

www.environment-agency.gov.uk

# Corporate Environmental Research

A review of environmental rating, ranking and indicies





The Environment Agency is the leading public body protecting and improving the environment in England and Wales.

It's our job to make sure that air, land and water are looked after by everyone in today's society, so that tomorrow's generations inherit a cleaner, healthier world.

Our work includes tackling flooding and pollution incidents, reducing industry's impacts on the environment, cleaning up rivers, coastal waters and contaminated land, and improving wildlife habitats.

Environment Agency Project Executive: Howard Pearce **Environment Agency Project Manager:**Faith Ward

## Written by URS Corporation Limited

Sally Vivian, Angela Glover, Satu Vahalato, Belinda Ridley and Estelle Morgan

## Published by:

Environment Agency Rio House Waterside Drive, Aztec West Almondsbury, Bristol BS32 4UD Tel: 01454 624400 Fax: 01454 624409

© Environment Agency December 2004

All rights reserved. This document may be reproduced with prior permission of the Environment Agency.

This report is printed on Cyclus Print, a 100% recycled stock, which is 100% post consumer waste and is totally chlorine free. Water used is treated and in most cases returned to source in better condition than removed.

# **Foreword**

This report looks at corporate environmental research. On reading it, you may be surprised by the range of organisations working in this sector and at the many types of approaches being used to rate and rank companies from an environmental perspective.

It would appear this diversity is in direct response to a growing demand for such research by various users who want to assess how different companies are managing their environmental risks, impacts or performance. The growth in the number of organisations involved would suggest that this work is economically viable and the market is evolving.

However neither the organisations working in the field, nor their various products or services, are yet as mature or established as those working with more conventional financial ratings, ranking and indices. This has led to criticism and calls for some standardisation from users as well as the companies being assessed.

Greater collaboration over the sources of input data could be advantageous to everybody and could help to improve the consistency and quality of the outputs. This in turn would increase their value for the companies being assessed and the financial investment world who are key users of the data. Better use of publicly available Environment Agency data may also have a role to play. There is also a need for greater dialogue with the companies being assessed and the existing and potential users of the ratings, rankings and indices if they are to become more useful for benchmarking or decision making.

We hope this study has an impact on your thinking. Your feedback on it would be most welcome.

Howard Pearce

Head of Environmental Finance and Pension Fund Management

# Acknowledgements

The Environment Agency and URS Corporation Ltd thank everyone involved in the review – particularly the Environment Agency departments, which provided information and interviews, and the organisations that, participated in interviews for the research.

CoreRatings

## Representatives of organisations interviewed:

Business in the Environment

Patrick Mallon, Director of Corporate Responsibility

Mehrdad Nazari, Director

Jim Haywood, Director of Business in the Environment

Jan Scherer, Analyst

Katia Martin, BiE Index Manager

SAM Indexes (DJSI) Eiris – Ethical Investment Research Service

Alexander Barkawi, Managing Director

Jeremy Baskin, Head of Research

Kelly Vanstone, Senior Analyst

Ethibel – Stock at Stake FTSE4Good

Dirk Van Braeckel, Head of Research

Jayn Harding, Head of CSR

Henderson Global Investors – Sustainable and Responsible Innovest Strategic Value Advisors

Investment Shami Nissan, Director

Nick Robins, Head of SRI Research Andy White, Director of Research

Morley Fund Management – Sustainable Futures Funds oekom research AG

Ronnie Lim, Head of Strategy

Matthias Boenning, Head of Research
Toby Belsom, SRI Analyst

PERFORM – Sustainability Performance Benchmarking SERM Rating Agency

Julia Hertin, Research Fellow and Co-ordinator Jonathan Barber, Director and Founder

Michael Levy, Director

Trucost Independent Advisor

Simon Thomas, Chairman Mark Mansley

Environment Agency:

Adrian Long, Head of Corporate Communications

Chris Howes, Policy Manager, Compliance Assessment and Enforcement

## Disclaimer

The views expressed in this document are not necessarily those of the Environment Agency. Their officers, servants or agents accept no liability whatsoever for any loss or damage arising from the interpretation or use of the information or reliance upon views contained herein.

URS Corporation Ltd (URS) has performed this research for the purpose stated in Section 1.1 of this report. The information contained in this document is for reference purposes only and no warranty or any other representation whatsoever is given in respect of such information (including, without limitation, as to its accuracy, completeness or suitability).

# Contents

Executive summary		5
1.	Introduction	9
1.1	Objective and scope of the study	9
1.2	Report structure	12
2.	Methodology	13
2.1	How was the research structured?	13
2.2	Background information and initial list of organisations	13
2.3	Screening of organisations	15
2.4	Interviews	16
2.5	Company environmental performance review	17
3. (	Overview of the industry	18
3.1	Introduction	18
3.2	What is corporate environmental research?	18
3.4	Some facts on the corporate environmental research sector	25
4.	Desk-based review of organisations	27
5. I	In-depth review of organisations	32
5.1	Introduction	32
5.2	Philosophy and background	34
5.3	Inputs	40
5.4	Process	44
5.5	Outputs	48
<b>6.</b> I	Environment Agency modern regulation strategy	53
6.1	Background	53
6.2	Discussion	54
7. I	Results of company performance review	58
7.1	Introduction	58
7.2	Which companies were included in this performance review?	58
7.3	Methodologies for standardisation	60
<b>7.4</b>	Performance comparison	61

8. Summary and discussion	65
8.1 Environmental content	67
8.2 Industrial coverage	69
8.3 Information and data sources	71
8.4 Assessment methodologies	72
8.5 Quality assurance	73
9. Conclusions	75
Glossary of terms	
	77
References	79
Neierences	13

Annex A Screen 1 information

**Annex B Organisation profiles** 

Annex C "Scoring" normalisation methodology

## **URS CORPORATION LTD**

URS Corporation Ltd (URS), the researcher for this study, is an international environmental, sustainability and engineering consultancy. URS integrates environmental and social management into an organisation's operating systems to ensure non-financial issues are managed effectively, risks are minimised, performance is improved and value is added. Its Sustainable Solutions team, which has performed this work, has a considerable track record in the field of corporate responsibility strategy development, corporate governance and assurance, and non-financial performance and disclosure. www.urseurope.com

# **Executive summary**

## What is this report about?

Businesses are increasingly recognising that the impact of the environment on them, and their impact on the environment, is an issue that can significantly affect their profitability, reputation, employees, and customers, and investors. The city and finance sector are also becoming aware that environmental issues linked to companies supply and distribution chains, product disposal and pollution events, and climate change risks can be important factors in their short and long term financial performance and valuation.

We carried out this study to compare and contrast the different approaches, content, robustness and credibility of the outputs of Corporate Environmental Research (CER) organisations. These organisations produce assessments, ratings, rankings, and indices that are linked to the environmental impact, risks, management and performance of companies listed on stock markets.

### What are the key issues?

In the last decade the number and variety of CER organisations have increased rapidly, as has the availability of their products and services. These are used by the companies being evaluated and trade bodies, as well as by the financial community and investors. The Environment Agency also makes available pollution inventory data and risk-rating information on companies (operators risk assessment). It also publishes an annual spotlight on environmental performance that ranks companies as good and poor performers.

However without understanding the rationale and differences between them some users perceive they have been provided with potentially inconsistent, confusing or contradictory messages regarding companies actual environmental performance. This has recently led to a reduction in confidence in the results and some products being the focus of criticism from various parties, rather than being seen and used as a tool to help companies improve their environmental and financial performance.

## Why was the study commissioned?

The Environment Agency commissioned this study to help end this confusion. They believe that a clearer understanding will contribute to a greener business world – one of the Environment Agency's core goals. The aim of this study is to provide a clear and accessible summary of the philosophies, assessment methodologies and outputs of the various CER organisations. The report is also intended to be a reference tool and guide for users of the different products and services.

The Environment Agency hopes that the findings will educate the information providers, their users, the media, financial investors, and key Environment Agency staff. They hope to improve communications with the organisations that research, assess and rate companies from an environmental perspective. The report is also intended to assist the users of these products in the finance sector and the City, and the managers whom the Environment Agency employs to invest its own pension fund.

#### How was the research conducted?

The research was carried out in stages by URS. We started with web-based information and previous surveys and reports. Later, we interviewed selected organisations to gather more in-depth information. The resulting analysis is both broad and detailed. Aspects of selected organisations are presented in a way that is intended will enable comparison of very different organisations. To make sure our analysis was sound we asked these organisations for feedback before we finalised this report.

## Whom did we investigate?

In total we identified 65 organisations from various countries around the world which research, rate, index and invest in companies based on non-financial issues - including the environment, social factors, health and safety standards, ethical concerns and other corporate governance issues. They do this through the use of publicly available information, detailed questionnaires, follow up dialogue and the use of quite simple to complex models and tools.

We found the emphasis on environmental concerns varied widely. Some gave it little more than token consideration; for others it was 100%. From the long list of 65, we investigated 37 organisations (60%) which included some environmental issues. We then made a more detailed assessment of 13 organisations (20%) which we chose for their perceived environmental content. These organisations were of different types: ratings, rankings, indices and investment funds.

What did we discover (for the 37 organisations)?

## Company participation

Only 30% obtained their information from companies voluntarily e.g by questionnaire and 46% involuntarily eg from public document. Information was not available to assess this for the other organisations (24%).

## Industry sector coverage

We could determine that 22 organisations (60%) applied exclusion policies. Seventeen (46%) screened out certain industry sectors (eg weapons manufacturing) and only five (13%) included all industry sectors in their assessments.

## Products and services

## We found that:

- 27% of the organisations do not charge for their product or service;
- 35% produce publicly available annual rating, rankings or indices;
- 40% provide subscription-based services for their clients;
- 49% provide their outputs through web-interfaces;
- 67% provide company or sector bench-marking;
- only 20% made reference to third-party verification of their processes.

## What did we discover (for the 13 organisations)?

## Environmental content and assessment methodologies

The environmental content for these organisations ranged from 20 to 100%. The average was 40 to 60%. The assessment methodologies included environmental risks, impacts, policies, management systems, external costs, performance, and incidents/events.

Currently only eight of the 13 organisations selected use any of the environmental datasets provided by the Environment Agency. This is because data is mainly stored on a site-by-site basis and not by company. The usefulness of the data sets is therefore felt to be limited. The aggregation of site data into corporate information could benefit not just the regulatory work of the Environment Agency, but also the companies themselves, the CER organisations evaluating environmental performance, and those in the finance sector making investment decisions.

Company and industry sector coverage The number of companies assessed range from 105 to over 2,700 mainly from the UK, EU, USA, Japan which appear in the FTSE, MSCI, S&P, Dow Jones, Nikkei and other leading financial indices. Only five organisations had no sector exclusion policies.

Analysts and metrics The organisations typically employ highly qualified staff with a good broad range of expertise and experience across their teams. The number of analysts available to perform assessments range between four and 23 in each organisation. They have environmental science, economic or finance backgrounds. The number of environmental metrics used ranged from 16 to 100.

Processes and quality assurance All the organisations use a combination of internal peer review and/or external advisory panels. Only six also use a quality standard and/or external verifiers.

<u>Products and services</u> There is great diversity in everything, from company scores, ratings, rankings and indices, to company briefings and sector profiles. It can also be seen in customised research, assessments, modelling, bench-marking, advisory and consultancy work, and in some cases in investment recommendations.

#### What does this mean for users and the future?

There is a rich diversity of tools available for users to choice from depending on ones needs. This diversity would not exist if there the organisations do not enjoy or for-see growing user demand and financial opportunities. Their methods, products and services are likely to continue to evolve a result of innovation, web technology, and a strong commitment to continuous improvement of their services and products.

Some of the organisations provide certain services and products at a relatively low cost or even for free. This is to encourage the use of their products and the consideration of environmental performance in decision-making. The growth of the sector suggests it is economically buoyant, although profit margins may be quite low.

The organisations reviewed use a wide range of quantitative and qualitative sources of data and information to ensure a consistent approach to collection, statistical analysis and technical assessment. There is a welcome trend towards including quantified measurements of actual environmental performance in the assessment process: five of the 13 organisations selected use a significant proportion of quantified environmental data, and two of those five only use quantitative environmental data.

Greater transparency of some organisations quantitative and qualitative methodologies and access and use of consistent data sources will assist the companies being assessed and other users and interested parties to compare the outputs and to interpret and understand the variations in the results. Information made available by some organisations shows that a high level of public transparency is possible without any loss of competitiveness.

For all organisations there are opportunities to improve internal quality control and external quality assurance. Within in some organisations there is need to review controls on how individual analysts' opinions influenced the overall assessment of companies. These aid consistency and repeatability, and increase confidence and trust in their products.

## **Next steps**

We hope this report will facilitate dialogue between the Environment Agency and organisations which research, assess and rate companies from an environmental perspective. Better communications between the Environment Agency, the CER sector and users of such information would also improve its value in decision-making, particularly by the finance sector.

# 1. Introduction

## 1.1 Objective and scope of the study

This review of Corporate Environmental Research (CER) is a comparative study of the methodologies and philosophies of company rating, rankings and indices, with a focus on their environmental content, robustness and credibility. It aims to summarise the philosophy, assessment methodology and outputs of CER organisations and to act as a guide and bench-marking tool for those users that need to gain a better understanding of environmental (and broader sustainability) rating and ranking organisations and the different services they provide.

### The context

Businesses are increasingly recognising that how they treat the natural environment is an issue that can affect profitability, reputation, employees, customers and investors. Parallel to this change in business thinking, investors are also broadening the way they review financial investments. Over the last decade there has been a significant increase in the number of organisations offering products and services associated with assessing and reporting on environmental, and broader sustainability performance of businesses. Some of these emerging products and services are being driven by the needs of the financial community to enable responsible investment, whilst others are responding to industry focused organisations and their demand for company benchmarking tools

As is often the case in developing and relatively immature markets, there is a wide variation in the products and services. This is most marked in the approach and scope of the tools and techniques developed and used by the organisations. This variation might be driven by a number of factors. For example, some organisations may focus on different target users (eg consumers, investors, businesses), or there may be a belief that a particular aspect of environmental or sustainability performance is more important or more directly linked to financial performance.

Without a clear understanding of the differences and the rationale behind these products, potential users are being provided with apparently confusing messages regarding company performance. This apparent discrepancy in results has been a contributing factor in the recent criticisms of company rating organisations and their products. There is also a tendency by users to focus on the negative outputs (ie perceived or reported poor or deteriorating environmental performance) rather than on the positive ones (ie perceived or reported good or rapidly improving environmental performance). All too often the media highjacks the outputs of these ratings organisations and uses them as a means of naming and shaming companies — only highlighting examples of poor performance. Businesses can lose the incentive to engage positively with rating organisations and to use them as a tool for improvement and best practice. Instead such companies can be seen as a nuisance, and working with them as a risk to corporate reputation.

### The Environment Agency's aims

The Environment Agency's Corporate Strategy states that the Environment Agency has a role in driving positive change in our environment. A key theme is contributing to the creation of a greener business world. The Environment Agency is committed to helping UK businesses to consider and manage their environmental impacts and performance.

Because of this, the Environment Agency has developed its own tools and techniques to assess industry environmental performance. This is part of a "risk-based, outcome focused" approach to its regulatory duties. For example, the Environment Agency publication Spotlight on business environmental performance identifies good and bad performers. Internal risk appraisal tools such as OPRA and OMA assist in prioritising resources for regulatory work.

These strategies and initiatives are being developed within a climate of increasing scrutiny and obligation on companies to disclose on their environmental and social performance. For example, the recent UK Company Law Review has led to proposals that companies produce an Operating & Financial Review (OFR) in addition to their Annual Report & Accounts. This will report mainly on non-financial (environmental, social, economic, etc) issues, which could have a material financial impact on a company's business and is aimed to enable the investors and shareholders of the company to make informed assessments of the company's operations, financial position and future business strategies and prospects. The OFR should be more forward looking (rather than based on past performance) and highlight the significant (material) non-financial risks for the company. The consultation period on the OFR ended August 2004, but their recommendations are set to apply to all large UK public listed companies in 2005, thus significantly raising the benchmark for best-practice in non-financial reporting

The Environment Agency has undertaken and published research into the link between corporate governance and financial performance<sup>1</sup> as well as on the current level of environmental disclosure of FTSE companies.<sup>2</sup> From this research and other data generated by its regulatory work, the Environment Agency has a large resource base of information and data on UK business environmental performance.

As illustrated in Figure 1.1, below, there many different organisations all requesting information in order to judge different aspects of company performance. Through this research project and others, developed in line with its "greening business" approach, the Environment Agency aims to improve communications with the CER organisations and the businesses they target.

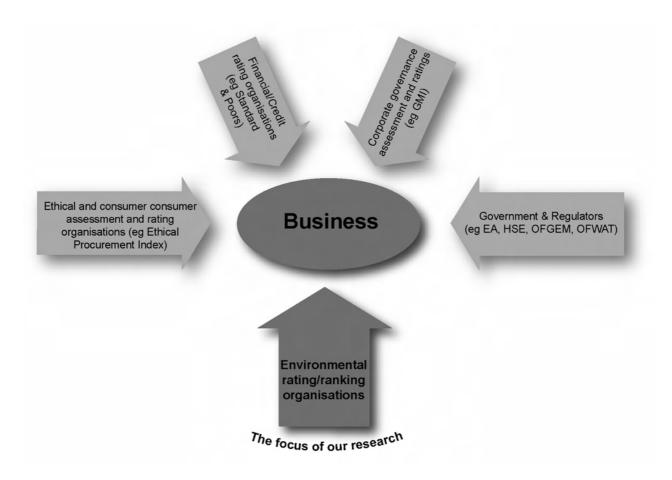
<sup>2</sup> "Environmental Disclosures", Environment Agency, July 2004

<sup>&</sup>lt;sup>1</sup> "Corporate Environmental Governance", Environment Agency, October 2004

The primary aim of this research was to:

provide an objective review of the environmental content, credibility and robustness of company indices, rating and ranking methodologies and in order to influence the environmental strategies and policies of the businesses, financial institutions and financial service sector (including banks, insurers and green investment funds.)

Figure 1.1: Organisations generating assessments of businesses



This report focuses specifically on the environmental rating and ranking organisations (Figure 1.1). There is a potentially complementary link between these organisations and the services they provide, and the aims and vision of the Environment Agency (as the key environmental regulator for England and Wales). This report asks whether this is being used to maximum effect.

The objectives of the project were developed to meet the Environment Agency's aims. These were:

To provide an overview of the methodologies used by each of the rating, ranking and index organisations - identifying the environmental content, its source, and its main users and audiences. A key element is the actual and potential use of Environment Agency data.

- To compare and contrast the results of these research rating methods and indices for a defined list of companies.
- To identify any opportunities to complement the Environment Agency's own datasets to assist in its own modern regulatory strategy.
- To make recommendations on which indices, rating and ranking methodologies might assist the Environment Agency in the management of its own pension fund.

## 1.2 Report structure

This report is structured as follows:

- Methodology (Section 2) this section presents the methodology applied to this research project. It identifies some of the decisions made that affected the direction of the research and therefore some of the outcomes.
- Overview of the industry (Section 3) this section contains our interpretation of the environmental rating and ranking sector, as well as a discussion of how the sector is perceived and represented in recent literature. It also provides some overarching facts about services and products as identified during this research project.
- More detailed findings of this research are presented in the sections titled **Desk-based review of** organisations (Section 4) and In-depth review of organisations (Section 5).
- Examples of Environment Agency initiatives and assessment tools are discussed in the context of this project within the Environment Agency Modern Regulation Strategy (Section 6);
- Results of the company performance review (Section 7) contains analysis and comparison of the assessment of company performance by the selected organisations discussed in section 5 of this report.
- Overall thoughts and themes from the study are then discussed in the **Summary and discussion** (Section 8) and Conclusions (Section 9). These include some ideas for recommendations to the Environment Agency.

# 2. Methodology

## How was the research structured?

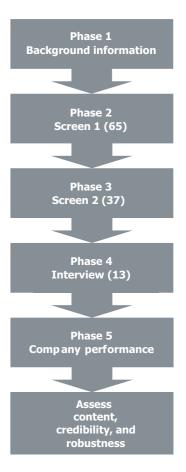
This section describes our approach to the review and outlines the key phases. The flow chart (see right) shows the progression of this research through six key steps. At the start of every chapter, the highlighted phase on the diagram indicates the subject of the chapter. The key steps outlined in the following sections were:

- a review of literature and recent articles to establish how the corporate environmental research sector is currently perceived and what are its reported strengths and weaknesses;
- high-level screening to identify organisations and products within this field;
- a more focused review/screening of a number of organisations, based on publicly available information;
- a detailed review of a small sample of organisations, focusing on methodology and data management issues;
- a company performance review.

We included various different types of organisations in the review and sorted them into four key categories: indices; ratings/ranking; investment funds; and other (definitions are provided in the glossary).

# 2.2 Background information and initial list of organisations

In order to build a clear picture of the industry and its current challenges, we identified other recent studies and relevant reports in the general field. The aim of this review was not to conduct a scientific literature review but to gain a flavour of the challenges and criticisms being levelled at the environmental rating and ranking organisations. We also wanted to identify recently launched organisations and products. The themes identified in this review gave us some key parameters for selecting the organisations to include in this report. We provide an overview of these themes in Section 3. From the review, we developed the initial list of organisations (and products). These totalled 65 (see Table 2.1 below). Readers should note that, during the course of the research, some of the organisations/products in question have changed name and/or merged with others. Also, new organisations and products have emerged. These changes



demonstrate the relatively fluid nature of this market. We have endeavoured to reflect the changes that occurred during the project period by making changes to our lists. However, further name changes and mergers may occur.

For this initial step in our research, we developed a database with the names of the identified organisations/products and key details such as their web location and launch date. It also detailed:

- the type of organisation/product
- its geographical coverage
- the environmental content of the assessment processes.

This information formed **Screen 1**. It is summarised in Section 3.2 and presented in full in *Appendix A*.

## Table 2.1 Initial list of organisations (Screen 1)

ACCA - Association of Charted Certified Accountants

Avanzi

Bank Sarasin & Co. Ltd Business in the Community CarBen (WS Atkins) Carbon Disclosure Project

Centre for Economics and Business Research Ltd (CEBR)

Centre Info

CoreRatings (formerly GRM and now part of DNV)

Covalence

CSE - Centre for Science and Environment

CSR Japan Research Institute

Deminor Ratings (see also Fortis Investment) DJSI - Dow Jones Sustainability Indexes

Domini Social Index **Dresner Funds** 

DSR – Dutch Sustainability Research Eiris - Ethical Investment Research Service

**Environment Agency Awards** 

Environment Agency – Operator Monitoring Assessment (OMA) Environment Agency – Operator and Pollution Risk Appraisal

(OPRA)

Environment Agency - Pollution Inventory (PI)

Environment Agency, Spotlight Ethibel - Stock at Stake

Etikanalytikerna

Fortis Investments (see also Deminor Ratings)

FTSE Group - FTSE4GOOD Index

Fundacion Ecologica **GES Investment Services** 

GMI - Governance Metrics International

(The) Good Bankers Co., Ltd

Good Corporation

Henderson Global Investors

Impax Environmental Technology (ET50) Index IMUG - Institut fur Markt-Umwelt Gesellschaft

Innovest Strategic Value Advisors Invesco Perpetual - fund managers

IRRC – The Investor Responsibility Research Centre

ISIS – Asset Management

Jupiter

Kempen/SNS Smaller Europe SRI Index

KLD Research and Analytics, Inc.

MJRA - Michael Jantzi Research Associates Inc. Morley Fund Management - Sustainable Futures Funds

Morning Star Japan KK (The) Natural Step oekom research AG

PERFORM – Sustainability Performance Benchmarking

PIRC - Pension Investment Research Consultants

**REMAS** 

Salter Baxter / Ecocontext

SAM - Sustainable Asset Management

Scoris

SERM Rating Agency (formerly Safety and Environmental Risk

Management)

SIRIS - Sustainable Investment Research Institute

SiRi - Sustainable Investment Research SIRS - Social Investment Research Service

Standard and Poors Triodos Advisory Services

Trucost

Verite

Vigeo (formerly Arese)

Wind Fund (Friends of the Earth)

WWF - World Wide Fund for Nature Ethical Investment

<sup>\*</sup> Although it is recognised that Ethibel and Stock at Stake are separate entities, they are linked in this report for the analysis of the total cycle from research through to rating. Ethibel is a not-for-profit quality label organisation, which bases its evaluations on information provided by Stock at Stake, a research company.

## 2.3 Screening of organisations

In order to develop a smaller list of organisations/products and enable more detailed research to be performed, we reviewed the 65 organisations/products in Screen 1. The criteria used filtered out those that, on the basis of the information identified in Screen 1, did not appear to have relatively strong environmental components. We also needed to reflect the Environment Agency's required geographic focus. This was to focus mainly on the UK but with some international coverage which included North America and Japan/Asia. Also, the sample focused on traditional research raters and rankers rather than other organisations e.g. awards, and those with a very specialist focus on one issue such as the Carbon Disclosure Project. The Environment Agency initiatives are reviewed separately in Section 6.

This process identified 37 organisations on which we carried out more detailed research in the form of a desk-based review. At this stage we started to draw out overarching themes and facts about the industry. This smaller set of organisations has been termed **Screen 2**. These are listed in Table 2.2 below.

## Table 2.2 List of organisations for more detailed research (Screen 2)

Business in the Community Carbon Disclosure Project

Centre Info CoreRatings

DJSI - Dow Jones Sustainability Indexes

Domini Social Index

Dresner Funds Eiris - Ethical Investment Research Service

Ethibel - Stock at Stake

Ethiscan

FTSE Goup – FTSE4Good Index

GMI - Governance Metrics International

Good Bankers

**Good Corporation** 

Henderson Global Investors

Impax Environmental Technology (ET50) Index

Innovest Strategic Value Advisors

IRRC - The Investor Responsibility Research Centre

ISIS - Asset Management

**Jupiter** 

KLD Research and Analytics, Inc.

MJRA - Michael Jantzi Research Associates Inc.

Morley Fund Management - Sustainable Futures Funds The Natural Step

oekom research AG

PERFORM Sustainability Performance Benchmarking

PIRC - Pension Investment Research Consultants SAM – Sustainable Asset Management

Scoris

SERM Rating Agency

SiRi – Sustainable Investment Research International Group

SIRS - Social Investment Research Service

Triodos

Trucost

Vigeo (formerly Arese)

During this second phase of research, we focused on determining these organisations as key products/services and their cost, the information sources used, and the financial indices covered. We also looked at methodological approaches: whether surveys or questionnaires were used; whether researchers engaged with company stakeholders; whether an organisation applied exclusionary policies or particular sector classifications; and whether it used quantitative or qualitative metrics or statistical tools in its analysis. This was done to obtain a more detailed, comparative picture of the sector. We wanted to show the many facets of the different organisations as well as their varied philosophies and approaches to the rating and ranking of companies.

Inevitably, this phase of the screening process produced a large volume of information, which had to be carefully managed and streamlined. We identified a series of information requirements to gather the

required facts for each organisation in a consistent way (see Table 2.3 below). During these initial webbased phases of the project some of the information we were seeking was not clearly presented on the websites of the organisations being reviewed. The lack of such information may have affected our selection as we could not identify some of the aspects of an organisation that we considered important in the context of this research.

## Table 2.3 Information searched for during Screen 2

Name of organisation Website reference Geographic coverage

Type of organisation (eg rating)

Launch date Generation

Ownership details

Description of service and products

Input/source information Use of Environment Agency data Industry sectors (and exclusion)

Exchanges

Assessment methodology Form of assessment

Metrics

Internal quality assurance

Outputs Content

Independent verification

Cost

Access/administration

Strategic relationships Target users/audience

Market share Proposed changes

## 2.4 Interviews

At the interview stage, the initial aim was to select a few organisations for detailed research by a defined set of criteria – as we had selected organisations from Screen 1 to Screen 2. However, it became clear during the desk-based research that we did not have consistent data across the screen. This was because of the diversity of organisations, the varied terminology used and the transparency, accessibility and variety of information presented on websites. For the in-depth stage of research, it was therefore not possible to develop a standardised set of selection criteria that properly reflected the Environment Agency's objectives. The Screen 3 (interview sample) was, as a result, selected loosely according to the perceived strength of the environmental component, organisation category (eg index) and geographic coverage. The list of organisations is shown in the box below. We aimed to select a broadly representative group of organisations, methodologies and financial markets (see Section 4).

We then conducted interviews: to fill information gaps; to obtain more consistent and detailed data than that immediately available from the web; and to clarify questions arising from the desk-based research. We focused on supplementing the information we had gathered so far on:

- information sources and the nature of information and data used;
- the structure and nature of the assessment methodology;
- the involvement of the company being ranked in the assessment process;
- the systems established to provide quality control on the process and outputs;

how industrial sector influences the outcome or methodology of the assessment.

This research was designed as a technical project. It focused on what was currently available and on the market in this area. It was therefore decided not to include the views of various types of existing or potential users. However, it is recognised that understanding these views and the related market forces would be an interesting piece of complementary research.

In order to align the interview process and to ensure that a consistent level of information was obtained, we interviewed senior management within each organisation. Where possible, we interviewed Directors of Research.

## Table 2.4 List of organisations for interview (Screen 3)

Research

**EIRIS** PERFORM

Ratings

CoreRatings

Ethibel

Innovest Strategic Value Advisors

oekom research AG

**SERM Rating Agency** 

Trucost

SAM (DJSI Indices specifically) - hereafter referred to as SAM (DJSI)

FTSE Group (FTSE4GOOD Index specifically) – hereafter referred to as FTSE4Good Index

**Investment Funds** 

Henderson Global Investors (SRI team)

Morley Fund Management

http://www.eiris.org

http://www.sustainability-performance.org/index.php

http://www.bitc.org.uk/

http://www.coreratings.com http://www.ethibel.org/

http://www.innovestgroup.com/

http://www.oekom-research.com/

http://www.serm.co.uk/

http://www.trucost.co.uk/

http://www.sustainability-index.com/

http://www.henderson.com/ http://www.morleyfm.co.uk/

We designed and used a pro-forma as a quality-control mechanism to guide the interview process. This provided us with a basic framework from which we could develop factual profiles for each interviewed organisation. We fleshed these out with the detailed responses to questions from our interview notes. Annex B sets out the profiles, giving key information for each of the organisations interviewed. Organisations were invited to feed back on the factual accuracy and asked to identify two or three key differentiators – or what they felt to be the unique elements of their approach or ethos. These unique elements can be found in the last section of each profile in Annex B. We also sought feedback from these 13 organisations on the accuracy of the factual information presented in this report. This included discussing and gaining evidence for any changes requested.

