESG

information in its sustainability reports. If a company is unable to report on a specific component of ESG, for example the environmental, which requires the total carbon emissions produced by the company to be reported, it is possible that the company may receive a poor ESG rating (MSCI, 2023). Currently, asset managers at Old Mutual in South Africa are making use of MSCI ESG metrics, which are usually public information as they are available on the internet (Old Mutual MSCI, 2023). For this reason, a JSE-listed company may incorporate both the JSE and the MSCI metrics to produce comprehensive ESG disclosures in its sustainability reports and to achieve a high MSCI rating. We will briefly explain the ESG factors of the JSE ESG metrics as follows (JSE Metrics, 2023):

Environmental disclosures required:

- Number of different gases or CO_2 produced by the company
- Ability to comply with the Paris Agreement
- Transition plan to reduce fossil fuel dependency
- Nitrogen oxides (NOx), sulphur oxides (SOx), volatile organic compounds and other gases used in the supply chain
- Certification process for, for example sustainable supply chains

Compliance with the international instrument, the Paris Treaty on Climate Change, forms part of the ESG factors that need to be complied with (JSE Metrics, 2023, refers to this Treaty in the ESG metrics). In terms of this requirement, the board of directors of a listed company must familiarise itself with the contents of the Paris Treaty and disclose compliance with this Treaty in the company's sustainability report. In a recent case, known as the 'dirty air case' – *The Trustees for the Time Being of Groundwork Trust v The Minister of Environmental Affairs* reported case number 39724/2019 – it was held that the South African Minister of Environmental Affairs has a legal duty to measure, for example, carbon emissions produced by companies in South Africa (paras 241.2-241.3 of the case). To measure carbon emissions and/or other gases, the Minister may make use of external companies with the necessary technology, for example the Finnish company Gasmet, which uses satellite technology and operates in 80 countries globally to measure the gases produced by individual companies (Gasmet, 2023). So far, the minister has not issued any regulations in this regard.

Social relations disclosures required:

- Percentage of employees per race
- Ratio of the CEO’s remuneration to that of company employees
- Involvement in human rights investigations or human rights violations in other countries
- Supply chains used by the company and their possible economic effects on employees
- Privacy of consumers (right to privacy) and client data, and number of reported breaches
- Risks posed to employees, the environment, and communities

In South Africa, unemployment is extremely high, estimated at 32.9% of the adult population (total population is estimated at 70 million people of which approximately 40 million are adults (16–65 years)) (Gumbi, 2023). A JSE-listed company has introduced a unique business model that could help unemployed people to receive income twice per year (interim dividend and final dividend). The company, known as Imagined Earth, has built vending machines all over South Africa, which allows a person to deposit recyclables in exchange for Imagined Earth listed shares (Imagined Earth, 2023). A depositor can continue indefinitely; there is no fixed number of deposits allowed, thus allowing them to receive an interim and final dividend from the company on an annual basis, with the possibility of increasing the amounts of dividends in the future.

Good corporate governance disclosures required:

- Composition of the board of directors and committees by race and gender
- Percentage of company employees that has received training in anticorruption measures
- Confirmed cases of corruption
- Communication strategies with stakeholders concerning the prevention of corruption
- Professional services available to explain ethics to the board of directors

In this component, companies must report any confirmed cases of corruption – cases reported to the South African Police Service. It is not a requirement to understand how many of those cases were successfully prosecuted by the state as this serves merely as a mechanism to understand the scope of corruption practices in a particular South African company. Companies are required to actively reduce

corruption if they are to attract investors, both local and foreign. If the company is unable to reduce corrupt practices, the number of reported cases will indicate that the company is not serious about promoting a corruption-free business environment (Gordon Institute of Business, 2023, foreword). It should be noted that the business environment in South Africa has deteriorated to such an extent that the economy is largely based on corrupt activities or practices (Judicial Commission of Inquiry, 2022, see in general the various written reports).

In addition to the above disclosures of ESG metrics, the JSE also has a partnership agreement with the London Stock Exchange (LSE) (FTSE/Russel, 2023). With the terms of this agreement, the LSE and JSE have developed the FTSE/JSE Top 30 Index – the Top 30 companies that comply with ESG disclosures. The ESG ratings of these companies are done by FTSE/Russell, and the individual rating for each company is not disclosed. The purpose of this partnership agreement is to educate South African asset managers on why ESG reporting is important and how such disclosures could affect ESG ratings for listed companies (FTSE/Russel, 2023). For this reason, we believe that until such time that FTSE/Russell feels comfortable with its ESG ratings or disclosures, it will be important to keep this type of information confidential to avoid unnecessary public comment. In summary, the ESG metrics used by the FTSE/Russell Index consist of approximately 300 factors, although the Top 30 Index is rated on an average of 100 factors (FTSE/Russel, 2023).

1. Definition of disclosures and how the lack of them adversely affects companies' ESG ratings

Before we focus on ESG it is important to make a few comments on corporate social responsibility (CSR) (King IV, 2016, the definitions for sustainability and capital). The online document should not be used by the public, as it changes constantly. This term, which lacks any technical reference to other relevant corporate governance documents, simply means that the company has a duty to promote social relations or social matters. In this regard, the acronym focuses only on the second component of ESG. However, without any technical references, it is possible to change the word order of the CSR to 'responsibility, social, and corporate', which would appear to change the meaning of the phrase. In this instance, social and corporate, the latter of

