Environmental, Social and Governance Handbook for Long Term Investors in Infrastructure

Second Edition
# ESG AS A KEY SUCCESS FACTOR FOR INFRASTRUCTURE INVESTMENT

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Preface

The purpose of this Handbook is to provide a descriptive summary of practices, standards and tools that infrastructure investors apply today to realize better performance on environmental, social and governance dimensions (ESG), and to sustain that performance over a long term.

ESG has grown considerably in its importance to the investor community – in the context of global calls for reducing carbon footprint, combatting poverty, promoting healthy and safe labour, tightening corporate governance. Most of those calls are particularly relevant to investments in infrastructure assets, because infrastructure includes all those installations and services – transport, energy, utilities, telecommunication, social facilities, etc – that nearly everyone in the world uses and depends on, every day.

For long term investors in infrastructure, there are even more reasons to be serious about ESG. Probability of a downside ESG event that can trigger financial liabilities – from environmental pollution to a governance malpractice – grows with a longer hold, hence implementation of ESG prevention and mitigation measures becomes much more important for sustaining financial performance of the investment.

Yet, notwithstanding the broad agreement on the importance of ESG, still relatively few investors understand what it takes in practice to invest in infrastructure responsibly.

More than forty organizations – institutional investors, asset managers, development banks, advisers and not-for-profits – have been involved in compiling and reviewing the Handbook. Compared to the first edition, that was published in 2015 and presented at COP21, this second edition has benefited from twice as many contributors and a much wider set of functional and geographic perspectives. References to individual ESG practices of the contributing organizations have been identified as such in the text, where appropriate. We are particularly grateful for substantial contributions that came for this second edition from Allianz Global Investors, Beyond Ratings, Carbone 4, Global Infrastructure Basel Foundation, GRESB Infrastructure, InfraVia, Norton Rose Fulbright and Skandia Asset Management.

We sincerely hope that this Handbook will help readers take their ESG practices in infrastructure investing to the next level. Readers interested in translating some of the Handbook’s concept into their investment practices are invited to check out ESG Indicators Library. Produced by LTIIA jointly with software provider eFront, the Library contains structured and harmonized definitions of indicators that infrastructure investors are using today to track their responsible investment performance.

At Long Term Infrastructure Investors Association, we will continue working with our members and the industry on raising the awareness as well as implementation standard of responsible investment in infrastructure.
ESG as a key success factor for infrastructure investment

The purpose of this ESG handbook is to provide stakeholders with an easy-to-use guideline that shall help incorporate an ESG approach in infrastructure investments. Such an approach may offer superior business models as well as long term performance advantages. However, to benefit from the ESG advantages, an appropriate incorporation of ESG factors into investment analysis and decision making is fundamental.
DEFINITIONS

Infrastructure, the organisational backbone of the economy

Although the definition encompasses various dimensions of infrastructure, this handbook will mainly deal with material infrastructure, “the sum of all physical assets, equipment and facilities” (Jochimsen 1966). Such material infrastructure includes water, sanitation, energy, housing, transport and information and communication technologies according to definition of the World DataBank of the World Bank Group.

Infrastructure plays a fundamental function in the development of societies. Since it connects capital and workers more efficiently, it increases Total Factor of Production (TFP), and therefore enhances economic growth while reducing the levels of inequality. Standard & Poor’s (2015) evaluated that an increase in infrastructure spending of 1 per cent of real GDP can have a multiplier effect of between 1.0 and 2.5 per cent for G20 countries over a three-year period. In addition to a potential boost of jobs and GDP, long term benefits from infrastructure can include improved efficiency and higher tax revenues.

In a conventional sense, infrastructure displays 8 specific characteristics (adapted from Weber and Alfen 2010). In first instance, infrastructure represents a key public service. Infrastructure assets enhance the development of a nation as they deliver fundamental public services such as the provision of clean water or electricity, enable the mobility of persons and goods and offer efficient communication.

