Has sustainability reporting become unsustainable?

By Kelsey Rolfe

Environmental, social and corporate governance rating is a burgeoning industry, and not without its growing pains

At Agnico Eagle's Nunavut operations, the company has a lofty goal of hiring 50 per cent of its employees from local Inuit communities, but that has not been easy. For many of Agnico's Inuit hires, the mine is their first formal job and their first time in an industrial setting – meaning they need extra training and more time to adjust to the work.

"It is expecting a lot from them to get a job and go for the long haul," said Louise Grondin, senior vice-president of environment, sustainable development and people. "They come, we hire them, they spend say nine months or a year and then they quit. Then six months or a year later, we hire them back…If we want local employees we have to train and retrain some people many times to allow them to experiment in an industrial setting and get used to it."

The Nunavut operations have at times reached turnover rates of about 28 per cent, though Grondin estimates it's around 19 or 20 per cent currently. In comparison, some environmental, social and corporate governance ratings agencies — a growing class of ratings firms that specialize in evaluating companies on their material environmental, social and governance (ESG) risk exposure and efforts at mitigation — consider turnover rates of higher than 10 per cent a red flag that the evaluated companies have simmering workforce issues.

"What is a responsible mining company supposed to do? Hire people from the south and ensure a low turnover like we have at [our] Abitibi [operations] or make an effort in training?" Grondin asked. "If you only look at the number, you say, 'well that's a bad company, you can't keep your employees.' If you actually listen to the story, this is a responsible company that knows one of the benefits of mining is local employment."

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Demand rises for ESG risk reporting

The growth of sustainable investing over the past decade has seen institutional investors put a high priority on understanding companies' exposure to broad and sector-specific ESG risks – spanning the gamut from water usage and how climate change could impact operations, to workforce issues and safety to board and executive diversity. As of 2017, according to New York-based McKinsey & Company, more than one-quarter of global assets under management were invested "according to the premise that [ESG] factors can materially affect a company's performance and market value." Closer to home, the Toronto-based Responsible Investment Association reported in 2018 that more than half of Canadian assets under management – an amount worth $2 trillion – were invested in what are deemed responsible ventures. Today, 70 per cent of global institutional investors use ESG principles when investing, according to an October 2019 RBC Global Asset Management survey of 800 investors.

The heightened importance of ESG ratings and reporting presents an opportunity for mining companies, but also a

challenge. Complying with ESG reporting standards that help companies explain how they address material risks can attract generalist investors and open new project financing opportunities. But companies must also decide which standards to follow and then contend with the large number of ratings firms whose assessments of the same company can diverge, sometimes substantially.

"The multiplicity of these ratings agencies makes it difficult," said Grondin. "They're all different questions with a slightly different angle. It's not so obvious."

Competing standards

While the popularity of sustainable investing is a relatively new phenomenon, ESG ratings have existed since the 1980s, primarily as a service for niche investors.

As ratings firms have multiplied, mining companies have had to learn what information they need and to adapt or augment their sustainability reporting accordingly. An alphabet soup of reporting standards has been developed – including the Global Reporting Initiative (GRI), which covers issues such as climate change, human rights and corruption; the Task Force on Climate-related Financial Disclosures (TCFD), which helps companies navigate how to disclose material climate risks to their business; and the Sustainability Accountings Standards Board (SASB). In addition, mining associations have developed their own industry-specific disclosure guidelines, such as the Mining Association of Canada's Towards Sustainable Mining and the International Council of Metals and Mining's forthcoming guidance on tailings disclosure.

"Everybody's coming out of the woodwork with standards. From the point of view of the miners, we're not going in the right direction. Somewhere somebody will have to bring these entities together and say, 'Can we have common ground?'… because otherwise the reporting will take over from doing," said Grondin. "We want to do the right thing, [but] if we spend more time reporting than doing it, to me that's not performance improvement."

Geoff Healy, BHP's chief external affairs officer, said he has gotten similar comments from some of the company's investors. "A point we heard from investors is there's a lack of commonality," he said. "As you look at it from an investor point of view, they want the standardization, so they're encouraging industries to work together to come up with what they think are the best set of measures and to make sure that the rules around reporting under those measures are specific enough to ensure you're getting proper data."

Jamie Bonham, manager of corporate engagement at responsible investment firm NEI Investments, said he's sympathetic to the concerns of mining companies that feel burdened by the number of reporting standards. "I do think it can be a challenge for a company to decide which one to follow, because they are all different in some way and all speak to a different audience," he said.

Bonham said he isn't picky about which standards the companies NEI invests in ultimately use – the most important part is that their disclosures tell a clear story of what they see as their most pressing ESG risks, and how they're working to address them.

While major miners have been telling their story for a long time, small and mid-tier miners are more likely to have not yet put pen to paper – and, according to Simon MacMahon, the head of ESG research at Sustainalytics, they may find themselves hit with an unflattering rating because they did not make the information available.

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– J. Bonham

"If they're not disclosing information and they're not communicating with us…we don't give them the benefit of the doubt," MacMahon said. "Perhaps if they spend more energy on disclosure, they would get a slightly lower risk rating. But we have to assume in the absence of any evidence that they don't have the management systems in place, policies or programs that we're looking for."

