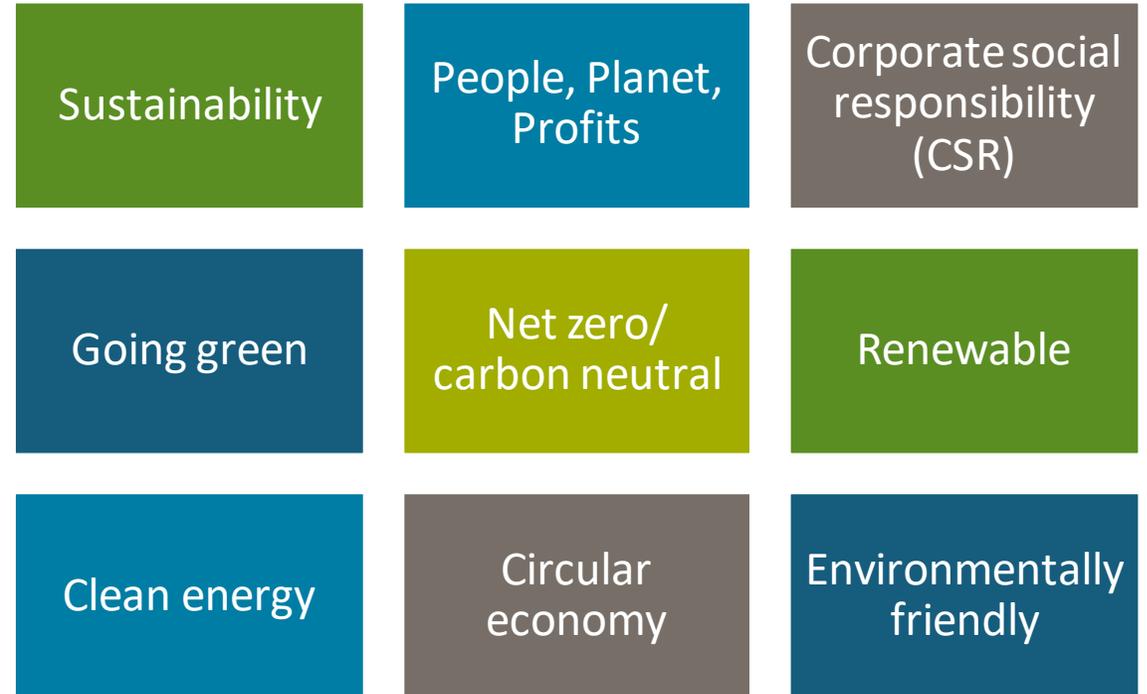


# Buzzword or strategy? How ESG trends are reshaping risk management

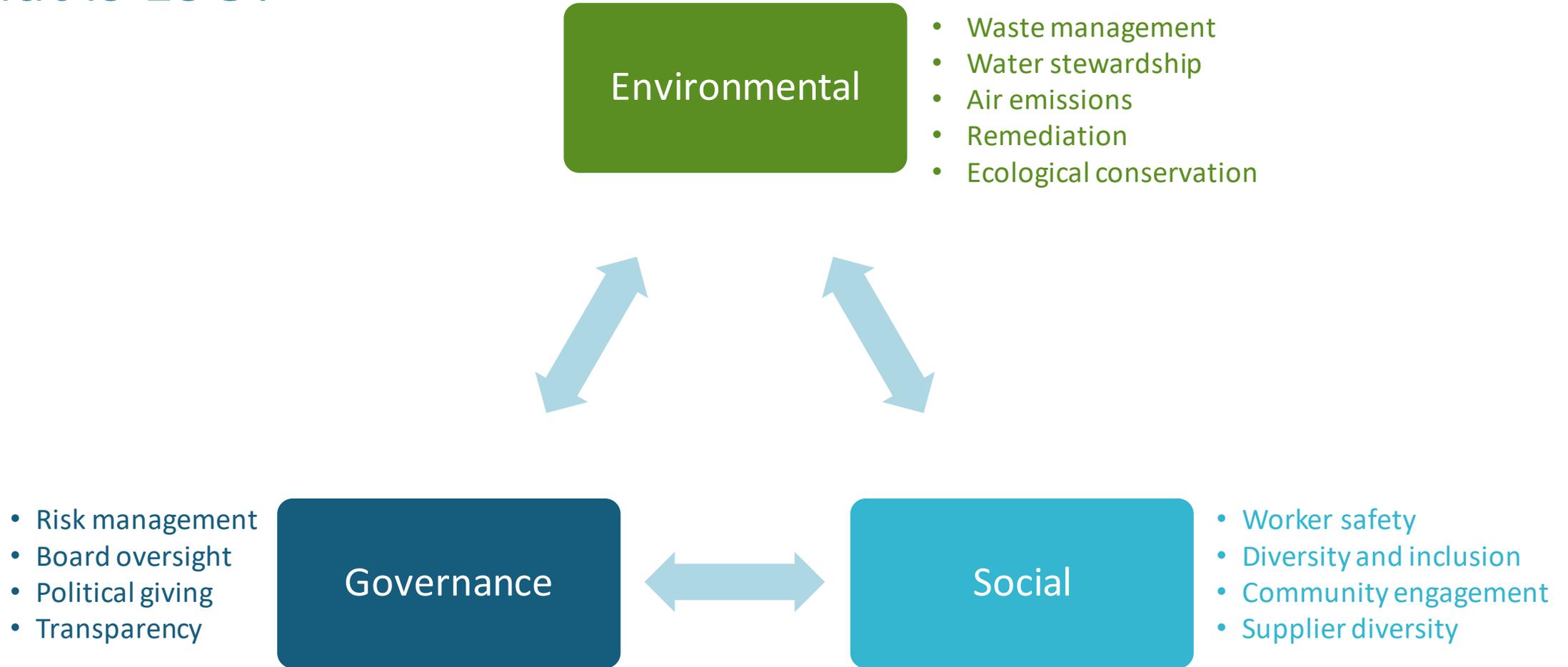
Dawn Santoianni  
Principal Consultant



# An evolving lexicon



# What is ESG?



# ESG - from niche to Wall Street to Main Street

## ESG is increasingly important to financial institutions

- Interest by large investors, cost of capital, insurability issues
- About three quarters of institutional investors conduct formal review of ESG disclosures
- Urgency to address climate risks, challenges for net zero transition

## Regulatory and litigation drivers for ESG disclosures

- Proposed SEC mandated climate risk disclosure rules will focus attention on value chains
- Some state commissions requiring planning to account for climate risk
- Litigation over greenwashing claims is on the rise

## Heightened awareness of inequity and social justice issues

- Consumers, neighbors, and policymakers want companies to take meaningful action on social issues
- Focus on environmental justice in enforcement and regulatory programs
- Remediation and construction are interwoven with social justice issues

# Follow the money

- Companies with favorable ESG ratings outperform sector peers
  - In U.S. managed assets, approximately \$16 trillion employ some form of ESG screening
  - ESG-integrated investment strategies grew by 143% from 2016-2020
  - In 2021, more than \$120 billion was invested in ETFs marketed as ESG performers (double 2020 level)<sup>1</sup>
- Accessibility of ESG ratings systems
  - S&P Global, MSCI, Moody's (and others) have publicly-available searchable ratings
  - Fossil fuel value chain still represented in ESG/climate funds

<sup>1</sup> Bloomberg, Dec. 1, 2021. The ESG Market is Controlled by a Few Big Investors.