which perhaps includes corporate governance, could be comparable to the last two components of ESG. However, responsibility is a very broad term, which could also include, among other things, the environment. Notably, King IV defines sustainable development using the following keywords: ‘environment or Corporate Social Responsibility’ (King IV, 2016). In this regard, it seems that the environment is not part of corporate social responsibility, but holistically both are necessary for sustainable development. King IV states that these terms are part of a triple context, economy, society, and the environment, but the triple context is not comparable to the definition for responsible investment. King IV defines responsible investment as a way of taking note of environmental, social, and corporate governance practices (ESG) – practices to allow the board to take better business decisions (King IV, 2016). For this reason, we could argue that corporate social responsibility is part of a triple context, but making proper business and investment decisions requires a responsible investment approach, which demands ESG disclosures that could be rated by a specific rating company, for example the AAA rating by MSCI – illustrated later in this report (King IV, 2016). For this reason, external companies such as MSCI, Sustainalytics and Moody’s rate companies in terms of their own ESG Metrics or practices with the purpose of allowing investors an opportunity to decide whether to invest in the companies or not which is the bottom line of ESG. Currently, investors will only invest in a listed company if it is sustainable within the long term, thus having the potential to create value for the investor by, protecting the environment, not exploiting social relations and/or exercising good corporate governance practices as a result of an assigned ESG rating, for example, AAA. However, MSCI can only rate a company successfully if it discloses all the factors that are required for a proper ESG rating in its sustainability report (MSCI, 2023). Although MSCI uses its own ESG metrics, and the MSCI metrics contain additional factors or disclosures that the JSE ESG metrics do not include, a listed company could avoid a poor ESG rating by incorporating other ESG factors as proposed by, for example, MSCI and those of the GRI and SASB etcetera (JSE Metrics, 2023; MSCI, 2023;SASB Primer, 2023). The SASB recognises the fact that it is impossible to develop ESG metrics that are relevant to all types of company; some companies in the same industry may have supply chains that need to be rated in terms of ESG, while others in the same industry may have no supply chains that require such ratings, meaning that they cannot be rated poorly on this basis (SASB Other Frameworks, 2023). It is thus important to understand which ESG factors are truly

relevant in promoting responsible ESG rating practices. While defining these practices falls outside the scope of this report, they may be classified into four separate categories:

a) *Stock exchange metrics that acknowledge other standards*

The ESG metrics recommended by the JSE to its listed companies also refer to those of the SASB and the GRI, among others (JSE Metrics, 2023). It is important to understand here that the JSE ESG metrics are largely based on the WFE metrics. These metrics only disclose baseline factors or indicators that companies should be able to report or disclose, in order to make companies familiar with ESG reporting. In the future, the JSE ESG metrics for reporting and disclosure purposes will become more complex. For example, at the end of 2022, the JSE ESG metrics consisted of approximately 30 factors, while currently the social relations component alone consists of approximately 30 factors. Although the JSE metrics refer to the SASB, GRI to mention a few, it is suggested that if a stock exchange decides on a particular external ESG rating company, for example MSCI, that MSCI metrics should, for the sake of transparency, also be incorporated in the JSE metrics, thus allowing listed companies an opportunity to report on those factors to obtain a good ESG rating from MSCI. If the company cannot do so, then the company would at least know what to do in the future to improve its rating (MSCI, 2023).

b) *The stock exchange uses its own ESG metrics and carries out ESG ratings without the assistance of an external rating company*

The Paris Stock Exchange, or Euronext, uses a unique method to rate whether companies are ESG compliant or not: its CAC 40 ESG Index consists of 40 listed companies which the administrator (Euronext) screens for ESG compliance (CAC 40 ESG Index, 2021). This Index is managed according to a rule book, which could be amended to include more appropriate mechanisms for screening companies' ESG compliance. Currently, the index is making use of international law instruments, for example the United Nations Global Compact. This instrument and its importance for corporate governance practices has also been explained in King II (King II, 2002, pp.

11). In terms of the United Nations Global Compact, companies that make use of child labour, that violate human rights (irrespective whether a violation is justified by a state), or that are ignoring the importance of collective bargaining between the employer (company) and its employees cannot be deemed ESG compliant (UN Global Compact, 2023). This instrument has 10 principles that should be complied with by companies that are part of the CAC 40 ESG Index including JSE listed companies as a result of King II (a popular misconception exists in South Africa that only King IV is relevant and applicable). If a company violates this instrument, it will be delisted or at least excluded from the CAC 40 ESG Index, but the same does not apply to the JSE. Other relevant business activities that are contrary to this UN instrument include companies that participate in the production of tobacco products and those that participate in the development or manufacture of biological and chemical weapons etcetera. On the other hand, the JSE lists, for example, companies that manufacture tobacco products and the public are allowed to buy and sell these companies shares.

However, we do not know how the Paris Stock Exchange (Euronext) will amend its CAC 40 ESG Index requirements in the future, owing to new developments in ESG that have taken place in Europe as a result of the recently adopted Corporate Sustainability Reporting Directive (CSRD) (CSRD, 2022). However, the CSRD and its implications fall outside the scope of this report. In addition to the UN Global Compact, the Paris Stock Exchange also makes use of unique ESG metrics to rate the individual companies on the CAC 40 ESG Index. These metrics are known as Equitics® (CAC 40 ESG Index, 2021). The content of these metrics is not public information, but the stock exchange rates the CAC 40 companies out of 100. We do not know how the actual rating is assigned to an individual company that is part of the CAC 40 ESG Index; however, one asset manager, BNP Paribas, which makes use of Morningstar, has rated the CAC 40 ESG as 4/5; meaning it has been assigned an 80% ESG rating (BNP Paribas CAC 40 ESG Index, 2023).

c) *The stock exchange proposes an independent company to assist with ESG disclosures and ESG ratings*

In our second ESG report, we mentioned the innovative approach of Wolturs Kluwer and how it has developed a software program to help companies record and disclose

ESG factors in their financial statements or sustainability reports. NASDAQ, has been sending a circular informing its listed companies to make use of a company called ESG Book (NASDAQ, 2023). ESG Book is an independent company that has also developed the ESG software program (CISION, 2023). This program considers approximately 450 ESG factors/indicators to assist companies with their ESG disclosures. The program provides a dashboard on which subscribers can view all 450 ESG factors and it informs the subscriber as to which ESG factors are relevant to the company and which factors should also be reported on by the company in future. A unique feature is the fact that the software program can rate a company for ESG automatically without the assistance of an external rating company such as MSCI or Morningstar (CISION, 2023). In this way, companies are compared to their peers and it enables them to establish immediately what should be done to improve their ESG rating – ESG Book is transparent in this regard. We do not know where ESG Book obtained the 450 ESG factors, but we believe that the source is probably a combination of different ESG frameworks, for example the UN Global Compact, the GRI, the SASB (in future only IFRS) and the WFE among others. The question remains how objective ESG Book is, since subscribers are allowed to disclose as many ESG factors as possible – probably without submitting objective evidence or without being ‘audited’ or ‘screened’ by a compliance officer of the listed company (CISION, 2023). An ESG compliance officer is someone who has successfully completed the SASB ESG exam (SASB Exam, 2023, level I and II are examples). In this regard, we do not know how the ESG Book information or data is being ‘audited’ for accuracy among other considerations (Bally’s Sustainability Report, 2022, pp.6 makes reference to a compliance officer).