Infrastructure is also characterised by a low elasticity of demand. This means that the use of infrastructure is often independent from business cycles for it plays fundamental roles in the economy: indeed, the rail and road networks are used even during downturns. Hence demand for infrastructure services is expected to remain relatively constant.

A further dimension of infrastructure is its quasi-monopoly situation with high barriers to market entry: given that the upfront cost of new infrastructure can be tremendous - sometimes amounting to some US$ billions- and that there are important returns to scale -once the network exists, connecting one more household for instance is relatively cheap-, competition appears limited or even inexistent.

As a direct consequence, infrastructure may witness specific regulation. In fact, in case of little or no competition, regulatory authorities do step in and correct the market by, for example, fixing prices while compensating the infrastructure holder through a set of guarantees.

Long service life is also a particularity of infrastructure. Some roads existing today in Europe were traced by the Romans some 2,000 years ago, illustrating the notion of infrastructure as the long term backbone of the economy. This example is certainly not representative, but infrastructure assets often have service lives of as much as a century. Of importance for investors is then to amortise their investment within the associated life span.

Infrastructure is also expected to provide inflation protection: revenues are likely to be combined with inflation adjustment mechanisms, be it through regulated income clauses, guaranteed yields or any other contractual guarantees. When revenues are generated by user charges,
prices follow the Consumer Price Index (CPI) or GDP growth.

**Regular, stable, yet late cash flows** are also a feature of infrastructure. Given the characteristics mentioned above, after an initial construction phase, infrastructure assets produce regular and stable cash flows. Thus, they generally represent safe investment opportunity for risk-averse institutional investors.

**Definition of Environmental, Social and Corporate Governance criteria**

ESG stands for environmental, social and corporate governance. ESG criteria represent the three dimensions that directly and indirectly affect the financial performance of investments.

There is a growing recognition that an effective analysis of ESG risk and opportunities is a fundamental part of assessing a project’s value. Investors also increasingly take into account the ESG issues impacting their own reputation in a society where sustainable development is becoming a major concern. Such concerns include - among other things:

- Environmental concerns such as climate change, hazardous waste, nuclear energy, biodiversity.
- Social concerns including diversity, human rights, consumer and worker protection, sin stocks, ageing population, animal welfare.
- Corporate governance concerns ranging from management structure, employee relations to executive compensation.

ESG requires investors to take a wider view, which provides insights into the long term prospects of projects. Therefore, an ESG approach may provide investors with a benchmark to judge the overall quality and spectrum of the project’s opportunities and risks.

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**Greenfield vs. brownfield infrastructure**

Greenfield projects are known as development or primary projects. They often start from “nothing”, i.e. they generally correspond to assets constructed for the first time in a specific location, the construction of a new highway for instance. Uncertainty may stem from cost and demand sides. On the cost side, these projects must pass the construction phase in particular. On the revenue side, and depending on the project framework, uncertainty may stem from the demand for the infrastructure and the associated price.

Brownfield projects are understood as operational or secondary projects. In contrast to greenfield projects, they are already operational or rely on existing infrastructure. For example, they may operate the reconstruction, renovation or expansion of an asset. As such, the risks associated with the early phases of greenfield projects are outdated; the remaining risks are operational, regulatory and market risks. Compare for instance the construction of a new Concentrated Solar Power plant with the addition of one more unit within the plant.

Therefore, the distinction between brownfield and greenfield infrastructure lies in their different level of risk and ultimately, their maturity (Weber and Alfen 2010). The first will thus tend to attract risk averse investors while the latter is more appropriate for investors that will participate in shaping the project in the start-up phase so as to ensure its value grows and possibly generates higher returns.
Primary sets of ESG criteria and elements are also related to international agreements such as the Rio Declaration on Environment and Development produced at the 1992 United Nations Conference on Environment and Development (UNCED), the International Labour Organization (ILO), a United Nations agency setting among others an international labour standard or the Convention on Biological Diversity, the United Nations Framework Convention on Climate Change and the Kyoto Protocol.