## 2.5 Company environmental performance review

Finally we asked the organisations interviewed to provide information/scores on the performance of specific companies. We used this information to compare and analyse companies' performance across the different rating methodologies of the organisations we had interviewed. We provided the selected organisations provided with five randomly selected companies from four FTSE sector classifications. Out of the total 20 companies, organisations were requested to specify which were included in their index or rating/ranking. On receipt of the scores we applied various mechanisms to normalise the scores in terms of a percentage. This allowed us make an effective comparison.

# Overview of the industry

#### Introduction 3.1

As discussed in the introduction to this report, the last decade has seen a dramatic growth in the number and variety of environmental (and sustainability) rating and ranking organisations. But what does this emerging industry look like? This section provides:

- an outline of the corporate environmental research sector;
- an overview of some of the key challenges and issues facing the industry;
- some key facts about the sector identified during this research project.

# 3.2 What is corporate environmental research?

Corporate Environmental Research (CER) organisations have proliferated in response to growing demand for research and information into companies' non-financial performance. This demand stems from increasing public and investor concern with the environmental, social and ethical impacts of business. It marks a gradual shift in society's values: in the past successful businesses were measured purely on their financial performance - their profit or 'bottom line'. However, broader factors are now seen to affect a company's long-term value and success. The issues involved are diverse. They could be a company's record in:

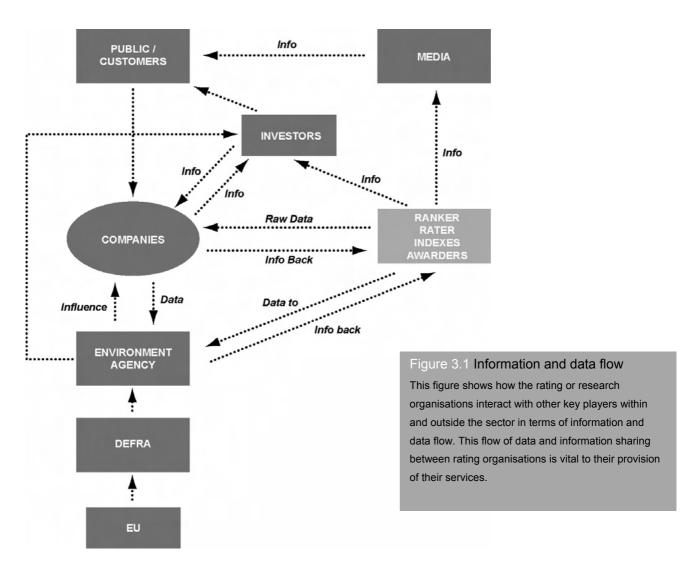
- polluting the atmosphere or natural environment;
- harming animals;
- displacing indigenous peoples;
- contributing to conflicts through involvement in weapons trading;
- promoting social and moral decay through gambling;
- selling products known to be harmful to health such as tobacco;
- the use of exploitative labour policies.

Adding such social and environmental dimensions to our measurements of business performance has given birth to the term 'triple bottom line'. The widespread adoption of this phrase is evidence that companies, and the shareholders who drive them, are becoming more aware of their responsibilities. These are to protect and safeguard the communities and natural environments in which they operate and

prosper. Significantly, they now acknowledge the potential, material risks to their business if they do not fulfil those responsibilities. The corporate environmental research sector has emerged to provide the tools and means to quantify and compare this non-financial performance across industries and sectors. The sector serves both companies which wish to track their own performance against that of their peers, and investors who hope to profit from that performance.

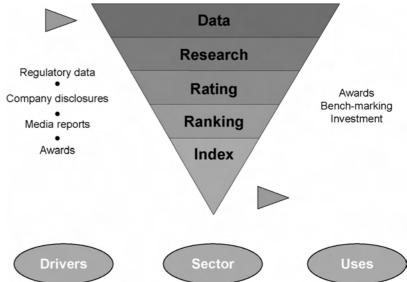
Some CER organisations have emerged to fill this information deficit through research. They deliver a bench-marking service to companies wishing to measure their green, social or ethical performance. They also provide the public with clearer information on private-sector activities. Other CER organisations have filled a more commercial gap in the market. They use this kind of research to serve the needs and interests of private and institutional investors. It is important to differentiate between these two distinct groups. The differing needs of their customers, and the ways in which they use their findings, influence both the information and the methodology used in an assessment. Within this report we have reviewed and considered many different kinds of organisations, including: pure research houses; organisations involved in rating and ranking which do their own research or buy it in; and analyst teams within investment companies that only provide internal support and management of Socially Responsible Investing (SRI) funds. Investors have different needs and interests. Some companies are interested in identifying whether a company is good or bad. Others wish to seek to understand impacts on value in an ethically neutral manner.

There is an element of information sharing and data flow within and between different types of organisation in this sector. For example, those providing advice to investors may often use or build on the outputs and products of the research houses to inform their own company assessments. An example of this is FTSE4Good which uses EIRIS research and data for its index. Figures 3.1 and 3.2 below provide slightly different graphical representations of this sector. They aim to demonstrate the relationships between the different types of organisation and research bodies within the sector. They describe the direction of information and data flow between them, as well as identifying some of the drivers and uses for this research.



## Figure 3.2 Sector drivers and outputs

This figure shows some of the information drivers for this sector. It demonstrates the flow of information, from data research through to benchmarking indices and performance awards - some examples of sector outputs or uses.



# 3.3 Corporate research and ratings challenges

The media has recently given considerable coverage to corporate environmental research, and the uses of this research for responsible investment. Based on a review of the key papers and articles, several common themes emerge. These elements form the basis of the discussion below.

In recent years corporate environmental research has become more mainstream and the use of this information for responsible investment has increased greatly. This growth can be attributed to the increased environmental and social awareness of the public. This is borne out

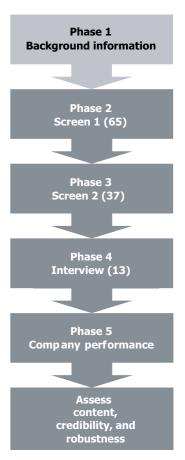
by numerous surveys. For example, a survey by the Guardian newspaper in 2004 identified that two-thirds of people interviewed intended to be more environmentally and socially responsible that year.

As many as 95% of those surveyed stated that they would be uncomfortable supporting certain activities with their investments. For many of these potential investors who are considering responsible investment, a company's attitudes towards environmental, social and ethical issues may be considered to be directly related to its investment value.

This increase in attention by the investment industry has been supported by the proliferation of ratings and rankings indices. These have been produced by various organisations and are based on combinations of environmental and social factors. The wide range of organisations currently in the market shows the diversity in philosophies and approaches. Some organisations collate information from public sources; others engage in dialogue with companies and their stakeholders. Some use simple scoring systems; others rely on complex models and tools.

We identified two main issues which dominated media and literature coverage both of corporate environmental research and of the subsequent use of information for responsible investment:

- whether responsible investment adds value for the investor concerned;
- the benefits and drawbacks associated with using environmental research rankings and ratings of companies.



## Does responsible investment add value?

The Environment Agency has recently commissioned research in this area. It undertook a literature review of studies in the last five years and carried out 15 new case studies. This research concluded that, in 85% of the studies, good environmental governance did benefit financial performance and poor performance could have damaging financial consequences. The work from the individual new case studies supported the positive findings from the literature review.<sup>3</sup>

#### Call for standardisation

Business literature and the media now often criticise the rating and ranking of companies for environment, social and corporate responsibility. The methodologies and criteria employed by various rating agencies are considered to be inconsistent and often to lead to contradictory results. A recent report, published by the Nordic Partnership (2004), found that the lack of standardised screening methods for the evaluation of company performance made it too difficult to compare responsible investment products and instruments. This made such ethical methods, products and instruments less viable and attractive.

There are calls for ratings agencies to standardise the methodologies they use in order to create confidence in their reliability and to establish standard practice across the various bodies (Ethical Performance, 2004). It is outside the scope of this research to perform a detailed comparison with financial research assessment processes and financial rating methodologies. However, the issues of accounting and transparency have already been identified and addressed for financial ratings by the financial sector. Recently we have seen the launch of the voluntary Corporate Sustainability and Responsibility Research Quality Standard (CSRR-QS 1.0). This aims to provide some measure of quality assurance for organisations within the sector (as detailed in the box below).

Evidence of inconsistencies, both reported and perceived, is extensive. However, there are also suggestions that not all parties favour complete standardisation across research and rating agencies. Differentiation, independence and competition are valued by many of the organisations themselves and by certain users (Baue, 2003).

<sup>&</sup>lt;sup>3</sup> "Corporate Environmental Governance, Environment Agency", October 2004.

## Table 3.1 Corporate Sustainability and Responsibility Research Quality Standard (CSRR-QS 1.0)

The voluntary Corporate Sustainability and Responsibility Research Quality Standard (CSRR-QS 1.0) has recently been launched. It is the first quality standard worked out at a sector level in the field of Corporate Social Responsibility (CSR) and corporate environmental research and analysis. The standard aims to improve quality management systems, stimulate transparency, facilitate assurance processes and form the basis for further verification procedures. The standard sets out the following ten criteria for the assessment of companies:

- sources must be independent, not just information supplied by companies;
- global activities of companies must be taken into account;
- best available techniques (BAT) should be used rather than minimum legal requirements;
- environmental and social aspects must be taken into account;
- a suitable balance must be found between environmental and social, quantitative and qualitative data sources
- content must be relevant;
- information must be comparable to others;
- stakeholders should be involved in the process as much as possible;
- information must be up to date;
- there should be transparency about methods.

(Information is available from www.csrr-qs.org)

The CSRR-QS 1.0 was initiated, supported and funded by the European Commission, Employment and Social Affairs. Partners and signatories of the quality standard represent many parties with vested interests in the sector, including Avanzi, SERM, Ethibel and oekom research. The involvement of these companies reflects their recognition of the need to improve quality and credibility. It is difficult to make informed judgements regarding the success of this quality standard before we can review the results of the pilot. A recent spin-off of the CSRR-QS 1.0 is the launch of a new trade association, the Association for Independent Corporate Sustainability and Responsibility Research (Al CSRR). One of the main objectives of this association is to develop, promote and maintain professional standards, expertise and codes of conduct for the CSRR sector.

The Environment Agency, however, believes that there are considerable benefits from having more consistent and comparable information across the rating and rankings sector.

There are also inconsistencies between and within ranking agencies in different countries and in different sectors. Different countries have different standards. There are significant disparities between the UK and the US, which causes problems in constructing an index that incorporates more than one market, (Targett, 2003). Cross-sector comparisons are also made problematic by the differences in the weightings used of the different components of sustainability (environmental, health and safety, social etc).

There is also concern about screening, which is used in several assessment methodologies. There is a belief that, if environmental and broader sustainability factors are to be used in mainstream investment, we should not screen companies in or out of portfolios on the basis of their business activity. Rather, assessments should take into account the extent to which corporate strategies and risk management approaches include social and environmental factors. However, where screening has been included in methodologies, this approach reflects demand from customers and investors. There is also much evidence and discussion about the methods used to gather and collect information. The focus of this debate is on

questionnaire fatigue. A project recently started by the London Stock Exchange (LSE) is hoping to address this concern. Working with a number of CER organisations, the LSE aims to rationalise information needs into a single electronic corporate responsibility exchange (CRE) (http://www.londonstockexchange.com/engb/products/irs/cre/). This should reduce questionnaire fatigue and the burden on companies. It will provide a generalised data depository from which rating organisations can draw their information.

## Walking the talk

Previous reviews of corporate environmental research rankings have been much discussed in business literature. Examples include SustainAbility Mistra (2003) and Triple P Performance Centre (2002). The SustainAbility Mistra report aimed to identify best practice within the research processes of corporate environmental research organisations. It concluded that, "SRI research organisations will have to review fundamentally, many aspects of their research processes if they are to retain and build their central role in socially responsible investment markets."

The Mistra report has had a mixed reception from the corporate environmental research community. It was seen to provide valuable insight into CER organisations and methodologies, but to lack the necessary transparency. Baue (2004a) comments, for example, that the report called on corporate environmental research organisations to disclose potential conflicts of interest when providing services to companies they assess and rate in order to 'ensure independence' and 'maximise transparency'. However, this report still makes an important contribution, since few comprehensive studies of a similar nature have been undertaken.

One of these was the Screening and Rating Sustainability report, produced by the Triple P Performance Centre of the Vrjie Universiteit Amsterdam. This profiled and compared 28 corporate environmental research rating agencies. This report criticised the rankings for a lack of independence and highlighted the need for greater standardisation and transparency (Baue, 2002). This is becoming a regularly repeated conclusion.

## Conclusions

Based on this brief summary of information published about CER organisations, we consider the following to be key themes:

- A positive correlation can be identified in many cases between sound environmental governance and financial performance. This has recently been demonstrated in research performed on behalf of the Environment Agency. This states that "Better financial returns can be obtained from investing in companies which integrate environmental considerations into corporate governance policies and policies." (Environment Agency, October 2004.)
- In recent years there has been much more interest in corporate environmental research and the use of ratings and rankings information for responsible investment. This interest continues to grow.

- Indices, ratings and rankings of companies that are based on relative environmental, social and ethical performance have been unfairly criticised for inconsistency and incomparable results. Such inconsistencies arise as the organisations target their products at different users and therefore have different philosophies, methodologies and data inputs. These inconsistencies have resulted in lack of confidence in some of the outputs. Reviews of indices have also been criticised for not following the advice they give to research and ratings agencies (eg in terms of transparency).
- A voluntary quality standard (CRSRR-QS 1.0) is in place. Two of its aims are to improve quality management systems and to stimulate transparency.
- LSE has developed the CRE to rationalise the information requests received by companies and so reduce questionnaire fatigue.

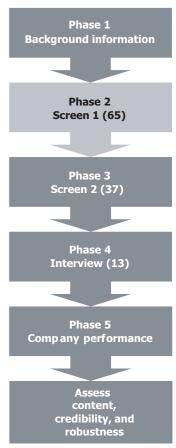
Studies relating to the corporate environmental research sector and responsible investment are published all the time. Certain recent publications may have been omitted from this research in order to establish a cut-off date for the report.

3.4 Some facts on the corporate environmental research

sector

The scope of information gathered on the 65 organisations in Screen 1 is limited. However, it does demonstrate the breadth of this sector. Based on information available on their websites, 62% of the organisations appeared to have significant environmental element/content. This was important for the selection of organisations for Screen 2. The Environment Agency had specified that the focus of the review should be to consider tools and techniques with a strong environmental content. This reflects its interest and role as a regulator.

The types and the geographical coverage of organisations are presented in Figures 3.3 and 3.4 below. The rating/ranking category is the largest category by some margin – with the exception of Other (Figure 3.3). Examples of some of the organisations/products that have been included in the Other category are shown below.



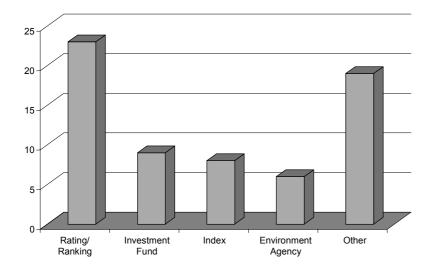


Figure 3.3 Number of organisations by category

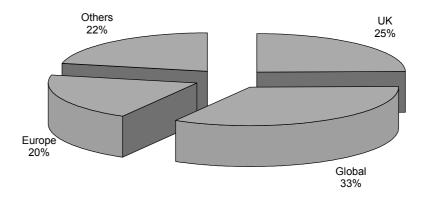
### Examples of organisations or products included in 'Other'

Reporting awards or bench-marks (eg ACCA Environmental and Social Reporting awards) - These are included because such awards are probably used by investors when making decisions. It is important, however, to recognise what an award signifies: that a company has published a report which is considered strong against emerging best practice for disclosure. It is not an actual or implied comment on that company's environmental performance.

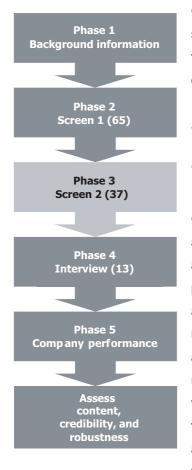
Research organisations (eg Perform) - Some providers of corporate environmental research gather information and data on various aspects of environmental impact, risk, management and performance but do not necessarily provide or publish assessments based on their research. Many of these organisations are the research partner for ratings/rankings or indices.

Figure 3.4 shows the geographical coverage of organisations in Screen 1. Figure 3.4 shows that Screen 1 included a fairly equal representation of organisations from UK, Europe, Global and Other. This was considered important.

Figure 3.4: Geographical coverage of organisations



# 4. Desk-based review of organisations



Our more detailed, desk-based review covered 37 organisations These were selected (see section 2.4) to provide broad coverage of the industry with a focus on environmental content. The greater depth of research in this phase enabled us to:

- identify key issues for subsequent interviews;
- start to identify the key themes for a comparative review of the range of philosophies and assessment processes.

One overarching finding from this stage was the great variability in the type and depth of information disclosed by organisations on their methodology, assessment approach and outputs. A few organisations do place a high premium on the transparency of their assessment approach and see this as a key differentiator of their services. For these organisations it was easier to understand relatively quickly and clearly what their outputs can tell us about a company's performance. Others have more complex, less user-friendly methodologies, or are less transparent in describing their approach. For these organisations it is more difficult for a lay user to understand how their findings relate to others in the sector. This is in line with previous studies and research. It is what might be expected from a relatively new, specialist and rapidly evolving industry.

Figure 4.1 shows the emergence of organisations according to their respective launch dates. These are based on the web research for Screen 2.

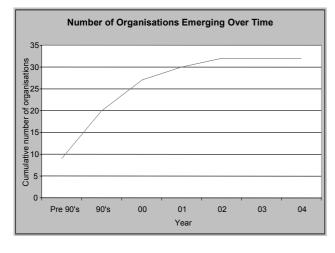


Figure 4.1: Sector growth by organisation launch

This graph shows the relatively rapid proliferation of organisations in the late 1990s and the early 2000s. The growth seems to tail off over the last two years, with fewer new organisations emerging. Our research points reveals that now the growth is in the number of different products and services which these organisations are offering.

Some of the key themes from this stage of review are discussed below:

## Sector coverage

The background information review showed that previous research documents have raised questions in about whether this industry should screen or exclude certain industry sectors and/or business activities. It is important to recognise, however, that typically this is done for organisations or products targeted at the investment community – which demands such exclusions. Out of the 37 organisations in Screen 2, only 22 websites made it clear whether they excluded certain industrial sectors. Of these 22, 17 organisations applied certain exclusion policies. Some actively screen out certain industry sectors completely; others provide their users with enough information to make their own decisions about screening, and will allow the exclusion of certain sectors to be guided by the client's specific investment needs. The remaining five organisations indicated that they include all industry sectors in their assessments.

Common industry sectors that are excluded are:

- tobacco manufacturers
- nuclear power
- · weapons manufacturers
- gambling/games of chance
- vivisection
- extractors of fossil fuels
- military contracting.

Among other industries less frequently excluded are those that produce fertilisers in large quantities and fur producers. If it was clearer to see whether or not an organisation used screening, users and interested parties would find it easier to understand some of the variations in outputs.

#### **Products and services**

The level and type of information presented on websites are extremely varied. It has not therefore been easy to make comparisons as clear as we had originally hoped. However, we have identified some patterns:

- Approximately one quarter (27%) of the organisations do not charge for their product or service. It
  would appear from this that these organisations are not making money and/or are competing for
  business for loss-leader reasons. Disparity in costs can confuse users. It also provides economic
  challenges for the sector.
- Approximately one third (35%) of the organisations provide information in the form of publicly available sector reports, company rankings and indexes published on an annual basis.
- Less than half (40%) service their clients through subscription services linked to certain products or packages.
- Approximately half (49%) provide outputs through web interfaces. These should aid access and usability. A good example is the provision of company reports as well a daily news monitoring service through a live secure website available to subscribing clients.
- Around two thirds (67%) include some element of company and/or sector bench-marking process.

## Table 4.1 What are the key products?

### Common key products:

- profiles of leading companies
- bench-marking
- compiling indices
- management of SRI funds
- client advice and consulting.

## Other key products:

- research
- issue analysis
- sectoral reports
- portfolio management
- policy advice.

## Methodology – information collection

We observed different approaches to information gathering. These ranged from initial desk-based research, followed by engagement with the company to fill in gaps, to full reliance on the company at the outset to complete a comprehensive questionnaire. Questionnaire fatigue is a common complaint from companies. However, for many organisations this approach is seen as one of the most effective in ensuring that the assessment reflects actual performance/activities. Some companies are known to have voiced concerns about the inaccuracy of initial profiles/assessments. This tends to be more significant when the rating organisation had based these on the findings of desktop research and then asked companies for comment.

## Company participation

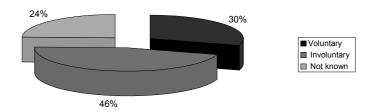
An important point is that companies do not always choose to participate in a number of these research processes. If a company decides not to provide feedback or not to complete a questionnaire, this does not necessarily exclude it from being rated. This may result in a rating that is not fully representative. It has

relied upon publicly available information and key pieces of data could be missing. Or it could contain a consistent error. For an organisation to meet the needs of its customers and clients, it needs to perform ratings whether or not a company provides feedback. A balance is needed between independence and impartiality (by using publicly available information) and accuracy and reliability (from gathering information directly from the company). It is a challenge to achieve this balance without imposing an excessive burden on industry to provide information. The recently launched LSE CRE was developed with the aim of addressing this issue. It will be interesting to monitor its progress.

Where companies participate in a best-in-sector assessment, users must therefore consider two important issues concerning accuracy and completeness:

- Is the assessment complete? Are all the relevant top performing companies included in an
  assessment, in order to achieve a complete best-in-sector rating? A voluntary process may not include
  all companies.
- Is the assessment accurate? An involuntary process may mean some companies have not provided the information themselves: the rating is likely to be based on publicly available information. There is a risk that this information may not be up to date, depending on the review cycle of the CER organisation. An example is the publication of a company's annual reports and accounts. Positively, this benefits those companies who provide comprehensive and updated information in the public domain, for example on a corporate website. The development of the Accounting Standards Board guidelines for environmental disclosure for the Operating and Financial Review may well help the scope and consistency of company disclosure.

**Figure 4.2**: Voluntary vs. involuntary participation



These questions are particularly relevant in our research. As Figure 4.2 shows, of the 37 organisations reviewed at this stage, it was not possible in nine cases to identify their policy towards voluntary or involuntary inclusion. Of the others, two out of three could be considered to use involuntary inclusion.

Users should be aware that the information in the company assessments made by ratings organisations may often not be provided by the companies themselves, but be gathered from publicly available sources.

## **Quality assurance**

Overall at this stage we found very little information on organisations' websites about either internal or external quality assurance processes. It was therefore difficult to make an informed comparison.

### **External verification**

In a large number of organisations it was not easy to identify the level of external verification of processes (see above). However, 20% of the organisations referred to third-party assessment or verification of methodologies and outputs.

### Content

All organisations reviewed during Screen 2 indicated that they consider environmental issues, typically alongside other issues such as sustainability, social and ethical. However, there is no clear information as to the relative proportion of environmental issues considered in the assessment. Comparative assessment of issues considered across the sustainability, social, ethical and environmental agendas is also complex: there is considerable overlap in definitions of these terms. In our review of the website information, we perceived that these terms were used and interpreted fairly loosely and inconsistently across different organisations.

It was also apparent that organisations consider different elements of environmental assessment in their methodologies. These included environmental governance, environmental management, environmental performance/impact, environmental risk, life-cycle environmental assessment (products and suppliers) and environmental and business strategy. Based on the information available, it is clear that some organisations focus on one or two of these areas, whereas others cover more.

# In-depth review of organisations

## 5.1 Introduction

The following section looks at the information gathered during in-depth reviews of a sample of 13 organisations. As noted in the methodology these organisations were selected to provide:

- a spectrum of indices, ratings and rankings and investment funds;
- a focus on worldwide and European market coverage;
- a focus on those organisations and products with a strong environmental element:
- a review of the use and consideration of quantitative performance data – which the Environment Agency considers to be potentially important in to meeting their objectives.

So far in this review, we have identified organisations by their main service or product, eg index, rating etc. This is a simplification, as some organisations cover more than one of these areas. Similarly, it is possible to see the different types of organisation – research, rating,

Phase 1
Background information

Phase 2
Screen 1 (65)

Phase 3
Screen 2 (37)

Phase 4
Interview (13)

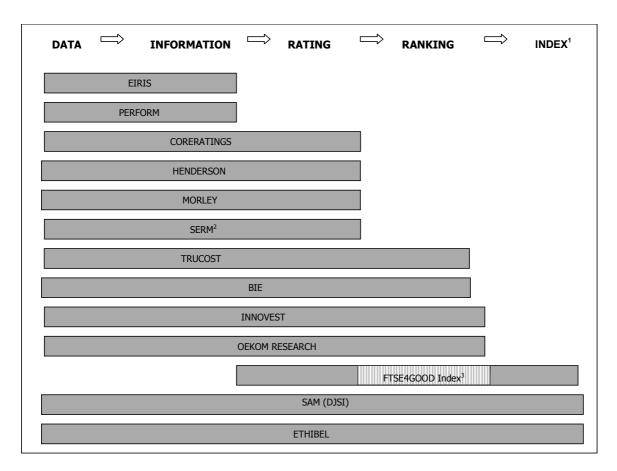
Phase 5
Company performance

Assess
content,
credibility, and
robustness

ranking, index – as steps in a sequence of an overall environmental business performance/risk assessment process. Each feeds into the others through flow of information and data. Figure 5.1 identifies the elements of the process as undertaken by each of the 13 organisations.

Throughout this section, the information presented is the opinion of the authors, based on interviews and discussions with representatives of the organisations and information provided. We have endeavoured to provide facts that are consistent across all the organisations reviewed. However, a lack of disclosure about certain items has sometimes presented difficulties. Where this was critical for our comparison we have identified information as not being disclosed.

Figure 5.1: Activities conducted by the interviewed organisations



## Notes:

- For the context of our representation, the term index relates to a published index. It does not include the influence an organisation may have on portfolio construction.
- 2. SERM's main product is rating, although on request it can, and has, provided some ranking products for clients.
- 3. The FTSE4GOOD bar in Figure 5.1 provides a representation of the flow of information/assessment only. It should not be taken literally. FTSE4GOOD use information provided by EIRIS to assess the organisations.

This representation is ours and is by no means definitive. It is constructed for the purposes of organising and comparing information for this review. The difficulties in accurately classifying and mapping the links between these organisations reflect a wider challenge: achieving consistency and repeatability across an industry which deals in indicators that are difficult to quantify and define.

## 5.2 Philosophy and background

Looking at a company's philosophy and how it differentiates itself in the marketplace can give an insight into what drives its business. For instance:

- What was the identified gap in the market at the time the organisation was launched?
- What factor makes an organisation unique? What can it provide above and beyond others?
- · How has its philosophy influenced its methodologies?

This comparative information can help investors and users of the products to identify an ideal provider for the service they require. We found that the philosophy of an organisation has often shaped its approach to company assessment. The following factors contributed to shaping the different philosophies of the organisations we interviewed:

- environmental content
- · industry sector coverage
- sector classifications
- · exclusion policies
- application of sector in the assessment process.

#### **Environmental content**

One of the initial objectives of the Environment Agency was to understand the relative environmental content of ratings, rankings and indices. This covers two elements:

- the proportion of environmental versus non-environmental information, as quantified by the organisations themselves;
- the type of environmental information, eg impact, systems, qualitative versus quantitative, financial, risk etc.

Table 5.1, below, looks at the core focus of each of the organisations considered. It is important to stress that it does not attempt to account comprehensively for all the issues and aspects covered within the organisations' methodologies. It highlights those that we consider to be central to their approach.

Table 5.1: Summary of organisations interviewed against environmental content aspects:

		Core focus of	Use	Consider actual incidents/	Environmental impact/performance		
Organisation	% Environmental content	Assessing appropriateness of management systems for environmental issues or risks	Assessment of the financial implications of environmental risk and performance	Environment Agency data	events and current 'good'/'bad' news*	with significant proportion of quantitative inputs	
Eiris	20-40	✓	X	✓	✓	✓	
PERFORM	40-60	X	X	✓	X	✓	
BiE	100	✓	X	X	X	X	
CoreRatings	20-40	✓	✓	✓	✓	X	
Ethibel	N/D	✓	X	?	✓	X	
Innovest	20-40 dependent on sector	<b>√</b>	<b>√</b>	<b>✓</b>	✓	X	
Oekom	40-60	✓	X	X	✓	✓	
research	Dependent on relative sector risk						
SERM	40-60	X	✓	✓	✓	X	
Trucost	100	X	✓	✓	X	✓	
Sam (DJSI)	20-40	✓	✓	X	✓	✓	
FTSE4Good	40-60	✓	X	✓	X	X	
Henderson SRI	N/A	✓	X	✓	✓	X	
Morley	N/A	✓	X	X	✓	X	

Key: ✓ = applies, x = doesn't apply, N/A = not applicable, N/K = not known, N/D = not disclosed

A tick in the column headed "Consider actual incidents/ events and current 'good/bad' news" indicates that an organisation's assessment might be influenced by an event indicating poor performance over and above the standard questions used in an assessment. Other organisations, such as BiE and FTSE4Good, might track and follow compliance issues/media stories but these would only affect an assessment if directly linked to a question or metric.

The range of environmental information used in the assessment will have an impact on the implications of the outputs. For instance, the use of actual performance information might enable the output to provide guidance on the relative environmental performance of an organisation. It is clear from our findings that most organisations mainly consider management of environmental issues within the assessment process. However, this does not indicate that the detailed elements of the approach taken by these organisations are all the same. It is also clear that a number would also like to consider relative environmental performance. However, few have been able to manage the general lack of consistent key performance indicators across companies' disclosure when there is a need for the assessment processes to be standard. A number of companies do consider environmental performance. They have addressed the issue of comparative indicators between companies by assessing company performance in terms of trends over a few years, rather than in comparison with other companies.

Trucost considers environmental impact and has based its methodology on assigning financial costs to natural resources used as well as to wastes and other outputs. In this regard, Trucost's methodology is distinct from most other organisations which focus on providing an opinion on the appropriateness and strength of management systems and in some case performance. In this regard, Trucost's approach is the most quantitative out of all those we considered.