December 23, 2021  
4:20 PM EST  
Last Updated 4 days ago

**U.S. Markets**

## Analysis: How 2021 became the year of ESG investing

4 minute read

By Ross Kerber and Simon Jessop

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1/3 Extinction Rebellion climate activists protest outside the Bank of England in London, Britain, September 2, 2021. REUTERS/Henry Nicholls/File Photo

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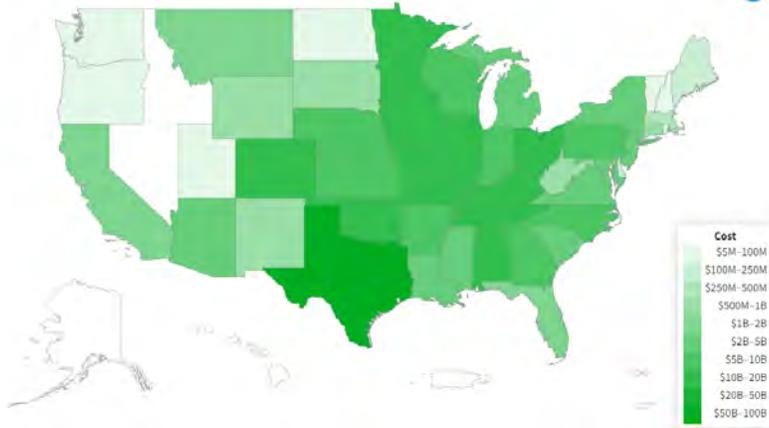
Register

BOSTON/LONDON, Dec 23 (Reuters) - Investors concerned about climate change and social justice had a bumper year in 2021, successfully pushing companies and regulators to make changes amid record inflows to funds focused on environmental, social and corporate governance (ESG) issues.

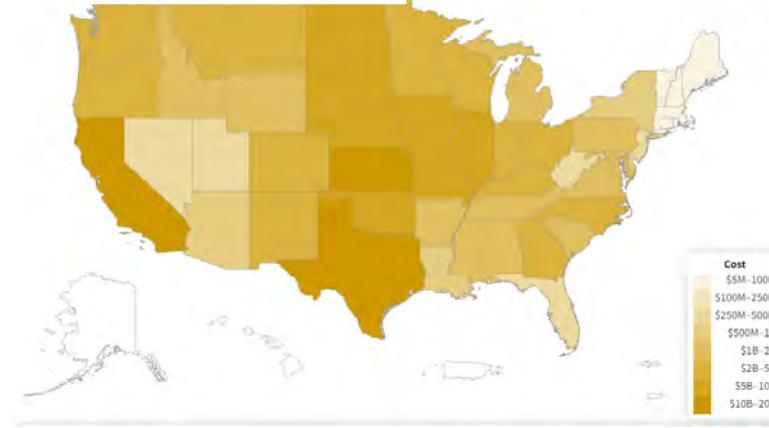
Extreme weather becoming more frequent and events highlighting social justice issues, such as the death of George Floyd in Minneapolis police custody, contributed to ESG rising to the top of the agenda of investors, companies and

# Escalating disaster costs

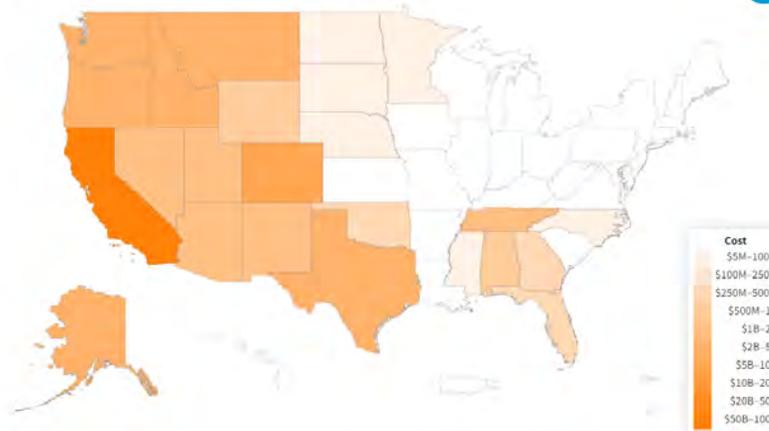
2001-2021 Billion-Dollar Severe Storm Disaster Cost (CPI-Adjusted)