However, the great heterogeneity of views, motives and practices regarding the ESG approach impedes comparison between firms’ claimed successes. A coordinated and effective responsible investing could be favourable and simplify investment decisions and would therefore lead to further investments and benefits. A uniform implementation would also be desirable to avoid “greenwashing”, the deceptive promotion of an environmentally friendly image.

Nonetheless, there is currently no global commonly agreed ESG scale/standard. As a result, it is difficult to state whether or not a firm invests in a sustainable and responsible manner. A clear universal definition could address this first issue. Another step would be to create an ESG scale firms could refer to. In such case, instead of evaluating whether the investments are green or not, it is the quality of firms’ engagement that would be assessed.

If one clear definition does not yet exist, there are however many examples of frameworks and tools providing practical guidance for investors to implement ESG in their investment decisions (see chapter 2. Existing frameworks and tools).

Definition of Sustainable Infrastructure

Sustainable infrastructure provides the same services as conventional infrastructure while bringing additional benefits flowing from the implementation of ESG criteria. Since any infrastructure facility is improved, or made more valuable, when incorporating the concerns of the triple bottom line, i.e. economic, social and environmental concerns, and since the ESG approach covers these triple concerns, adopting an ESG approach brings added value to the environment, civil society and investors.

Referring to a publication from the World Bank Group (2012), introducing ESG into infrastructure project is indispensable for a country to stay competitive: “Infrastructure can be a vector of change in addressing some of the most systemic development challenges of today’s world: social stability, rapid urbanization, climate change adaptation and mitigation and natural disasters. Without an infrastructure that supports green and inclusive growth, countries will not only find it harder to meet unmet basic needs, they will struggle to improve competitiveness.”

Sustainable infrastructure is therefore not only a key component of a functioning economy; it also forms the basis of good livelihoods for billions of people, and can significantly contribute to achieving sustainability and addressing global climate challenge. Indeed, the UN Open Working Group includes the potential of infrastructure in their proposal for the Sustainable Development Goals (SDGs) by directly mentioning sustainable and resilient infrastructure in two of the seventeen SDGs. This underlines the potential power of infrastructure to drive sustainable development.

Climate and Infrastructure

Climate change affects all regions of the world and impact and consequences of global warming are truly intimidating: melting polar ice sheets are fueling rising sea-levels that will leave no shore unaffected. Other regions are likely to face extreme cold episodes and rainfall more often while others may suffer from extreme heat waves and droughts. In fact, many poor developing countries as well as a wide range of economic sectors that rely strongly on their natural environment (e.g. agriculture, forestry, energy and tourism) are particularly exposed to climate change. Other potential negative effects are the damages incurred to property and infrastructure by natural disasters, losses of productivity due to disruption in daily life and harmed trade related to climate change, mass migration of climate refugees- people who are forced to leave their homes because of hostile environments. Different quantifications regarding the costs of climate change were made by economists however, as Nicholas Stern, a former chief economist with the World Bank...
As described by the World Wide Fund for Nature (WWF), biological diversity – or biodiversity – is the term given to the variety of life on Earth. It includes the variety within and between all species of plants, animals and micro-organisms and the ecosystems within which they live and interact. This diversity forms the natural capital that keeps our ecosystems resilient and economies productive. Indeed, only by preserving such diversity will our environments adapt to a changing climate and maintain human life in these particular locations. For example, drought-resistant crops will be of decisive importance to populations living on the border of the Sahara or other expanding deserts. However, the world is currently experiencing a dramatic loss of biodiversity mainly as a result of urbanisation, deforestation and overexploitation of natural stocks. A continuing pressure on ecosystems may lead to them becoming too small, depleted or isolated to further ensure human presence.