### Environment Agency data

The Environment Agency is specifically interested in how its own datasets are used by CER organisations. This therefore comprised a specific element of our research. It was found that Eiris, SERM, Trucost, Henderson SRI <sup>4</sup>, FTSE4Good<sup>5</sup>, PERFORM, CoreRatings and Innovest use Environment Agency data as an information source. This is shown in Table 5.1 above. Eiris considers various types of Environment Agency data such as figures for waste, water pollution, air pollution, regulatory data and *Spotlight*. Henderson SRI and FTSE4Good source at least some of the data from Eiris. SERM uses Environment Agency data including Spotlight and the Pollution Inventory. Trucost uses data on waste, water use and abstraction, and the pollution inventory for fertilizers and pesticides. PERFORM uses the Pollution Inventory. Innovest and CoreRatings use *Spotlight* as one of their data sources. The other organisations are not known to use any Environment Agency data sources.

During discussions, however, it was clear that the UK-based organisations were aware of the range of datasets held and made publicly available by the Environment Agency. They recognised the potential benefits that the use of such information could have, especially when considering environmental performance. Based on the interviews, the use of the data seems to be limited by the manner in which it is referenced and by its coverage. CER organisations are typically assessing an overall business or company. This might have any number of sites and facilities, both in the UK and aboard. The Environment Agency data is held and referenced by site operating name, which is not always the same as the company entity to which it belongs. Also, the geographical and industrial coverage is limited to that required by the Environment Agency's regulatory work. If the Environment Agency were to link clearly the operating site name to the corporate entity, the CER sector could make more use of its data.

### Industry sector coverage

Industry sector coverage covers three elements:

- How do sectors affect the assessment methodology?
- Are sectors excluded from the assessment process?
- Which financial index sector classifications systems are used in the research process eg FTSE/MSCI World?

\_

<sup>&</sup>lt;sup>4</sup> Use Eiris for part of their research

<sup>&</sup>lt;sup>5</sup> Use Eiris for their research

**Table 5.2**: Summary of how these organisations reflect sectoral information:

		E. ducina		How indust	ry sector impacts	assessment me	ethodology
Organisation	Financial index	Exclusion policies (Yes /No/On request)	Number of companies	Sector affects scope or type of question	Higher requirements for high risk sectors <sup>1</sup>	Sector affects score weightings	Assessments rate in sector performance against peers
Eiris	FTSE	On request	2,700 <sup>3</sup>	✓	Х	N/A	N/A
PERFORM	N/A	No	105 companies and 217 production sites (so far).	<b>√</b>	X	N/A	N/A
BiE	FTSE350, DJSI (sector leaders) <sup>4</sup>	No	176	X <sup>5</sup>	X	X	X
CoreRatings	FTSE 100, Eurotop 300 and MSCI (key sector coverage)	On request	1,500	<b>✓</b>	<b>✓</b>	✓	X
Ethibel	N/A	Yes (for the Ethibel Label only)	600	Х	very basic spilt between industrial and service provider	X	Х
Innovest	MSCI, FTSE 350, FTSES&P, CAC40, Eurostoxx 500 (MSCI Europe), Nikkei	No	N/A	<b>✓</b>	N/A (sector specific rating)	•	<b>✓</b>
oekom research	MSCI	On request	800	✓	X	✓	X
SERM	FTSE350, Eurotop 300	No	600	✓	X	✓	X
Trucost	FTSE/MSCI	No	1,700	X	X	X	Х
SAM (DJSI)	DJSI	On request	770	<b>√</b>	X	<b>✓</b>	<b>✓</b>
FTSE4Good	FTSE	Yes	2,500	X	<b>✓</b>	N/A	N/A
Henderson SRI	N/A	On request	1,200 <sup>6</sup>	✓	✓	X	X
Morley	N/A	Yes	Database of 350 company profiles and 200+ screens. New ones added as required.	<b>√</b>	<b>~</b>	Х	X

Key:  $\checkmark$  = applies, x = doesn't apply, N/A = not applicable, N/K = not known, N/D = not disclosed Notes:

<sup>1.</sup> A tick in this column indicates that an organisation might collect the same data set for different sectors but requires higher performance from higher risk sectors ie the bar is raised for higher risk sectors – as a basic requirement of the assessment, a company in a high-risk sector is expected to demonstrate that it has more performance management elements in place than one in an industry sector with a lower risk or impact.

- 2. The standard outputs rate performance across the scope of the whole assessment within sector peer group. They therefore cannot be compared across sectors.
- 3. Of the 2,700 assessments, 1,100 are performed by EIRIS and the others by research partners following scope and methodology requested by EIRIS.
- 4. Organisations from these financial indices are provided the opportunity to participate along with BiTC.
- 5. Although BiE don't alter the scope of questions, participating organisations can self-select two out of the four environmental performance indicators for their response.
- 6. Henderson SRI has 1,200 companies included on their approval log. This represents the number on which they have made decisions. The level of assessment of these companies would vary as some would be excluded purely on the basis of their sector or business activity.

#### Sector classifications

A number of the organisations we considered use the MSCI World Index classifications as their reference point. Others rely on a range of FTSE Index classifications. The majority indicated that it was possible to link their outputs to one or the other of these systems, such as Dow Jones Index, S&P 500, Eurotop300, Nikkei, CAC40 and Eurostoxx 500.

### **Exclusion policies**

As identified in the results from Screen 2 (section 3.4), it is still common place in corporate environmental research to exclude or screen companies from investments – the so called sin stocks of companies active in industries such as nuclear power, tobacco or weapons.

Of the 13 organisations interviewed, three (23%) have strict exclusion policies applied to business activities perceived as controversial. These are FTSE4Good and Morley, which exclude companies involved specifically in tobacco, weapons, nuclear, GM, and fossil fuels. In addition, for the Ethibel Label, Ethibel excludes companies involved in arms, nuclear energy and animal testing. Another five organisations (38%) exclude companies according to client specifications. These include SAM (DJSI), Eiris, Henderson SRI, oekom research and CoreRatings. The remainder do not adhere to any strict exclusion policy.

The two investment funds only focus their assessment methodology and processes on those companies that they wish to consider for their ethical indices. Unlike many of the other organisations covered, they are not selling a rating or ranking product to third parties.

### Application of sector in the assessment process

We considered the ways in which sector classification can affect methodology or assessment processes across different organisations:

The differing scope of each assessment may reflect perceived risks or issues specific to each sector.
 For example, different information is used to focus the research for different sectors. This is true for PERFORM, Eiris, oekom research, CoreRatings, Innovest, SERM, SAM (DJSI), Henderson SRI and Morley. Although the BiE survey does not propose different questions for different sectors as such, it

requires a company to report on four key impact areas – two core impact areas and two self-selected impact areas.

More stringent assessment process or criteria are applied to those sectors which are defined by the organisation as being higher risk. This approach is taken by CoreRatings, Ethibel, Henderson SRI and Morley. The sector can affect the weighting applied to scores when individual element scores are aggregated (Innovest, oekom research, SAM (DJSI), SERM and CoreRatings). Outputs comprise sector specific assessments which only enable the overall rating to be reviewed within the sector. SAM (DJSI) and Innovest take this line.

The ways in which sector affects the assessment processes across the different organisations is shown in Table 5.2 above.

Business activities of the companies being rated can fall into more than one sector. Different organisations account for this in slightly different ways. However, approaches are usually associated with the relative financial turnover for each activity. CoreRatings, for example, gives an overall weighting based on the

turnover of various activities.

Various sector exclusions are in place. For example, a user may be looking for fixed, absolute exclusion of certain controversial business activities or industry sectors. If so, the investment funds managers and indices Morley and FTSE4Good will provide this. They exclude a set selection of industry sectors from their ratings. These include tobacco, armaments, animal testing, gambling, nuclear, military and alcohol. No sectors are excluded from the DJSI composite indices although SAM offers subset indices of the DJSI with exclusions

Table 5.3 What are the sources of data and information

Combinations of techniques for collecting data are used. These include:

- self-assessment questionnaires
- company reports (eg annual, environmental and corporate responsibility, including website);
- media sources
- web search engines and databases (eg FACTIVA, SOCRATES)
- academic journals
- industry association publications
- government and government agency publications and reports
- supranational agencies (eg UN, World Bank)
- stakeholder engagement (eg direct engagement with the company, community consultation, NGOs, Trade Unions)
- drivate research (in-house or research houses EIRIS, KLD etc).

based on the Investor Responsibility Research Centre (IRRC) guidelines. Alternatively, the user may be looking to make their own decisions about sectors to exclude from an assessment. CoreRatings, oekom research, Henderson SRI and Eiris will make exclusions as directed by client or investor specifications. These organisations provide the necessary information about all industry sectors, including those associated with controversial business activities, and then let the client make informed choices. BiE, PERFORM, Innovest, SERM and Trucost do not exclude any industry sectors from their research.

### 5.3 Inputs

We have identified the following key inputs into the assessment processes:

- data collection methods
- information sources
- metrics.

The robustness and credibility of the outputs depend on the quality and completeness of the data and information used in any company assessment. During the interview process we therefore focused on understanding the source and range of data and information used by the organisations.

#### **Data collection methods**

As discussed in Section 3, complaints about the organisations and CER in general revolve around the methods used to gather the information and the accuracy of information used:

- "There are too many questionnaires to fill in."
- "All the information this questionnaire asks for is on our website."
- "The information used in the collation of the draft profile is out of date and inaccurate."

For the organisations interviewed, four main approaches to data collection and company engagement were observed:

- Questionnaires are sent to companies to be completed. BiE takes this approach for companies that have not participated previously.
- Partially completed questionnaires, based on information held from previous years, are sent to companies for updating. This approach is used by SAM (DJSI), Eiris, FTSE4Good (through Eiris) and BiE(where companies have previously participated in the survey).
- Partial desk-based research is supplemented with information gathered during on-going dialogue with companies. This approach is used by Eiris, PERFORM, oekom research, SAM (DJSI), FTSE4GOOD (through Eiris) and Morley.
- Desk-based research is undertaken first to generate draft profiles for review by the company. This is then followed by interviews with company to fill in specific gaps and queries. This is done by CoreRatings, Ethibel, Innovest, Trucost and Henderson SRI.

Desk-based research is carried out with no discussions/feedback with the company being assessed.
 This is SERM's approach.

These approaches are summarised in Table 5.4 below:

Table 5.4: Data collection methods

Organisation	Self-assessment questionnaire with follow-up company interviews	Part-completed questionnaire provided to guide information collection	Part desk- based, part ongoing dialogue or information data requests	Desk-based with follow-up company interviews to fill gaps	Desk-based; no company involvement
Eiris	X	✓	✓	X	X
PERFORM	X	X	✓	X	X
BiE	✓	✓	X	X	X
CoreRatings	X	X	X	✓	X
Ethibel	X	X	X	✓	X
Innovest	X	X	X	✓	X
oekom research	X	X	✓	X	X
SERM	X	X	X	X	✓
Trucost	X	X	X	✓	X
SAM (DJSI)	X	✓	✓	X	X
FTSE4Good	X	✓ (see Eiris)	√ (see Eiris)	X	X
Henderson SRI	X	X	X	<b>√</b> ¹	X
Morley	X	X	✓	X	X

Key:  $\checkmark$  = applies, x = doesn't apply, N/A = not applicable, N/K = not known, N/D = not disclosed Notes

### Direct engagement with company

As is clear from the above table, all but one of these organisations use some form of company engagement as part of their data collection methods. Initially, this engagement focused on sending out questionnaires. More recently some organisations have moved away from this approach because of perceived problems associated with it — questionnaire fatigue.

Opinion on the use of questionnaires varied. Some (eg oekom research) reported that they had formerly used a questionnaire approach to gather information. They had changed the collection methodology because companies were unhappy with filling in questionnaires. Eiris (who also researches for FTSE4Good) has taken the decision to still use a questionnaire but suggests that where information requested is contained in other disclosures these should be referenced. Alternatively, BiE considers that the act of completing the questionnaire provides the company with an additional opportunity to engage different business functions on environmental issues. It is therefore a mechanism to raise awareness, which has its own benefits.

There are various levels and degrees of company engagement that organisations may undertake with companies in collecting information. These are shown below in Table 5.5. The table differentiates those that engage with companies for data input at the start of the process, from those that will only go to the

<sup>1.</sup> Henderson SRI buys in research from third parties such as Eiris and then may engage with companies to gain further information as appropriate.

company to fill information gaps, once all other sources have been exhausted and comprehensive desk-based research has been undertaken. It shows which organisations will send their draft report or profile to the company in question at the end of the research process, for their feedback and comments or corrections. This is classified as a different or additional form of final engagement, for quality assurance purposes, from the active, ongoing dialogue employed by some organisations. This latter approach invites the company's input and corrections throughout the research process itself. The table also accounts for those that engage with other, external or non-corporate level stakeholders for information.

**Table 5.5**: Levels and stages of engagement with companies when collecting information:

Organisation	Engage company for input at outset – as information source	Ongoing dialogue with company as part of research process	Engage company when other sources exhausted	Send draft profile report to company	Engage external stakeholders: NGOS, lobby groups
Eiris	✓	✓	X	✓	X
PERFORM	X	✓	X	<b>√</b>	<ul><li>✓ (eg trade associations)</li></ul>
BiE	✓	✓	X	X	X
CoreRatings	X	X	✓	✓	X
Ethibel	X	X	✓	✓	✓
Innovest	X	X	✓	X	✓
oekom research	✓	✓	X	<b>√</b>	✓
SERM	N/A (no contact with company)	N/A	N/A	N/A	N/A
Trucost	√	X	Χ	✓	Χ
SAM (DJSI)	✓	✓	X	X	✓
FTSE4Good	√ (through EIRIS)	✓ (focus on those being dropped from the index)	X	<b>✓</b>	X
Henderson SRI	X	✓ ′	X	X	✓
Morley	X	✓	Χ	✓	✓

Key: ✓ = applies, x = doesn't apply, N/A = not applicable, N/K = not known, N/D = not disclosed

#### Information sources

Overall, annual reports, websites and position statements appear to be the sources which are most relied upon for information on companies' Corporate Social Responsibility, ethical and environmental policy and performance. The use of web-search tools such as FACTIVA is common at this stage of the research. It can help with achieving a repeatable structure, consistency and depth in each assessment. The other sources identified in table 5.5 are then used to supplement findings.

There is variation in how organisations access data sources. For example, some organisations systematically refer to the same set of sources for each assessment (eg Innovest); in others the selection of key reference sources for a particular assessment is left to the discretion of the analyst at the time of writing (eg Morley Fund Management).

In some organisations, particularly the fund managers and indices, research is purchased from or subcontracted to research houses. For example:

- FTSE has a strategic relationship with the research organisation EIRIS.
- Henderson SRI purchases some of its research from KLD and EIRIS and undertakes some of its own.

The majority of organisations which do not use questionnaires indicated that, once the initial research phase is completed, they will undertake some level of direct engagement with the companies. This ranges from discussions to fill knowledge gaps to the presentation of a draft profile or assessment for review and comment.

#### **Metrics**

For the purposes of this study, metrics are defined as key questions or indicators. They are the factors or units of assessment by which a company's performance is measured and compared.

Once the information has been collected, a researcher or analyst will use it to compile a number of metrics. These may be quantitative: based on numerical data points which can be calculated and compared. Examples include: How much CO<sub>2</sub> does a company emit with each x volume or quantity of raw material? How many accident or pollution incidents has the company reported over the financial year? Or metrics may be qualitative, based on informed opinions or value judgements (which are harder to measure) and compare companies across different companies. Examples are: How fair or ethical is the company's policy towards suppliers in developing countries? How well integrated and understood is the company's equality and diversity policy? Both types of metrics are important in assessing company non-financial performance. Qualitative metrics, however, are often thought to be less reliable. This is because they are likely to be shaped and influenced by the subjectivity and personal value system of the analyst or rating agency.

As Table 5.6 indicates the number of metrics used by the different organisations varies considerably. Some organisations, such as CoreRatings and Ethibel, use three to four core metric domains, for example environmental, social, economic, and governance. They split these into numerous sub-metrics or subsidiary issues. Others such as Trucost use only one set of metrics referring to a certain aspect of performance, for example environmental impact metrics. Others apply a core set of generic metrics and then use additional ones specific to different industry sectors. This is the approach taken by SAM (DJSI). For others, such as Morley FM, there is no standard set of metrics applied. Confidentiality limited the number of organisations that were willing to provide more than a few examples of their questions/data points.

**Table 5.6**: Approximate number of metrics used in each of the organisations interviewed.

Organisation	Approximate number of general metrics	Number of environmental metrics	Additional information
Eiris	100	35	
PERFORM	35	16	
BiE	N/A	16	15 main questions, plus one on verification of information presented.
CoreRatings	168	48	
Ethibel	65	24	
Innovest	101	48	
oekom research	200	100	
SERM	56	22	Additionally each direct impact is looked at in terms of a further 12 indirect or reputational aspects
Trucost	30	30	The methodology maps the use of over 700 resources and emissions to over 130 different business activities. However, for the purposes of this comparison it was noted that the most appropriate metrics are selected for each organisation being assessed. On average 30 are used in an assessment.
SAM (DJSI)	100	30	100 metrics used that are subdivided. The number of total and environmental metrics depends on the industry; the figures given here are averages.
FSTE4Good	45	25	45 key criteria, which are further subdivided. Specific environmental metrics are not necessarily applied to all the companies.
Henderson SRI	N/A	N/A	Does not use a set number of metrics
Morley	N/A	N/A	Does not use a set number of metrics. The nature and number of metrics varies between sectors.

Key: N/A = not applicable, N/K = not known, N/D = not disclosed

### 5.4 Process

### Methodologies

The review revealed the following four types of methodology in approaching company ratings/rankings. These are detailed in Table 5.7. To assist the user we have also provided one example of each type of organisation that uses this methodology. However, this is not an indication that the organisation listed provides the most robust or best example of each methodology.

Table 5.7: Types of assessment methodologies

Types of assessment methodologies						
Risk based	Qualitative assessment of key issues which create financial, reputation, and other risks (litigation), eg SERM.					
System based	Measuring appropriateness of policies and systems in place to manage and control impacts, eg BiE.  This also includes those organisations who assess management quality for key areas of perceived financial risk, eg Innovest.					
<ul> <li>Environmental performance or impact</li> </ul>	Measurement of actual environmental impact and/or improving performance over time, eg Trucost .					

The credibility of assessment results can be affected by the transparency of the assessment methodology and its conceptual accessibility for users. If it is not clearly understood, users will intuitively blame the methodology used when the result is unsatisfactory.

To achieve full transparency some of the organisations interviewed present full details of their assessment methodology and the criteria on their websites. FTSE4Good does this. For others the constraints of commercial confidentiality meant only limited details could be discussed during the interviews for this research.

What is apparent, however, is that the complexity of assessment methods varies. SERM for example, applies a mathematical methodology to its company ratings in order to calculate risk in relation to capital percentage. Trucost employs a complex modelling technique based on established economic theory to quantify and price environmental externalities. Other organisations apply what they describe as tools to calculate ratings. The complexity of these varies widely. However, they often comprise straightforward processes that involve a standardised series of research steps, which have been trademarked to seal their association with the brand of a given organisation. These are then marketed as research tool products for sale or subscription. An example is Innovest's EcoValue 21 investment analytics platform.

The relative level of subjectivity/objectivity applied was another key differentiating aspect of the assessment methodologies we examined. Organisations held wider-ranging views on the value of subjectively informed research in this field, than they did on that of more quantitative, objectively gathered data.

These different stances reflect a broad range of different philosophies and target audiences, as well as a variety in the intended uses for the outputs of the research. This will be discussed in greater detail below.

#### **Quality assurance**

**Table 5.8** below shows levels of quality assurance undertaken by organisations:

Organisation	Analysts with relevant environmental/financial backgrounds	Guidance handbook/ rule book (to assist with subjective assessment)	Internal QA/ Review processes	Adhere to independent quality standard	Use external advisory panel/ Independent experts	External verification
Eiris <sup>1</sup>	✓	✓	✓	X	X	Commissioning an audit
PERFORM	<b>√</b>	N/A	<b>√</b>	Х	<b>√</b>	x <sup>2</sup>
BiE	✓	X	✓	X	X	✓
CoreRatings	✓	✓	✓	X	✓	x <sup>3</sup>
Ethibel <sup>1</sup>	<b>√</b>	X	<b>✓</b>	<b>√</b>	<b>√</b>	X
Innovest	✓	<b>√</b>	<b>√</b>	X	✓	✓ <sup>4</sup>
Oekom	✓	✓	✓	✓	✓	X

research <sup>1</sup>						
SERM <sup>1</sup>	✓	✓	✓		✓	<b>√</b> <sup>5</sup>
				<b>✓</b>		
Trucost	✓	N/A	✓	X	✓	X
SAM (DJSI)	✓ (SAM analysts)	✓ (rulebook methodology)	X	X		<b>√</b> <sup>6</sup>
FSTE4Good	N/A (research by Eiris)	N/A (research by Eiris	✓	X	✓	X
Henderson SRI	✓	X	✓	X	✓	X
Morley	✓	X	✓	X	✓	X

Key:  $\checkmark$  = applies, x = doesn't apply, N/A = not applicable, N/K = not known, N/D = not disclosed

### Notes:

- 1. Founder member of the AICSRR aiming to develop a European Voluntary Quality Standard for CSR Researchers.
- 2. Although Perform does not have verification of their work, they do note if the data they use has been subject to external verification.
- 3. CoreRatings noted that, although there is no standard verification, clients have visited to review/audit assessment work.
- 4. PWC checked the Innovest methodology/model in 1995.
- 5. Copenhagen Business School has performed Monte Carlo testing of SERModel on one occasion.
- 6. PWC conducts an annual audit of the SAM (DJSI) process. This includes taking a sample of the companies and the received information (questionnaire) and repeating the SAM assessment process.

**Table 5.9** below shows the number of companies analysed and number of analysts (where known) in each organisation:

Organisation	Number of companies analysed	Number of analysts
Eiris	2700	19
PERFORM	105 companies and 217 production sites (so far)	4 core analysts in addition to a number of graduate researchers
BiE	176	4
CoreRatings	1500	18
Ethibel	600	9
Innovest	1800	23 permanent full-time analysts
oekom research	Universe of 800 companies worldwide (look at approximately 30-70 largest in each sector)	10
SERM	600	8
Trucost	1700	9
SAM (DJSI)	770	10
FSTE4Good	2500)	N/A (see EIRIS)
Henderson SRI	1200	7
Morley	Database of 350 company profiles and 200+ screens. New ones added as required.	3 analysts and 1 support. Also work together with the 20 mainstream analysts.

Key: N/A = not applicable, N/K = not known, N/D = not disclosed

Quality assurance procedures also vary across organisations, but are characterised by a number of clear common themes:

- Analysts' backgrounds: in all 13 organisations analysts are recruited from financial, environmental science or closely related academic fields. As mentioned above, they are also often selected on the basis of their knowledge or experience of a certain industry: they are assigned responsibility for specific sector research accordingly. The methodologies of many of these organisations often rely partially and sometimes wholly on the knowledge and expertise of these sector specialists to make the initial analysis of key sector issues and risks.
- Independent Quality Standards/ Guidelines and Handbooks: in a few cases organisations have developed their own quality standard to assure research (eg oekom research). Others adhere to an independent quality standard such as the EU standard (eg Ethibel and SERM). oekom research also uses a handbook tool, developed in co-operation with senior academics. This contains guidance notes on research for its analysts, and defines its criteria for metrics and scoring system. It is used by all analysts as the standard reference point for compiling company profiles, and is kept constantly updated according to recent company events and academic developments in the field.
- Internal assurance: internal review and quality checking are undertaken at some level by all the organisations we have analysed. This may range from analysts peer-reviewing one another's work, to all research being systematically reviewed and verified by one or more senior members of the research team.
- External verification: as far as we can ascertain, only two organisations currently have their process and methodology externally verified BiE and SAM (DJSI). Eiris is aiming to put this process in place soon. Two others (Innovest and SERM) have had their methodology validated. However the process has not been repeated or applied to the content of their assessment.
- Advisory Panels: ten of the selected organisations employ either a scientific or academic advisory
  board to make the final decisions on company ratings and scores. These were Ethibel, Henderson
  SRI, Morley, oekom research, Perform, Trucost, CoreRatings, Innovest, SERM and FTSE4Good.
  These boards are mostly comprised of senior academic experts. Others employ senior industry experts
  or high-level non-executive directors to oversee the process in a governance capacity. In these cases,
  names and professions of members are publicly disclosed.

## 5.5 Outputs

**Table 5.10** below shows the varied types of outputs products and services across the organisations reviewed:

Organisation	Score/Rating	Ranking/Index	Company profile	Sector profile	Country profile	Other (consultancy etc)	Web based/Pape r based
Eiris	Provide information to enable their clients to do this	Provide information to enable their clients to do this	<b>√</b>	х	X	Ethical Investment guides, customised services and investment software product – Ethical Portfolio Manager	PC and paper based
PERFORM	N/A	X	✓	Х	x	Sustainability management tools, statistical analysis of company data	Data collected web based
BiE	✓	✓	✓	X (short discussion by sector in overall report)	X	Overall review report, Benchmarking Plus in-depth feedback on index performance, trend analysis, index shadowing service	Paper based (executive summary of index report is web based)
CoreRatings	✓	X	✓	<b>√</b>	X	Issue reports (on client request and on ad hoc basis), daily news monitoring, bespoke client services: engagement, workshops and training, briefing and issue papers, and bench-marking.	Web and paper based
Ethibel	✓	✓	✓	✓	X	Quality label/register, tailor- made research	Web and paper based
Innovest	<b>√</b>	<b>√</b>	<b>✓</b>	<b>√</b>	Х	Customised research, advisory work for financial institutions and companies wishing to improve their rating, EcoValue 21	Web and paper based
oekom research	<b>√</b>	<b>√</b>	<b>✓</b>	<b>✓</b>	<b>✓</b>	Rating Tool Customised investment recommendation lists, quarterly update on investment universe	Web and paper based
SERM	<b>√</b>	x	<b>✓</b>	<b>√</b>	X	Reputational risk assessments, strategic risk consultancy, scenario planning, CSR/corporate governance benchmarking reviews	Web and paper based
Trucost	<b>√</b>	X	<b>✓</b>	<b>✓</b>	Х	Environmental modelling tool (cost calculator), customised research, briefing reports on legislation	Web and paper based
SAM (DJSI)	<b>√</b>	<b>√</b>	<b>✓</b>	Х	X	Detailed bench- marking report (for assessed organisations)	Web and paper based
FTSE4Good	In or out only	✓	✓	X	X	X	Web and

Organisation	Score/Rating	Ranking/Index	Company profile	Sector profile	Country profile	Other (consultancy etc)	Web based/Pape r based
							paper based
Henderson SRI	√ (not made public)	X	X	X	X	Investment recommendations	N/A
Morley	<b>✓</b>	x	√(for internal purposes only)	<b>✓</b>	X	Investment recommendations	Paper based

Key: ✓ = applies, x = doesn't apply, N/A = not applicable, N/K = not known, N/D = not disclosed

### Scores and reports

While the details of the outputs vary quite widely across the interviewed organisations, a number of common types of outputs have been identified. These are summarised below:

- Score/Rating: nine of the organisations produce either scores or ratings. These are BiE, SAM (DJSI), CoreRatings, Ethibel, Innovest, Morley, oekom research, PERFORM and Trucost. Henderson SRI does produce ratings but these are not made public. Eiris also produces individual critieria ratings but allows the client to collate these scores to suit their purpose.
- Reports: the majority of the organisations produce company profiles with descriptions, information on activities and specific issues. These range in detail and scope. On the one hand a one-page profile sheet for each company rated summarises key incidents, achievements, scores and rankings. In other cases, lengthy and detailed documents of up to 15 pages contain analysis and case studies of company performance. Seven of the organisations also produce separate sectorwide reports dealing with issues across specific areas of industry. All organisations produce reports in one form or another. The vast majority of these are available for public and external use. Only one organisation produced a report solely for internal purposes.

#### Update and review

The regularity of updates and reviews varied, from a continual rolling process to 18 monthly and three yearly reviews. Of the organisations compared, one has a continual update programme in place and seven have an annual update and review programme. Several of the organisations have update frequencies which are dependent on the service in question and the size and scope of the company being considered.

**Table 5.11**: Shows frequency of updates and review of reports/profiles:

Organisation	Annual	Bi-annual	Monthly	Other and comments
Eiris	<b>√</b>	X	х	Information in one product is partially updated weekly (publicly sourced documents).
PERFORM	Х	x	Х	Frequency of updating is dependent on the company which is required to input the data, so can be at any time.
BiE	✓	x	X	
CoreRatings	<b>✓</b>	х	Х	Bespoke quarterly reports may be available. Ratings are reviewed upon the occurrence of significant events affecting the company.
Ethibel	Х	✓	Х	Ongoing monitoring system of companies in the label universe if necessary interim updates and re-evaluations may be undertaken
Innovest	<b>√</b>	х	X	May be exceptional updates with merger/acquisition/major events.
oekom research	х	Х	х	Every 18 months.
SERM	X	X	X	Assessment based only on public sources and therefore database is continually updated. Frequency of updated assessments to clients is dependent on client specific agreements.
Trucost	<b>✓</b>	X	x	clicitis is dependent on cliciti specific agreements.
SAM (DJSI)	✓	х	×	Annual questionnaire and assessment process. Also the media is tracked and performance on extraordinary events can impact on index inclusion at the discretion of the Monitoring Committee.
FTSE4Good	х	<b>√</b>	х	Two opportunities for updating company information and amending the index during the year at six monthly intervals. One is based on questionnaire completion process (Eiris). For the other, the company profiles are sent to the company for their review.
Henderson SRI	√ (major UK)	х	х	3 yearly.
Morley	X	Х	x	Updates on an as-needed basis.

Key:  $\checkmark$  = applies, x = doesn't apply, N/A = not applicable, N/K = not known, N/D = not disclosed

### **Products and services**

Products and services are mainly reports and published updates on investment issues. However, three organisations also provide bench-marking services. There is also a wide variety of small-scale services and products, such as:

- consultancy and advice on improving performance (Innovest);
- quality standards (Ethibel);
- media monitoring (Innovest);
- country profiles and ratings, including analysis of socio-political investment risk (oekom research);
- web-based and electronic tools for management of strategic risk assessment (SERM) and rating (Innovest);
- analytical modelling of environmental performance (Trucost).

