ESG considerations for private equity firms
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What do we mean by ESG issues?

Environmental, social and governance (ESG) issues cover a broad agenda. Therefore, we break the issues down into five categories: Environment, Workplace, Community, Marketplace and Governance. The ‘ESG wheel’ below shows examples of issues within each category. The relevance of the issues will depend on the specific situation, for example, related to a portfolio company’s sector or geography.

We recommend that a wide range of activities – from strategy and policy development to tools creation and use, and training are needed to appropriately manage ESG risks and opportunities.
**What are the different elements of ESG reporting?**

As the name suggests, private equity has traditionally remained ‘private’ and has not reported non-financial issues. However, that stance is changing:

- Public perception of the industry remains poor following the financial crisis and other high profile incidents in portfolio companies.
- ‘Soft’ regulation is growing, for example, the Walker Guidelines for Disclosure and Transparency in Private Equity.
- Demand for non-financial reporting is rising from a range of stakeholders e.g. from investors, industry initiatives and the public.
- Only 8% of private equity firms indicated, in our 2013 survey, that they did not expect to report on responsible investment activity in the next two years*.

ESG reporting means reporting up from the portfolio companies to your private equity firm, and then from your firm to a range of stakeholders. This document addresses the four elements described below:

* Source: ‘Putting a price on value’ – PwC’s global responsible investment survey, 2013
Reporting from portfolio companies

What do we mean?

- Information related to the ESG activities of the portfolio companies, and how they are responding to your encouragement to improve ESG performance.
- Quantitative (e.g. metrics) and qualitative information (e.g. case studies).

Why is this important?

- ESG performance is directly related to revenue and costs – it is important to monitor how your portfolio companies are managing these issues and encourage performance improvement.
- Reporting to external stakeholders requires robust, relevant information from the portfolio companies.
- Maximising value on exit is dependent on monitoring ESG performance during ownership so that you have a ‘great ESG story to tell’ in a prospectus.
- Placing a monetary value on ESG activities relies on data from the portfolio companies.

How are firms responding?

- 88% of portfolio companies formally report ESG monitoring results to their firm*.
- Some firms have developed tools (or used proprietary ESG software) to collect information and agreed KPIs, integrating these into existing reporting processes.
- Firms have conducted ESG assessments of portfolio companies to check that significant ESG risks and opportunities are being managed.

* Source: ‘Putting a price on value’ – PwC’s global responsible investment survey, 2013 | ESG considerations for private equity firms | PwC
Getting the right support

How can PwC help?

We can:

• **Advise on developing ESG KPIs** to monitor the portfolio companies which directly link to value protection/creation. These will support your external reporting and balance the practicalities of data-collection.

• **Develop tools, templates and the internal control environment** for collecting data at the portfolio companies for efficient reporting to you.

• **Interpret the data you receive** from the portfolio companies, giving you an expert perspective on the quality and scope of information, as well as the underlying performance.

• **Assess the significant ESG risks and opportunities** through a portfolio review and evaluate the existing management activities at the portfolio companies, making recommendations for improvement.
Reporting to the Principles for Responsible Investment (PRI)

Who is this relevant for?

- The Principles for Responsible Investment (PRI) is an initiative to promote responsible investment across various asset classes, including private equity.
- It is becoming mainstream with over 150 private equity firms now being signatories.
- Furthermore, 250 investors are signatories and must report on their responsible investment performance, driving increased demands on private equity firms for action and information.

When do you need to report?

- It is now mandatory for almost all signatories to report annually on their responsible investment performance (except those in a ‘grace’ period), in line with the reporting framework released in 2013.
- The reporting window for mandatory reporting closes on 31st March each year.

What is going to happen?

- Signatories must complete the three mandatory reporting ‘modules’ plus further modules, depending on the composition of their portfolios by asset class e.g. private equity, infrastructure, property.
- The PRI will publicly disclose a defined set of each signatories’ responses and there will be the option for signatories to disclose additional responses voluntarily.
- Assessment of signatories’ reporting is round the corner – the assessment framework will be rolled out to all signatories in the coming years.
Getting the right support

How can PwC help?

We can:

- **Demystify the requirements** of the PRI reporting framework, determining which modules are applicable to your firm. Explain which responses will be publicly reported and how the responses will be scored.
- Perform a ‘shadow’ review so you can understand the process and see how you will rate absolutely and relative to your peers (if data is available), before completing the official submission.
- Provide you with **tools to easily collate the information**, saving you time and taking the burden off your hands.
- Use your report to **identify gaps in your approach**, advising on how to address them before next year’s report.
- **Provide assurance** on your report so you can give additional comfort to your stakeholders. External assurance will also boost your score in the report assessment.
**Reporting to investors**

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**Investors**

- Principles for Responsible Investment

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**Your private equity firm**

- Portfolio companies

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**Public and other stakeholders**

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### What is happening in the market?

- More investors are interested in the ESG activities of private equity firms – currently 85% of UK firms report an interest and no firms expect this to decrease in the next two years*.
- The ESG Disclosure Framework now gives firms a guide to reporting to investors – 42% of firms plan to use this Framework*.
- The latest ILPA guidance suggests specific ESG disclosures from a firm to its investors.

### How are firms responding?

- The majority of firms (56%) are already reporting some ESG activity to investors*.
- Some investors are now looking for firms to report on ESG issues throughout the life of a fund, not just at fund-raising.

### Why is this important?

- There is evidence that some investors are beginning to restrict access to capital due to poor ESG performance.
- Reporting can build trust and confidence amongst investors on how non-financial, as well as financial, issues are being managed.
- A proliferation of different information requests from investors may be time-consuming to respond to – proactively articulating your ‘ESG story’ once, would be more efficient.
- Investors expect to find out about material ESG incidents before reading about them online. Determining materiality and incident report timing is critical.

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* Source: ‘Putting a price on value’ – PwC’s global responsible investment survey, 2013

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Getting the right support

How can PwC help?
We can:

• Support you to **decide on what to report**, for example, aligning a report to the ESG Disclosure Framework. This could include discussing expectations with investors.

• **Draft or review content** of reports/questionnaire responses to investors, using our expertise to interpret information from the portfolio companies and our knowledge of the market, and saving you time.

• Assess your report to **identify gaps in your approach**, advising on how to address them.

• **Provide an assurance opinion** on your report so you can give additional comfort to investors.

• **Build fundraisers’ knowledge and confidence** through tailored ESG training sessions.

• **Present at investor meetings** using our understanding of your business to showcase your work.
Reporting to the public and other stakeholders

What is happening in the market?

- Numerous stakeholder groups are increasingly interested in a private equity firm’s ESG activities e.g. public, regulators/governments, employees, the media and interest groups.
- There are growing expectations for transparency and accountability across the corporate world.

How are firms responding?

- The trend is increasingly for private equity firms to use their websites to publicise their ESG positions e.g. publishing their ESG policy or profiling ESG activities in specific portfolio companies.
- Firms are reporting more to the public and other stakeholders in line with ‘soft’ regulation, such as the Walker Guidelines and the Stewardship Code.
- Some firms are using extensive public ESG reporting to differentiate themselves e.g. voluntary Walker assessments or specific ESG reports.

Why is this important?

- Public reporting of ESG activities has become mainstream and expectations are set to increase further.
- Regulatory requirements are unlikely to get any easier.
- If a portfolio company exit is expected through an IPO on the London market, mandatory carbon reporting will need to be addressed.
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