Referring to the United Nations (UN) Millennium Ecosystem Assessment (MA), Europe’s territory is more fragmented than any other continent’s. This is mainly due to the fact that vast areas have been transformed into urban zones or blended by transport infrastructure. This had decreased the resilience of once biodiversity-rich ecosystems. As an attempt to limit the trend, the Convention on Biological Diversity (CBD) has been agreed upon. It is a multilateral treaty with three main goals: 1) conservation of biological diversity (or biodiversity) 2) sustainable use of its components, 3) fair and equitable sharing of benefits arising from genetic resources.

Sustainable infrastructure can play - if biodiversity conservation is adequately implemented - a crucial role in protecting the functionality of urban and rural ecosystems and enhancing the quality of life (e.g. health, tourism, protecting historic and cultural heritage). As such, biodiversity conservation is often associated with the term of green infrastructure. Green infrastructure refers to a network of public and private areas that provide ecological, environmental, social and even economic services. Green infrastructure can include reforestation zones, parks, green bridges, fish migration channels, floodplain restoration or high-value farmland. Such connectivity encourages the mobility of organisms (e.g. plants and animals) and enables therewith ecological processes and flows to unfold undisturbed. Sustainable infrastructure needs to grasp the concept of green infrastructure in order to contribute to the conservation of biodiversity.
Business and Human Rights Considerations

The identification and mitigation of actual and potential human rights impacts is inherent to effective ESG management in the context of any infrastructure project. The potential for human rights issues arising from construction, which can range from “land grabs” to on-site labour welfare issues, are well-known. Equally, an infrastructure project - once completed - can adversely affect the rights of workers (e.g. through health & safety and other labour standards issues), as well as those in close proximity to it through its day-to-day operation. Consider, for example, the implications of pollution, expatriate “fly-in / fly-out” workers and security forces (charged with protecting infrastructure assets) for local communities.

Although framing these issues in “human rights” language is perhaps a more recent phenomenon for investors, it has long been acknowledged that such “social impacts” can arise from the financing of infrastructure projects. Whilst certain soft law standards applicable to businesses have explicitly referenced human rights for some time (e.g. the UN Global Compact, founded in 2000), the shift towards human rights terminology is largely attributable to the UN Guiding Principles on Business and Human Rights and subsequent developments, which we discuss below.

UN Guiding Principles

The UN Guiding Principles emphasise that businesses need to ‘know and show’ that they respect human rights through policy commitment, human rights due diligence, the provision of remedy for those whose rights have been infringed (where appropriate) and external reporting on human rights impacts. A key tenet of the UN Guiding Principles is that businesses have a responsibility to respect human rights. This responsibility is discharged through human rights due diligence, which is fundamental to the effective identification and management of human rights impacts associated with a businesses’ operations, supply chains or value chains.

Effective human rights due diligence pursuant to the UN Guiding Principles has several key defining characteristics. Firstly, the process must be targeted at assessing and mitigating impacts to the rights-holders (rather than risks to the business). Secondly, it must not be “company” or “group” specific; a business can cause, contribute or be linked to human rights impacts through any number of business relationships, such as with suppliers, customers or joint venture partners. Finally, due diligence is an ongoing process, as the potential for human rights issues can change over time. This final point is particularly relevant to long term investment projects.

The UN Guiding Principles were unanimously endorsed by the UN Human Rights Council in 2011 and garnered widespread support from governments, businesses and civil society. As is explained below, they remain the most authoritative voluntary standard for businesses in terms of ensuring respect for human rights. However, as the UN Guiding Principles are intended to apply to any business in any sector or operating context, they are - by design - high level principles.

For investors, specific additional standards or guidance documents - which draw from the UN Guiding Principles - may apply, depending on the nature of their investment, including the Principles for Responsible Investment, Equator Principles and OECD Guidelines for Multinational Enterprises (OECD Guidelines), which we discuss below. Investors are increasingly incorporating these standards into their decision-making and monitoring processes in response to the growing awareness that the value of an investment can be significantly impacted by the prevalence of human rights issues.
rights issues. This is particularly true of infrastructure investments, where the potential for severe human rights issues is well-documented.