**Table 5.9** above also provides a summary of the key outputs from these organisations.

### Cost

**Table 5.12**: Shows cost/basis of charge for products and services:

Organisation	Set cost per product	By negotiation with client	Other eg dependent on service	Anything free₁	Not disclosed
Eiris			✓		
PERFORM	X	X	X	Whole service	
BiE	X	X	Shadow bench- marking service provided at cost and publication report can be purchased at a cost of £70		
CoreRatings	X✓	X	✓	X	
Ethibel			<b>✓</b>	Composition of Ethibel Sustainability Index and short profiles	
Innovest					✓
oekom research	350 Euro for company rating report		✓		
SERM			✓ Cost of rating and report with companies benchmarked in peer group varies between £5,000 - £20,000. Corporate services £5,000-£10,000, Fund manager service £10,000-£50,000.		
Trucost			✓ (eg £2,000 for sector reports, financial indices from £8,000, £35,000 peryear access to whole model)		
SAM (DJSI)			<b>✓</b>	Company feedback, high- level details for 18 market leaders, industry overview and index composition	
FTSE4Good	✓ (licence and data fees) <sup>2</sup>			No cost to assessed companies	
Henderson SRI	N/A	N/A	N/A	N/A	N/A
Morley	N/A	N/A	N/A	N/A	N/A

Key:  $\checkmark$  = applies, x = doesn't apply, N/A = not applicable, N/K = not known, N/D = not disclosed Note:

- The majority of organisations will provide a company's individual assessment report for free.
- Licensing revenues are contributed to UNICEF.

For PERFORM no cost was applicable to their services and products. For the majority of the other organisations, however, the costs incurred are dependant on the nature of the service being provided and the depth and scope of the information required. Many of the organisations provide information to the public and to participating companies free of charge and charge only for additional services provided.

As these themes show, there are many broad similarities between the organisations we have reviewed. However, all use their own combination of elements to create a unique service/product tailored to their own ethos/values and priorities.

# Environment Agency modern regulation strategy

### 6.1 Background

The Environment Agency is modernising its approach to regulation. Important themes of the new approach focuses on outcomes and is based on risk. It promotes the use of the most appropriate mix of approaches to deliver the desired environmental outcomes.

Direct regulation still plays an important role in the work of the Environment Agency. However, it recognises that it also has a role in developing innovative approaches that deliver better environmental outcomes more efficiently. The aim is that the regulatory function will also become more focused, with resources targeted on the greatest environmental risks and less time spent on good performance and lowrisk routine inspections.

The Environment Agency has been developing its own tools for assessing operators risk and communicating environmental performance. As part of this review, the Environment Agency is keen to identify opportunities to complement its own dataset and assist delivery of its more focused regulation strategy.

This section outlines a selection of Environment Agency initiatives:

- Operator and Pollution Risk Appraisal (OPRA)
- Spotlight on Business Environmental Perfromance
- The Pollution Inventory (PI)
- REMAS.

Each of these initiatives is discussed here in terms of their key aspects with regard to some of the attributes of organisations that we have considered. We also consider opportunities for developing these initiatives to aid the Environment Agency's modern regulatory strategy and examine how CER organisations might potentially use the outputs from these initiatives.

PERFORM is an EU sustainability performance project for which the Environment Agency is one of the key sponsors. It has not been included in this section as an Environment Agency initiative because it was assessed as a rating organisation in an earlier section.

### 6.2 Discussion

Generally, most information held by the Environment Agency is collected and stored at site level, as this is the level at which regulations tend to be applied. On the one hand this provides a challenge for the Environment Agency to link site level information to a corporate entity. However, it also provides a great opportunity. Much of the research and assessment performed by CER focuses on corporate level systems, performance and risk etc. There is little consistent consideration of site-level performance or management control. If Environment Agency data can be linked to corporate entities, it would provide assessment processes with an additional level of robustness.

#### **OPRA**

One methodology currently in place is the Integrated Pollution Control (IPC) OPRA. Introduced in 1995, it was developed to appraise environmental risks from processes under IPC, and the performance of operators managing these risks. A similar programme also covers waste management sites. It aims to target regulatory effort on high-risk processes, to improve the effectiveness and efficiency of regulation and to encourage transparency between regulators and operators. The OPRA methodology enables two scores to be assigned to a site:

- the inherent level of risk associated with the process process hazard assessment (PHA)
- the operator performance assessment (OPA).

In each case, the assessment comprises five questions. These can be assigned a score from one to five with documented guidance as to what level of risk or performance merits a particular score.

By 2007, the IPC OPRA methodology will be replaced by the Environmental Protection (EP) OPRA methodology. The changeover will happen as companies make Integrated Pollution Prevention and Control (IPPC) applications. As with the IPC OPRA methodology, the new approach will look at the environmental hazard of the operation and the operator performance. The EP evaluation will start with a self-assessment by the operators when they submit their IPC application. The Environment Agency will review the assessment along with the application.

In short, this Environment Agency programme gives a site-based ranking for those sites covered by the specific regulatory regimes. It provides an assessment of the inherent environmental hazard of the site and the ability of the operator to control risk. Its coverage of industry is clear-cut, as it is set out by the regulatory regimes.

OPRA has a **rating** tool that considers **environmental risk** and the capacity of an organisation to manage the risk (**environmental management systems**). There is **guidance** on the scoring of each metric in the system, and the assessment can be performed and thus updated on an **annual basis**. However, the move to self-assessment under the IPPC applications could reduce the level of consistency and objectivity given

to scores. Clear requirements for supporting evidence to the self-assessment could enable robust validation by Environment Agency inspectors. This could largely remove concerns in this area.

As well as being an Environment Agency rating tool, the outputs form a potential metric that could be used by CER organisations. OPRA only covers certain sectors – those controlled by Waste Regulation and IPPC regulations. Therefore it might be considered to be only a partial or additional dataset. Potentially more significant is that it is a site-by-site assessment process. Currently, there is not always a clear link between the individual sites and the parent company. Also the assessment process may not cover all sites within an organisation. Many research organisations therefore consider the information to be incomplete. The potential to link individual sites to a corporate organisation, or even to give the relative proportion of financial turnover, could result in this information being more readily useable for different users and uses.

### Spotlight

Spotlight is an annual report on the environmental performance of business produced by the Environment Agency. It presents a sector-by-sector analysis of UK business and industry, highlighting good and bad performances and detailing major prosecutions. The report is based on the information that the Environment Agency collects during the course of its activities to control pollution and improve industry's environmental performance. Information in the Spotlight report includes:

- pollution inventory, containing information on all main pollutants
- pollution incidents
- prosecution information
- information on repeat offenders
- operator performance scores (from OPRA).

This initiative rates top and bottom performers on a number of different aspects. It thus provides a measure of environmental performance. It gives the ranking for each element individually and does not aim to combine and thus identify overall performance. It is a tool that presents factual information with little interpretation or analysis and it could be put to many different uses. Its industrial coverage is broader: all the sectors covered by the Environment Agency's remit. However it only sites in England and Wales and the industrial coverage per element, eg pollution incidents, does vary. If sector coverage for each element could be clearly identified, this would improve the clarity of the findings.

Spotlight partly links site-based data to corporate entities. CER organisations may immediately find this data to be more readily accessible. Also, access to additional information from other sources might increase the usability and value of some of the information currently presented.

For instance, the fines paid section could be extended to include information on environmental related expenditure. This would provide information not only on the efficiency of the pollution control mechanisms in place but also on the level of control or management focus and on commitment to continuous improvement.

### The Pollution Inventory (PI)

The Pollution Inventory (PI) is the annual record of pollution from activities regulated by the Environment Agency. It records pollution released to air, waters, sea, and the sewage network, or transferred off site as waste. The objectives of the Pollution Inventory are:

- to provide the public with accessible data about pollution from industry and other sources;
- to help environmental regulators to protect the environment
- to help the Government to meet national and international commitment and obligations for reporting.

The Pollution Inventory comprises a raw dataset that could be used as a data source by CER organisations in their assessments. Currently, as with many of the Environment Agency datasets, the Pollution Inventory is made up of site-based information. To be readily useable by CER organisations, it needs to be linked to corporate entities. This dataset does, however, have actual discharge/release information and is presented in a consistent format. It could therefore provide useful quantitative **information** that is infrequently used in assessment processes due to the reported difficulty in getting data in a consistent form. The Pollution Inventory, as currently recorded, is absolute data. In order to make comparisons on environmental performance, users need to be able to understand the context for those figures, ie in terms of such factors as sector, process, production volumes, and permit limits.

### **REMAS**

REMAS is a three-year project to examine environmental management systems in business and industry across EU member states. Its purpose is to investigate whether companies and organisations with an environmental management system (EMS) have an improved environmental performance. There is currently a lack of evidence to support this theoretical link.

At present this is an active project, and so it cannot be used immediately by CER organisations. However, the concept on which the project is based – namely identifying whether an environmental management system drives environmental performance – is highly relevant for CER organisations. Many assessments of so-called environmental performance consider which elements of management systems are in place but make no direct consideration of environmental impact or performance. The outcomes from this study may therefore be useful in identifying appropriate questions for assessing the strength of a management system. This would benefit both the CER organisations and the Environment Agency (in terms of its OPRA assessment process and the sharpening up of its regulatory efforts).

### **Environment Agency Awards**

The Environment Agency has two main awards that it runs or sponsors: the Environmental Awareness awards (one of the National Business Awards) and the Water Efficiency Awards. The purpose of the Environmental Awareness Award is to recognise leaders in environmental strategy as well as recognising efforts in this area. Organisations of any size, age and type can enter for the Environmental Awareness Award. It is thus a method of identifying companies which have good performance, whether they are large corporate entities or small and medium-sized enterprises.

Information required as part of the application is collected on a questionnaire. It includes:

- details on environmental strategy (including an initiative illustrating this);
- how the strategy has had a positive financial impact and competitive advantage;
- internal and external communication of impacts and performance;
- management systems;
- the application of environmental management within the supply chain.

The judges of the Environmental Awareness Award look for a clearly articulated and widely communicated environmental strategy that is incorporated into the overall business strategy of the company. They also want to see a company-wide commitment to reducing environmental impacts. In particular, the judges seek out innovative approaches to the environment and policies that improve the financial performance of the organisation. Regulatory compliance is considered by the judges as evidence of the award winner's credibility.

The only rankings or ratings published are the short-listed organisations and the eventual winner. The results of the Environmental Awareness Award would be of most use to organisations as a benchmarking tool, providing insight into good practice for environmental strategy and policies. However, the applications for an award are clearly voluntary and therefore coverage may be relatively focused on those organisations which consider their environmental performance/management to be generally good.

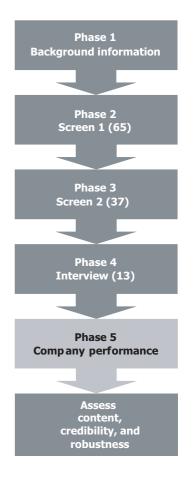
The Water Efficiency Awards recognise, highlight and celebrate good policies in water conservation – in industry and a variety of other sectors. For the purposes of this research these awards are considered to be too limited in terms of environmental aspects to be considered (ie only water minimisation).

# 7. Results of company performance review

### 7.1 Introduction

An important part of this study was to compare how the organisations we interviewed assessed a broad sample of companies. All of the 13 selected organisations either review or assess companies, but two of the selected organisations do not give an overall score. These two organisations are therefore not included in the comparison section, but are included in remainder of this chapter

- PERFORM does not assess or rank organisations (only collects and presents information).
- Eiris does not calculate an overall assessment score of companies for its clients, but scores each company on a range of individual criteria. Clients select from these according to their own investment criteria.



# 7.2 Which companies were included in this performance review?

We identified four sectors:

- utilities
- basic industry (chemicals) referred to as chemicals in this section
- basic industry (construction) referred to as construction
- non-cyclical consumer goods referred to as consumer goods.

Five companies were selected from each sector. Organisations were asked whether they did cover the selected companies and, if so, to provide their scores. Confidentiality is important for many of the rating organisations, so we agreed not to name the companies in this comparison by sector. Table 7.1 below shows which companies were assessed by the eleven CER companies involved. It also shows those which are covered by EIRIS and PERFORM – for which coverage information is available but not company specific ratings or results.

 Table 7.1: Which companies were assessed by the CER organisations

	Ţ	2	m	4	2	als 1	als 2	als 3	als 4	als 5	ction 1	ction 2	ction 3	ction 4	ction 5	er	er	er	ıer	er
	Utilities	Utilities	Utilities	Utilities	Utilities	Chemicals	Chemicals	Chemicals	Chemicals	Chemicals	Construction	Construction	Construction	Construction	Construction	Consum goods 1	Consum goods 2	Consum goods 3	Consum goods 4	Consum goods 5
Eiris	<b>✓</b>	✓	<b>✓</b>	<b>✓</b>	<b>✓</b>	~	✓	<b>√</b>	<b>✓</b>	<b>√</b>	<b>√</b>	~	<b>✓</b>							
PERFORM				✓																
BiE	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓			✓	✓	✓		✓	✓
CoreRatings		<b>✓</b>	<b>✓</b>	<b>✓</b>	<b>✓</b>	<b>✓</b>				<b>√</b>						<b>✓</b>	<b>✓</b>		✓	
Ethibel				✓	✓												✓			
Innovest	✓	<b>✓</b>	✓	<b>✓</b>	✓	<b>✓</b>	<b>✓</b>	✓	✓	<b>✓</b>	✓	✓	✓	<b>✓</b>						
oekom research				<b>✓</b>	<b>✓</b>	<u> </u>				<u> </u>						✓	✓		✓	
SERM	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓
Trucost	✓	<b>✓</b>	<b>✓</b>	✓	<u> </u>	<u> </u>	<b>✓</b>	<b>✓</b>	✓	<b>✓</b>	<u> </u>	<b>✓</b>	✓	✓	<b>✓</b>	✓	<b>✓</b>	✓	✓	<u> </u>
SAM (DJSI)	✓	✓	✓		✓	✓			✓	✓	✓	✓				✓	✓		✓	
FTSE4GOOD	✓	✓	✓	✓	✓	✓	✓	✓	<b>✓</b>	✓	✓	✓	✓	<b>√</b>	✓	✓	✓	✓	✓	✓
Henderson SRI	~	<b>✓</b>	<b>✓</b>	<b>✓</b>	<b>✓</b>	<b>✓</b>		<b>✓</b>		~				<b>✓</b>		<b>✓</b>	~		~	<b>✓</b>
Morley Fund Management	<b>✓</b>	<u> </u>	<u> </u>	<b>✓</b>		<u> </u>	<u> </u>	<u> </u>	<u> </u>	<u> </u>	<b>✓</b>	<u> </u>	<u> </u>	✓	<u> </u>					

### 7.3 Methodologies for standardisation

Eleven organisations participated in this phase of the research. Eight produced scores. Three – FTSE4Good, Henderson SRI and Morley – presented their outputs purely in terms of entry into an index. (or not). The scores were presented in various forms: percentage scores, various alpha ranking forms and ratios. These are indicated in table 7.2. To compare results we needed to show the scores in a consistent form. To do this we applied a normalisation technique. Several organisations gave their scores as a percentage – we chose this as the normalised form. Details of the normalisation process are contained in Annex C. Table 7.2 below also identifies where the outputs are ranked within sector. This limits cross-sector comparisons.

Table 7.2: Nature of rating outputs presented

Organisation	Type of score	Details
BiE	Percentage range	For BiE's Public Index report, the main source of information was company scores indicated by % range. Exact scores were used where available.
CoreRatings	Alpha	Letter gradings from A+ to D (seven gradings in total).
Ethibel	Numeric score	Scores calculated out of a total of 0 to 6.
Innovest	Alpha	Innovest issues 7 ratings AAA (best), AA, A, BBB, BB, B, and CCC (worst). Organisations are only ranked within sectors and therefore comparisons across sectors cannot be applied. Companies are rated against their global counterparts. No direct comparison can therefore be made against other ratings unless they have the same universe.
oekom research	Alpha	Letter grading from A+ to D
SERM	Alpha	SERM ratings cover a 31 point scale from AAA+ to E (Net/Residual risk values are in brackets) AAA+ (5%), AAA (6%), AAA- (7%), AA+ (8%), AA (9%), AA- (10%), A+ (11%), A (12%), A- (13%), BBB+ (14%), BBB (15%), BBB- (16%), BB+ (17%), BB (18%), BB- (19%), B+ (20%), B (21%), B- (22%), CCC+ (23%), CCC (24%), CCC- (25%), CC+ (26%), CC (27%), CC- (28%), C+ (29%), C (30%), C- (31%), DDD (32-34%), DD (35-37%), D (38-40%), E (41-73%)
Trucost	Ratio	Impact ratio – representing costs associated with environmental externalities.
SAM (DJSI)	Percentage	% is the % of the maximum possible score.

### 7.4 Performance comparison

Table 7.3 below shows the normalised percentages from the original scores/ratings achieved given to each of the companies by the rating/ranking organisations we reviewed.

Table 7.3: Scores for companies by each of the organisations reviewed – normalised where required

				Fund Jers							
	BiE	CoreRatings	Ethibel	Innovest	oekom research	SERM	Trucost	SAM (DJSI)	FTSE4G00D	Henderson	Morley
Utilities 1	85	-	-	71	-	85	85	52	Υ	Υ	Υ
Utilities 2	95	86	-	71	-	85	71	63	Υ	Υ	Υ
Utilities 3	99	71	-	86	-	85	80	63	Υ	Υ	Υ
Utilities 4	93	71	70	86	34	89	41	-	Υ	Υ	N
Utilities 5	85	86	76	100	50	90	93	61	Υ	Υ	Υ
Chemicals 1	89	71	-	86	50	78	87	42	Υ	Υ	Υ
Chemicals 2	65	-	-	43	-	81	78	-	N	N	N
Chemicals 3	85	-	-	43	-	84	77	-	Υ	Υ	Υ
Chemicals 4	98	-	-	71	-	82	82	69	Υ	N	N
Chemicals 5	75	71	-	86	59	78	81	71	Υ	Υ	Υ
Construction 1	78	-	-	71	-	85	97	37	N	N	N
Construction 2	77	-	-	57	-	72	97	47	N	N	N
Construction 3	-	-	-	57	-	76	95	-	N	N	Υ
Construction 4	-	-	-	71	-	76	96	-	Υ	N	Υ
Construction 5	65	-	-	86	-	82	97	-	Υ	N	N
Consumer 1	90	86	-	100	59	94	96	68	Υ	Υ	Υ
Consumer 2	93	43	61	86	59	90	96	44	Υ	Υ	N
Consumer 3	-	-	-	57	-	88	94	-	Υ	N	Υ
Consumer 4	95	71	-	100	59	92	91	72	Υ	Υ	Υ
Consumer 5	75	-	-	71	-	95	92	-	Υ	N	Υ

Overall there were clear variations in the scores. This reflects variations in the methodologies used. For example, Innovest presents and analyses data on a sector basis. We cannot directly compare their scores with those of an organisation that scores on a company basis. Such issues need to be taken into account when analysing and comparing company performance. It should be borne in mind that the normalisation of scores does not overcome the differences between methodological approaches.

when analysing and comparing company performance. It should be borne in mind that the normalisation of scores does not overcome the differences between methodological approaches.

In the sections below, we present the scored results graphically on a sector-by-sector basis (graphs 7.1 through 7.4). Please note that this section only includes the 8 organisations that have an overall score.

Figure 7.1 - Utilities Sector

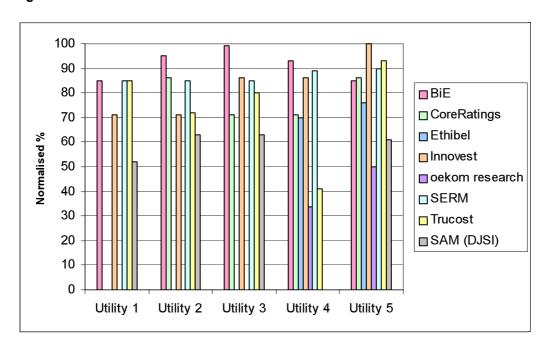


Figure 7.2 - Chemicals Sector

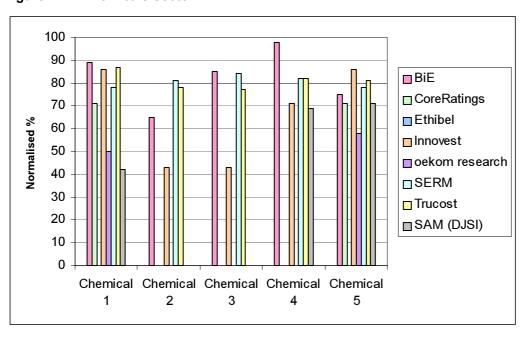


Figure 7.3 – Construction Sector

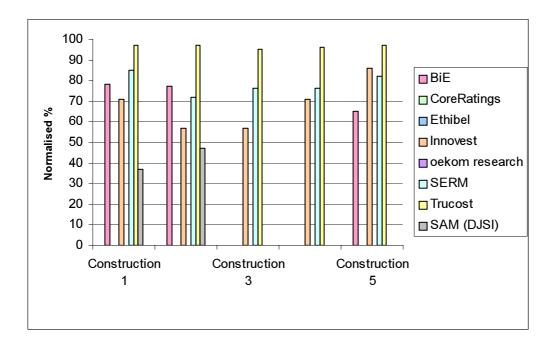
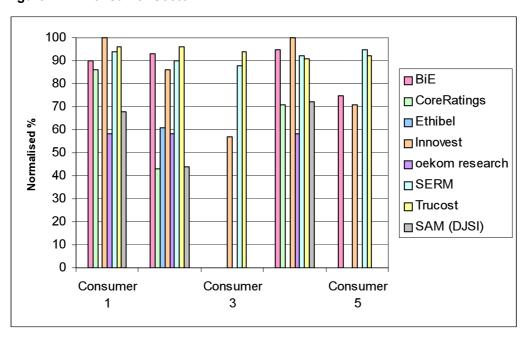


Figure 7.4 – Consumer Sector



#### Overall themes and conclusions

We had thought that this review of company performance would identify clear themes of value to users. However, as the results of the analysis we performed show, there is considerable variation in the scoring of different companies across the methodologies of the eleven organisations reviewed. Even with if we try to present the results in a standardised form, no strong themes emerge within or across the industry sectors. Our conclusion from this analysis was that such comparisons of scores are not straightforward, either before or after normalisation. As organisations use different sources of data for their assessments, it is possible that part of the apparent variation in scores might be due to different levels of disclosure by companies. For instance, the range of scores provided for Utility 1 appears to be less than the range provided for Utility 4. This might indicate that Utility 1 has a greater level of disclosure that Utility 1. Further research would be needed to identify how much this and other factors, such as sector and business activities, influence the assessments and outputs. This is beyond the scope of this part of research.

The results suggest that there could be is a risk in using a combination of organisations because this may lead to contradictory, results. The variability in scoring is such that a user will have to have a good understanding of the methodologies used if they are to find the organisation which most suits their needs.

# 8. Summary and discussion

This report aims to help users and stakeholders to make informed choices for:

- their own business purposes
- · comparative bench-marking of sectors or companies
- financial investment (eg pension funds).

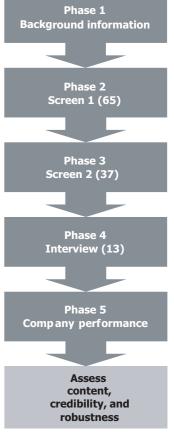
We have therefore identified what we see as the key information any user would need about an organisation in order to assess and compare relative environmental content, credibility and robustness. This key information is presented in a summary table of core facts (see Table 8.1), and as a set of key guiding questions. A user may ask a ratings organisation these questions with his/her own needs in mind. Drawing on all this, as well as on the matrices of comparative information set out in this review, users should be able to better understand what CER organisations can offer them. This should help users to make informed choices. Importantly, this approach avoids unhelpful generalisations and judgements on an organisation's relative strengths and weaknesses, based upon our own subjective opinions.

The Environment Agency's wants this report to provide an independent review of the environmental content, credibility and robustness of company

indices, rating and rankings. This is therefore the focus of the following discussion. We hope that we have created an explanatory tool for a prospective user of any or all of these organisations' services.

It is important for the clarity of the following discussion that there is a clear understanding of what we mean by credibility and robustness. The definitions used are given in Table 8.2 below. Based on this research we have identified the most important aspects for identifying the environmental content, credibility and robustness of a CER organisation. These form the basis of this section and are:

- environmental content
- industrial coverage
- information and data sources
- assessment methodologies
- quality assurance.



Name	Eiris	PERFORM	BiE	CoreRatings	Ethibel	Innovest	oekom research AG	SERM	TRUCOST	SAM (DJSI)	FTSE4Good	Henderson SRI	Morley
Type of	Rating	Other	Rating	Rating	Rating/ Index	Rating	Rating	Rating	Rating	FM/Index	Index	FM	FM
organisation Product name			BiE Index	Rating	Ethibel Quality Label and Ethibel	EcoValue 21	Corporate Responsibility			DJSI Indices	muex	T W	1 101
					Sustainability Index		Rating						
Geographical coverage	UK/Europe/World	UK/ Europe	UK (some World)	Europe/Some world	World	World	World	World	World	World	World	World	UK/World
No of metrics (environmental)	35	16	16	48	24	48	100	22	30	30	25	Not applicable	Not applicable
Focus of philosophy:	Appropriateness of EMS for environmental issues and risks	Environmental Performance	Appropriateness of EMS for environmental issues and risks	Appropriateness of EMS for environmental issues and risks and financial implications of environmental risks	Appropriateness of EMS for environmental issues and risks	Appropriateness of EMS for environmental issues and risks and financial implications of environmental risks	Appropriateness of EMS for environmental issues and risks	Financial implications of environmental risks	Financial implications of environmental risk	Appropriateness of EMS for environmental issues and risks and financial implications of environmental risks	Appropriateness of EMS for environmental issues and risks	Appropriateness of EMS for environmental issues and risks	Appropriateness of EMS for environmental issues and risks
Financial index	FTSE	N/A	FTSE 350, DJSI (sector leaders). BiTC members are invited to participate	FTSE 100, EUROTOP 300 and MSCI (key sector coverage)	N/A Ethibel construct their own universe based on major stock exchanges	MSCI, FTSE350, FTSESS&P, CAC40, Eurostoxx 5000 (MSCI Europe), Nikkei	MSCI World	FTSE 350, EUROTOP 300	MSCI/ FTSE	DJSI/	FTSE	N/A	N/A
No of companies covered (10/100/1,000))	2,700	105 companies (217 production sites)	176	1,500	600	1,800	800 worldwide (look at 30-70 largest in each sector)	600	1,700	770	2,500	1,200	350 company profiles, 200+ screens
Sector exclusion: yes/no/optional	On request	No	No	On request	Yes (for the Ethibel label only)	No	On request	No	No	On request	Yes	On request	Yes
	Desk-based using publicly disclosed information, with additional information from survey responses and other information sources	Desk-based, part on-going dialogue	Self-assessment questionnaire with follow-up company interviews (questionnaire will be partially complete for previous participants)	Desk-based with follow-up company interviews	Part desk-based, part on-going dialogue	Desk-based with follow-up company interviews	Desk-based with part on-going dialogue	Desk-based; no company involvement	Part desk-based and part on-going dialogue	Part-completed questionnaire with desk-based review and on-going dialogue	Part completed questionnaire with follow-up company interviews	Desk-based with follow-up company interviews, plus purchase of??follow-up information	Part desk-based and part dialogue
Company engagement (at outset/during/at end for input or comment)	At outset and during for input	During and at end for comment	At outset and during	Towards end for input and comments	Towards end for input	Towards end for input	Ongoing and at end for comment	No company engagement during assessment	At beginning and at end for comment	During	During for input and end for comment.	During for input .	At end for input and end for comment
QA: Internal/Externa I erification	Internal	Internal	Internal and external	Internal	Internal	Internal and external (one off testing of model only)	Internal	Internal and external (one off testing of model only)	Internal	Internal & External	Internal	Internal	Internal
No of analysts	19	4 core plus graduate researchers	4	18	9	23	10	8	9	10	N/A (see Eiris)	7	3 core and 1 support (also work with 20 mainstream analysts)

Table 8.1 – Summary of key features of interviewed organisations

Table 8.2: Key definitions for discussion

Key definitions	s for discussion
Credibility	For an assessment process to be credible, users need to believe that the information produced is true and accurate. An assessment process that supports credibility would:  • be based on reliable, authoritative sources;  • use an assessment methodology that is appropriate for the intended use – the user needs to sufficiently understand the basis for the assessment methodology;  • present clearly the limitations of scope or coverage;  • be clearly subject to quality control or verification.
Robustness	Analysis must:      be repeatable;     be subject to rigorous quality control;     be based on reliable, authoritative sources;     stand up under scrutiny;     be regularly updated – so that assessment is based on up-to-date information;     be internally consistent, with a systematic approach to every assessment.

### 8.1 Environmental content

The Environment Agency considers that there are a number of aspects which can influence the credibility and robustness of environmental content:

- the relative proportion of environmental to social and ethical content;
- the breadth, depth and specific nature of environmental content;
- the relative balance of actual to synthesised data (synthesised data uses analysis to assign a numerical value to a word or phrase);
- whether the framework of the assessment focuses on key environmental impacts, quality of management controls and/or environmental performance.

We have found that the number of environmental indicators used ranges widely. Generally, it would be expected that a greater number of metrics would reflect greater depth and rigour. In theory more data points imply greater accuracy. Use of greater number of indicators could results in a detailed analysis of a few issues or in a broader environmental perspective. For this reason, it is just as important for users to consider the breath of the assessment when judging its robustness and credibility. The user needs to ensure that the right questions are being asked to suit his or her needs. For example, will 13 specific questions on greenhouse gases and provide the required information on a company? Would three broader questions on general environmental performance be better? The user should not assume that a large total number of metrics is a certain indication of robustness. Metrics still need to cover an appropriately broad set of issues to achieve a robust and credible assessment.

The detail of the assessment in terms of the number of metrics must also be set against the availability of data time allocated per company assessment and the frequency of updates. Typically, analysis based on actual data would tend to be considered important for robustness. Subjective and qualitative assessment is less scientifically rigorous and consistent. It is therefore usually seen as being less reliable, credible and robust. However, subjectivity can lend an important analytical dimension to some aspects of company assessments. This might be the case when assessing the quality and embeddedness of an environmental policy, for example. The factual response can be

'Yes' to a question such as: "Does the company have an environmental policy?" However, a positive score for this metric may not show whether the policy is appropriate, reflects key risks and affects how the company performs. An assessment against these factors demands an element of subjectivity. This qualitative analysis can be useful but t is difficult for an assessment to maximise its robustness and credibility without some quantitative analysis.