d) *United Nations Sustainable Stock Exchanges Initiative (SSE)*

The Sustainable Stock Exchanges (SEE) Initiative of the United Nations refers to the WFE metrics (UNSSE ESG Metrics, 2023). Currently, the SSE has 130 stock exchanges as members that are part of this initiative (UNSSE, 2023). The SSE gives training to exchanges on how to understand and develop their proposed ESG metrics. Currently, only 72 stock exchanges globally have proposed ESG metrics in writing, and only 49 have a dedicated ESG index, for example the CAC 40 ESG Index (UNSSE,

2023). Furthermore, only 34 stock exchanges have mandatory ESG listing requirements (UNSSE, 2023). In the future, we believe that the SSE will play a greater role in managing and overseeing stock exchanges and will provide or require similar ESG disclosures that apply to all SSE member stock exchanges. In this regard, it is important to focus on the fact that in the present there is no difference between lawful and unlawful human rights violations in South Africa: if the stock exchange subscribes to the SSE as a member, there should be in principle a universal application of human rights and what constitutes violations thereof (Press, 2023). To illustrate this, the JSE ESG metrics require listed companies to report on human rights violations committed in other states, but domestically South Africa practises lawful human rights violations due to relevant provisions of the South African Constitution of 1996 being embedded in various legislation that is relevant to a company's business activities (Ackerman, 2023 a white owned company in South Africa, with less than 50 employees or greater than 50 employees is subject to legislation to transform the business from white to black (employees and shareholding included) – known as level 1 of BBBEE, the legislation does not apply vice versa; see in general Walubengo, 2022; Press, 2023 in principle, the latter approach is contrary to the main objective of the social relations leg of ESG). Other states that have accepted the UN Guiding Principles on Human Rights and Business into civil law, for example the French Duty of Corporate Vigilance, 2017, cannot justify human rights violations in other parts of the world – the French authorities will penalise French companies (subsidiaries of holding companies that are operating in different parts of the world) that are part of these violations (Cossart, Chaplier and Beau de Lomenie, 2017, pp.317). The SSE is also considering different ESG frameworks or standards, and in principle seems to prefer the SASB over the International Sustainability Standards Board (ISSB), for example (UNSSE, 2023). The SSE acknowledges or supports stock exchanges that incorporate the GRI, the SASB (which will eventually become the IFRS), the Task Force on Climate-related Disclosures (TCFD), the International Integrated Reporting Council (IIRC), the Climate Disclosures Standards Board (CDSB) and the Carbon Disclosure Project (CDP) to mention a few. The SSE makes no reference to other institutions that are part of ESG disclosures, for example the Science Based Targets Initiative (SBTi), the Enterprise of the Environment (EpE) and ISO 14001 to mention just a few (UNSSE, 2023). Therefore, the SSE takes a flexible approach to allow stock exchanges to develop their own ESG metrics; however, eventually all stock exchanges - in our opinion - will have

to be standardised in terms of required or mandatory SSE ESG disclosures. In future, we foresee that if a listed company has not been ESG rated, it will be impossible for it to participate in global business affairs. What we have also observed on the SSE website is that while the NY Stock Exchange participates in SSE initiatives, the NASDAQ is not a frequent participant.

2. ESG data disclosure levels

Stock exchanges play a dominant role in grading listed companies for ESG compliance. For example, the Singapore Stock Exchange (SGX) makes use of Systainalytics as well as other external rating companies to rate listed companies (SGX ESG Ratings, 2023, disclosure of different external rating companies). It is noteworthy that an external rating company develops its own ESG metrics to rate companies (MSCI, 2023). For this reason, different external rating companies could assign various ESG ratings to listed companies; for instance, a listed company could be rated very highly by MSCI but lower by other external rating companies (SGX ESG Ratings, 2023). On the SGX, for example, China Aviation was rated by MSCI as A while Sustainalytics in contrast rated it in terms of ESG as being at high risk for noncompliance – discussed later in this report. In another example, CapitaLand Invest is rated by MSCI as A and by Sustainalytics as a low-risk company (SGX ESG Ratings, 2023).

The SGX also discloses ESG ratings from FTSE/Russell, S&P ESG and Moody's ESG. SGX has developed a baseline factor or indicator of ESG metrics for its listed companies, known as ESG Core Metrics, to be used as a reference by listed companies that want to report on ESG in their financial statements or sustainability reports in future (SGX Core ESG Metrics, 2023). The ESG Core Metrics contain approximately 30 factors, while the FTSE/Russell ESG metrics contain approximately 300 factors. Accordingly, in future it will remain difficult to rate a listed company that does not report on all 300 relevant ESG factors. Yet, on the SGX, CapLand Ascendas is rated in terms of ESG by FTSE/Russell as 2.9, MSCI as A, Systainalytics as low risk, S&P as 23 and Moody's as 31 (SGX ESG Ratings, 2023). In such cases, it is imperative to understand that the highest score allocated by MSCI is a AAA and the lowest is a CCC, but the other rating companies make use of numbers such as 2.9 or

23 or 31. Consequently, the meaning of these ratings must be established to understand whether the score reflects a high or a low ESG rating. Therefore, through the SSE Initiative, stock exchanges could insist that external companies should make use of universally accepted ESG metrics and rating methods, for example based on the alphabet only. What is certain is that future directions of ESG ratings will unfold over time.