Bonham agreed, calling it a "red flag" if companies fail to identify important ESG issues as relevant to disclose. "If your disclosure's not there, you're just not going to be considered," he said.

Mid-tier miner Equinox Gold will issue its first-ever sustainability report in 2020. To prepare, it underwent a materiality assessment that involved gathering input from its mine site staff and investors as well as determining that its key focus areas would be carbon, water and tailings disclosures on the environmental side, and community-related topics such as local hiring, spending, training programs and the company's engagement process as social metrics.

Christian Milau, Equinox's CEO, said the company ultimately decided to follow the SASB and TCFD standards, and default to the GRI when there are gaps between topics covered in the materiality assessment and its chosen standards.

"There are obviously many reporting standards that all have slightly different lenses and are intended for different audiences. The difficulty for a company is in gauging which of the many standards provide information that is both compelling for the reader and also allow true comparisons to be made with other reporting companies," he said.

Evaluating the evaluators

Aside from reporting, multiple mining executives noted the sheer number of ratings and research houses – and the developing field of ESG research – can complicate matters.

Omar Jabara, a corporate communications executive at Newmont Corp., said the data-collection methods of some firms – which involve asking miners to fill out questionnaires or speak to analysts in addition to reviewing public information – means the company needs to be thoughtful about which raters it engages with.

"We have to be strategic in some ways. Because there are so many of them, you could literally spend all your time just responding to questionnaires," he said. "There are a number out there that are very reputable, very thorough. Those ones provide value and have the profile. And then there are others that may have further to go on the maturity curve."

It is not just the mining companies making note of the conflicting standards. Academic papers published in the past decade have posited that ESG assessments may not be entirely reliable, noting the lack of agreement across several ratings houses. A 2015 *Strategic Management Journal* study that compared six social ratings firms, for example, found "low convergence in their assessments of [corporate social responsibility]," not just due to difference in how those firms understood CSR, but how they measured the same factors.

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"If the ratings are not actually valid and cannot consistently identify socially responsible firms, then the hypothesized benefits of CSR cannot occur. For example, if [companies] cannot deduce whether their low rating is due to poor operations and performance, a different conceptualization of CSR than the raters, or simply poor measurement…then they will be unable to craft the appropriate response," the authors wrote.

Researchers from the Massachusetts Institute of Technology's Sloan School of Management and the University of Zurich came to much the same conclusion in a 2019 paper that evaluated the disagreement between the ESG ratings of five major ratings agencies. The study found three sources of disagreement: scope, or how raters selected various categories to form their ratings; how much weight or importance was placed on each attribute within a category; and, most importantly, the different attributes raters used to evaluate various categories, which the authors said accounted for more than 50 per cent of disagreement between firms.

"For example, if you're looking at gender metrics, you could look at remuneration and salaries or the women in management. What you want to get at is how women are treated in the workforce. Both are proxies," said Florian Berg, the paper's lead author and a postdoctoral associate in economics, finance and accounting at MIT Sloan. "If one rating agency opts for one of those approximations, it will definitely come to different conclusions than other ratings agencies."

Sustainalytics' MacMahon said he expects there will be more correlation between ratings firms in the future as more companies disclose their risk and performance, and the investment world settles on clear definitions of ESG and sustainability. But the fact that ratings agencies are working with unstructured and often incomplete data means a certain amount of disagreement is here to stay.

Berg, for his part, said he is most interested in seeing agencies agree on some commonality in how they measure ESG categories. His paper identified 64 category groupings between the five agencies – including climate risk management, labour practices, human and Indigenous rights, corruption, business ethics, toxic spills and unions – and low agreement between agencies on how those categories were evaluated, if they used them at all. Berg proposed raters could evaluate companies with a smaller set of categories, and an agreed set of attributes for each category. Doing so would give companies being rated a better understanding of how they are being evaluated across the board, without sacrificing raters' competitive advantage.

From a mining perspective, while working with multiple raters may take plenty of time and effort, their evaluations as a whole are fairly capturing the state of the industry, and of individual companies' sustainability progress, said Jabara.

"One on its own may get close to the target, but if you look at them all in aggregate, I think you get a better picture of the industry as a whole," he said. "If it was just one [positive rating] and we weren't performing well in the others, we'd have to take a hard look at ourselves."

Seeing the bigger picture

Reflecting on what ESG firms sometimes miss, Grondin pointed to another workforce metric. Agnico's operations in Nunavut and the Abitibi region of Quebec are not unionized, though its mines in Mexico and Finland are. Regardless, all its sites have "collaboration committees" where employee representatives can bring issues to the attention of management and resolve them in a non-confrontational way. Despite that, Grondin said, some ratings firms have dinged Agnico because its Canadian mines are not unionized.

"It's not because we've prevented unionization, it's because we have a manner of doing our labour relations that people feel they don't need unions," she said. "We believe that system works, but…for some scoring agencies it's a negative, and why would that be? It's not necessarily a negative."

While Grondin is frustrated with the disconnect, she said the responsibility ultimately falls on both sides.

"That tells us we need to disclose more and that's [what] we're trying to do now, we're trying to look at what else should we disclose so that the score [better] represents what we do," she said. "The score is the score, but we want to at least have the score represent what we do. If it's not, both sides have to work on it." CIM