A difficulty for this sector is providing a balance between quantitative and qualitative information. A common theme in the interviews was the difficulty in collecting good quantitative data and maintaining its quality and reliability. For users this creates difficulties in making informed choices. Different companies use different amounts of quantitative and qualitative data, and the relative proportion of each is not always clear. For example, the presentation of quantitative data on environmental performance is likely to vary between companies (eg total energy use per tonne of production, total energy use – excluding transportation). Quantitative assessments of environmental performance rely on access to sufficient comparable, numerical or/and quantitative datasets. Environmental performance can be measured by comparing improvements in a single company's actual performance over a number of years. This method is employed by several of the organisations interviewed.

Good quantitative data should form the fundamental framework for assessments. A key on-going priority for rating and ranking organisations which want to show clearly the credibility and robustness of their work should be the identification, collation, maintenance and continual verification of such data. However, where quantitative data is not available, or an aspect of a company's performance cannot be quantified, there is a need for informed subjective analysis. Without this an assessment will be only partially complete. There are recognised techniques for improving the credibility and robustness of qualitative assessments in order to address potential concerns about unsubstantiated subjective opinions dominating analysis. These techniques are discussed in the section below on quality assurance.

To ensure the environmental content is both credible and robust, the methodology must be appropriate for the use to which the assessment will be put. For example, if a user wants to identify companies with a good environmental performance it may not be appropriate to use the outputs of an organisation that only focuses on environmental risk. For this reason, a user needs a firm understanding, ideally from reviewing publicly available information, of the basis of the assessment and of what the outputs are measuring. Clearly the level of quantitative information that may be available and appropriate will also vary according to the purpose of the assessment.

A common message is that a user needs to be able to understand what environmental information is being considered in an assessment and what the outputs measure. Related information may also be helpful, such as the scope of an assessment, the number of metrics and the time allocated to an assessment.

Table 8.3 What information might a user need to assess the credibility and robustness of environmental content?

- · What proportion of the assessment focuses on environmental issues, as opposed to social and ethical issues?
- · What is the scope of the assessment in terms of the breadth, depth and specific nature of the environmental topics covered?
- What proportion of metrics is based on actual data rather than on synthesised data or information from a qualitative/subjective assessment?
- What is the basis of the assessment, eg is it based on risk, on management of risk or on delivery of actual environmental performance or impact?

### 8.2 Industrial coverage

Credibility can be affected by the number of companies that an organisation assesses. If a user is basing decisions on the outputs, he or she will wish to know that the assessment of a top performer is based on a meaningful sample size. It is also important to know which financial exchanges a rating organisation covers. This information helps the user to understand the level of coverage compared to his or her needs. Once again, if the assessment outputs are to be credible they need to be appropriate for their use. A user needs to know whether number and range of companies assessed and the financial exchanges covered are appropriate for his or her specific needs.

During the assessment process, a company's industrial sector can be used in a number of ways: from a basis for exclusion through to a sector-based comparison. Most organisations also have methodologies for assessing multi-sector companies to ensure that the appropriate risks and issues are considered.

Not all users will be interested in exclusion use or sector policies. Some may want a specific company focus, without reference to industry peers. These may be organisations with non-financial or solely ethical interests in a company's performance – such as lobbying groups, NGOs or affected stakeholders–(local communities or employees). In contrast, investors which use sectors in their decision-making may be most interested in comparative or peer ratings.

How can industrial coverage affect the robustness and credibility of the outputs?

- If an organisation uses exclusion criteria, it is important to identify these clearly, particularly where nonenvironmental (or sustainability) factors might result in exclusion.
- Some organisations, but not all, change the scope of the assessment or down-grade scores for sectors that are perceived to have higher environmental risks, such as oil and gas or chemicals compared to for instance consumer goods. It is important for this type of scope change to be understood and communicated to users and the companies being rated. It may at least partly explain some of the apparent fluctuations in relative scores between companies of different sectors. An example from our research illustrates this. Morley Fund Management assesses companies according to management processes and sector risk. It assigned a higher

score to Consumer 1 compared to Utilities 3. The opposite occurred with the scores presented by BiE, which does not have a significant element of sector influence in its assessment.

Coverage of the organisation refers both to financial exchanges and to whether the process is voluntary or not.
 These factors are particularly important for completeness and accuracy. These, in turn, are important for credibility. If an organisation is quoting a best-in-class or best-in-sector rating, a user needs to understand what other companies are in that peer group.

# Table 8.4 What information on industrial coverage might a user need in order to assess the level of credibility and robustness?

- How many companies are assessed by an organisation?
- Which financial exchanges are covered?
- Is the assessment voluntary or involuntary ie does the company willingly participate in the assessment and voluntarily contribute information to the process, or does the rating organisation undertake the rating without the company's involvement?
- Which sectors are excluded from assessment, and how this exclusion is applied? For instance, is exclusion absolute regardless of the relative importance of the activity for the company?
- Is the assessment methodology sectorally neutral or is there weighting to reflect the perceived environmental risk of a sector?

### 8.3 Information and data sources

"The outputs are only as good as the inputs." Even if assessment methodologies are robust and carefully monitored and verified, the use of poor information and data will not produce a robust or credible output. Information sources need to be reliable, independent and authoritative. Organisations use a variety of methods to gather information, including: questionnaires sent to the companies being rated; extensive media searches; engagement with NGOs. So which methods are the most credible and robust?

The sourcing of data and information has been the focus of much media attention in this sector. It causes companies a lot of concern. Questionnaire fatigue is frequently cited as a limitation to the accuracy and completeness of ratings research. However, we are also aware of occasions when rating organisations have relied on publicly available information in an attempt to counteract this problem and avoid requesting large volumes of data from companies. In these cases organisations have then submitted draft assessments to companies for review. If the company does not respond to this draft there is a risk that inaccuracies in the data used will go unchecked, thus negatively influencing the assessment and output rating. Companies can find it frustrating and time consuming to review and correct these draft assessments, suggested changes are not always taken on board by the rating organisation. For example, sector may affect the scope of the assessment. If no account is taken of a change in a company's ownership or a merger between companies in two different sectors, the credibility and reliability of future assessments can be affected. It can also be argued that involving companies in the review of draft assessments removes objectivity and may introduce error. It is important that CER organisations distinguish

between changes suggested to present the company in a better light and those that address factual inaccuracies backed up with evidence. On the other hand, if a company continually inputs into an assessment there are benefits of consistent accuracy and reliability. It is for this reason that many of the organisations we reviewed have opted to engage in some way with the company being assessed.

As we have seen, engagement does not always take the same form or happen at the same stage in the research. Some organisations have more dialogue than others. For example, some organisations establish contact at the outset and maintain dialogue throughout the rating process. They also consult with all sorts of stakeholders, to gather a broad range of views at all levels of the business. Others send a draft profile to the company for review or hold interviews with senior management in the final stages of research. This is to fill in identified gaps and avoid possible guestionnaire fatigue.

CER organisations use engagement and secondary source data gathering to balance the need for independence with the need for reliability. They must try to source independent research based on publicly available information as well as use company data that is authoritative and up to date. Increasingly this has to be achieved without putting repetitive and excessive pressure on companies to supply the information. The recently launched London Stock Exchange project is an important step in helping organisations to achieve this balance by engaging more efficiently with companies they assess. The LSE project attempts to rationalise the questions and information requested by some CER organisations into a single, up-to-date questionnaire for companies to complete.

# **Media sources**

During the research process we noted that some organisations refer to and use standard sources of information but might not make use of adverse media stories. It is clearly important to recognise bias in certain media accounts and exclude those that may be misleading. However it may be risky to disregard all examples of adverse publicity, without considering the message they convey and impact on a company's reputation. If a company rated as a strong performer subsequently appears negatively in the media, the credibility of the rating organisation and its assessment process can be called very publicly into question. A user therefore needs to understand which sources are used as standard, and how negative publicity may or may not affect the assessment outcome.

Sourcing the data in a consistent way is also key to ensuring that each company being rated is subject to the same process. With some of the organisations, it was clear that the data and information sourcing followed a series of defined and repeatable steps. A few organisations, however, appeared to rely more on analysts' experience, knowledge and their views on relevant hot topics. Such expertise has the potential to add value or error. We believe that, to ensure credibility and robustness, the same basic data and information sources should be used as an initial framework for each and every assessment – before an analyst's knowledge is applied. The one exception to this might be for internal investor decisions (such as those made by the investment funds, Morley and Henderson SRI). In these cases, research is tailored to the client's specifications. Identifying certain poor or bad information might automatically categorise the company as a certain risk, thus excluding it from becoming SRI approved.

No one, definitive source or technique can meet all requirements. This is shown by the numerous different approaches to information gathering. It can be argued that increases in robustness and credibility can only be

brought about by the use of multiple information sources. This attempts to achieve an optimum balance and avoid major gaps in the data. Our research suggests that rating/ranking organisations predominantly do use a variety of sources, from structured web searches to information gathered directly from companies. However the number and range of sources are certainly far greater in some methodologies than others. The data and information sources used are central to the ethos of the assessment. They will often be tailored to the needs of a specific user.

Table 8.5 What information might a user need to assess level of credibility and robustness in relation to data and information sources?

- What information sources are used for each company assessment?
- How is information and data validated to assess the level of accuracy?
- What guidance is in place to ensure that the data and information sources referred to are consistent across all assessments?

# 8.4 Assessment methodologies

The assessment methodologies show the greatest variation between the organisations interviewed. These variations largely reflect the different ethos or philosophies of the organisations. They have been developed to achieve desired outputs. Because of the variations and inconsistencies in company results, there have been calls for standardisation across the sector. Our research begs the question as to what this standardisation might achieve, and indeed whether it is required or not. There is great diversity of organisations and products: each focuses in its own way on different aspects of environmental impact, performance or risk. This allows the user to choose the service that best suits his or her requirements. Such choice is characteristic of a thriving marketplace. It also encourages a broad range of views, values and priorities in the investment community. Equally, such a marketplace depends upon information being transparent and accessible to all users. This means that a user needs ready access to the relevant data in a clear, concise and user-friendly manner. For this reason a balance needs to be struck between achieving transparency in CER organisations without biasing research and ratings through the influence of any one standardised ethical or even commercial viewpoint. Also, methodologies are developed to suit a desired output. Standardisation could change the number of applications to which the outputs could be applied. For this reason some variation can be beneficial.

What are the other aspects of assessment methodology that are important for credibility and robustness? A few of the organisations interviewed have employed third parties to review and validate their methodologies. If these independent assessments include making a judgement on the appropriateness of the methodology to achieve a stated outcome, this can be considered to increase the credibility of the methodology.

Table 8.6 What information on an assessment methodology might a user need to assess its level of credibility and robustness?

- What has the assessment process been designed to measure? An understanding of this will allow the user to decide if it is appropriate for his or her own needs.
- Are assessors provided with guidance on how to make valued-based judgements?
- Has the assessment methodology been peer-reviewed by an independent organisation?

# 8.5 Quality assurance

As we discussed earlier in this report, this sector has been criticised for the apparent inconsistency in outputs from different organisations. Our company performance review did identify some potential reasons for some of this variation. However, it was not possible to identify a reason in every case without carrying out a detailed review of every decision made during an assessment.

Strong quality control and assurance should ensure consistency throughout the assessment process. It could provide interested parties with increased confidence in the reliability of the outputs. This has been recognised by a number of CER organisations, as demonstrated by the collaborative project to develop a quality standard. While quality assurance in general is clearly central to a robust and credible assessment, we have endeavoured to identify the aspects that we consider to be especially important. These are:

- Rigorous quality control and checking should prevent errors in assessments and judgements being made in
  final company profiles or scores. This may be either through the requirement for a peer analyst to review
  an initial assessment, through independent third party verification or validation of the assessment and
  content and/or by detailed review by a peer review panel. This independent level of validation is particularly
  important where the assessment relies to a large extent on company self-assessment.
- A quality control process that tracks changes to the assessment methodology. Users and assessed companies with access to these would be able to understand how and why outputs may have altered.
- The use of peer review panels or technical quality boards. This provides regular, independent assessment of how appropriate the assessment methodology is for the desired objectives. Such forums can also review the methodologies to ensure that they consider and apply best practice.
- A defined frequency of review and update of company assessments. This will enable users and assessed companies to know the date of the assessment and thus to see which information/events would have been considered.

However, we need more than the inclusion of guidance documents for questions such as which data sources to include and how to place value judgements. As with any professional service, technical understanding of the issues and the context for the assessment is important. What are the competencies that an analyst requires? Clearly, this is dependent on the methodologies used. However, a standard requirement should be a good understanding and experience of environmental issues and their management in a business context. Also, some methodologies are closely linked to investment decisions and financial performance. For these, an understanding of financial investment and financial analysis is also important. The time allocated to a particular company assessment might also affect quality.

There are recognised ways of improving the credibility and robustness of qualitative assessments, to answer concerns about unsubstantiated subjective opinions dominating analysis. For example, some of the organisations we interviewed have systems in place to correct the weaknesses of qualitative analysis. They do this either by removing or reducing personal opinion or by systematically applying the same set of values to each and every assessment. For example: Some organisations require a second individual to review the entire assessment process and check the judgements made. Such a review may also consider whether all required data/information has been included, whether the information used is sound etc.

Other organisations provide analysts with clear guidance as to what is considered to be a good or bad example.
 During the interviews it was not possible to get examples of all of these guides or rulebooks, but it was apparent that their level of detail varied considerably.

Table 8.7 What information might a user need to assess whether the assessment processes includes the quality assurance elements that provide credibility and robustness?

- Does the organisation have a peer review panel or board to review the assessment processes to
  ensure that they reflect best practice, meet the desired outcomes and are applied independently?
- How are changes to the assessment methodology tracked, documented and communicated to interested parties?
- What provisions for checking or validating assessment decisions are included in the methodology?
- What are the competencies of the analysts? Does this appear to tally with the desired outcomes of the assessment process?
- How frequently are assessments updated? Can extraordinary events or performance be taken into account between assessment reviews?

# 9. Conclusions

Our research has shown that research organisations are still expanding and evolving. In the period of time since this study began, considerable change has occurred: some rating and ranking organisations have merged and new products and services have been developed.

The level and type of information presented by research organisations vary widely. Many of these organisations present relatively little clear, user-friendly information on what is being assessed and how. Some companies and users may find the services of CER organisations interesting and valuable; others may find them confusing and difficult to use effectively.

A significant proportion of research organisations consider environmental performance to be part of a broader assessment of overall sustainability performance. While most assessments do consider environmental issues, the relative proportion of environmental content varies widely. For specialist governance or social assessment providers, it can be little more than a token consideration. For those organisations specialising in environmental performance it may be 100%. This report was commissioned by the Environment Agency, for which the key consideration is a focus on environmental issues. However, many of our findings on the robustness and credibility of environmental content may apply equally to other elements of non-financial performance assessment by CER organisations, which may have a broader or alternative focus.

Assessments draw on many different types of environmental information. Some organisations focus on a few specific topics or issues, which they perceive to be key areas of risk for companies in terms of financial performance. Their assessments look at the control of these issues or risks through appropriate management systems and procedures. Others aim to assess actual environmental performance or the impact of a company's activities. Outputs may appear to contradict each other because they are assessing different aspects of a company's environmental or sustainability risk, management, performance and impact.

The variation in approaches shows that it is not a simple matter to measure and rate companies' environmental risk, impact or management performance, either compared with their peers or more broadly. Company environmental performance can be often more complex and multi-layered than is allowed for in a straightforward 'good practice/bad practice' assessment. A relatively good performance in a low-impact sector, for example, might be considered a poor one in a high-impact sector. This changes the starting point for an assessment, depending on the industry sector. Similarly the absolute quantification of environmental performance is an ongoing challenge. It presents the more fundamental problem of how to measure good and bad performance and judge the difference at the outset of an assessment. What is a measure of environmental performance? Can different sectors be judged on the same issues? How do you reflect differences in company sizes, geographic spread, or in portfolios of businesses and activities?

These are questions which clearly still challenge rating organisations assessing relative environmental performance. Few have fully tackled the difficulties of quantification, or been completely transparent about the limitations of their methods.

There is no one source or type of information used during assessments by research organisations. Sources of information include: public databases; self-assessment questionnaires; company engagement; and regulatory body databases. If only one of these sources of information were used, this might present a biased viewpoint and could compromise credibility. Using a range of sources can improve credibility, by providing a more balanced look at the qualitative areas. It is essential to understand the relative reliability and value of the sources of information used in an assessment. The input data will have a direct bearing on the outputs. For the Environment Agency, the use of quantitative data on environmental performance is the most important indicator in assessing the relative strengths of a rating organisation.

Research organisations do apply a certain amount of subjectivity. In part, this is due to the low level of quantification in information gathered. It is the Environment Agency's view that, in order to reduce this subjectivity and increase credibility, quantitative data should be used wherever possible and supplemented by qualitative data where necessary. It therefore calls for efforts to be made to improve methods and increase levels of quantification in ratings/rankings research and indices. The Environment Agency also recognises that for some environmental issues, high levels of quantification cannot be achieved. It believes that effective and comprehensive assessment requires the development of internal quality assurance processes, which would enable consistent interpretation and repeatable analysis of qualitative information.

When a company is deciding whether to participate in an assessment, or a user is considering relying on outputs, it is vital that there is access to information about an organisation's approach and methodology. Some organisations do not provide this type of information in a clear and accessible format. Straight facts can often be difficult to extract from marketing prose. In other cases, publicly available information is clear and easy use. This shows that a high level of transparency is possible.

The variety of definitions and terminology used by research organisations makes it difficult to compare outputs, not least because different providers assess different aspects of corporate environmental performance.

For all these reasons there have been calls for greater consistency. While some standardisation may be useful, complete harmonisation may not be needed. However, if all research organisations could provide a much greater level of transparency this would give companies and users a better understanding of what CER outputs mean and allow them to match these outputs more easily to their needs. Greater transparency would also help to increase confidence in the credibility of research organisations.

# Glossary of terms

**Best Available Techniques (BAT)**: Procedures going above and beyond legal requirements for environmental and social compliance and diligence.

**Corporate Governance**: The system by which companies are directed and controlled from within. The relationship between all stakeholders in a company, including shareholders, directors and management.

**Corporate Social Responsibility**: Integration of social and environmental concerns into business operations and the interaction with stakeholders on a voluntary basis. Exceeding minimum legal compliance and using BAT.

**Environmental Management Systems (EMS)**: The part of an overall management system that includes organisational structure, planning activities, responsibilities, practices, procedures, processes and resources for developing, implementing, achieving, reviewing and maintaining the environmental policy.

FTSE sector classifications: Aerospace and Defence; Automobiles and Parts; Banks; Beverages; Chemicals; Construction and Building Materials; Diversified Industries; Electricity; Electronic and Electrical Equipment; Engineering and Machinery; Food and Drug Retailers; Food Producers and Processors; Forestry and Paper; Gas Distribution; General Retailers; Health; Household Goods and Textiles; Investment Companies; Leisure, Entertainment and Hotels; Life Assurance; Media and Photography; Mining; Oil and Gas; Personal Care and Household Products; Pharmaceuticals; Real Estate; Software and Computer Services; Speciality and Other Finance; Steel and Other Metals; Support Services; Telecommunication Services; Tobacco; Transport; Water.

**Indices**: Bench-mark against a fixed point (criteria/standard). Company is either included or by reference to a fixed standard Indices often use information from both ratings and rankings organisations.

**Integrated Pollution Control (IPC)**: Regulation of Part A Processes under Part I of the Environmental Protection Act 1990 and the Environmental Protection (Prescribed Processes and Substances) Regulations 1991. A UK-wide pollution control system for industry in which any person carrying out a prescribed process must obtain authorisation from the regulator. Objectives of IPC include:

- the use of BAT to prevent or minimise release of prescribed substances and to render harmless those that are released;
- to ensure consideration of releases from industrial processes to all media in the context of effects on the environment.

Integrated Pollution Prevention and Control (IPPC): The new IPPC regime implements the EU's IPPC Directive in the UK, building on IPC and gradually replacing it. The principle of IPPC is similar to that of IPC: any person operating an installation or mobile plant (as described in the regulations) after the prescribed date must obtain a permit from the environmental regulator and comply with the conditions of the permit. Certain issues are included in IPPC that were not previously included under the IPC Regulations. These include energy efficiency, waste minimisation, vibration and noise.

Investment Funds are fund managers of social, ethically and environmentally responsible investments (RIs).

**Ratings/Rankings:** Ratings use positioning on a scale of relative values and rankings use positioning in order or sequence, usually numerically or alphabetically. A ranking is derived from a series of ratings. Research and positioning are combined to constitute ratings, ie rankings can be seen as part of the products/services of ratings agencies. Therefore, these two categories will be combined throughout the review.

**Socially Responsible Investment (SRI)**: The integration of personal values and ethical concerns with investment decisions. Considers both the investor's financial needs and the impact of investment on society.

**Transparency**: The degree to which information regarding environmental and social policies and practices within business operations are made available to the public, and the way in which they are reported.

**Triple Bottom Line**: Including environmental, social and financial aspects of business and acknowledging the interaction of these aspects.

**Verification**: A process of review to determine the accuracy of information contained within the index, ranking or rating. Conducted either by an internal department or an external independent body.

# References

ABI (2004) Risk Returns and Responsibility

Author unknown (2004) Rating agencies will submit to new standard. Ethical Performance, p5

Author unknown (2003) How to win friends and influence people. Governance 113.

Author unknown (2001) Rating the environmental raters. ENDS Report, 313, pp19-22

Baue, W (2002) 'SRI ratings need greater independence and standardisation, says new Dutch guide.' From www.socialfunds.com

Baue, W (2003) Corporate Social Responsibility Rating agencies Balance Standardisation and Differentiation. From <a href="https://www.socialfunds.com">www.socialfunds.com</a>

Baue, W (2004a) Report on SRI Research Organisations Characterised as Valuable but also Controversial. From www.one-report.com

Baue, W (2004b) Welcome to the jungle – CSR Questionnaire Incompatibility Hampers Applicability. From www.socialfunds.com

Butz, C (2003) Can doing good benefit the wallet and the conscience? Financial Times, 15 December 2003

ERM (2001) Rating the Raters Briefing Document

Haurant, S (2004) Ethical Investment 'gains momentum. The Guardian, 2 February 2004

(date unknown) Carbon cuts make top of league. Industrial Environmental Management

SustainAbility Mistra (2003) Value for Money. Reviewing the Quality of SRI Research

Targett, S (2003) Race to start governance index. Financial Times Fund Management. 15 December 2003

WestLB Equity Markets (2004) Insurance and Sustainability: Playing with Fire

# Annex A – Screen 1 information

Indices , Ratings and Rankings	Website	Coverage	Category	Comments (including environmental content)
ACCA – Association of Charted Certified Accountants	http://www.accaglobal.com	UK	Other	ACCA operates an award process for corporate sustainability reporting on an annual basis. Often used by organisations as a judgement of a businesses performance/disclosure.
Avanzi	http://www.avanzi-sri.org	Italy / Europe and North America	Ratings/Rankings	A number of services including SIRI Pro a rating tool focusing on environmental, social and corporate governance criteria
Bank Sarasin & Co. Ltd	http://www.sarasin.ch	Europe	Investment Funds	Environmental and social criteria
Business in the Community	http://www.bitc.org.uk/programmes/programme_directory	UK	Ratings/Rankings	Business focused organisation that has developed two rating programmes one (Business in Environment) that focuses on environmental management and performance and a second (Corporate Responsibility Index) that covers broader CSR issues.
CarBen (WS Atkins)	http://www.wsatkins.co.uk/wsainternet/skill s/environmentalservices/environmentalcon sultancy/climatechange/bench- markingyouremissions/	UK	Other	A rating system developed to bench-mark on climate change performance and issues.
Carbon Disclosure Project	http://www.cdproject.net/	UK / Worldwide	Other	Greenhouse gas emission information  Does not fit into any one category – most closely aligned to an index
Centre for Economics and Business Research Ltd (CEBR)	http://www.cebr.com/	UK	Other	Little information available.
Centre Info	http://www.centreinfo.ch/en/	Switzerland / Europe	Ratings/Rankings	Organisation provides research and advice on corporate responsibility based around SIRI profile. Covers environment, social and corporate governance.
CoreRatings (see also GRM)	www.coreratings.com	France / Europe	Ratings/Rankings	Rating agency with two key products, research and ratings. Consider corporate governance, social and environmental management.
Covalence	http://www.covalence.ch/	Switzerland/ Worldwide	Ratings/Rankings	Focus on ethical performance Includes environmental criteria
CSE — Centre for Science and Environment	http://www.cseindia.org/	India	Ratings/Rankings	Broad science and environmental organisation that is running a "Green Rating Project" focusing on environmental criteria for various sectors and bench-marking performance of Indian companies.
CSR Japan Research Institute	www.csrjapan.jp	Japan	Other	Includes environmental issues.  No further information readily available to determine category
Deminor Ratings (see also Fortis Investment)	http://deminor.org/	France	Ratings/Rankings	Rating approach that focuses on corporate governance criteria.
DJSI — Dow Jones Sustainability Indices	http://www.sustainability-index.com/	Switzerland / Worldwide	Index	Listing index covering broad sustainability criteria including environmental management
Domini Social Index	http://www.domini.com	Worldwide	Index	Investment organisation that applies social and environmental screens to investments. One key product is Domino 400 Social Index that considers environmental issues as well as product and elements of social
Dresner Funds	http://www.dresnerco.com/	Worldwide	Investment Funds	Investment bank that provides investor relations and communication programmes through a Corporate Services Department.
DSR - Dutch Sustainability Research	http://www.dsresearch.nl/dsr/	The Netherlands	Other	Information not readily available

Indices , Ratings and Rankings	Website	Coverage	Category	Comments (including environmental content)
Eiris - Ethical Investment Research Service	http://www.eiris.org/	UK / Europe	Ratings/Rankings	A research organisation focusing on environmental and social criteria to help organisations to assess relevant performance of businesses
Environment Agency Awards	http://www.environment-agency.gov.uk/	UK	Environment Agency	Award programme run by the Environment Agency
Environment Agency - OMA - Operator Monitoring Assessment	http://www.environment- agency.gov.uk/commondata/105385/omag uidev2.010703 199726.pdf	UK	Environment Agency	Assessment process to determine robustness of monitoring techniques and procedures.
Environment Agency - OPRA - Operator and Pollution Risk Appraisal	http://www.environment- agency.gov.uk/business/ 444217/444661/444671/466170/411964/?l ang= e	UK	Environment Agency	Assessment process to determine the level of environmental hazard from an industrial facility and the effectiveness of the management of process and environmental issues.
Environment Agency - PI - Pollution Inventory	http://www.environment- agency.gov.uk/business/444255/446867/2 55244/255263/?lang= e&theme=&region= &subject=&search for=	UK	Environment Agency	An annual record of pollution in England and Wales from activities regulated by the Environment Agency.
Environment Agency - Spotlight	www.environment-agency.gov.uk/ business/444255/518536/?version=1⟨ = e	UK	Environment Agency	Environment Agency initiative, looks at company environmental performance based on monitored emissions, reductions and fines/prosecutions
Ethibel (Stock at Stake)	http://www.ethibel.org/subs_e/6_stock/main.html	Belgium, Luxembourg, Japan, Hong Kong, Singapore	Index	Organisation that undertakes research covering environmental and social performance and has also developed an index (Ethibel Label)
Ethiscan	http://www.ethiscan.ca/	Canada	Other	Ethics consultancy providing tools and research. This work includes company reports that discuss environmental, social, corporate governance performance
Etikanalytikerna		Sweden	Ratings/Rankings	Analysis company that focuses on ethical criteria.
Fortis Investments (see also Deminor Ratings)	http://www.fortisinvestments.com	Worldwide	Investment Funds	Investment assess management organisation that includes CSR criteria. Fortis Investment and Deminor Rating have signed a pan-European co-operation agreement in relation to CSR proxy voting.
FTSE4Good Index Series	http://www.ftse.com/ftse4good/	UK / Worldwide	Index	Published index that includes companies that have satisfied certain requirements relating to environmental, social and corporate governance systems.
Fundacion Ecologica y Desarrollo	http://www.ecodes.org	Spain	Other	Organisation that works to improve the environment by analysing and communicating information. Covers primarily environmental issues.
GES Investment Services(formerly Caring Company)	http://www.ges-invest.com/(formerly http://www.caringcompany.se/)	Sweden / Europe	Index	An analysis house using Global Ethical Standard for assessment that focuses on human rights, business ethics and environmental issues. Ethos focuses on identifying companies not compliant with international norms for exclusion.
GMI - Governance Metrics International	www.gmiratings.com	Worldwide	Ratings/Rankings	Global corporate governance agency that focuses on governance issues but includes small elements on environmental issues in company assessment.
The Good Bankers Co., Ltd	http://www.goodbankers.co.jp/	Japan / Worldwide	Other	Provides variety of services including research into environmental and social performance of companies to assist in assessment decisions by third parties.
Good Corporation	http://www.goodcorporation.com/en/	UK	Other	A standard that has been designed to help organisations to develop, manage and monitor their corporate responsibilities. Provides framework and minimum criteria for full members, compliance with which is assessed through verification.