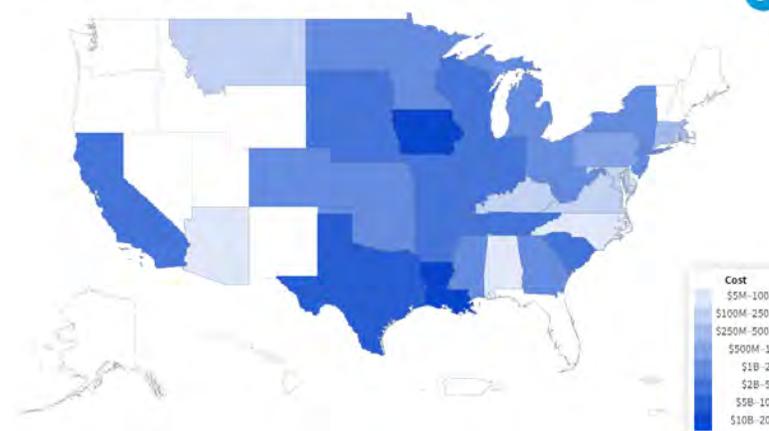
2001-2021 Billion-Dollar Drought Disaster Cost (CPI-Adjusted)



2001-2021 Billion-Dollar Wildfire Disaster Cost (CPI-Adjusted)



2001-2021 Billion-Dollar Flooding Disaster Cost (CPI-Adjusted)



Almost every part of the U.S. has been affected by billion-dollar disasters over the last two decades:

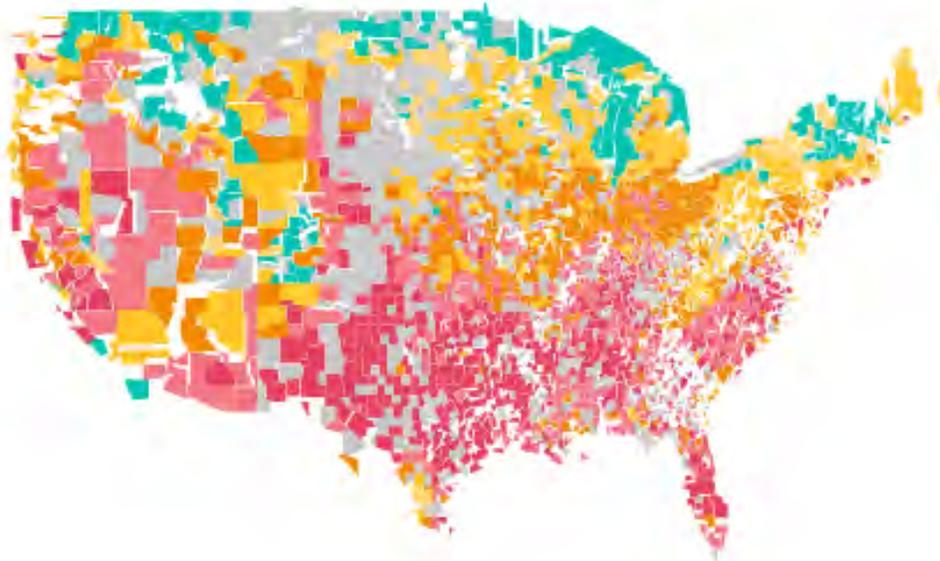
- Severe storms \$250B+
- Drought \$100B - \$200B
- Wildfires \$100B - \$200B
- Flooding \$50B - \$100B

Source: NOAA National Centers for Environmental Information, [Disaster and Risk Mapping](#)

# Compounding physical risks

## Emerging Hot Spots for Physical Climate Risks in the US

Aggregated Physical Climate Risk Score



Source: MSCI (2020)

# U.S. SEC mandatory disclosure regulations

Publicly traded companies would be required to assess and disclose climate-related risks and opportunities