Additionally, the largest Asset Management company globally, Blackrock, also discloses any controversies relevant to listed companies, for example companies that are in breach of the UN Global Compact or that participate in the production of tobacco, violation of human rights among other issues (Blackrock ishares, 2023). The Blackrock-managed iShares Core MSCI World UCITS ETF Index is a very good example of these disclosures, which also form part of CAC 40 ESG requirements, although iShares companies are not included in this index. Such controversies include (Blackrock ishares, 2023):

- Critical controversies related to the United Nations Global Compact 0.53%
- Any involvement in the production of tobacco 0.68%
- Any involvement in thermal coal 0.30%
- Any involvement in tar sand and oil shale extraction 0.31%
- Production or sale of civilian firearms 0.16%
- Involvement with controversial weapons, biological weapons, chemical weapons, etc. 0.63%

We do not know which of the companies on the iShares Core MSCI World UCITS ETF Index (the index/fund comprises more than 1000 companies but only eight are disclosed on the Blackrock factsheet for the iShares index/fund, for example Apple, Tesla) have contravened the prohibitions listed above or how the percentages have been calculated (Blackrock ishares, 2023, probably 0.53% of a 1000 companies violated the UN Global Compact or 0.68% is involved in tobacco production). The JSE, for example, does not require the disclosure of such controversies for its listed companies, but since King II refers to the UN Global Compact, we may assume that companies in South Africa may report voluntarily on this document – for any violations or breaches – similar to the example above provided by Blackrock, for example tobacco, sale of firearms etcetera. .

a. *Why are pension fund managers/trustees, especially in listed companies, not releasing relevant data that will assist in accurately assessing their compliance with ESG principles?*

Pension fund managers or trustees generally use asset managers to invest pension funds on stock exchanges. Without giving a technical explanation in terms of the South African Pension Funds Act of 1956, pension fund managers or trustees invest in companies that will at least be able to maintain or increase the relevant pension funds for sustainability purposes. Sustainability purposes require appropriate investment decisions and those decisions should be based on ESG data or criteria. To rate companies in terms of ESG compliance is a very expensive exercise – estimated to be US$480 000 per rating (CISION, 2023). If a pension fund were to use member funds for rating purposes this could have a negative effect on the future sustainability of the fund. An asset manager may, for example, manage 30 pension funds, making it much more convenient to rate companies individually that are aligned to the investment strategies of the pension fund. Therefore, if 30 funds invest collectively in 60 listed companies, in various combinations, it is possible for the asset manager to rate an investment portfolio in terms of ESG instead of the pension fund. The Old Mutual Equity Fund is an example in this regard – the investment portfolio consists of the following JSE-listed companies (Old Mutual Equity Fund, 2022):

a) ABSA Group Ltd.
b) British-American Tobacco
c) First Rand Ltd.
d) Standard Bank Group Ltd
e) Prosus NV
f) Sasol Ltd.
g) Glencore PLC
h) Naspers Ltd
i) MTN Group Ltd
j) Anglo-American PLC

The asset manager, Old Mutual, used MSCI to rate this portfolio (see the above list) as AAA on November 2022. Of the companies included in this portfolio, Sasol is a

fossil fuel company and Anglo American is a mining company in South Africa. The individual rating for each company in the portfolio is not disclosed, only the aggregate ESG rating. Hence, pension funds that invest in this Old Mutual portfolio will be able to tell their members that they are contributing to a sustainable investment portfolio that is currently rated as AAA, the best possible rating a portfolio can receive. However, if the JSE were to take a similar approach to the SGX, dedicating a specific webpage to listed company ESG ratings, pension fund members/contributors could view the individual ESG ratings for listed companies in an investment portfolio. The SGX discloses the following (SGX ESG Ratings, 2023):

Table 1

Company name	FTSE/Russell	MSCI	Sustainalytics	S&P	Moody's
CapitaLand Ascendas	2.9	A	Low risk	23	31
CapLand Ascott	2.2	BB	Low risk	39	-
China Aviation	-	A	High risk	14	-
ComfortDelGro	3.1	AA	Low risk	62	39

Therefore, it is clear that the ESG ratings given to listed companies by outside rating companies differ. It is therefore possible that the companies in an investment portfolio could supply their individual MSCI rating, for example, to the asset manager of a pension fund which in turn will merely ask MSCI to calculate the aggregate ESG rating for the portfolio; which could be for far less than $480 000 as mentioned above. We are merely speculating here, since we do not have written material to support this statement. However, it may also be asked, how many AAAs should be required in an investment portfolio to obtain a AAA rating? Sasol in the Old Mutual Equity Fund is a fossil fuel company and may have received only a CCC rating (lowest rating), for example.

b. *Why are companies failing to disclose detailed plans to reach net zero and to publish data that will allow stakeholders to assess and measure their performance in relation to ESG?*

In the case of *Trustees for the Time Being of Groundwork Trust v Minister of Environmental Affairs* (39724/2019) [2022] ZAGPPHC 208, the court had to decide whether the South African Minister of Environmental Affairs has a legal duty to monitor, inter alia, carbon emissions. While the minister indicated that no such legal duty exists, the court held that the Minister has a legal duty based on a provision in the South African Constitution of 1996, which imposes a fundamental human right; namely, that everyone has a right to enjoy a safe environment. For this reason, the Minister was ordered to draft regulations pertaining to the monitoring of the carbon emissions of individual companies in South Africa. Such regulations should stipulate that if a company violates the regulated carbon emissions, it will either be fined or deregistered as a company. Technology for monitoring companies' individual carbon emissions exists, for example, Gasmet, a Finnish company, uses satellite technology to monitor carbon emissions. In future, we believe that as a result of the *Trustees* case, companies will be more diligent in monitoring and/or reducing carbon emissions. It is also possible to simply focus on a company's electricity bill, that is its electricity consumption, to understand the amount of carbon it currently emits. Eskom, the South African electricity provider, uses coal-powered plants to generate electricity; hence, the greater a company's invoice or bill amount, the greater its carbon footprint. The Generally Accepted Accounting Principles (GAAP) recommend that companies should disclose their business strategies for reducing their carbon footprints in their sustainability reports (Jenifer, 2022, no page numbering).

Currently, it is only JSE-listed companies that are required to make ESG disclosures in either their financial statements or sustainability reports – unlisted companies or businesses in South Africa are not required to do so (JSE Metrics, 2023). What regulations to be issued by the minister in the above case as to how listed and unlisted companies will also be monitored by the government in the future will unfold in time. However, it is possible to assign a different weight to each ESG component to make a company ESG compliant during its transition period – United Nations Sustainability Goals for 2030 where 2030 could be interpreted as the transition period (UN Goals, 2023). The Old Mutual Equity Fund portfolio is restated here to support the discussion that follows:

a) ABSA Group Ltd

b) British-American Tobacco
c) First Rand Ltd
d) Standard Bank Group Ltd
e) Prosus NV
f) Sasol Ltd
g) Glencore PLC
h) Naspers Ltd
i) MTN Group Ltd
j) Anglo-American PLC