Ladiana D. C.				0
Indices , Ratings and Rankings	Website	Coverage	Category	Comments (including environmental content)
Henderson Global Investors - Sustainable and responsible investment	www.henderson.com	UK, Europe	Investment Funds	Investment managers that include environmental and social criteria for certain funds.
Impax Environmental Technology (ET50) Index	http://www.impax.co.uk/asset/et50.htm	UK / Worldwide	Index	Index dedicated to organisations that have a core business in developing and operation of environmental technologies.
IMUG - Institut fur Markt-Umwelt Gesellschaft	www.ethisches-investment.de/	Europe - predominantly German	Ratings/Rankings	Organisation that conducts corporate research using social and environmental criteria.
Innovest - Strategic Value Advisors	http://www.innovestgroup.com/	US / Worldwide	Ratings/Rankings	Agency that assesses business performance across the areas of environment, social and corporate governance.
Invesco Perpetual - fund managers	http://www.invescoperpetual.co.uk	UK / Europe / Asia	Investment Funds	Fund managers who apply elements of environmental and social assessment but little information readily available.
IRRC - The Investor Responsibility Research Centre	http://www.irrc.org/	US / Worldwide	Other	Research organisation providing information on corporate governance and social issues affecting investment. Have developed rating tools to help clients to make investment decisions.
ISIS - Asset Management	http://www.isisam.com/PrivateInvestors.as p?pageId=5.3	UK / Europe	Investment Funds	Management of bonds and investments with companies being assessed for social and environmental management prior to inclusion in their Approved List.
Jupiter	http://www.jupiteronline.co.uk/	Worldwide	Investment Funds	Asset management that includes consideration of environmental, social and ethical criteria
Kempen/SNS Smaller Europe SRI Index		UK / Netherlands	Index	No further information readily available
KLD Research and Analytics, Inc.	http://www.kld.com/	US / Worldwide	Index	Organisation that provides social investment research and other services. Also the developer of a online social research database and the KLD Domini 400 Social Index, which has since been established as a separate entity.
MJRA - Michael Jantzi Research Associates Inc.	http://www.mjra- jsi.com/about.asp?section=1&level 2=0≤ vel 3=0	Canada	Ratings/Rankings	Social investment research, in particular through its in-house database, which contains social and environmental profiles of companies.
Morley Fund Management - Sustainable Futures Funds	http://www.morleyfm.co.uk/	UK / Worldwide	Investment Funds	Investment fund that uses environmental and social criteria for inclusion
Morning Star Japan KK	www.morningstar.co.jp/sri	Japan	Other	Limited information available in English.  No further information readily available to determine category
The Natural Step	http://www.naturalstep.org/	Sweden / Worldwide	Other	A sustainability management standard
oekom Research AG	http://www.oekom.de/index_english.html	Germany / Worldwide	Ratings/Rankings	Organisation that bench-marks performance and management of social and environmental issues.
PERFORM - Sustainability Performance Bench- marking	www.sustainability- performance.org/index.php	UK /Europe	Other	Research project developing environmental performance metrics and undertaking the collation and presentation of associated data. No rating or ranking is performed on this data.
PIRC - Pension Investment Research Consultants	http://www.pirc.co.uk/	UK / Europe	Ratings/Rankings	Provide rating and ranking with a primary focus on corporate governance including environmental management elements
REMAS	http://remas.ewindows.eu.org/index.htm	UK	Environment Agency	Europe-wide study to measure benefits of formal environmental management systems (EMS) used by businesses

Indices , Ratings and Rankings	Website	Coverage	Category	Comments (including environmental content)
Salter Baxter / Ecocontext	www.salterbaxter.com	UK	Other	A combined corporate reporting bench-marking survey.
SAM - Sustainable Asset Management	http://www.sam-group.com/	Switzerland / Worldwide	Investment Funds	Asset management company that also performs sustainability research for DJSI.
Scoris	http://www.scoris.de/	Germany / Worldwide	Other	Predominantly a research body considering sustainability research criteria.
SERM Rating Agency (formerly known as Safety and Environmental Risk Management)	http://www.serm.co.uk/	UK	Ratings/Rankings	Organisation that provides company assessments focused on management of key social and environmental risks.
SIRIS - Sustainable Investment Research Institute	http://www.siris.com.au/	Australia	Ratings/Rankings	Independent research group providing sustainability profiles on company performance.
SiRi - Sustainable Investment Research International Group	http://www.sirigroup.org/	Europe, North America, Australia	Ratings/Rankings	SRI research and consulting services that considers environmental, social and governance issues. Information presented in profiles
SIRS - Social Investment Research Service	http://www.socialinvestment.ca/Additional Advisory Services/SuzanneFallender.htm	US	Ratings/Rankings	Provision of screening research covering environmental and social issues.
Standard and Poors	http://www.standardandpoors.com	Worldwide	Ratings/Rankings	As part of its services produces Corporate Governance Score reports and ethical fund data.
Triodos Advisory Services	http://www.triodos.co.uk	Netherlands / Europe	Ratings/Rankings	Provider of investment research and consulting on corporate sustainability and SRI including ranking of companies in sectors.
Trucost	http://www.trucost.co.nz/	UK	Ratings/Rankings	Mainly environmental criteria
Verite	http://www.verite.org/	US / Worldwide	Other	Social auditing organisationthat publicly review results that could be used in investment decisions. Does not include environmental criteria
Vigeo (formerly Arese - Agence de Rating Social et Environmental sur des Entreprises)	http://www.arese-sa.com/	UK/Europe	Ratings/Rankings	Provides CSR rating products that have a CSR focus, including environmental criteria.
Wind Fund (Friends of the Earth)	www.windfund.co.uk	UK / Europe	Other	Ethical investment fund investing in small scale renewable energy projects. Recently become part of Tridos Bank.
WWF - World Wide Fund for Nature Ethical Investment	www.wwf.org.uk	UK	Other	They guide their investments away from companies that conflict with their environmental concerns. Certain companies (specifics not given) are excluded completely from being invested in. 10% of funds are put directly into ethical funds and the environmental impacts of the companies that they invest in are discussed through a questionnaire. WWF utilise the services of Eiris.

# Annex B – Organisation profiles

EIRIS (ETHICAL INVESTMENT RESEARCH SERVICE)		
Key Information		
Website: http://www.eiris.org/	Launch Date: 1983	
Geographical Coverage: UK, Europe, North America, Asia Pacific	<b>Ownership</b> : Owned by a charitable foundation and is registered as a charity. Does not invest or campaign and is a non-profit organisation.	
Category: Ratings research	<b>Financial Universe/ Exchanges:</b> FTSE All-share (Eurostoxx, various national indices, MSCI World 90% estimated). 2700 companies.	
Content: Sustainability including environmental, corporate responsibility, social and ethical	<b>Description/Product:</b> Independent sustainability and corporate responsibility research.	

# **Philosophy**

# **Background**

Established purely as a research body, Eiris does not provide investment advice, financial advice or consulting as they consider these to be in conflict with their research work. Provide research to a wide range of clients (see Audience); do assign scores to individual elements but do not roll up the scores. Focus of the research is identifying effectiveness of management process for key areas of risk.

# **Exclusions Policy**

No exclusion policies - researches on arms, alcohol, gambling, tobacco, pornography, animal testing - both negative and positive screening undertaken.

#### **Audience**

Majority of clients in the UK. Main clients include pension funds, asset managers, charities, indices and some multilateral organisations.

# **Memberships and Partnerships**

Set up the FTSE4Good family of indices in association with FTSE Group and remains the research provider for FTSE4Good. EIRIS works with research partners in 8 countries: Avanzi (Italy), CAER (Australia) Fundacion Ecologica y Desarrollo (Spain); Stock at Stake (Belgium); Good Bankers (Japan); Imug (Germany); IRRC (USA); Ethifinance (France).

# Inputs

# **Sources of Information**

- Annual company social, environmental and ethical reports – environmental performance data from environmental reports, company websites and survey responses. Summary assessments are available for companies (not the raw data);
- Annual questionnaire/survey;
- Media reviews; dialogue with companies; independent/external sources including regulatory authority databases where available; and
- Other publicly available information

Typically all FTSE 100 companies respond to the survey and of the other 2600 companies 42% do (the response rate from large caps is higher and from small caps it is lower). If a company doesn't respond and the availability of information on the web is good an assessment can and will still be undertaken.

# Information/Metrics

**Environmental Sector classifications:** 

Generally use the FTSE sectors. One particular company can be assigned to up to three sectors. This is based on turnover (15% rule). There is scope for adjustment, however, and Eiris can reclassify sectors if needed.

Generic approach covers approximately 100 total criteria over four clusters including social, environmental, governance and areas of specific ethical concern. 35 of these are specifically environmental.

Environmental research areas environmental policy, environmental management systems, environmental reporting, environmental performance, biodiversity, greenhouse gases, mining and quarrying, nuclear power, ozone depleting chemicals. pesticides, pollution convictions, PVC and phthalates, tropical hardwood and water pollution.

# **EIRIS (ETHICAL INVESTMENT RESEARCH SERVICE)**

#### **Process**

#### Methodology

EIRIS categorises environmental sectors as HIGH, MEDIIUM or LOW based on risk of typical direct and indirect impacts associated with the activities. The risk category of a sector determines the level of research that might need to be performed, for instance a lower requirement is set on low risk sectors.

The companies' environmental performance is researched based on four key areas environmental policy, management systems, reporting and performance (direct and indirect).

Eiris uses sector guidance when analysing companies particularly in terms of the scope of the research. This guidance was developed by the environment team and is constantly reviewed (last revised a year ago).

Eiris ask to see evidence of, for example, the management system when companies are responding to the questionnaire ie they do check that appropriate plans are in place etc.

# **Quality Assurance and Verification**

# Assurance:

Quality control procedures are in place which include checking aspects such as:

- All data before it goes out to companies.
- Monthly audit and information.
- Quarterly quality review in place includes a check of a sample and approval system is daily. (6 week promise means that information is updated within 6 weeks from date of receipt).

Eiris also have a training and complaint system in place and are currently commissioning an audit.

# Analysts:

Eiris have 19 in-house analysts with experience in environmental, governance and social areas. They are split into three teams covering 1100 companies in total with each analyst covering approximately 60 companies. All research/assessment work done by a researcher will be reviewed by a second person.

#### Verification:

No external verification of research or research methodology has been performed, although an audit of their processes is to soon be commissioned. However, one client has performed an audit of the process.

# **Outputs**

# Score/rating

Not applicable

# Reports

Company profiles include information on main activities, sector issues, corporate governance, environment, human rights, supply chain, employee issues.

#### **Update / Review**

Regular review and update. The information in the Ethical Portfolio Manager is updated every week. Eiris send companies full reports detailing the data held on them on an annual basis.

# **Products and Services**

Eiris produce a variety of reports and Ethical Investment Guides. They undertake independent research into social, environmental and ethical performance of companies as a tailor made service to match clients' social and environmental concerns and chosen ethical criteria. This involves constructive dialogue with companies. They have also produced a software tool, Ethical Portfolio Manager and a website.

Data is also provided to clients which do not use Ethical Portfolio Manager. Research is available to all clients (briefing papers, research papers, and a monthly newsletter)

#### Cost

Charging structure is determined by:

- Geographical region required (1-4),
- Depth of information required etc.

Ethical Portfolio Manager (EPM) is charged within quite a broad pricing structure depending on the level of information a client requires.

# **EIRIS (ETHICAL INVESTMENT RESEARCH SERVICE)**

# Other information

Cover 2600 companies globally (large and medium caps). Cover approximately 700 UK companies and 1300 European companies.

Eiris are aiming to develop a new set of criteria based on sectors that will give a more in depth analysis of companies' process and product environmental impacts.

For example, within the oil and gas sector, Eiris aims to determine how carbon intensive a company is, as well as examining investment in renewable energy and devising ways to assess companies' progress within the sector.

# **Differentiators**

- 1. Financial and organisational independence.
- 2. Do not assign a final score to companies.
- 3. Breadth and depth of research.

#### **PERFORM Key Information** Website: http://www.sustainability-Launch Date: 2000 performance.org/ Geographical Coverage: UK and EU (open for Ownership: An independent research project conducted by SPRU - Science and Technology Europe, but data collection is focused on the UK) Policy Research at the University of Sussex in collaboration with the Centre for Research in Innovation Management at the University of Brighton and the RSA Environment Forum. Category: Other Financial Universe/ Exchanges: n/a **Content:** Social and environmental Description/Product: Provides bench-marking services, statistical analysis into sustainability performance bench-marking service and sustainability management tools.

# **Philosophy**

# **Background**

The MEPI Project was the background project from which PERFORM originated. This earlier project focused on environmental performance during 1997-1999. It included approximately 300 companies within a few sectors in 6 European countries.

PERFORM has developed the MEPI methodology further. PERFORM is aiming to develop KPIs for certain sectors and sub-sectors and gather and publish the quantitative information for these KPIs. No overall rating is given by PERFORM although it is hoped that the data will be used by third parties for such assessments and to help companies understand their performance relative to other organisations.

# **Exclusion Policy**

No exclusion policy

#### Audience

Main audience for the bench-marking are companies themselves. Data will also be used for statistical analysis that will be of interest to policy, NGOs and academics.

# **Memberships and Partnerships**

PERFORM's advisory panel has members for example from DTI, Defra and Environment Agency.

# Inputs

# **Sources of Information**

Environmental and social reports, EMAS statements and the Environment Agency Pollution Inventory data. PERFORM also use the IPPC European database. The company under scrutiny also contribute some of the data.

#### Information/Metrics

Sustainability performance indicators address the following areas: environmental performance (air emissions, water emissions, energy and resource input, waste environmental management), social responsibility performance (employment, health and safety, training and education, equal opportunities and economic community), and performance (turnover, profit, return to capital and labour productivity). PERFORM uses 16 environmental performance indicators, 7 social responsibility performance indicators and 3 economic performance indicators.

On average a further 8-9 sector-specific indicators are used for each industry included in the study.

The analysis will only look at standard indicators and nothing beyond them.

PERFORM originally wanted sectors suitable for their methodology and sectors with a strong environmental profile (mostly manufacturing). During the early stage of the project consultation with organisations such as trade associations, they identified the 14 current sectors currently presented on the PERFORM web site. However it is recognised that some of these sectors may be dropped out as the data / information from them may not be sufficiently comprehensive.

PERFORM always need a production figure to normalise environmental indicators, which can limit the use of some data sources.

#### **PERFORM**

#### **Process**

#### Methodology

Initially, PERFORM review all possible indicators including sector specific ones. They cross check these indicators against reports and undertake several consultation rounds with Trade Associations etc. The selection of indicators is made based on all publicly available information and data.

Data collection is continuous and is collected both at site and company level. So far 105 companies (including subsidiaries and business units) and 217 production sites have been analysed. Results are sent out to companies that have taken part shortly after data was submitted and participants are given the opportunity to feedback.

PERFORM also engage with companies directly and use online interactive bench-marking to help in the data collection.

# **Quality Assurance and Verification**

Assurance:

The Advisory Panel has members from DTI, Defra and Environment Agency. PERFORM has an internal checking procedure in place ie with each of its analysts reviewing and verifying another's findings. In addition they check against the company itself, and the questionnaire requests disclosure of the % of data and information that is verified in the report.

# Analysts:

The team consists of 4 core members in addition to a number of graduates researchers, who are all environmental in focus but have a diverse academic background.

#### Verification:

No third party verification of the process or data is currently performed.

# Output

# Score/rating

No score or rating is produced. PERFORM aims only to identify and list key indicators and plot company's performance against them as objectively as possible.

# Reports

Companies that provide the project with data about their sustainability performance will receive a bench-marking report. This Sustainability Bench-marking Report will show for each indicator how a company compares against others in the same sector. Depending on the data available, the report may also provide information about trends over time and technologies used.

# **Update / Review**

Data and information collected on an annual basis.

# **Products and Services**

Bench-marking: Companies in 14 industrial sectors are compared with their competitors on social, environmental and economic performance data.

Tools: Sustainability management tools are developed to help companies use the benchmarking data in the management of their sustainability performance.

Analysis: Statistical analysis of company data can identify patterns, trends, and drivers of sustainability performance in industry

A separate part of the PERFORM project is currently investigating the practical value of the information collected for the company concerned.

# Cost

No cost applies

# Other information

PERFORM is aiming for a more active European inclusion.

Also aim to keep the project running and are considering diverse funding options.

#### **Differentiators**

- 1. Perform aims to develop tools that can help companies to manage their sustainability performance more effectively.
- 2. The indicator set includes commonly used social and environmental KPIs from a broad number of UK and international organisations.
- 3. Perform publishes data on individual companies (although giving the option of providing data anonymously).

#### **Key Information** Website: Launch Date: 1997 http://www.bitc.org.uk/programmes/programme\_d irectory/business in the environment/ Geographical Coverage: mainly UK (but also Ownership: Private – affiliated to Business in the including egeg FTSE listed companies reporting Community on their world-wide operations) **Category:** Rating (voluntary participation) Financial Universe/ Exchanges: FTSE 350, sector leaders from the Dow Jones Sustainability Index, and the larger BITC members. Total universe invited to participate: approx. 500 companies (BITC have a total of 700 members, of which the larger ones, approx. 250, are invited to participate in the BiE Index). 176 companies participated in latest survey. **Content:** Environmental **Description/Product:** Company rating index environmental management focused on processes.

# **Philosophy**

# **Background**

The BiE Index was originally developed to provide a bench-mark of corporate environmental engagement across UK industry. Initially it considered management processes only, but over the last 4 years it has started to expand to consider also performance. In 2000 a compulsory performance section was added to the management section of the survey. This new section still focuses mainly on processes, and captures a company's level of measuring, reporting, target setting, and performance improvement in four key impact areas (only in terms of systems for measuring performance - not actual performance).

The BiE Index is seen by BITC as an important mechanism for engagement, and it highlights both good and poor performance. The survey aims to prompt in-depth engagement both internally and externally on the environmental issues affecting companies and through this process, to help facilitate continual improvement in environmental management.

In 2002, a broader Corporate Responsibility Index was launched which includes the environmental questions of the BiE Index, but also considers additional marketplace, workplace and community issues in the bench-marking process.

This review has focused only on the stand-alone Business in the Environment Index. BiE consider that the process of completing a survey adds value by prompting internal engagement. For this reason BiE requires that all companies fill in a survey, even with information that can be sourced on their website.

#### **Exclusions Policy**

All companies (from the above-defined universe) are invited to participate; no sectors are excluded.

#### Audience

Institutions, companies, NGOs and public.

# Memberships and Partnerships

The BiE Index was developed and is regularly reviewed in close consultation with the business community, led by the BiE Leadership Team and Practitioners Group, both of which include representatives of 16 committed companies.

In addition, BiE are working with third parties such as Earthwatch, English Nature, the Carbon Trust and Wrap to help develop the questionnaire both in terms of continual improvement and expansion, eg to cover additional environmental topic areas such as resource productivity.

# Inputs

# **Sources of Information**

Annual self-assessment questionnaire that participating companies are required to complete. As part of the survey, participants are required to provide additional supporting evidence as appropriate. Submissions are also reviewed against relevant public reports, such as companies' annual environmental/sustainability reports. Finally, validation and follow-up result in direct company engagement through face-to-face meetings or telephone interviews.

#### Information/Metrics

The questionnaire contains 15 questions, with a number of sub sections. 12 cover environmental management processes including assurance, and 4 cover environmental performance processes.

In the environmental performance section of the survey, organisations are required to complete 2 core areas: Global warming or Energy & transport, and Solid waste, with the remaining 2 being selected by the company from a selection of ten key impact areas. This is designed to enable companies to focus on those issues most material to their sector. BiE undertakes some checking of the appropriateness of the areas chosen during validation.

Key survey questions require companies to state the business coverage of their activities. For example participants are required to state the proportion of the business that is covered by their environmental audits, targets, data and other information given in the survey.

# **Process**

# Methodology

Participation in the BiE Index is free and voluntary. Self-Assessment Questionnaires are sent out, and the survey is filled in online. Companies are given a unique and confidential user name and password. The data is captured by the IT system, which creates a spreadsheet of company data and scores.

Upon receiving the completed questionnaires, BiE goes back to companies with follow-up queries as necessary (via phone calls and/or e-mails). BiE emphasise the need for this kind of engagement to ensure reliability of results and consistency within the review process. BiE therefore asks for the internal company contact responsible for completing the questionnaire to be identified, in order to facilitate this. In 2003 nearly all participants were contacted either by phone or e-mail, and asked to provide further evidence/clarifications as required.

In addition, BiE always carry out random validation visits to add a further level of assurance - for the 2003 survey 18% of respondents were visited as part of this process.

These validation visits form an integral part of the Index process, and serve as a reality check for both the company and BiE. Visits are used to evaluate the completeness, accuracy and significance of survey responses, and particular focus is given to queries or inconsistencies identified during the review. The validation process is intended to be a constructive and positive exercise, and also provides participants with the opportunity to ask questions about the methodology, etc. Company visits are conducted at random, but within this BiE aim to cover all sectors.

Weighting for the environmental index is as follows: 45% management, 45% performance and 10% assurance. Within these, each question is weighed equally (except for supply chain and environmental stewardship) and the totals for each question are simply summed to provide the overall score.

At the end of the process, participants receive a detailed, company specific feedback report, which bench-marks their own performance in the different survey questions against the performance of other companies in their sector, and against the overall Index averages.

# **Quality Assurance**

Quality assurance occurs at a number of levels:

Completed questionnaires are only considered valid if signed off as being accurate by a company's Chairman, Chief Executive or Board Director responsible for the Environment.

The interviews during these visits aim to cover a company's whole survey submission to ensure completeness, reliability and accuracy throughout, and consistency within the review process. Particular focus is placed on survey responses identified during the review as areas in need of further clarification/supporting evidence.

All submissions are reviewed and checked against supporting evidence provided as part of the survey, and against relevant public reports, such as companies' annual environmental/ sustainability reports. The first five submissions are usually reviewed by each analyst independently, and results are then compared to ensure consistency in review. A member of the team and the team leader reviews thereafter all submissions.

A proportion of respondents are subject to validation visits.

#### Analysts:

The BiE team comprises 4 key individuals who conduct the review process, all of whom have a scientific and business background.

#### Verification:

A third party (Arthur D Little in 2003) undertakes an audit of the Index process, taking samples of submissions and following the process in its entirety (from review and assessment of submissions, to collation and manipulation of data, to final scoring and ranking of companies). The scope of validation covers the entire Index process, excluding however actual company visits.

# **Outputs**

# Score/rating

The public index ranks all companies individually (according to their overall BiE score), except for companies scoring greater than 95%, which are grouped at the top, alphabetically, as "Premier League".

Rating is also provided on a comparative basis by sector, where sectors are defined following FTSE classification criteria.

# Reports

8th Index of Corporate Environmental Engagement report: details results of the 8th BiE Index. Includes full company rankings, both overall and within their sector, and in-depth analysis of the results.

The Executive summary of this annual index report is published and available free on the web. Case studies and details of recent research and publications/ surveys are also available on the website.

Confidential reports provided to participating organisations as part of the feedback process: these identify scores assigned to each element, and compare company scores with average sector and Index scores.

#### **Products and Services:**

BiE also provide (for a fee): 1. Bench-marking Plus services, for participants who wish to receive a more detailed feedback report on their Index performance, including egeg trend analysis (not available for new entrants), best practice examples by sector, and recommendations for possible next steps. 2. Index shadowing services, for companies which do not yet wish to participate on a public basis, but would like to shadow the Index on a confidential basis instead. Companies signing up for this service follow the entire Index process, and receive a detailed feedback report (including the hypothetical ranking they would have received in the last public Index).

# **Update / Review**

Process is performed annually. The assessment process, including the questionnaire, has been subject to review since its launch, partly to raise the requirements and thus help facilitate continuous improvement in environmental management and performance. Note that the questionnaire has not been significantly changed over the last couple of years to enable meaningful comparison of performance over a period.

# Cost

£35 per copy of published annual index report (for the 7<sup>th</sup> BiE Index report). The 8<sup>th</sup> BiE Index is covered in a combined report together with the 2<sup>nd</sup> Corporate Responsibility Index. The cost of this combined report is £70 per copy.

# Other information

BiE has started a review of the Index. They have also recently carried out a consultation exercise involving all 2003 Index participants and non-participants. <u>mailto:</u>A possible way forward could include additional questions on indirect impacts, a more sector-specific approach, and an increased focus on capturing/bench-marking actual environmental performance.

However, further work is required on this to identify the most appropriate manner in which to deal with quantitative data.

#### **Differentiators**

- 1. Business in the Community (BITC) is a business-focused and business-led organization, which is prepared to work inclusively with any business prepared to make a commitment to improve its impact on society.
- 2. Business in the Environment (and the BiE Index) forms only one part of BITC's approach to encouraging and supporting companies in improving their impact on society so the BiE Index is complemented by (for example) a broader Corporate Responsibility Index and other BITC programmes addressing community, workplace, marketplace and environmental issues.
- 3. As a self-assessed but independently verified and scored measure of where companies are in managing their environmental impacts, a significant feature of the BiE Index is the way its company-specific feedback can be used by companies internally to increase awareness and engagement, and encourage performance improvement.

# **CORERATINGS**

#### **Key Information**

Website: http://www.coreratings.com/

**Geographical Coverage:** European focus – particular strengths in UK, Scandinavian and French companies, and Large Cap Global Sectors.

Launch Date: 2000 (previously called GRMS)

**Ownership**: Private. Wholly owned by Fimalac, which also owns Fitch Ratings, the world's third largest financial rating agency.

Category: Rating/Ranking

Financial Universe/Exchanges: 1500 companies profiled. Particular focus on FTSE 100, Eurotop 300, Scandinavian large and mid cap, and large cap US, Japanese and Asia Pacific stocks. Also bespoke coverage of over 850 emerging market and small/mid cap companies.

**Content:** Environmental, employment, social and governance/business ethics criteria.

**Description/Product:** Research into investment risk to generate ratings by company as well as facilitate engagement. Engagement based around a structured product, which utilises a real-time online database.

# **Philosophy**

# **Background**

The philosophy of the service is to assess and rate organisations based on their ability to manage key corporate responsibility risks, which CoreRatings considers could impact on the company's financial performance. Much of the focus is therefore on assessing the quality of management systems in place.

# **Exclusions Policy**

CoreRatings' approach is to highlight exclusionary criteria based on client requirements, egeg alcohol, pornography, tobacco, military, gambling and nuclear power.

It also provides a Shariah screening on client request.

#### **Audience**

Investment houses and pension funds.

#### **Memberships and Partnerships**

CoreRatings is a member of both UKSIF and Eurosif and is looking at potential partnerships with organisations that provide synergies.

# Inputs

#### **Sources of Information**

Typically source information from about 20 different key sources including company reports (annual, HSE & CSR) and media sources (stakeholder sites etc). The actual sources and the level of research detail are standardised; analysts follow an established methodology that is clearly defined in an internal process manual.

It is standard procedure for an analyst to contact a company, either by meeting, phone or email, to discuss outstanding issues relevant to the company, its activities and impacts and incorporate this into company analysis. The company has an opportunity to comment on the report before it goes to the client. CoreRatings does not classify this contact with companies as engagement but as a normal part of the research process.

#### Information/Metrics

Coverage includes four main risk metrics, environmental, social, employment, and governance/ business ethics that are considered to have potential impacts on investment value.

These are then broken down into 16 subsidiary issues: Use of natural resources, Emissions, Climate change, Ecosystem & biodiversity, Society and community, Human rights, Product safety, Marketplace, Diversity, Working conditions, Recruitment and retention, Strategic positioning (incl. industrial relations), Business ethics, and Governance policy. Sub-categories are then assessed: For example, Emissions covers Air, Ground, Water and Waste Management.

# **CORERATINGS**

#### **Process**

# Methodology

- 3 Stage Process:
- 1. Sector Risk Analysis (SRA): Identifying specific environmental, social, employment & governance/ business ethics risks for a sector
- 2. Risk mapping: Mapping those risks against their effect on investment value drivers (egeg brand value, legal action, regulatory imposition) to indicate materiality of risks to investors. The outcomes of this process are weighted to provide input into the scoring for a company.
- 3. Risk management: Reviewing how companies are managing each risk. The company process and systems are reviewed for each risk in the SRA through a standard set of twelve questions covering five topics: policies, implementation, validation, performance, and disclosure. Following review of publicly available primary and secondary sources, focused engagement with the organisations occurs to clarify and complete gaps in disclosure.

Scoring for each element is assigned by the analyst drawing on their knowledge and comprehensive scoring guidance documents. Companies with activities in more than one sector will have their scores considered for each appropriate sector with the overall weighting based on turnover of the various activities.

Following the initial research and the generation of the initial rating, the analyst may rebalance the rating to enable the final rating to more accurately reflect the company's performance, egeg critical management failures that may have been identified. Draft reports are subject to peer review and are edited by sector specialists (see below).

The revised draft report (and rating) is provided to the company for review, allowing seven working days for comment.

# **Quality Assurance and Verification**

#### Assurance:

The methodology is consistently applied to each assessment (see above). SRAs are developed internally and with input from external experts. A formalised editorial process - implemented by sector specialists trained in editorial standards ensures that the SRA (investment risk weighting). the analysis of the company's performance (investment risk management) and its scoring are aligned. Borderline scores may be subject to additional review by a scoring committee. The Director of Research and team managers provide quality assurance through staff training, editing of research products, and monitoring of internal systems and procedures. Feedback from companies and clients form an integral part of quality assurance. Where possible, individual analysts are responsible for coverage of a core universe of companies to strengthen in-depth understanding of a company's risk management.

All company reports are entered and scored on a live database to ensure systematic data capture, to enable sector and cross-sector comparisons as well as to provide clients with online access to products. The database includes a facility for systematic recording of contact/engagement with companies.

# Analysts:

CoreRatings' analysts have diverse experience from a range of consulting fields, industry, investment, non-governmental organisations and government bodies, and speak a broad range of languages. Analysts are organised into four sector teams: Financial Institutions; Consumer Sectors; Industrials, IT & Telecoms; and Resources, Utilities & Healthcare.

# Verification:

External verification based on client requests has been carried out, and will continue. Also, CoreRatings features in prominent studies such as the Mistra/ Sustainability Report *Values for Money*.

# **Outputs**

# Score/rating

A rating is generated on a comparative basis within and across sectors and is based on a seven point rating scale from A+ to D. It measures how well the company is managing its material risks, ie an analysis of management practice and performance of the company weighted towards risks that are most material to

Sector and Issue Reports: These are produced and distributed periodically. Sector reports highlight key issues, impacts and risks in a sector and map these against investment value drivers. Issue papers are produced on an ad hoc basis, and on client request for screened portfolios.

# **CORERATINGS**

the company, reflecting its industry and countries of operation.

#### Reports

Company Report: The ten-page company ratings report includes a corporate responsibility rating and a two page summary section. The ratings summary presents bar charts and pie diagrams and covers investment risk management, environmental risks, social risks, employment risks, and governance/ business ethics risks. The body of the report contains a company description, key environmental, social, employment, and governance/business ethics impacts and risks, company analysis and any excluded activities.

# **Update/Review**

All company analysis, including SRA, is updated at least once a year. For certain bespoke services there is a quarterly update.

#### **Products and Services**

Report Subscription: the client can specify the required universe egeg Euro 300. Other related services include daily news monitoring: which looks at company specific news as well as sector and issue news and is available online to clients through a live secure website.

#### Cost

Subscription rates vary according to the service required. There is currently no standard pricing as packages are tailored to client requirements. CoreRatings provides prices on request.