## Physical risks

- Disclosure of locations of assets at risk (by zip code)
- Percentage of buildings/plants/properties exposed to hazards



## Transition risks

- Financial impacts from price on carbon
- Stranded asset risk
- Technology risk
- Liability and reputational risks



## Greenhouse gas emissions reporting

- Scope 1 and 2 emissions, total and disaggregated
- Third-party validation
- Progress on climate goals
- Large companies required to disclose Scope 3 if material or included in targets



## Risk management

- How risks are identified and managed
- Metrics, targets, scenario analysis
- Governance

# Accounting for climate risk

## Financial Stability Oversight Council (FSOC)

- Voted to create the Climate-Related Financial Risk Committee on Dec. 17
- Treasury Secretary Janet Yellen chairs the FSOC, member agencies include SEC
- Report to Congress warned of the emerging threat of climate change to U.S. financial system

## Climate-Related Financial Risk Committee (CFRC)

- CFRC will identify priority areas for assessing and mitigating climate-related risks to financial system
- Will serve as coordinating body to share information across U.S. financial system

## Treasury's Office of the Comptroller of the Currency (OCC)

- Released draft guidance Dec. 16 on incorporating climate-related financial, operational, and legal risks, seeking public input
- OCC appointed climate change risk officer
- Formed Climate Risk Implementation Committee to identify risks and provide recommendations

## SEC Climate and ESG Task Force

- On March 4, SEC announced the creation of Climate and ESG Task Force in the Division of Enforcement
- Charged with proactively identifying ESG-related misconduct, including material gaps or misstatements
- Will pursue tips, referrals and whistleblower complaints

# ESG pressures

## Investors

Shareholder proposals on ESG issues are gaining momentum, and largest investors are voting “yes”

In 2020, BlackRock voted against 69 companies, and put another 191 companies “on watch”

Hedge funds buying majority stakes in companies to replace Board members

## Financial institutions

66% of major global companies have at least one asset at high risk of physical climate impacts

Better ESG scores translate to about 10% lower cost of capital

The insurance industry has been a key driver of ESG movement

## Regulatory and Litigation

Stakeholder interventions in permitting, utility IRPs, rate cases

Companies can no longer rely only on FTC Green Guides to mitigate liability risk

SEC enforcement arm examining public statements compared to regulatory filings

## Markets and customers

Supply chain ESG risks erode competitiveness

Increasing customer expectations for sustainable products and services

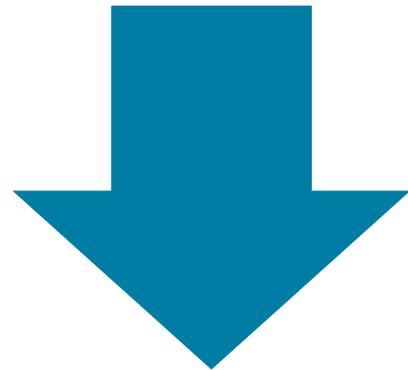
Industries are coalescing around frameworks to assess suppliers on ESG

# What does this have to do with coal ash?



## Recycling supports ESG initiatives

- Beneficial use can mitigate long-term risks
- Marketers and ash users are part of the value chain
- Environmental benefits from avoided disposal



## Coal ash management is a material issue

- Costs for managing ash can be in the billions
- Reputational impacts can be severe
- Regulatory uncertainty for unencapsulated uses
- ESG risks from supply chain

# ESG ratings example: materials/construction

## Environmental

Issue	Average Weight
Carbon Emissions	18.3%
Toxic Emissions & Waste	17.3%
<b>CS</b> Water Stress	1.9%
<b>CS</b> Biodiversity & Land Use	1.3%
<b>CS</b> Opportunities in Green Building	0.2%
Packaging Material & Waste	
Product Carbon Footprint	
Climate Change Vulnerability	