**Project Specific Financing**

The Equator Principles (EPs) is a risk management framework which signatory financial institutions (EPFs) must adhere to when determining, assessing and managing environmental and social risks arising from project financing. The EPs were revised in 2013 to create new requirements for businesses to conduct human rights due diligence in order to qualify for financing from EPFs, which include 79 of the largest financial institutions.

The EPs apply to all project financing with a value of over US$10 million and to certain types of corporate loans, bridge loans and project finance advisory services (e.g. advice on the provision of equity and project management), and EPFs are required to ensure clients comply with the detailed requirements of the International Finance Corporation Performance Standards on Environmental & Social Sustainability (IFC Performance Standards), upon which the EPs are based.

The IFC Performance Standards, which were first published in 2006, are addressed to parties responsible for implementing and operating projects financed by the IFC or the recipients of that financing. They cover a range of potential risk areas for infrastructure projects including environmental and social risks, labour and working conditions (including child and forced labour), pollution prevention, community health, safety and security, land acquisition and involuntary resettlement, biodiversity conservation, indigenous peoples and cultural heritage.

The principal aim of the IFC Performance Standards is to ensure that potential issues in these risk areas are properly identified, avoided, mitigated and managed, over and above the requirements of host country laws and regulations where necessary. In 2012, the IFC Performance Standards were updated to require “specific human rights due diligence” of the type endorsed by the UN Guiding Principles in “high risk circumstances”.

This is a narrower approach than the UN Guiding Principles, which envisages the performance of human rights due diligence to avoid actual or potential human rights impacts regardless of the operating context [in all circumstances]. In that sense, some form of proportionate human rights due diligence is necessary precisely to inform the decision of what risks of adverse human rights impacts may be present which either need to be addressed or otherwise subjected to further due diligence.

In addition to any of the above soft-law standards, it is important to ensure in any infrastructure project that all applicable laws are complied with, throughout the construction (and subsequent operation of) infrastructure. An increasing number of countries are adopting laws which directly address human rights in the context of infrastructure projects. Most recently, Senegal passed a new Mining Code in 2016 which requires mining companies to respect, protect and implement human rights in the areas affected by their operations.

**Institutional Investors**

Beyond the pure project finance context, institutional investors including banks, pension funds and asset management firms are under growing pressure to perform human rights due diligence on their investee companies, on the basis that even a minority interest in a company can constitute a “business relationship” for the purposes of the UN Guiding Principles. In terms of infrastructure, an investor’s responsibilities under the UN Guiding Principles may be engaged where, for example, that investor acquires an interest in a company which works on construction projects.

The need for some form of human rights due diligence in such a scenario is well-highlighted by a 2012 determination by the Norwegian National Contact Point (NCP) that an investor violated the OECD Guidelines in part because it did not have a strategy to react to human rights risks related to the companies in which it invested, apart from in relation to child labour issues. This matter is of interest because the relevant investor held around a 1% share in a steel company which had been accused of human rights abuses in connection with the construction of a plant. For context, all member states of the OECD are required to establish NCPs to receive complaints from third parties about corporate conduct which is alleged to fall short of the expectations of the OECD Guidelines. Upon receiving a complaint, an NCP will determine whether or not the relevant business has complied with the OECD Guidelines, which are broadly aligned with the UN Guiding Principles in...
Firstly, investors frequently struggle to acquire relevant human rights impacts which might arise in connection with circumstances. Moreover, investors face a number of challenges in ascertaining, managing and accounting for human rights impacts which might arise in connection with their investments.

Secondly, when faced with potential human rights (and other ESG) issues, institutional investors charged with managing funds on behalf of beneficiaries (e.g. pension funds managers) may find that their response is constrained by certain legal duties, depending on the jurisdiction and the nature of the human rights issues in question. Under English law, trustees need to bear in mind the overriding duty to promote the purpose of the trust. Some trusts give investors specific ethical mandates, but the majority of trusts are established solely for the accrual of profit on behalf of beneficiaries. Although it is well-established that certain human rights issues can impact on the value of an investment (e.g. by causing an investee company’s share price to underperform), it can be difficult to predict when such human rights-related risks may materialise. In an infrastructure context, for example, rights issues may lead to community protests. Until the protest which triggers a fall in the investee company's stock price, the underlying issues would not be quantified by an investor absent effective human rights due diligence.