#### Other information

CoreRatings is currently developing its research programme and refining its methodology.

# **Differentiators**

Industry-recognised methodology covers critical corporate responsibility risks and how these may materially impact investment value. The rigorous analytical approach ensures that all issues are systematically covered.

CoreRatings is transparent about its rating process, which is described in detail on its website. Clients consider it a fundamental resource behind their value added approach

CoreRatings' analysis supports both SRImandates, where clients are integrating valuesdriven criteria into portfolio decisions, and a mainstream investment approach, where managers are applying a deeper analysis of company risk and management performance to the investment process.

#### **ETHIBEL Key Information** Website: http://www.ethibel.org/ Launch Date: 1991 Geographical Coverage: Europe, Asia-Pacific Ownership: Established by non-profit and North America. organisations. Ethibel is the major shareholder of Stock at Stake (SaS) and Ethibel shareholders are a range of non-profit organisations. **Category:** Rating and Index (non voluntary) Financial Universe/ Exchanges: some 1,200 leading companies worldwide. Assessments performed for 600 companies. Description/Product: Company evaluation and **Content:** Sustainability including environmental. screening, the Ethibel quality label for SRI funds, the Ethibel Sustainability Indices.

# **Philosophy**

# **Background**

The assessment considers broad sustainability issues and concerns and how these are reflected in a company's management processes and performance.

There is focus in the Ethibel process on identifying companies that show leading performance in all fields of corporate social responsibility. This is done by considering policies, management systems and performance data. The evaluation process takes into account the region and sector in which a company operates, as well as the company's performance and evolution over time.

# **Exclusions Policy**

There are no sector exclusions, but for the Ethibel label and index there are some exclusionary criteria such as major involvement in armaments and nuclear energy

#### **Audience**

Target users are ethical investment funds. Also includes public authorities, consumers and large charities.

# **Memberships and Partnerships**

Stock-At-Stake; CSR Europe Institute for Social and Ethical accountability (ISEA); Standard and Poors; SRI Compass.org; SIRI; SIRI Accountability; Avanzi; Caring Company; Centre Info; Centre for Science and Environment; EIRIS; Fundacion Ecologia y Desarrollo; Imug; KLD; Michael Jantzi Research Assocs; PIRC; Scoris; SNS asset management; Dutch sustainability research.

# Inputs

# **Sources of Information**

Company reports, information from external and internal sources including NGO contacts, trade union and NGO documents and contacts, news, media and other available information including SaS research and specialist database, active dialogue with company and stakeholders. The publicly available documents form the basis for a dialogue with the companies.

#### Information/Metrics

Scope of the topics is divided into 4 main domains; environmental, internal social policy, external social policy and economic policy (egeg responsibility towards competitors). For example the environmental domain is divided into four themes:

- Strategy (principles, public commitments and reporting),
- Management (EMS, certification, involvement of employees)
- Production (input, output, and waste, also including the supply chain), and
- Products (environmental impact, and whether they have measures in place to reduce environmental impacts of products).

There is no weighting between these different themes.

There are currently 12 topics within the environment domain and within these there are approximately 24 indicators.

# **ETHIBEL**

#### **Process**

#### Methodology

Publicly available information is gathered for the profile template. The company is then contacted to enable collection of the additional information. At this stage the profile is submitted to the company for their review and feedback; the response rate at this stage varies from industry to industry (the average in Europe is over 50%).

Analysts use calibration guidelines, which define which performance relates to which score. These guidelines distinguish between industrial and service companies for the environment. Companies are rated for each topic and scores are then aggregated under themes (egeg products). Themes are then aggregated under the main domains (egeg environment).

Final rating is a series of numbers between 0 and 6 from which averages are calculated. Each company has 4 final scores, one for each domain, with sub scores. Companies are then arranged into 5 categories, which are Pioneers = A, Best in class = B, Better than average = C, Average = D, and Below average = E.

Scores are reviewed by:

- Industry sub-teams internal quality check, and
- 2) Advisory Board, which comments on the scores and can also amend them

Company receives a copy of the profile if they cooperate. If they do not co-operate they do not automatically receive the final profile (only on request).

# **Quality Assurance and Verification**

#### Assurance:

A team will work on research and evaluations within an industrial sector and all research will be subject to a peer review within this team.

# Analysts:

9 analysts with a diverse background both in terms of education and culture.

Knowledge across economics, environment, social sciences, chemistry with experience in corporate, NGOs, banks and academia.

#### Verification:

Ethibel are involved in developing the European Quality Standard. Ethibel also aim to have external verification procedures in place. Evaluation of companies is done by an independent advisory board

# Output

#### Score/rating

The index will only contain companies which have achieved the A or B rating.

# Reports

Company profile includes an evaluation summary together with perceived strengths and weaknesses identified. Key figures and controversial activities are also identified.

#### **Products and Services**

The Ethibel European quality label for socially responsible investment; Ethibel register; and Ethibel Sustainability Index, which is derived from the register.

#### Update / Review

All industries in all regions are updated biannually. Although a continuous update also takes place on a basis of major news / controversies.

The methodology and calibration guidelines are also updated on an annual basis. At this time researchers also review the calibration guidelines as a team and adjust them according to the changes in the society. New guidelines are then passed onto the Board of Directors and the Advisory Board, for comments and amendments.

# Cost

Cost depends on service and assets under management. Ethibel will also provide tailor made research.

# Other information

Universe - for some industries they can add more companies ie fine-tune the universe. No consulting services are provided to the organisations being evaluated. 1000-1500

They are aiming for annual update of the methodology but otherwise no changes are foreseen for the basic methodology

ETHIBEL	
companies in the basic universe. Ethibel has a complete profile for approximately 600 companies.	
Differentiators	
Stakeholder involvement in criteria development, research and evaluation.     Evaluation of companies is undertaken by an independent advisory board.	3. Evaluation of companies is done in an integrated way (taking into account all aspects of CSR and the full context in which companies operate).

#### **INNOVEST Strategic Value Advisors Key Information** Website: http://www.innovestgroup.com/ Launch Date: 1995 Geographical Coverage: US/Worldwide; 1700 Ownership: Private companies Category: Rating Financial Universe/ Exchanges: Exchanges used include 2000 global stocks, FTSE Euro Top, S&P 500, FTSE 350, and KAK 40. 1800 companies have been assessed. **Description/Product:** Provides company ratings Content: Environmental, social, corporate to investors, based on intangible value drivers and governance exposure to risk.

# Philosophy

# Background

Established in 1995 to provide advice on intangible value of companies to investors. Clear opinion that social and environmental performance can drive value. There is a focus on exposure to risk and investment opportunities.

Independent third party organisations and Innovest have analysed the correlation between Innovest company ratings and their financial performance over time. These studies have provided evidence of the link between ratings and the bottom line, and therefore between companies run in responsible manner and financial performance.

# **Exclusions Policy**

The Innovest approach can be described as best-in-class: Innovest do not exclude any sector or industry from their assessments. However, users of Innovest ratings can apply exclusions in accordance with their policies, for instance, by excluding the lowest rated companies (CCC) and/or high impact sectors.

#### **Audience**

Institutions, fund managers, and NGOs, government and multi-national organisations.

# **Memberships and Partnerships**

Have cooperated with Morgan Stanley Asset Management and PWC in creating the EcoValue21 investment analytics platform, one of the key models used by Innovest.

# Inputs

# **Sources of Information**

Information sources include company publications, online news databases (search back 3-5 years) and FACTIVA web search platform, which allows searches on companies under preselected search terms and can automatically repeat searches and email them on a weekly update basis. Sector specific sources are also commonly used.

Information will also be requested from the company after Innovest has performed initial assessment using the above sources.

# Information/Metrics

Content covers environmental, social, and strategic governance; impact on competitiveness, profitability, and share price performance.

Uses a combination of both qualitative and quantitative metrics egeg environmental policy and communication / experience of management team versus how many sites are audited to accredited standard/emissions, GHGs etc. However, the scope of the metrics focuses on management elements and risk rather than actual performance. In total there are 48 different questions/scores.

# **INNOVEST Strategic Value Advisors**

# **Process**

#### Methodology

Sector specialists identify key perceived issues and risks for the sector, taking into consideration regulatory standards and guidelines to enable the assessment to cover relevant topics.

Sector specific performance criteria are developed and grouped together under six key value drivers, which are historical contingent liabilities, financial risk management, operating risk exposure, sustainability risk, sustainable profit opportunities and strategic management capacity. These are sorted by 'Management', 'Opportunity' and 'Risk' and assigned a sector-specific weighting. This forms a sector overview matrix

Companies are rated by sector against the set performance criteria. Each company within a sector is given a weighted score on the sector impact index (1= Low and 5= High), and aggregated numerical score (1-10) as well as a correlated letter rating (AAA, BB etc).

# **Quality Assurance and Verification**

Assurance:

Senior Research Director reviews both sector overview matrix and company profiles carried out by sector specific analysts.

Research Managing Director gives final reality check on ratings and rankings before they are sent out.

# **Analysts**

The number of analysts with background in environment is 23, finance 14, mixed 4 and other 9

#### Verification:

No verification in place at present. PWC undertook original audit of methodology, not repeated since 1995.

# Output

# Score/rating

Rating on a comparative basis within sector.

Sector overview: looks at financial performance in terms of Top Performers, Bottom performers and Out-performers and scored as best/worst in its sector.

# Reports

Company Profiles

Sector Reports (rated on sector impact index 1-5) against industry peers

# **Update / Review**

All company analysis is updated at least once a year. Exceptional updates are conducted in the case of merger and acquisition or more often for unusual events of relevance.

# **Products and Services:**

Associated products/services include:

- Weekly Stock Monitor briefing note to clients on weekly developments, on nontraditional sources of risk and competitive advantage;
- Specific customised research projects on particular issues egeg bench-marking, climate change, HIV/AIDS;
- Sub-Advisory work helping financial institutions to create new funds based on Innovest's ratings;
- Positive and negative screening if requested - will cover compliance data, best practice and norms and regulations as well as activity in nuclear power, weapons, tobacco;
- Will interact on an advisory basis when approached by companies that wish to improve their performance.

# Cost

Non-disclosable for reasons of competition

# **INNOVEST Strategic Value Advisors** Other information There was a comment that there is some potential confusion with terminology in criteria and guidance is planned to address this. **Differentiators** Focus Investment Sub-Advisory Management Work -Performance on 3. World class analyst team - At 30, Innovest has environmental, social, and governance issues is one of the largest, if not the largest, global analysed from a purely investment point-ofanalyst teams in this industry, with a physical view. presence in London, New York, Paris, Toronto and Madrid. 2. Research Methodology & Information Sources - Innovest has developed a proprietary rating methodology, audited by PwC, which is comprehensive, rigorous, detailed (includes

sector-specific weightings of criteria), and has been recognised as of the highest quality by

several independent studies.

# OEKOM RESEARCH AG Key Information Website:

http://www.oekom-research.com

**Geographical Coverage:** Germany / Worldwide. Assessments performed for 800 companies.

Category: Ratings and research

**Content:** Sustainability including environmental, social responsibility

Ownership: Private

Launch Date: 1993

Financial Universe/ Exchanges: DJ STOXX 50 and DJ EURO STOXX 50 of 100%, DJ STOXX 600 of approx. 90% and MSCI World of over 80%.

Description/Product: An independent rating agency providing various services including the corporate responsibility ratings.

# **Philosophy**

# **Background**

Under the umbrella of Ökom GmbH, the leading publishing house for environment and sustainability related magazines and books in Germany, oekom research AG has been active in the sustainable investment field since 1993. oekom research separated from the publishing house in 1999. The company is a provider of information on the general social and environmental performance of companies, sectors and countries rather than a specific focus on certain risks.

# **Exclusion Policy**

As standard, oekom research will undertake to identify if a company has controversial business activities, and will carefully analyse business in critical sectors – alcohol, nuclear power, genetic engineering, chloro-organic mass products, biocides, non-renewables, animal testing, human rights violations, child labour, gambling, arms, pornography, tobacco.

In terms of specific sector exclusions, oekom research does not define these but is guided by the client's decision based on their specific investment needs.

#### **Audience**

Institutional, church and religious orders, banks and SRI fund managers

# **Memberships and Partnerships**

Co-operated with university professors in developing the Frankfurt-Hohenheimer Guideline, which forms the basis for the assessment process. Also co-operate with CRIC – Corporate Responsibility Interface Centre and Forum NG – Forum Nachhaltige Geldanlagen; Association for Independent CSRR.

# Inputs

# **Sources of Information**

Assessment is based on information derived from the companies themselves and from independent expert research including evaluation of company documentation such as annual, social and environmental reports, interviews with company representatives, media screening, interviews with independent experts, and assessments from independent specialists from governmental and public institutions, business associations, social and environmental research institutes, consumer protection groups etc.

Only in individual cases, the companies are not contacted. Mainly if the clients ask to make a short-term ad hoc screening of a company.

# Information/Metrics

The assessment covers approximately 200 individual criteria and questions, which have been selected from the original set of 800 from the Frankfurt-Hohenheimer.

Guideline (a scientific study which developed a comprehensive set of criteria for the ethical assessment of companies). Of the 200 criteria, approximately one third are quantitative and the rest qualitative. Criteria cover environmental and social cultural issues including environmental management, products and services, eco efficiency, staff relations, social/cultural management and external relations.

# **OEKOM RESEARCH AG**

However, those companies will be contacted within the framework of the next general rating update for the respective industry sector.

Approximately 40% of the criteria are industry specific to enable relevant aspects to be covered, and the actual number of questions/criteria can vary between sectors. Examples: product responsibility; environmental impacts of products and services; types of resource consumption and emission.

#### **Process**

# Methodology

Using information from the identified sources researchers assess an organisation's performance against the appropriate criteria for the relevant sector using the research handbook as guidance. Each criteria is given a score from 1 to 4.

These scores are aggregated to provide a corporate responsibility rating (approx: 200 criteria, depending on the industry) comprised of two major components: one for social cultural and the other for environmental issues. Within each of these, weighting has been predetermined as follows: Social cultural rating (approx. 100 criteria): staff relations 40%, social/cultural management 20% and external relations 40%.

Environmental rating (approx. 100 criteria): environmental management 25%, products and services 50%, eco-efficiency 25%.

The weighting between environment and social cultural is assigned on a sector basis based on a Sustainability Matrix developed by oekom research and approved by their scientific advisory committee. This enables the relative importance/risk associated with environmental and social/cultural issues within that sector to be reflected in the weighting. The score is then translated into a letter grade. The draft profile is at this stage sent to companies for correction/feedback and comments.

Note: The client can influence weighting of social vs. environmental issues in research according to his investment/research needs.

# **Quality Assurance and Verification**

Quality Assurance:

oekom research has developed a detailed handbook that covers all criteria. This includes documentation of pre-determined scores for given achievements and practices in corporate ethics and sustainability in order to provide a standard and consistency across assessments. The handbook is constantly updated and reviewed as analysts identify new aspects/issues.

Other controls assigned by oekom research are that two analysts work together to provide a level of quality assurance and following completion the assessment is always reviewed by the second individual. Also where an entirely new industry area is being assessed, experts are used to identify criteria and assign grades.

oekom research has developed an independent quality standard, grounded in the principles of independence, completeness and comparability. This was defined through close co-operation between the Ethical/Environmental Rating project team at Frankfurt University, headed by Prof. Dr. Johannes Hoffmann, and oekom research's Scientific Advisory Committee (comprising 9 social and environmental scientists, who meet twice a year to review the quality and transparency of oekom research's research).

#### Analysts:

10 analysts – all academics with a broad knowledge base covering areas including economics, science and engineering.

# Verification:

No external validation yet. Currently participating in CSRR-QS, a quality standard for sustainability rating agencies that was initiated by the EU commission and will be undergoing an external quality audit in 2005.

# **OEKOM RESEARCH AG**

# **Output**

# Score/rating

Detailed corporate responsibility rating report giving numerical rating and rank, using environmental and social weightings matrix; includes separate social cultural rating with rank, and an environmental rating with rank. Total translated into letter grade (A-D) ratings, by company.

#### Reports

Provide list of recommended companies to invest in, tailored to client's specified interests and investment needs (egeg regarding minimum rating grades and exclusionary criteria).

# **Update / Review**

Company ratings are updated approx. every 18 months. Ad hoc news on companies are integrated continuously.

# **Products and Services**

Accessibility:

Provides quarterly update of the investment universe and monthly ad-hoc research.

Company profile databases remain confidential - for client use only.

#### Cost

oekom research primarily offers research services to institutional investors. For these services a fee is charged depending on the volume and type of investment funds or portfolios (in base points). In some cases, oekom research also sells single rating reports or industry reports. The price for rating reports is 350 euro. The price for industry reports depends on the number of participants in the rating.

# Other information

Universe of 800 companies worldwide. Look at the approximately largest 30-70 companies in each sector.

Overall try to cover 80-85% of market capitalisation of index - select largest companies within index.

# **Differentiators**

- 1. The success of oekom research is based on a scientifically based rating system with a strong focus on industry specific challenges, problems and risks. The system is constantly updated.
- 2. For the credibility and quality of its work, oekom research's independence has been crucial. Independence is guaranteed with regard to both its owners and its products and services.
- 3. Among other things, clients appreciate that products and services are extensively tailored to their individual investment needs, eg with regard to assessment criteria, weightings, exclusionary criteria.

#### **SERM Rating Agency Key Information** Launch Date: 1996 Website: http://www.serm.co.uk/ Geographical Coverage: International Ownership: Private Category: Rating Financial Universe/ **Exchanges:** Primarily FTSE350 and Eurotop 300 (cover approx. 500+ companies). Primarily FTSE 350 and Eurotop 300 (cover approx 600) Description/Product: Rating service using a Content: mathematical model to measure net non-financial Sustainability including environmental, health & (social, ethical, health & safety, corporate safety, social and ethical and corporate governance as well as environmental) risks to governance issues. capital.

# **Philosophy**

# **Background**

The SERM Rating Agency Ltd is an independent environmental rating agency set up to achieve the focused aim of bringing the concept of financial rating to safety and environmental risk management.

SERM's ratings are geared towards the needs of the financial community and companies. The rating assessment is based on identifying the level of risk to market capital associated with environmental, safety and corporate governance issues.

# **Exclusion Policy**

No sectors are excluded

# Inputs

# **Sources of Information**

All input data is public domain information, no direct contact with the company occurs. SERM uses a proprietary search tool as well as its own in-house database that has been populated with key pieces of information since SERM's establishment in 1996.

# Audience

Key audiences comprise the financial investment community and corporate organisations. Insurance companies and consultancies have also expressed interest.

# **Memberships and Partnerships**

UKSIF, founding member of AICSRR (Association for Independent CSR Researchers)

# Information/Metrics

Sector identification:

Use FTSE global classification system plus MSCI (and further tailor made subsets). Twenty-four different issues considered covering environment, safety, social and ethical. Twelve environment "metrics" covering the key issues that have been identified to be of concern for the sector. Different sectors will have different weightings placed on different issues. Eg Climate Change will be a far more significant risk for extractive industries than for financial companies.

#### **Process**

#### Methodology

Researcher gathers information on the company from the sources. A "rater" or "senior researcher" then summarises all of the information, ensuring that all issues have been covered and appropriate information has been entered into the SERM database. A guidance document provides assistance on how to analyse certain information as well as where to search for information. There is no contact with company being rated unless

- Score of the organisation's specific level of risk or concern (negative company issues); and
- Score of the organisation's specific control mechanisms for the issues of concern (positive score).

The SERM model then calculates the overall "score" of inherent and residual risk for the organisation in terms of:

# **SERM Rating Agency**

they purchase the final product.

The top level scores applied to each company are:

- Master score for a given sector based on macro level issues (acts partially as a weighting of overall organisational risk); (the master score goes into deciding the negative risk side of the model – as in this should come first followed then by the positive and negative risk assessment)
- Master score for a given sub-sector (also acts particularly as a weighting); and

- Direct risk to market value;
- Indirect risk to market value:
- Indirect reputational risk value.

The positive "score" for the company is then used as an indication of risk reduction to provide an overall net residual risk level.

# **Quality Assurance and Verification**

#### Assurance:

SERM has established an advisory panel of independent experts, in finance, environment and CSR, to review the master inputs to its model and reflect macro-economic and sector environmental changes. This panel is supplemented and assured by a number of non-affiliated observers.

No third party assurance of inputs occurs although the guidance document is reported to help provide consistency between researchers and raters.

SERM is a founder member of the AICSRR, whose first and specific aim is to create a Voluntary Quality Standard for CSR Researchers.

#### Verification:

Copenhagen Business School provided review of the SERM model using Monte Carlo testing to identify variability of outputs and thus provide confidence in the model.

Work has also been undertaken to track financial performance of good and bad performers (from SERM ratings). This has shown that generally the financial performance of good performers has significantly exceeded those of poor.

# Analyst experience:

Analysts are multilingual and have backgrounds in various technical and financial disciplines with a bias towards journalistic experience. Eight analysts are involved in assessments.

# **Output**

# Score/rating

Rating by sector and sub-sector

Output comprises three numbers (percentages).

- Inherent risk to market capital (does integrate past and sector and sub-sector issues).
- Extent/level of risk reduction through specific company activities/processes.
- Net residual risk to market capital.

# Reports

Company rating reports — Report contains information on findings in terms of risk to capital, from Environment, Health & Safety and Social & Ethical. Summary analysis charts highlight the most significant areas in which a company's inherent risk is managed well or where there is scope for more effective risk reduction. The report also identifies the sourced articles and the raw scores that were entered into the system

# **Products and Services**

Rating reviews

Regularly updated reports (quarterly) with review meetings at which analysts explain and discuss high and low-performing areas and changes to the rating over time

# Reputational Risk Assessments

Uses underlying risk assessment methodology applied to the client's own risk register (rather than SERM's research data). Reputational risk management tool designed in collaboration with a FTSE 100 company. Facilitates company managers in construction of defensible risk assessments, with a clear audit trail, encompassing wider reputational issues.

#### Also:

Strategic Risk Consultancy

SERM Rating Agency	
Peer Group/Sector reports – Custom-built detailed rating reports for benchmarking. These provide information on a number of competitors or collaborative peer companies that the client company has specified as targets. Delivered through a series of review meetings and, if required, consultancy on the implications for the client company's strategy.	
Update / Review	Cost
This information is updated within the model on a quarterly basis for extra-ordinary items, with formal review occurring on an annual basis.	Cost of rating and report with companies benchmarked in peer group varies between £5000 - £20000
Other information	
Investigating ways for information to be "real time" with an ongoing review/updating process.	Currently developing
Differentiators	
<ol> <li>All risk is measured on an external basis only. This creates a level and objective bench-mark, while removing bias and other issues associated with surveys.</li> <li>All risks are quantified as a percentage of risk to market cap.</li> </ol>	3. Scenario testing capabilities of the model can make it forward looking as well as current.

TRUCOST	
Key Information	
Website: http://www.trucost.com/	Launch Date: 2000
Geographical Coverage: Global	Ownership: Private
Category: Rating, voluntary and non voluntary	Financial Universe/ Exchanges: MSCI World Index; Trucost currently covers 1700 global companies although aim for increase to 2500 by end 2004.
Content: Environment	<b>Description/Product:</b> An environmental research and rating organisation (includes Environmental System and Environmental Cost Calculator).
Philosophy	
Background Trucost helps companies to identify the environmental impacts that are material to their business by assigning costs to environmental	Trucost hope that this will enable their process to be used by industry to assist procurement processes.
performance issues. Trucost only includes quantitative environmental elements in its analysis as it does not wish to base assessment on value judgements. This approach allows Trucost to assess and compare companies of	Exclusion Policy None – methodology applies to all companies in all sectors.
Trucost to assess and compare companies of	Audience

The coverage of the Trucost assessment process includes both direct and indirect environmental issues (and costs), which they believe is important for service industries where the direct impact is dwarfed by impacts from within the supply chain.

any size in any geography. Trucost's focus is on

providing a channel for information flow between

companies and mainstream investors.

#### Audience

Institutional investors, companies, analysts and regulators.

#### Memberships and Partnerships

Casella Group

Waterman

**RPS** 

Research Recommendations and Electronic Voting (RREV) (joint venture between National Association of Pension Funds and ISS)

#### Inputs

#### **Sources of Information**

Three types of data/information:

- Financial and business information Information on a company's business activities and interests are gathered to enable mapping of its activities to environmental resource use.
- Quantitative environmental data Includes information such as emissions to air, land and water, and extraction statistics.
- Purchase ledger data (for corporate clients only). This allows Trucost to assess supply chain impacts in detail.

#### **Verification of Inputs**

For institutional investor clients. Trucost independently reviews publicly available company annual reports and accounts environmental/CSR reports in order to compile their reports. A complete "pre-distribution" report is then sent to companies for verification of the facts. Response time is 2 weeks and the response rate is 15%. The feedback is incorporated into the reports before they are provided to Trucost's institutional investor clients.

#### **Process**

#### **Process**

Trucost has a 4 step process to assess the environmental performance of a company:

· Review of annual report and accounts to identify scale of business and specific

This enables Trucost to estimate the typical direct impacts for companies engaged in a given set of activities.

**Indirect Supply Chain Impacts:** 

#### TRUCOST

business activities.

- An Environmental quantity profile is then estimated based on size of operations for the different business activities/sectors that the company is engaged in. Trucost has modelled the environmental impacts of 130 different sectors, and these impacts are proportionally allocated to the company by calculating the company's market share of that sector.
- Trucost analysts then check publicly available environmental/CSR reports and substitute disclosed quantities against Trucost estimated quantities.
- External environmental costs are then applied to determine the ranking of each impact.

#### Methodology

Estimating direct environmental impacts

Where no public disclosure has been made environmental impacts have been estimated using Trucost's model, which has been developed with the assistance of its Advisory Panel of experts in the fields of economics and the environment. This methodology maps the use of over 700 resources and emissions to over 130 different business activities.

#### **Quality Assurance and Verification**

Assurance:

An academic advisory panel convenes at least once a year as whole group (and throughout the year in smaller groups).

#### Verification:

mechanism.

External costs:

Trucost relies on verification of annual reports, environmental reports as well as companies verifying the data when they are provided with the reports.

The model also measures the indirect supply chain impacts of the goods and services

purchased by a company, by using information on

interactions between industries. Trucost employs

an input/output model to estimate indirect impact.

The model identifies the inputs required to

produce a unit of output for each sector or

business activity. This model identifies both

sectors that supply the company and the sector's

environmental impacts. The model can measure

the entire supply chain of the company from first

tier back to source using a proportional weighting

Trucost prioritises its analysis of environmental impacts by allocating an environmental damage

cost to each resource or emission (not necessarily

paid for by the company). Trucost uses external

costs as a way of weighting the impact of

unsustainable resource use and pollution. By

applying a price to each resource based on its

environmental impact, the model is able to

analyse in financial terms, the economic and

environmental performance of each sector.

#### Output

#### Score/rating

Rates by company against peer or sector group, according to measured environmental performance using quantitative metrics. Scoring is adjusted to size of business and is therefore proportional (Impact ratio: total cost/turnover). The score also takes into account the supply chain's impacts.

Trucost also has a measure of data disclosure:

% Absolute = Number of resources disclosed by the company divided by the number of resources considered significant (by Trucost) in the relevant operating industries; and

% Weighted = As above, but weighted by direct external costs of the resource (thus indicating the level of disclosure of a company's most important impacts)

Companies can also be compared on specific issues, such as CO<sub>2</sub> emissions.

Contains key recommendations on how improve environmental performance relative to peers. This report can provide a basis for annual environmental reports.

Sector Report - identifying the financial impacts of current and future legislation on companies within a sector.

#### Cost

Annual membership fee starts at £3,000 (ex-VAT). Various reports are extra.

#### **Update / Review**

Usually annual. Depends on requirement of company.

#### **Products and Services for Investors**

Trucost provides modelling tools and reports that allow fund managers and analysts to understand the environmental impacts of their investment.

#### TRUCOST

#### **Products and Services for Companies**

Trucost provides tools and reports to help companies measure, manage and communicate their environmental performance.

**Environmental System** 

This is a web-based analytical tool for companies that provides modelling capabilities. This tool allows companies to:

- Model the financial implications of future environmental legislation or regulation
- Assess the materiality of environmental impacts
- Plan scenarios, set targets and measure progress over time

Companies can also receive three different types of Report:

Trucost Briefing - summarising the key elements of upcoming legislation, regulation and other issues affecting companies and the environment. Company Briefing - one page report summarising the environmental performance of a company including its top ten direct impacts, the top ten impacts of its supply chain and an analysis of its peer group.

Company Report – 10-15 page report describing in detail environmental impact of company and its supply chain.

Environmental cost calculator, annual subscription - an online system for modelling the environmental impacts of companies in financial terms, the calculator allows the analyst to incorporate the environment into their company and sector assessments.

It provides comparative analysis of performance between companies of any industry, size or geography. This subscription includes Trucost briefings and Company Briefing reports summarising the environmental performance of their portfolio companies. These Briefings are based on publicly available information and environmental disclosures.

Commissioned Research - Trucost undertakes commissioned research on companies and sectors enabling assessment of likely impacts of legislation or regulation on companies around the globe.

#### Cost

Different levels of fees. Sector reports for £2000 (ex VAT). Various financial indices can be purchased from £8,000 (ex VAT). Or annual access to the model can be purchased..

## **Update / Review** Annual.

#### Other information

Aim is to increasingly incorporate actual and agreed company data in the input output tables to increase

The accuracy and transparency of the system for both companies and investors analysing the companies.

- 1. Focus on quantification of environmental impacts.
- 2. Able to analyse performance of supply chain.
- 3. Uses external cost based methodology to present analysis in a context relative to the financial performance of the company, and relative to the size of the company (materiality).

# SAM (DJSI) Key Information

Website: http://www.sustainability-indices.com/
Geographical Coverage: Worldwide, Europe

and Eurozone

Category: Index, non voluntary

**Content:** Sustainability, including environmental social and economic issues.

Launch Date: 1999

Ownership: DJSI is a cooperation of DJ Indices,

STOXX Ltd and SAM Group.

Financial Universe/ Exchanges: 2,500 largest

companies out of the Dow Jones Global Index for the global index and DJ STOXX 600 Index for the European and Eurozone indices.

**Description/Product:** Global Sustainability Index that contains the top 10% of companies in each of 60 industry groups, which is aimed to cover 20% of market cap in each group. European Sustainability Index that contains the top 20% of companies aimed to cover 45% of market cap in each group.