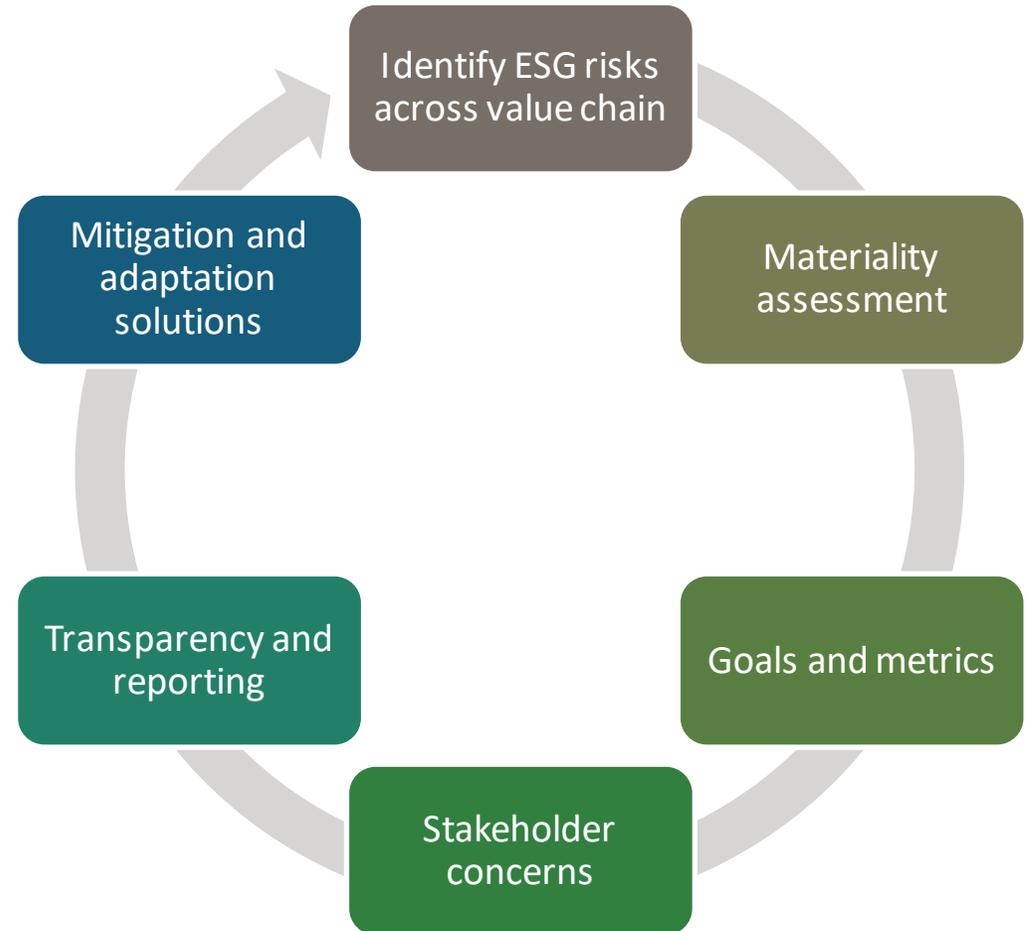
## Social

Issue	Average Weight
Labor Management	13.1%
Health & Safety	13.1%
<b>CS</b> Community Relations	1.6%
<b>CS</b> Product Safety & Quality	0.1%
Human Capital Development	
Supply Chain Labor Standards	
Consumer Financial Protection	
Privacy & Data Security	



# ESG as a risk management framework

- EHS and workforce protection
- Vulnerability of strategy to regulatory changes
- Integration with net zero goals
- Environmental justice and cumulative impacts
- Reputational impacts
- Supply chain sustainability
- Engineering solutions to address physical risks



# Questions?



**Dawn Santoianni**

[dsantoanni@haleyaldrich.com](mailto:dsantoanni@haleyaldrich.com)

(919) 638-0139

Haley & Aldrich