KPMG

Conversation with Sacha Sadan

The Audit Committee Institute
Part of the KPMG Board Leadership Centre

Sacha Sadan, Director of Investment Stewardship at Legal and General Investment Management (LGIM) offered our FTSE100 audit and risk chairs' group his perspectives on how businesses can communicate better with their investors; both equity and fixed income, and sheds light on why this is so crucial for success.

Environmental, Social and Governance (ESG) reporting was front and centre in the discussion. If ESG is not the only priority, Sacha is clear that it is one of the largest.

ESG issues are broad and while Governance has always been a top priority for UK companies, boards often struggle to articulate their strategy, risk and performance when it comes to Environmental and Social matters – particularly the opportunities.

Companies, and their boards, he asserts, must take advantage of the opportunities associated with ESG – for those who don't, it will be their downfall.

While environmental activists call for pension funds to abandon their investments in 'Big Oil', Sacha believes that divestment is not the solution. Fossil fuel extraction is about far more than a few oil companies, however, the lack of transparent reporting on the subject allows the confusion to perpetuate and makes it difficult for responsible fund managers to defend their position.

Sacha called for much greater transparency across the capital markets, and noted that LGIM are in a unique position to help drive that change by more effectively engaging with boards.

Here, we summarise his key asks of boards looking to engage with investors and take full advantage of the imminent and inevitable transformation of annual reporting.

The responsibility is yours

Just as governance has been high on the board agenda since Cadbury wrote his seminal report, it is essential that boards accept responsibility for the company's Environmental and Social responsibilities as well. Arguably, while Governance is 'owned' by the chair, Environmental and Social matters – embedded as they should be in the corporate strategy – need to be delivered by the CEO.

It's not always the 'E'

If you're a Telco, whether or not you recycle a thousand tons of paper each year is largely irrelevant to institutional investors. More important is "what you're doing to stop Big Tech taking your lunch and how are you getting the skills that you need onto your board?" Financial materiality.

When discussing ESG, Sacha looks for boards to focus on the needs of the business and its stakeholders. "If there is a gap in technology capabilities at a board level, how are you working in society to give more technologically capable individuals access to senior positions?" Understanding your own priorities is paramount.

Empower your company secretary

Investor relations teams play an important role – and often very well – but they cannot be a substitute for a strong company secretary.

Boards should empower company secretaries to hold them to account and to challenge them to deliver on what they have promised. Offer them oversight over the relationship with the investor community to ensure that the right messages are landing.

Allow them to filter out any 'marketing bumph' and instead deliver the reporting that investors want to see – reporting on succession planning, on whistleblowing, on R&D, and yes, on emissions.

Be prepared for Investors to stand up

Reportedly, Sir Jon Thompson, the new chief executive of the Financial Reporting Council, is clear that a policy on voting is not enough to keep investor houses safe from scrutiny. He will be measuring actions and calling up investors whose voting record does not match their policy.

Similarly, Larry Fink's annual letter to CEOs is clear that profit and purpose are inextricably linked and in managing their index funds they cannot express disapproval by selling securities. As a result, BlackRock's responsibility to engage and vote is more important than ever. The regulators are clear – voting which does not correspond to policy will be called out.

Be generous with your data

There are number of different bodies rating companies on their ESG performance – each looking at different groups of metrics. Get the company secretary or the investor relations team to work out which ones your major shareholders are using and focus on any gaps in your current reporting.

Equally, take the opportunity to tell your story and articulate the ESG metrics linked to your strategy. If the key rating bodies are looking at different metrics, then articulate why they are of less importance to your business model, strategy and performance. Use a slide in executive and non-executive meetings.

Use advisory committees

When you need to shift the dial on ESG but the skills and knowledge required don't exist in the business – then use advisory boards as a supplement to the main board committees. Don't be afraid to call this out – be proud of your self awareness. Explain to investors what you wanted to achieve and why.

Be brave about the conversation

Investors meet regularly with remuneration committee chairs, but that shouldn't mean that they don't also meet with the rest of the board.

Just as Health and Safety has been front and centre in communications from Mining, and Oil and Gas companies for years, ESG needs to be upfront for all. Board members, executive and non-executive alike - need to be ready to engage with investors on material ESG matters. Don't hide behind the chair and CEO.

Consider an investor engagement session through which the chairs of committees can engage directly with key shareholders. This can help ensure clarity of message and help rebuild any lost trust.

Design the future of reporting

The US Sustainability Accounting Standards Board (SASB) – funded by Bloomberg and supported by BlackRock – will likely lead sustainability reporting across the world. Take this opportunity to influence it. Get involved and make reporting work for you – be an influencer.

Report transparently

Very few companies will meet the expectations for the Task Force on Climate-related Financial Disclosures reporting during the early years, so no matter how advanced you think you are, push harder. Look to the market for what others are doing and be inspired. Don't be afraid to emulate, but remember to stay focussed on your own priorities. Some companies have famously written down their assets on the basis of the 'Paris assumptions'. If that doesn't fit your business, consider applying the assumptions and disclosing the impact within the notes.

Integrate your ESG policy and report on outcomes

A good ESG policy is not a bolt-on to business activity – it should be built in to everything that you do. Positive ESG outcomes must factor into every business proposal and material ESG implications should be considered as part of all impact assessments. And reporting needs to go far beyond laying out the policy – it must describe outcomes. Use your reporting to help investors understand how the ESG policy impacts the business – how it influences the decisions made. Tell investors how ESG policy impacted what you did in the year.

Visit the LGIM website for insights from Sacha and his team, such as A guide to climate governance: Changing of the guard or guardians of change?.

Corporate reporting will likely see ground-breaking change over the coming years. Companies which report transparently, taking the opportunity to speak to their shareholders on the subjects which matter most will reap the rewards.

The KPMG Board Leadership Centre

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Contact us

Timothy Copnell
Board Leadership Centre
T: +44 (0)20 7694 8082
E: tim.copnell@kpmg.co.uk