#### **Philosophy**

#### **Background**

Integrated assessment of economic, social and environmental criteria with a strong focus on long-term shareholder value.

#### **Exclusions Policy**

No industries are excluded for the composite indices. However, a standard range of subset indices excluding certain activities are available and additional exclusions can be built in upon request on a customized basis. Investor Responsibility Resource Centre (IRRC) is used for exclusions (0% tobacco, gambling and alcohol and 5% armaments and firearms).

#### Audience

Banks, global insurance companies, large pension funds and private clients. Access is provided through licences that are provided mainly to Asset Managers, with some other individual and institutional users.

#### **Memberships and Partnerships**

DJ Indices: creates and licenses indices for use; SAM focuses on sustainability investing; and STOXX Ltd provides and services the DJ STOXX indices.

#### Inputs

#### **Sources of Information**

Information sources include 1) Questionnaires, 2) Company documents (publicly available / non-publicly available and verified / non-verified), 3) Stakeholder analysis (FACTIVA database searches companies that they analyse) and 4) Direct company interaction.

Each year the questionnaire is pre-filled by SAM Group and from year to year companies are asked to provide updates and make changes directly to the questionnaire. SAM does not update information in the questionnaire from environmental reports or other sources of information themselves.

#### Information/Metrics

The questionnaire has approximately 90 questions and each of them has 5 subcategories. The response rate in 2003 was around 20%. Where responses are not received, additional research is undertaken by SAM. 770 companies were analysed in total in 2003.

There are an approximately equal number of questions for each of the three sustainability elements. (Social, environmental and economic.) Social criteria include health & safety.

The questionnaire has weightings for each section and also has sub-weightings for specific questions. 100 points is the maximum score that can be achieved. The total score is obtained from the base data provided in the questionnaire and other sources. Economic, environmental and social breakdowns are provided separately.

DJSI has common sector criteria in place ie 60% of the questionnaire is generic and 40% sector specific. The proportion of economic, environmental and social criteria in the sector specific elements varies to enable capture of key sector issues. In total, companies in each of 60 industries are assessed against a set of around 20 issues. The number of general and industry-specific criteria in each of the questionnaires

#### SAM (DJSI)

averages around 90. Roughly a third of the criteria relate to each of the three sustainability elements.

#### **Process**

#### Methodology

DJSI allow companies 2-3 months to complete the questionnaire and provide a user name and password for an internet questionnaire via targeted letters to each company.

The current process comprises criteria development between December to March with analysis starting in April.

The first step in the strategic planning towards criteria is to determine the most important sustainability (social, environmental and economic) trends by sector. There is a time lag from identifying a hot topic to developing criteria to capture it.

A consistent rule-based methodology is applied to the analysis. Scores are assigned to each area as per predefined guidance in the rulebook. Analyst subjectivity is reported to be limited.

#### **Quality Assurance and Verification**

#### Assurance:

Rulebook methodology limiting analyst subjectivity. Cross-referencing of all the sources is in place. Will also ask for evidence and links directly from companies for certain questions if needed.

#### Analysts:

There are currently 60 employees in the SAM group out of which 10 analysts focus exclusively on the assessment of companies in the DJSI universe.

There are a high number of financial analysts in the team. It is reported that the group was rated highest amongst other similar organisations for financial 'expertise'.

#### Verification:

PriceWaterhouseCoopers perform independent verification, which includes the allocation of an error margin for their overall process. The process covers a sample of 20-30 companies and redoing all the calculations. Last year the error margin was 0.4%.

#### **Outputs**

#### Score/rating

Rating companies on a comparative basis within sector.

#### Reports

Company reports contain:

- · Company description,
- Discussion on its sustainability performance and outlines of sustainability scores (including separate scores for environment, social and economic dimensions);
- Discussion on industry driving forces;
- Company performance versus industry average and best achieved score for specific criteria (environmental, social and economic).

Only the reports of companies in the index can be bought, (currently 315, although 770 were analysed in 2003). Also provide company briefings in which an analyst will explain the scores directly to the company. Market sector leaders reports are also publicly available.

This yearly review aims to reflect best practices and ensure continuous monitoring of companies. In addition, companies in the index are monitored on a daily basis.

Minor modifications to the process are ongoing, with larger changes identified for implementation every 2 years. There is also an aim to include further studies into the process, such as the motor industry study published in October 2003.

Annual review of indices with component changes is implemented on the third Friday in September and is effective on next trading day.

#### **Products and Services**

Dow Jones Sustainability Indices is the 'product name'

#### Cost

Access to the high level details for 18 market sector leaders is free of charge (also publicly available). Companies participating obtain detailed feedback of themselves for each criteria

SAM (DJSI)	
Update / Review	free of charge.
Annual refinement of criteria is carried out and figures where applicable are normalised according to turnover.	All other costs are dependent on the nature of the product/services being requested.
Other information	
SAM are reportedly not sponsored by any corporate body that they have investment interest in.	Criteria are linked to performance.
Differentiators	
<ol> <li>Clear Focus on linking sustainability to long-term shareholder value.</li> <li>Coverage of general and industry-specific criteria in all three sustainability dimensions – economic, environmental and social.</li> </ol>	3. Best-in-class selection of companies with additional possibility for client-driven exclusions.

FTSE4GOOD	
Key Information	
Website: http://www.ftse.com/ftse4good/	Launch Date: 2001
Geographical Coverage: UK / Worldwide	<b>Ownership</b> : FTSE Group is 50% owned by the Financial Times Limited and the London Stock Exchange.
Category: Index, (non voluntary participation)	Financial Universe/ Exchanges: FTSE All-Share Index (UK), FTSE Developed Index (Global), 2,500 companies
Content: Environmental, Stakeholder and Human Rights (also sector exclusions)	<b>Description/Product:</b> A Socially Responsible Investment Index Series incorporating environmental, stakeholder, and human rights selection criteria.

#### **Philosophy**

#### **Background**

Due to an increased interest in Social Responsible investing among mainstream investors and FTSE's belief that in the future companies will not be measured for financial performance alone, FTSE Group developed the FTSE4Good Index, which was launched in July 2001.

Transparency of the inclusion criteria is an important part of FTSE's ethos and these are available on the internet.

The Index is an investment tool, used by fund managers globally as a basis for SR funds and as a bench-mark to measure the performance of SRI. However, because of its evolving criteria and the Engagement Programme that FTSE has put in place to support companies with interpreting and meeting the new, more strict criteria, it is also considered to be a tool to help drive continuous improvement in management of environmental, social and stakeholder, and human rights within businesses.

The inclusion criteria are set at what is perceived to be "good practice" not "best practice" with the aim that some 50-60% of businesses should be able to meet them (currently approximately 40% of businesses assessed achieve the requirements). In addition, the inclusion criteria are regularly enhanced, these revisions occur at least once a year (three times since its launch in 2001).

#### **Exclusions Policy**

Excluded industries are tobacco producers, manufacturers of nuclear weapons in whole/part, manufacturers of whole weapons systems, owners/operators of nuclear power stations, and extractors/processors of uranium.

Any company with an interest in one of these excluded industries will be excluded from the FTSE4Good index. "Interest" would extend to "strategic parts or services" within the supply chain.

In order to be eligible for inclusion in the FTSE4Good index a company needs to be within the FTSE original universe. Therefore changes in ownership, market capitalisation or liquidity can impact the companies' inclusion.

#### **Audience**

Target users include investors, asset managers, and companies.

#### **Memberships and Partnerships**

FTSE Group sources the information regarding companies' performance against the FTSE4Good criteria from EIRIS (Ethical Investment Research Service, www.eiris.co.uk) and its network of international partners who undertake the research and associated analysis.

#### Inputs

#### **Sources of Information**

EIRIS source the information from publicly available sources including annual reports, company websites and more general web searches. A company questionnaire is also submitted for completion on an annual basis. (Researchers reference web sites and annual

On environment specifically there are 25 environmental indicators, however not all will apply to all companies.

Companies are assessed against criteria on practices and disclosure in the areas of the environment, stakeholder relations and human

#### FTSE4GOOD

reports for answers as appropriate, to reduce work involved in completing the questionnaire.)

#### Information/Metrics

45 criteria indicators (3 sections: environment, social & stakeholder, and Human Rights. Within those, policy, management systems and reporting, and within those are a larger number of criteria indicators all of which determine whether companies meet the criteria).

#### rights.

- Within the environment elements there are three inclusion criteria, but the requirements vary dependent on sector risk.
- Social and stakeholder has seven criteria divided into areas of policy, management and performance. A company needs to pass at least two of these.
- Human rights has two different sets of criteria dependent on sector and operating location.

#### **Process**

#### Methodology

FTSE's methodology is based on assessing performance against the inclusion criteria. The criteria are based on international standards as it is a global index. The requirements set against the inclusion criteria vary according to the perceived level of environmental and social risk associated with a particular sector. Sector classifications are based generically on FTSE designations.

An organisation that has activities across a number of sectors will be classified based on the highest impact classification that applies to at least 15% of its operation. For example, a telecommunications company with 15% of its turnover arising from high impact activities such as chemical manufacture would be classified as high impact in terms of the environmental criteria.

EIRIS, FTSE4Good's research provider, uses sector guidance when analysing companies. This guidance was developed with FTSE and is regularly reviewed (last revised a year ago). An initial company report is developed based on the identified information sources. This report is then sent to the company for correction. Companies therefore have an opportunity to amend the information.

# Based on these company reports, suggestions for Index inclusions are formally presented to the independent FTSE4Good Policy Committee which makes the final decisions.

FTSE Group has a strong engagement programme with all companies but focus in particular on those which do not meet new criteria that are being implemented.

The development of new criteria is determined by a sub-committee. This committee looks at possible new criteria developments and prioritise them. They are currently developing supply chain labour standards criteria. FTSE Group has developed a consultation process for criteria development:

The first stage consists of meetings or focus groups with experts and important stakeholders, including NGOs, and trade associations/companies.

The second stage involves the proposed criteria options being put onto the FTSE4Good website. Relevant stakeholders are notified and have an opportunity for formal feedback. This public consultation takes 4-8 weeks. Criteria that companies do not agree on do not necessarily get dropped, but will get modified. FTSE Group will also test the proposed criteria for robustness.

#### **Quality Assurance and Verification**

#### Assurance:

FTSE have a quality assurance department which performs internal audits of FTSE processes. FTSE Group also monitors EIRIS research, focussing on interpretation and analysis. FTSE Group also monitors all related correspondence between companies and EIRIS.

The overall review is formalised, and procedures are documented as part of FTSE Group's quality system. Part of the responsibility of the FTSE4Good Policy Committee is to look at any possible operational issues relating to the

#### Analysts:

N/A - research is performed by EIRIS. The CSR team at FTSE Group manage the Index, engagement program and criteria development.

#### Verification:

There is presently no audit in place because much of the criteria relate to disclosure, though there is an aspiration to audit companies on their reported information. EIRIS verify company evidence with the companies, and both FTSE and EIRIS meet with the companies as required.

#### FTSE4GOOD

FTSE4Good index.

#### **Output**

#### Score/rating

Companies are not assigned scores within the Index. If they meet the selection criteria and are in the underlying universe they are included in the FTSE4Good Index Series. If they do not meet all the criteria they are not included. The weightings, as with all FTSE equity indices, are by market capitalisation.

#### Reports

Company specific feedback reports include information on company assessment process, FTSE4Good company selection process, evolving criteria and the criteria development programme.

The report details and identifies pass or fail for the company's overall status, overall criteria requirements, environmental criteria, human rights criteria, and social and stakeholder criteria.

A public report was published in May 2004. The FTSE4Good Criteria Development and Company Engagement Report details companies' responses to the changes to the index entry criteria over the last 18 months. It draws upon the work of FTSE's in-house engagement programme, which was set up to provide support and guidance to companies eligible for inclusion in the FTSE4Good Index Series. The report shows that FTSE's work on the FTSE4Good series has made a positive impact on the development of CSR practices among listed companies around the world.

#### **Products and Services**

Bench-mark Index Series: FTSE4Good UK Index FTSE4Good Europe Index FTSE4Good US Index FTSE4Good Global Index

Tradable Index Series: FTSE4Good UK 50 Index FTSE4Good Europe 50 Index FTSE4Good US 100 Index FTSE4Good Global 100 Index

FTSE Group can also create customised SRI indices to match investor needs.

#### **Update / Review**

Index is reviewed twice a year, March and September. The September review includes consideration of company questionnaires that are circulated in June. The March review considers company updates.

#### Cost

Fund managers that use the FTSE4Good index as a bench-mark pay licence and data fees to FTSE Group. All licence fees in relation to the FTSE4Good index are contributed to UNICEF. No cost for companies.

#### Other information

There was a comment that some companies find the criteria terminology difficult to understand and interpret, and guidance is planned to address this. Note: FTSE4Good is an SRI Index Series produced by the FTSE Group and is used for raising money for UNICEF. It is primarily a basis for SRI products and bench-marks, however it is also used as a CSR standard for companies, and a reference point for academics, NGOs, consultants and other interested parties.

- 1. FTSE Group is a global leading index provider for investors around the World. FTSE indices are respected for their rigour, and independence. The FTSE4Good Index series is no exception. FTSE also contributes all FTSE4Good license fees to UNICEF.
- 3. FTSE4Good is a catalysis for improved CSR practice and disclosure The criteria evolve, representing good practice as it develops. Companies need to meet the more demanding criteria to remain a constituent (see Engagement Report launched May 2004). The criteria are robust, risk focused, increasingly sector specific and are based on international consensus.

FTSE4GOOD	
2. FTSE4Good index criteria are challenging but achievable in order to encourage companies to strive to meet them. Around 40% of the companies in the eligible universe meet the criteria.	

HENDERSON SRI		
Key Information		
Website: www.henderson.com	<b>Launch Date:</b> Current methodology established in 1997, Henderson started ethical investment in 1977	
Geographical Coverage: UK, Europe, International	Ownership: Private – fund managers	
Category: Investment Funds	<b>Financial Universe/ Exchanges:</b> None formally excluded/included. Will consider any companies in which they are interested in investing.	
Content: Broad sustainability; comprising social, environmental, workplace and corporate governance.	<b>Description/Product:</b> SRI fund managing; SRI screening and research, corporate engagement, investment advice, identifying CR leaders: (focus of this study is the SRI screening process)	

#### **Philosophy**

#### **Background**

Henderson undertakes screening of companies to assess their eligibility for inclusion in their socially responsible investment funds. In addition, the outputs of the SRI research process are used as part of the implementation of Henderson's Responsible Investment policy for its mainstream funds.

The SRI research process identifies two linked but separate agendas: sustainability – which addresses the long-term social, ethical and environmental challenges and opportunities facing different sectors; and responsibility – which relates to how companies are managing their practices in the marketplace, the workplace, the community and the environment. Henderson believes that sustainability is providing new secular growth opportunities, while responsible companies will out-perform others in the market place. Henderson links a company engagement process to this assessment.

#### **Exclusion Policy**

Henderson's SRI research process involves three steps. The first step is to assess whether companies comply with the negative screens applied to its range of funds. Each of Henderson's 10 funds have different negative screens from the very strict ethical and environmental avoidance of Global Care Growth (eg alcohol, animal testing, fossil fuels, gambling, GM, ozone depletion, strategic military, nuclear, pornography, tobacco) to more limited screens (generally strategic military, tobacco and nuclear) for segregated institutional clients. Then a quick corporate responsibility review is undertaken to understand whether the company meets basic requirements, and if so, a full SRI analysis is carried out. This means that they do not carry out analysis of the [N.B We exclude companies involved in the provision of strategic military goods and services as defined by EIRIS; companies providing dual use products may be included in the investment universe] Also noted however, that links to military such as investment in construction of barracks by an otherwise non-military company would be considered on judgement. So if the general product/service could be used by civilians as well as military then company is less likely to be excluded]

No formal sector definitions used, as Henderson only apply sectors to assist in their analysis.

#### **Audience**

Internal assessment only

#### **Memberships and Partnerships**

Collaborative Engagement: Institutional Investor Group on Burma; Carbon Disclosure Project, Institutional Investors Group on Climate Change, Access to Medicines in Emerging Markets, Payment Transparency.

Policy Dialogue: UK public debate on GM crops: Henderson SRI response; Just Pensions, IIED - Race to the top project; DTI Innovation and Growth Team for the Environmental Goods and Services Sector.

#### **HENDERSON SRI**

environmental practices of tobacco companies, as this is irrelevant for the SRI funds.

#### Inputs

#### **Sources of Information**

Henderson purchases screening information from EIRIS for Europe and Asia, and KLD (Socrates) for USA. Henderson analysts also undertake their own research using company reports and websites; media research databases (FACTIVA); engagement with NGOs and trade unions, and the company itself answer specific queries once other information has been used to complete their assessment as far is as possible.

#### Information/Metrics

Undertake analysis and categorisation of companies in relation to a matrix covering:

 Business Sustainability - 'Industries of the Future' grouped into performance themes: Environmental Management, Health, Knowledge, Low Carbon Economy, Quality of Life, Resource Efficiency, Safety. Also other categories: gatekeepers (service sectors), sensitive (manufacturing) and controversial (environmental/social impact intensive)  Corporate Responsibility – assess policy and performance in key areas such as corporate standards, workplace practices, environmental management and social interactions.

In terms of corporate responsibility, each company is assessed for corporate standards/ethics/governance, environmental policy and physical performance, social and community and workplace/employees. For the environmental elements each company is assessed on policy and performance and climate change with associated sector elements such as biodiversity and ozone depleting substances.

The information used to identify scoring under each question is therefore composed of various qualitative and quantitative data rather than rigorous consideration of a set number of metrics. Companies in particular sectors may be compared for performance on specific issues (eg safety and carbon intensity in oil).

#### **Process**

Apply a series of criteria under qualitative topics (eg performance, climate change, policy) to assign a score of 0-4 for three mandatory elements and other sector specific elements.

Consider Sector specific elements based on knowledge/opinion of analysts.

Engage with the company to fill in gaps in understanding, gain information not publicly available and encourage improved practices and disclosure. In addition, discuss issues and company practices with NGOs, trade unions and regulators to triangulate judgements for contentious companies.

No feedback is provided to companies unless considered that there is a benefit for the organisation and Henderson.

As yet have not received requests for profile/score by any companies.

If company profile is requested, it could be provided but this will tend to be written and designed for internal use only.

Companies will not be aware that they are being rated until the meeting request and have no influence over whether they are considered.

Scoring is by simple addition to produce an overall score as an indication of whether the company should be included. Allocation of the score for each question is based on the experience of the analyst team with the focus being on financial investment implications.

Particular "performance" aspects still may determine that a high scoring company is considered inappropriate for inclusion or vice versa.

#### **HENDERSON SRI**

#### **Quality Assurance and Verification**

Assurance:

Each assessment is performed by one team member and then reviewed and checked by another.

In addition there is an annual internal quality audit of the process and procedures (established two years ago).

Quarterly team presentation to the independent advisory committee. [This tends to be information provided by the team rather than complete independent audit/assessment of the scores/assessment work].

#### Analysts Experience:

Team comprises four analysts with mainly environmental backgrounds and a range of business versus consultancy balance; these work closely with two responsible investment analysts who also cover environmental and social questions for Henderson's mainstream funds. One member is a specialist economic analyst with a financial background.

Verification:

N/A

#### Output

#### Score/rating

N/A

#### Reports

Each company is assigned to a sustainability category and receives a corporate responsibility grade. The assessment of these two factors determines whether a company is approved for the different SRI funds. For Henderson's institutional SRI funds, the corporate responsibility grades are also used to over- or under-weight large cap stocks in the index.

The report is for internal documentation purposes only and comprises a score, summary profile sheets and supporting information, which will be in the company file.

#### **Update / Review**

Three-yearly systematic review of all approved companies. Major UK companies are also updated annually.

Significant or controversial news reports would result in an immediate review of position.

Considering undertaking a twice-yearly media review to inform on additional companies that might require review.

#### **Products and Services**

Do not provide a ratings service. Henderson is essentially identifying the eligibility of given companies for inclusion in their SRI funds.

#### Cost

Not applicable

#### Other information

- 1. Benefit from sustainability drivers
- 2. Going beyond 'best in class' analysis to place priority on real corporate leadership
- 3. Recognising the need to transform market frameworks to reward good practice.

MORLEY FUND MANAGEMENT		
Key Information Website: http://www.morleyfm.co.uk/	Launch Date: 2001 – Expansion from corporate	
	governance coverage into social and environmental issues – birth of 'Sustainable Futures Funds'	
Geographical Coverage: UK / Worldwide	Ownership: Private (Aviva)	
Category: Investment Fund	Financial Universe/ Exchanges: Global exchanges	
Content: Sustainability including environmental, social responsibility, corporate governance and ethical issues	Description/Product: Socially Responsible Investment (SRI) fund management, including 7 funds ranging in risk profile and geographical coverage. SRI funds under management in 2004 are £580m. Part of SRI process includes rating companies by sector against environmental, social and governance criteria. This element is the focus of this study.	
Philosophy		
Background  Morley Fund Management (Morley) is an independent London-based institutional asset management business wholly owned by Aviva plc.  The Morley SRI funds were established in response to some investors' desire not to invest in unsustainable industries.  Morley's SRI team is driven by the philosophy that the successful alignment of corporate, societal and investor interests will generate long-term benefits, consistent with sustainable development. We believe that the appropriate approach for investors to evaluate the investment impact of corporate responsibility is via an integrated analysis of the financial impact of social, environmental and ethical issues.	Sector exclusions include tobacco manufacture and sale, nuclear power, and armaments.  Audience Institutional investors (eg pension funds) as well as retail investors (ie the public).  Memberships and Partnerships Morley's key strategic partnerships include those with Norwich Union, Royal Bank of Scotland, Nationwide, Scottish Equitable and Natwest Life. All of these highly reputable companies act as distribution channels for Morley funds, under their own brand name.	
Inputs  Sources of Information  The SRI's dedicated research team uses its relationship with companies as a key source of primary information. However, additional sources include online research databases, NGOs, company published reports and other publicly available information.  All research is conducted internally and/or in cooperation with external analysts (incl. Sell-side)	Information/Metrics Sector coverage is based on FTSE sector definitions. Selection of metrics is based upon analysts' knowledge of sector — detailed justification of metrics chosen for each business area given in a 6-7 page review ("Sector Guidelines"). The nature and number of metrics varies between sectors. Morley does not use a particular set of quantitative indicators but more qualitative, experience-based, knowledge and research.	

research.

#### **MORLEY FUND MANAGEMENT**

#### **Process**

#### Methodology

Identification and evaluation of the significant social and environmental issues by sector and the production of a sector report is key to the process. This includes identification of the key products and services and assessing company's management of corporate responsibility issues. This analysis covers:

- Business position: a company will be assigned a rating of A to E according to its primary business — ie the services or products a company produces or provides;
- Management vision and practice: a score of 1-5 will be assigned depending on the extent to which management adopts appropriate policies, general awareness and how these processes are integrated into business practices;
- Within researched themes, the incremental investment impact is evaluated and incorporated into the overall assessment of a sector or companies;
- The two scores are then applied to the 'Morley Sustainability Ratings Matrix' to identify whether the company is acceptable for inclusion in the fund; and

#### **Quality Assurance and Verification**

Assurance:

Internal reviewing: researcher has continual guidance from senior analysts.

Advisory Board meet 3 times annually (Jonathan Porritt, Lord Terry Thomas, Deborah Leipziger, Sir Geoffrey Chandler (ex Amnesty), Director of SRI, Morley, Morley CIO, and Morley CEO). Focus of review/discussion is on the strategic direction of the SRI team.

 Segregated mandates allow a bespoke screening process, based on the Sustainability Matrix.

#### Engagement:

Engagement is a continuous process of dialogue with companies being used in as a means of both gaining knowledge about the companies and also discussing SRI issues with companies that impact their business. The engagement process is documented and enables clarification and filling of gaps in publicly disclosed information. However, where this research highlights issues of concern to either the Morley SRI team or the company, further discussion will be undertaken. Company profiles and sector overviews will be sent to companies for comments and correction, and discussions as part of this process are frequent. Morley also has a Corporate Social Responsibility voting policy as part of its overall governance activities. Companies, which fail to adequately report on significant issues, may have their annual reports voted down. Ultimate sanctions include the divestment from certain portfolios.

#### Analyst Experience:

Morley has 3 SRI analysts of which 2 are financial and 1 non-financial and one support researcher with a financial/scientific background. All analysts are qualified to IMC (Investment Management Certificate) and have working relationships with Morley's 20 mainstream investment analysts.

#### Verification:

No external validation. Subjected to Morley internal audit.

#### Output

#### Score/rating

Performance is plotted on matrix of product SEE impact/contribution (A-E) and Management Systems (1-5): measuring performance outcome versus management systems.

#### Reports

Sector Guidelines: tool for identifying Social Environmental and [Ethical] (SEE) issues with probable financial impacts within specific industry sectors.

Provides framework for company profiles and

- Investment recommendation, and justification for the recommendation.
- Risk-weighted matrix to derive the rating. Not publicly available – intended to contribute to Morley's investment strategy and thus are competitive assets; also corporate engagement often more effective when conducted discreetly.

#### **Update / Review**

Updating is a rolling process. Companies may be up or downgraded as events, which may

#### **MORLEY FUND MANAGEMENT**

Morley Sustainability Ratings and Matrix.

 Aims to communicate the methodology in evaluating a company in its sector and to assist companies in managing corporate responsibility issue of significance to investors.

Company Profiles: made up of summary, SRI analysis and management analysis contain:

- Summary of corporate governance issues.
- Record of relevant communications with the company, including engagement notes.
- Selected themes, scenario analysis and incremental impact on valuation.
- A SWOT analysis in tabular format (strengths, weaknesses, opportunities and threats).

materially affect them unfold. Priority for reviewing performance/rating is given to those companies which are on the borderline of inclusion in the fund(s).

#### **Products and Services**

Published sector reports and ratings for FTSE: these are publicly available documents actively informed by companies, industry experts, CSR practitioners and opinion leaders. Company profile and rating are only provided to institutional clients. Graded ratings are published.

#### Cost

Not applicable as work is only used for internal purposes or as part of client agreement

#### Other information

Database of 350 company profiles and 200+ screens. New ones added on as required.

- 1. Privileged access to company management owing to Morley's size. Access to internal & external analysts
- 2. Engagement prioritised by financial impact.
- 3. Resources & experience of SRI team. Integrated analysis of financial, social, environmental issues.

# Annex C – "Scoring" normalisation methodology

## **Scoring methodology**

As presented in Section 7.0, in order to compare the performance of a number of the reviewed organisations, it was necessary to normalise their scores. We decided that all normalised scores would be presented in terms of a percentage score. The table below outlines the methodology applied.

Organisation	Key Elements of Score	Method to Normalise
oekom research	Letter grading from A+ to D-	Standardised to percentages by dividing the number of grades by the percentage range (100), thereby giving a difference of 8.3% between each grade. A+ = 99.6%, A = 91.3%, A- = 83% etc.
Ethibel	Numerical out of a total of 0 to 6	Converted to percentage values
Trucost	Impact ratio	Trucost issues specific impact ratios to each of the companies based on an assessment of the cost associated with environmental externalities. In order to normalise the values, the impact ratios were subtracted from 100 to give standardised percentages for each of the companies.
Innovest	Alpha score	Innovest issues 7 ratings AAA (best), AA, A, BBB, BB, B, and CCC (worst). Standardised to percentages by dividing the number of grades by the percentage range (100), thereby giving a difference of 14.3% between each grade.  Organisations are only ranked within sectors and therefore comparisons across sectors cannot be applied. Companies are also rated against their global counterparts. No direct comparison can therefore be made against other ratings unless they have the same universe.
SERM	Alpha score	SERM ratings cover a 31 point scale from AAA+ to E (Net/Residual risk). The scale represented by these alpha scores is not linear and the % scores in brackets indicated that % scores that are used by SERM for graphical representation. For the normalisation in this report, these values were subtracted from 100.  AAA+ (95%), AAA (94%), AAA-(93%), AA+(8%), AA(9%), AA-(10%), A+(11%), A(12%), A-(13%), BBB+(14%), BBB(15%), BBB-(16%), BB+(17%), BB(18%), BB-(19%), B+(20%), B(21%), B-(22%), CCC+(23%), CCC(24%), CCC-(25%), CC+(26%), CC(27%), CC-(28%), C+(29%), C(30%), C-(31%), DDD(32-34%), DD(35-37%), D(38-40%), E(41-73%)
CoreRatings	Alpha	CoreRatings has 7 scores (A+, A, B+, B, C+, C and D). For the purposes of this comparison the scores were standardised to percentages by dividing the number of grades by the percentage range (100), thereby giving a difference of 14.3% between each grade.

#### **CONTACTS:**

#### THE ENVIRONMENT AGENCY HEAD OFFICE

Rio House, Waterside Drive, Aztec West, Almondsbury, Bristol BS32 4UD. Tel: 01454 624 400 Fax: 01454 624 409

www.environment-agency.gov.uk www.environment-agency.wales.gov.uk

enquiries@environment-agency.gov.uk

#### **ENVIRONMENT AGENCY REGIONAL OFFICES**

**ANGLIAN** 

Kingfisher House Goldhay Way Orton Goldhay

Peterborough PE2 5ZR

**MIDLANDS** 

Sapphire East 550 Streetsbrook Road Solihull B91 1QT

**NORTH EAST** 

**Rivers House** 21 Park Square South Leeds LS1 2QG

**NORTH WEST** 

PO Box 12 Richard Fairclough House **Knutsford Road** 

Warrington WA4 1HG

**SOUTHERN** 

Guildbourne House Chatsworth Road

Worthing

West Sussex BN11 1LD

**SOUTH WEST** 

Manley House **Kestrel Way** Exeter EX2 7LQ

**THAMES** 

Kings Meadow House Kings Meadow Road Reading RG1 8DQ

WALES

Cambria House 29 Newport Road Cardiff CF24 0TP



ENVIRONMENT AGENCY GENERAL ENQUIRY LINE

08708 506 506

ENVIRONMENT AGENCY F L O O D L I N E

0845 988 1188

ENVIRONMENT AGENCY EMERGENCY HOTLINE

0800 80 70 60





### www.environment-agency.gov.uk

We welcome feedback including comments about the content and presentation of this report.

If you are happy with our service please tell us. It helps us to identify good practice and rewards our staff. If you are unhappy with our service, please let us know how we can improve it.

For further copies of this report or other reports published by the Environment Agency, contact general enquiries on 08708 506 506 or email us on enquiries@environment-agency.gov.uk