Since Sasol is a fossil fuel company, based on the environmental component of ESG it will not be sustainable in the long term – the same applies to Anglo American a mining company. However, an external rating company could assign a weight of 10% to the environmental component for Sasol and weights of 45% to social relations and good corporate governance, respectively. Accordingly, during its transition period, Sasol may be rated as 90% ESG compliant despite failing the environmental component to assign an aggregate or overall rating of AAA to this Old Mutual investment portfolio, even though it contains a mining company, tobacco company and a fossil fuel company. The tobacco company (British American Tobacco) may be assigned a 10% weight for social relations, since tobacco products decrease a person's life expectancy, thus violating the right to life or UN Global Compact (Prescient, 2022, see for a general discussion). It is unclear how long the transition period will be – the United Nations Sustainable Goals refers to 2030 as the 'deadline' for achieving sustainable practices. However, most companies have agreed, in public, to be carbon free by 2040 in South Africa (Toyota, 2023). It is therefore possible to assign a 10% weight to Sasol's environmental component for the next 20 years or so, unless the South African Government can issue environmental regulations as required by the *Trustees for the Time Being of Groundwork Trust v Minister of Environmental Affairs* (39724/2019) [2022] ZAGPPHC 208, as discussed earlier, moving 2040 to 2030, as an example.

c. *Discussion of the environment component in terms of greenhouse gas emissions, the social leg in terms of employee welfare and fair practices, and the governance leg in terms of practices like board diversity*

On a domestic level, the JSE has proposed that ESG metrics for listed companies could also be used by unlisted companies in South Africa (JSE, 2023). However, in future, we believe that more and more unlisted companies should be participating in ESG disclosures in their financial statements or sustainability reports. We believe that the South African government will follow a similar approach to that of the Organisation for Co-operation and Development (OECD) by focusing first on the environmental component of the ESG, and as time passes the other two components will be focused on (OECD ESG Ratings and Climate, 2022, Foreword of the document). We have noted that in the *Trustees* case the Minister of Environmental Affairs was issued with a court order that requires the drafting of regulations on how to monitor, inter alia, carbon emissions, as well as the penalties in the event of non-compliance – relevant to both listed and unlisted companies. While King IV is relevant to both listed and unlisted companies, the King I, King II and King III reports should also be considered by these companies. For example, King II refers to the UN Global Compact and its importance for companies, and companies could examine the CAC 40 ESG Index to understand why the UN Global Compact should be a benchmark for ESG compliance.

The OECD has developed an ESG Ratings and Climate Transition document, focusing on the environmental leg of ESG and metrics to measure compliance with this leg only. This document was issued in June 2022, and could also be applied by countries that are not members of the OECD such as South Africa. The OECD recognises the risks associated with climate change and what countries should be doing in order to become carbon-free states in future (OECD ESG Ratings and Climate, 2022, pp. 39 in general). The OECD suggests that countries could start by implementing the TFCD to promote disclosures relevant to the environmental component of ESG. Any shortcoming in the TCFD could be addressed by domestic legislation. Therefore, the OECD clearly recognises the TCFD as part of *ius cogens*; that is, those rules of international law that are germane to each, and every country and cannot be violated by any country or state (OECD ESG Ratings and Climate, 2022, pp.39 the importance of climate change cannot be ignored). However, the OECD also recognises that a high score for the environmental component of ESG based on metrics is not always a true indication of a clear commitment to be carbon free, among other issues (OECD ESG Ratings and Climate, 2022, pp.30-44). In this regard, an ESG metric might only measure companies' policies or internal documents, rather than their actual practice and performance in reducing carbon emissions (OECD ESG

Ratings and Climate, 2022, pp.19). The importance of this is highlighted by the following example in Table Two of the ESG metrics used by MSCI (MSCI, 2023):

Table 2

Geographic exposure to carbon regulation/legislation	1 or 0
Business exposure to carbon-intensive operations	1 or 0
Geographic exposure to climate-vulnerable regions	1 or 0
Reliance on a carbon-intensive supply chain	1 or 0
Climate change controversies	1 or 0

Key: 1 = yes; 0 = no

The example in Table 2 does not actually imply that if there were domestic legislation, a company would actually reduce its carbon footprint. There needs to be mechanisms and penalties and constant monitoring on the part of the government to understand the extent of carbon emissions and to implement an effective carbon emission monitoring scheme. Although Table 2 is only an example of some of the environmental metrics for ESG used by MSCI, it is important that external rating companies should also consider the actual gas emissions produced by the company which are not indicated in this table. The easiest method for doing this is to monitor a company's electricity bill, which is a clear indication of its carbon footprint. The above MSCI ESG metrics could be amended to include the following:

Table 3

Reliance on Eskom	1 or 0
Reliance on fossil fuel generators	1 or 0
Reliance on other fossil fuels, for example gas	1 or 0
Geographic exposure to carbon regulation/legislation	1 or 0
Business exposure to carbon-intensive operations	1 or 0

Geographic exposure to climate-vulnerable regions	1 or 0
Reliance on a carbon-intensive supply chain	1 or 0
Climate change controversies	1 or 0

Key: 1 = yes; 0 = no

With reference to the above table, reliance on Eskom and fossil fuel generators presents a clearer picture of the dependence of some South African companies on fossil fuel for electricity. If Eskom is unable to produce electricity, forcing companies to resort to fossil fuel generators and to a lesser extent to solar panels or gas; this should be reported in ESG disclosures, and the data should be verified to understand companies' dependence on alternative forms of power in the event of a blackout. (Blackout refers to loadshedding, a method used by Eskom to rotate blackouts throughout South Africa daily.)

In South Africa, board diversity is also measured by the JSE ESG metrics. Although the ESG metrics refer to 'male' and 'female', we suggest the word 'gender' should be used, thus allowing the JSE to also consider the LGBTQ+ community as part of board diversity and also to consider the implications of the UN Global Compact with reference to human rights. If there is no true definition for diversity, understanding board diversity and social justice initiatives will be difficult. As was discussed earlier, the Constitution of South Africa is considered a form of social justice, but if more harm than good is being done, it is suggested that it might have to be reconsidered (Press, 2023). In this regard, it is important to focus on the recent warnings issued by the CEO of Pick & Pay, Ackerman, concerning the implications of the UN Global Compact (Ackerman, 2023).