Thirdly, investors can struggle to establish “leverage” over investee companies once a specific human rights issue has been identified. Largely, the degree to which an investor is positioned to exert leverage will depend on the size of its investment (e.g. its shareholding) and the extent to which it is represented on the board of the investee company (assuming its appointed board representatives have had appropriate human rights training). “Leverage” for these purposes is a UN Guiding Principles term; effectively the steps a company can take – as appropriate – to influence another person with which it has a relationship to cease or mitigate identified human rights impacts. It is distinct from the more traditional duty incumbent on institutional investors to undertake on-going monitoring of an investment’s performance.

In grappling with these and other challenges, investors can have regard to the Principles of Responsible Investment (PRI). The PRI is a member-driven UN supported initiative aimed at helping institutional investors discharge their fiduciary duties by managing any ESG governance issues that could affect the performance of investment portfolios. The six principles which signatory investors commit to include the following:

- We will incorporate ESG issues into investment analysis and decision-making processes.
- We will be active owners and incorporate ESG issues into our ownership policies and practices.
- We will seek appropriate disclosure on ESG issues by the entities in which we invest.

On 23 February 2017, the PRI announced a new infrastructure work-stream that will focus mainly on private debt and equity investments in infrastructure, both direct and via funds. It will also ensure consideration of material ESG factors in investment decision making, and provide guidance on integrating responsible investment throughout the investment process from origination to exit. An Infrastructure Advisory Committee composed of 17 representatives from nine countries will share their expertise and guide the new infrastructure strategy.
External Reporting

As businesses (including investors) come under increasing scrutiny from stakeholders such as regulators, NGOs, shareholders, customers and employees to demonstrate their respect for human rights, notions of moral and ethical responsibility (as set out in soft-law instruments such as the UN Guiding Principles, Equator Principles and PRIs) are transforming into harder edged legal duties through legislative and regulatory developments.

This is most evident in disclosure requirements which, like the CHRB, seek to encourage competition between businesses. This emphasis on transparency is reflected in the UN Guiding Principles, which advocate that businesses report publicly on their human rights impacts and responses. Examples of specific “disclosure” laws include the following:

- The UK Modern Slavery Act 2015 requires certain companies to report on the steps they are taking to eradicate slavery and human trafficking in their own operations and in their supply chains, by publishing a statement in a prominent place on the business’ website. An amendment is currently proceeding through Parliament that would oblige UK authorities to exclude any economic operator from participating in procurement processes unless they have produced a slavery and human trafficking statement: this could be significant in terms of UK-funded infrastructure projects. In February 2017 the Australian government commenced an inquiry into whether Australia should adopt similar legislation to combat modern slavery which would be comparable to the Modern Slavery Act.
- In early 2017, the French Parliament voted to pass a new French “duty of vigilance” law which will require certain French multinational companies to implement (and publish) due diligence plans identifying risks of adverse human rights impacts, assuming it survives a pending constitutional challenge.
- From 2017, pursuant to amendments to the EU Directive on the disclosure of non-financial and diversity information, large listed companies and other public interest entities across the EU will be required to publish a non-financial statement containing information on, amongst other things, human rights matters necessary to understand the “impact” of the company’s activity.

Reflecting the demand for increased reporting by companies on their human rights performance, the UN Guiding Principles Reporting Framework was launched in 2015. The aim of the Reporting Framework is to provide guidance for “adopting” companies regarding how to report meaningfully on their respect for human rights, to facilitate their engagement with investors and other stakeholders.