3. Dangers pertaining to company ratings and success in relation to the quality of disclosures

The quality of disclosures is discussed in the above section with reference to the MSCI ESG metrics relevant to the environment. In this section, we will focus on the quality of ESG disclosures. As an example, the Old Mutual Equity Fund portfolio will be used again:

a) ABSA Group Ltd
b) British-American Tobacco
c) First Rand Ltd
d) Standard Bank Group Ltd
e) Prosus NV
f) Sasol Ltd
g) Glencore PLC
h) Naspers Ltd
i) MTN Group Ltd
j) Anglo-American PLC

MSCI has rated the above portfolio as AAA, the highest rating on the MSCI rating scale. Owing to the involvement of some of the companies in the portfolio with fossil fuels, tobacco products and mining, it might be supposed that they would achieve the lowest score – CCC. And if the three companies involved were to have achieved the lowest score, how would the average AAA assigned to the portfolio by MSCI be calculated? This is not clear, as only MSCI knows how this was calculated. However, opinions expressed by mining company CEOs such as Natasha Viljoen, the CEO of Anglo American, have mentioned that the internal combustion engine (ICE) will probably still be in service for a long time to come. This opinion is factually based in that the metals mined to build such engines have shown an increase in global demand. An example here would be motor manufacturers which have shown an increased demand for the metals needed to build ICEs (Stoddard, 2023). If this is true, it means that ESG ratings will allocate a different weight to each component of ESG during the transition period, as discussed earlier. In this regard, for the next 20 years or so the ESG ratings obtained should be explained by external rating companies so as not to confuse investors such as pension funds and asset managers in South Africa. Certain warnings or disclosures should be attached to an ESG rating, informing the public, investors, and pension funds as to why a high ESG rating has been allocated and whether this is due to a change in business activities that promote ESG, or whether different weights are being used during the transition period, or whether the ESG rating was obtained by analysing the company's ESG policy documents only (Prescient ESG, no date).

a. *What are the main measures currently demanded by regulators and the government in South Africa?*

The JSE metrics are a work in progress – at the end of 2022 they comprised approximately 30 factors in total, and in the present one component of ESG has approximately 30 factors or so. The JSE is a member of the WFE and we assume that in the future, only companies that are ESG rated will be able to participate in the global economy. If a company is not ESG rated and the domestic stock exchange is reluctant to impose ESG requirements on its listed companies - in our opinion - that company will not be able to obtain a dual listing on another stock exchange, for example listed on the JSE and Paris Stock Exchange (Prescient ESG, no date). Therefore, ESG compliance will be an endorsement of good corporate governance practices, allowing the company to conduct business operations both globally and locally in the future. The Financial Sector Conduct Authority (FSCA) is encouraging pension funds to invest only in ESG-compliant JSE listed companies. As early as 2019, the FSCA published Guidance Note 1 – Sustainability of Investments and Assets in the Context of Retirement Funds – which sets out the FSCA's expectation that pension funds will promote ESG investment in future. However, the note is silent on two UN instruments, the UN Guiding Principles on Business and Human Rights and the UN Global Compact (De Villiers, 2022).

During the 1990s, more than 600 companies were listed on the JSE, but this number has since dropped to fewer than 300 companies currently (Hasenfuss, 2023). The fact that pension funds and asset managers invest only in the top 100 JSE companies may be problematic, as the number of listed companies on the exchange tends to be a barometer of the South African economy. In addition, regulation 28 of the Pension Funds Act of 1965, has introduced infrastructure as an investment 'product', allowing pension funds and asset managers to invest in companies whose main business activities involve the building of infrastructure in South Africa (FISCA, 2019; Hasenfus, 2023). Although the construction of infrastructure supports sustainability, it is not truly part of ESG. Infrastructure and its development forms part of the business initiatives of the Development Bank of South Africa, which is a state bank (FISCA Verbatim, 2019; FSR, 2022). Nevertheless, the transitions from ESKOM to renewable energy resources could be interpreted as infrastructure.

b. *Assess the impact of the UK Taskforce on Climate-related Financial Disclosures and the Corporate Sustainability Report of the European Council, for example, which affects grants given to the South African government to institute renewables projects which are carried out by South African companies, as well as the IFRS's attempts to standardise and internationalise accounting measures, on the implementation of ESG disclosures*

The FSCA in partnership with the Swedish International Development Co-operation Agency, the Swiss Confederation, the International Finance Corporation (IFC), the Swiss secretariat for economic affairs and the World Bank have implemented sustainable investment practices in South Africa in order to transform retirement funds or pension funds into more sustainable future funds (IFC, 2020). What is important about such initiatives is that although South Africa is a sovereign state, it needs the assistance of other organisations or states during its transition period – from unsustainable pension funds to pension funds that incorporate ESG practices or from coal power plants to renewable energy etcetera. These initiatives or programs initiated by the IFC, Swiss Federation and so forth would appear to be part of a global initiative to help South African pension funds and the South African government during their transition periods – we do not how long the transition period will last. The IFC operates in more than 100 states and has invested more than US$22 billion dollars in companies or pension funds and institutions globally to assist them to become more sustainable in future (IFC, 2022). Currently, the IFC is a leader in ESG investments during transitions for pension or retirement funds and or developing countries.

The IFC, in partnership with Amundi asset managers, has established the world's largest green bond fund, Amundi Planet Emerging Green Bond, for developing countries (Amundi, 2023). By 2020, more than 170 of these green bonds had been issued in more than 22 currencies at a value of US$10 billion. The IFC has also developed the Green Bond Market Development programme in South Africa which is not managed by South Africans but by the IFC (IFC, 2022). The transition in South Africa is focusing on climate transition practices only; in other words, as it involves bringing South Africa in line with the Paris Treaty on Climate Change. Information on these initiatives is not made public but they seek to change South Africa's propensity

to generate electricity from coal to renewable energy and will require investments of US$97 billion or R1,5 trillion (Cost of Transition, 2023). The magnitude of this amount would appear to make it impossible for the IFC initiatives to be truly effective. In the IFC initiatives, the IFC's own ESG metrics are used to measure the South African government's commitment to change from coal powerplants to renewables and how they are complying with specific environmental targets after being granted the necessary capital for transition, also known as impact finance (IFC, 2022). These initiatives indicate the purpose of ESG investments and therefore the use of ESG ratings to monitor the progress of the IFC investments in South Africa. In other words, foreign investors need ESG data to make decisions on whether to invest in South Africa as well as to be able to monitor the country's ability to comply with the Paris Treaty. The ESG metrics used by the IFC are not made public.

As a result of the above initiatives, the JSE is also expecting to introduce green bonds specifically to meet the $97 billion target for South Africa. This green bond initiative has also created the Energy Independent Power Producer Procurement (EIPPP) in partnership with the public and private sector, and requires funding from South African pension funds to provide the capital to promote a green transition for South Africa (JSE Green, 2023). In order to make sure that pension fund contributions will not be squandered by corrupt companies or state departments, among others, it seems that the EIPPP will probably be managed by individuals who are already part of the IFC initiatives to make sure that money received is allocated to correctly, not only to the benefit of South Africa in the long term but also to the benefit of the pension fund contributors (IFC, 2022). In South Africa, the value of pension funds is US$154 billion, and thus pension funds alone could be able to finance South Africa's green transition – estimated $97 billion is required as discussed earlier (Statista, 2023). The IFC predicts that US$20 trillion is required to help just 20 developing countries successfully, excluding South Africa (IFC, 2022). Although these 20 developing countries account for 48% of global carbon emissions and a practical solution to this is in the process of being implemented, the financial resources required to fund the entire transition process for all developing countries are just not available (IFC, 2022).

The environmental component of ESG is subject to various treaties and conventions, for example the United Nations Framework Convention on Climate Change (UN Climate Change, 2023). To reach the goals set by this international instrument, the United Kingdom (UK) has also instituted programmes in South Africa,

Colombia, and China, among others, to promote the transition from a coal power economy to a more sustainable alternative energy economy. These programmes are known as the UK Pact transition (UK Pact, 2023). In South Africa, the UK is in partnership with various organisations, for example Nelson Mandela University of South Africa. Nelson Mandela University is currently promoting green transport research, for example the viability of electric vehicles and electric vehicle charging infrastructure in South African cities (Nelson Mandela University, 2023).

The UK Pact is also in partnership with DNA Economics, developing a South African asset manager tool to enable asset managers to make investment decisions as to whether or not specific listed companies are sustainable in future (DNA Economics, 2023). This tool discloses carbon emissions information and other gases, thus indirectly supporting the JSE ESG metrics, for example nitrogen oxide emissions.

DNA Economics also discloses information on environment and the climate to parties such as pension funds to understand whether or not companies are reducing their carbon emissions (DNA Economics, 2023). The tool will be similar to that of the Financial Stability Board's Task Force on Climate-related Disclosures (TCFD), which seeks to improve accurate disclosures on climate-related information. The TCFD also indicates how both listed and unlisted companies should be disclosing such information to insurers, lenders, and other relevant stakeholders (TCFD, 2023). The OECD is envisaging a greater role for the banking system in monitoring TCFD compliance (OECD ESG Ratings and Climate, 2022, pp.39; the importance of climate change cannot be ignored). If companies fail to do this, thus ignoring the importance of TCFD disclosures, OECD membership banks should avoid granting loans to them. In this regard, banks could play an active role in understanding the ESG business activities of companies and how they are complying with, for example the TCFD among other things.

The JSE ESG metrics incorporate some of the factors included in the GRI and the SASB, which will eventually be known as the IFRS, as discussed earlier (JSE Metrics, 2023). For example, the JSE ESG metrics refer to the GRI and SASB when requiring disclosure on a specific factor. This makes the JSE ESG metrics user-friendly when attempting to understand where the specific factor has originated from or whether being independently regulated by the SASB. The following information is relevant to our discussion and serves as an example:

Good corporate governance disclosures or factors required by the JSE ESG metrics for GRI, SASB and the WFE:

- Composition of the board of directors and committees by race and gender – part of GRI 2-9; GRI 102-22 and WFE
- Percentage of company employees who have received training in anti-corruption measures – part of GRI 205-2; SASB 510 and WFE
- Confirmed corruption cases – part of GRI 205-3 and WFE
- Communication strategies with stakeholders to prevent corruption – part of GRI 205
- Professional services available to explain ethics to the board of directors – part of GRI 2-26

When one considers the aims of the SASB, clearly it does not exclude other ESG frameworks, standards or metrics but acknowledges the fact that it is impossible for individual companies to regulate all aspects of ESG, as discussed earlier. Even when companies operate in the same industry there may be differences between them, which was also explained earlier. To address these differences, the SASB has identified 77 industries and has developed metrics unique to each industry. On the other hand, not all stock exchanges explain the relevance between a factor (for example, the composition of the board of directors) and GRI as illustrated above (WEF ESG Metrics, 2023 with reference to the World Economic Forum ESG metrics).

In June 2020, the European Parliament adopted Regulation 2020/852 which states that stock exchanges should not make use of the acronym ESG in their indexes (also known as a stock or fund index) unless the index is truly ESG compliant (Oostrum, 2021, pp.15; ERFRAG, 2023). The reason for this is simply to prevent greenwashing. In other words, the European Parliament has tried to create a common language so that investors can understand the sustainable practices of listed companies. From January 2023, it is also expected that stock exchanges in the European Union will distinguish between the so-called 'light green funds' and 'dark-green funds' (Davidson, 2023). From 2024, the Corporate Sustainability Reporting Directive (CSRD) will be relevant, and companies will have to comply with the European Sustainability Reporting Standards (ESRS) in future. These are the most far-reaching mandatory disclosures on ESG globally. By mid-2024, individual European Union member states will have to adopt relevant legislation to implement

the CSRD (Frecautan and Andrea, 2022, pp.109 for a general discussion). Accordingly, the Old Mutual Equity Fund, as explained earlier, should not be rated by MSCI since the fund does not contain the acronym ESG. Therefore, to avoid confusion in the market, MSCI should only be able to rate funds or portfolios that use the acronym ESG. Currently, it seems that if a fund has been rated; it is considered to be an ESG compliant, as was seen above with regard to the Old Mutual Fund which obtained a AAA rating, which contains inter alia a fossil fuel company

4. Greenwashing: A major impediment to standardising disclosure - more than 30 fund managers, consultants, lawyers, and regulators interviewed by Reuters said that despite UK/European Union rules demanding more disclosure, funds remained hard to compare and greenwashing difficult to spot

Before we discuss greenwashing, it is important to focus on the following: Although social relations are one of the components of ESG, it is difficult to comprehend in practice. Generally, this component deals with human rights and the respect for human rights displayed between the company and its employees and/or the company and the community in which the company is doing business. To understand human rights, the UN Global Compact and UN Guiding Principles on Business and Human Rights are relevant. But how does one draw a line between the social relations expected of companies and the social relations imposed by states through legislation? The South African economy is struggling due to the severe consequences of the global COVID-19 pandemic. The CEO of the JSE, Leila Fourie, has explained that a great duty rests on the private sector (privately owned companies or businesses, including JSE listed companies) in South Africa to save the South African economy (Anonymous, 2023). The ruling of the Competition Commission against Google should be noted here, which allows other South African companies to acquire the tools to be a ‘Google’ one day. Accordingly, Google is required to invest R300 million in small and medium businesses owned or managed by a designated race group in South Africa, ignoring other designated race groups (Mcleod, 2023). A similar ruling was made against Takealot (the largest online retailer in South Africa and Africa) and Amazon, requiring them to invest in small and medium companies in South Africa and thus enabling such

companies to become an ‘Amazon’ one day. Similar rulings have also been applied to Uber South Africa.