Human Rights Due Diligence

Although there is a growing consensus that human rights due diligence is centrally important to the effective identification and management of human rights issues, there remains a lack of clarity amongst businesses about what it requires. International law firm Norton Rose Fulbright and the British Institute of International and Comparative Law (BIICL) conducted a joint research project with the aim of helping businesses understand the scope, meaning and consequences of human rights due diligence as described in the Guiding Principles.

The results, published in October 2016, showed that due diligence with a specific focus on human rights proved to be more effective: 77% of the survey respondents that conducted specific human rights due diligence identified actual or potential human rights impacts in their operations through the process. By contrast, only 19% of companies who did not conduct due diligence with an express focus on human rights identified these impacts.

The project further concluded that where companies undertook specific human rights due diligence:

- most did so with reference to the UN Guiding Principles;
- actual or potential human rights issues were more likely to be identified;
- impacts linked to the activities of third parties were more likely to be identified (74% identified actual or potential human rights impacts linked to the activities of their third party business relationships vs. 29% in the cohort which did not undertake specific human rights due diligence);
- findings were more likely to be reported both internally and externally;
- the CSR function, which has a company-wide mandate, would most often have responsibility for the identification, response to and monitoring of human rights impacts often in co-operation with other functions, particularly the legal department;
- human rights experts were more likely to be engaged; and
- the effectiveness of actions taken in response to identified issues were more likely to be monitored.
Conversely, where companies did not undertake specific human rights due diligence, but incorporated human rights issues into other processes:

- the exercise was more likely to result in identifying mainly highly regulated human rights issues, such as health and safety and labour related rights being considered, most likely in response to the prevailing legal imperatives;
- issues which are connected to unregulated or less regulated areas (including the impacts of third party relationships) were unlikely to be identified or monitored at all;
- the human resources function would usually be responsible for human rights-related work, which is likely correlated to focus on regulated issues highlighted above with special emphasis on labour rights only; and
- the effectiveness of the company's human rights-related actions were unlikely to be monitored.

http://human-rights-due-diligence.nortonrosefulbright.online/
Reporting on ESG policy
Country ESG factors: global approach

Numerous academic and empirical works seek to assess sustainable development such as the Human Development Index (HDI, inequality-adjusted or not), the Inclusive Wealth Indicators (IWI) and the Sustainable Development Goals (SDG) proposed by the United Nations, complementary indicators to GDP Calculated by the European Statistics Office (Sustainable Development Indicators, SDI) and many other national statistical bodies (the Netherlands, Bhutan, France, etc.) or the Social Progress Index (SPI) proposed by Harvard University and Strategic Management Professor Michael Porter. Each of these approaches defines a set of indicators (aggregated or distinct) that composes a sustainable development model based on ESG factors (Environment, Social and Governance). These indicators provide an "absolute" view of the magnitude of ESG development reached at country level and allow for an international ranking.

As previously mentioned, ESG performance can’t be evaluated without taking into account specific development pathways and income levels and a multi-criteria approach is often useful for operational processes. An expected GDP based on ESG KPIs can be computed as the theoretical GDP that is compatible with the level of ESG performance achieved by a country. Such GDP is called “sustainable” GDP and reflects the actual level of ESG development. If it is equal to actual GDP, the sustainable and economic developments are coherent, if it is higher (or lower), the wealth produced has made it possible to develop a higher standard of ESG environment (or, respectively lower standard) compared to the peer countries.

The larger and wider the input scope is, the more accurate the ESG evaluation is. ESG indicators are usually split in 36 major domains to consider:

The main challenge is estimating the most accurate weights for ESG indicators while keeping the overall GDP structure. It gives a financial valuation of every criteria.

Such statistical econometric approach can be differentially applied based on countries development levels. It allows for better consideration of ESG priorities according to a country’s current economic development path.

This methodology provides an assessment of a country’s ESG development based on its level of economic development. This approach makes it possible to refine the relative weight of ESG development indicators per stage of economic development of a given country. One of the significant benefits is not to systematically penalize the less developed countries to the profits of the most advanced countries in terms of ESG criteria. This is an additional tool for assessment.