These social requirements resulting from legislative implications should be disclosed in sustainability reports in order to understand what constitutes good social relations from a South African perspective and, also to report on how social relations are being regulated in South Africa (Cossart, Chaplier and Beau de Lomenie, 2017, pp.317; Anonymous, 2023). On the other hand, this could also be interpreted that government interventions are required to support good social relations in South Africa. Only time will tell how the United Nations and global foreign investment companies will perceive such South African legislation and whether it will contribute to growing the economy. In this regard, the social relations component and ESG metrics developed by the JSE are very different to those of other stock exchanges that do not have similar legislation to that of South Africa pertaining to the social relations leg.

5. Value considerations: How do we define both financial and non-financial value when disclosures remain low and hidden by the overarching rubric of sustainability which remains so ill-defined?

The SGX has, to a certain extent, overcome the problem of ill-defined nonfinancial value by means of ESG and the way in which ESG compliance relates to increased profits and cash flow for listed companies. The SGX discloses the following, which is repeated here for practical purposes (SGX ESG Ratings, 2023):

Table 4

Company name	FTSE/Russell	MSCI	Sustainalytics	S&P	Moody’s
CapitaLand Ascendas	2.9	A	Low risk	23	31
CapLand Ascott	2.2	BB	Low risk	39	-
China Aviation	-	A	High risk	14	-
ComfortDelGro	3.1	AA	Low risk	62	39

How does 2.9 relate to A? And how does 2.9 relate to 31 for CapitaLand Ascendas? The best MSCI score is AAA. Sustainalytics has rated CapitaLand Ascendas as very low risk, but S&P has rated it as 23, which is far lower than ComfortDelGro at 62, which is also very low risk in terms of Sustainalytics. Obviously, CapitaLand is not particularly low risk when one considers S&P for example. What value can be attached to the above? Firstly, companies are trying to disclose ESG compliance voluntarily, and these disclosures may be incomplete in terms of the specific ESG metrics, for example as used by S&P. Secondly, investors are required to select external companies they believe to be reliable in terms of their ratings. If MSCI is compared with S&P with regards to ComfortDelGro and CapitaLand Ascendas, one could probably assign investment attractiveness or value to both companies. Thirdly, ESG metrics should be public information to give a company at least a fair chance to try and improve on its business activities in future. If ESG metrics remain part of the trade secrets of an external rating company, companies generally will simply have no basis on which to improve the non-financial value of their business activities, even if they have high financial value as a result of attractive profits or cash flows. If ESG metrics were to remain a trade secret then a fourth observation could be made: it is better to rate a company and disclose individual ratings, as in the case of SGX, to gain a holistic overview of a company in terms of ESG and to conclude whether the company is actually ESG compliant or not (SGX ESG Ratings, 2023). For example, CapitaLand is probably not a low ESG risk company and should have less nonfinancial value than, say, ComfortDelGro. In our opinion, SGX ratings above is probably the best option to understand ESG ratings holistically (CISION, 2023, for a general explanation of ESG ratings).

6. Recommendations: The way forward for dealing with the lack of a proper understanding of what should be disclosed in sustainability reports and how regulators and governments need to work more closely with asset and pension fund managers, and trustees

1. The JSE ESG metrics are a step in the right direction in that they incorporate the GRI and the SASB among others. In addition, they indicate the factors or indicators that emanate from various regulatory bodies, for example the GRI.

2. The JSE metrics should point out that listed companies could consider reporting based other ESG frameworks, but that the JSE ESG metrics remain the minimum, core factors that need to be disclosed by listed companies.

3. The JSE could follow a similar approach to the SGX by disclosing various ESG ratings obtained from external ESG rating companies.

4. The SSE should actively participate in identifying core or baseline ESG indicators for all its stock exchange members. The SSE should also state the ESG factors or indicators that it considers important for listed companies to report on.

5. Pension funds could rate their own individual funds by considering individual ESG ratings for listed companies – as indicated by SGX; however, how the aggregate should be calculated is unclear.

6. Other asset managers in South Africa should follow Old Mutual's example of disclosing the MSCI ratings of investment portfolios of pensions funds etcetera.

7. ESKOM (coal power plant with renewable energy) is possible to replace. The JSE green bond established, together with the international contributions (from, for example, the IFC) received to change the South African coal power plants, are sufficient to finance such a transition – keeping in mind that pension funds must also invest in infrastructures. Consequently, businesses and households in South Africa should generate also their own sustainable, renewable electricity.

8. In South Africa, JSE-listed companies and other businesses should be aware of the importance of 2030. Asset managers should also understand the significance and should not label investment portfolios as ESG compliant when companies will clearly only be carbon free by 2040 or beyond. If asset managers fail to do so, the weights attached to the different components of ESG should be explained to the stakeholders involved to make them aware of the importance of fossil fuel companies being ESG compliant during the transition period – before 2030 and beyond, for example to pension funds and their members or contributors. This would allow for transparency and a better understanding of ESG.

9. The number of companies on the JSE has dwindled – from more than 600 twenty years or so ago to less than 300 today. South Africa needs to attract foreign investors and therefore should reconsider its interpretation of the social relations component of ESG. In this regard, the UN Global Compact and the UN Guiding Principles on Business and Human Rights should be accepted and implemented by the South African government, as an active member of the UN.

10. External ESG rating companies such as Morningstar should be able to disclose publicly the ESG metrics they apply in order to allow listed companies an opportunity to comply with their requirements.

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