

## TACKLING ESG<sup>1</sup>: SCALABLE AND CONCISE REPORTING PRINCIPLES TO NAVIGATE INFORMATION OVERLOAD

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Are you an investor trying to make sense of the volume of ESG including DEI information you receive from some advisors and the lack of ESG information received from others? Or, are you an investment manager investing in a world where ESG matters are front and center, and you know you should be addressing the topic but are not sure what is too much vs. not enough for your organization, products or strategy?

As Head of ESG Strategy at Heitman and an expert in ESG for over 16 years, I have found existing ESG reporting guidance complicated and redundant. Many reporting guidelines exist, but none that target the private real estate industry in an approachable and scalable method. Not to mention, many of these frameworks are developed without investment materiality factored in. To add to the complexity, every organization is unique – organizational structures, investment strategies, and product types are oftentimes not comparable. Unfortunately, most reporting guidelines do not consider these unique characteristics. As ESG including DEI efforts continues to evolve, a reporting framework must evolve with it.

In 2021, with the help of a group of industry experts, the NCREIF PREA Reporting Standards Board and Council began to prioritize ESG. The Reporting Standards construct takes a multi-stakeholder, collaborative approach and identified the need to develop ESG reporting guidelines. An ESG framework complements their mission to “develop and promote reporting standards and guidance which facilitates investment decision-making by filling gaps where existing standards and guidance do not specifically address the private institutional real estate investment industry”. In other words, ESG reporting guidelines had to fill a void and add value. Due to the wide spectrum of ESG reporting considerations for our industry, it was also determined that any guidance provided must be scalable. The *ESG Principles of Reporting for Private Real Estate (the “Principles”)* is a significant milestone on our ESG journey.

The Principles are organized into the following sections:

- Firm ESG Information
- Vehicle ESG Overview
- Vehicle ESG Strategy and Objectives
- Vehicle ESG Performance

Collectively, the Principles serve to:

- Prioritize and facilitate ESG discussions between investors and investment managers;
- Provide a reporting framework for all phases of the investment cycle; and
- Evaluate measures of firm and vehicle key performance indicators within and across managers and vehicles.

This article briefly summarizes how the Principles were developed, current collaboration efforts, and future initiatives related to ESG reporting for our industry. It is important to note that the Principles provide a framework for ESG reporting best practices. As such, compliance with the Principles is not currently required to claim compliance with the NCREIF PREA Reporting Standards.

### *Diverse industry representation*

To start, the Reporting Standards Council formed a “Think Tank” consisting of senior ESG professionals from large global investment manager and investor organizations, as well as senior professionals from small investment manager and investor organizations tasked with developing and managing ESG matters. “CalPERS is supportive of the ongoing effort to standardize and increase transparency of ESG reporting in Private Real Estate,” said Rina Lessing, Investment Manager at CalPERS, and member of the Think Tank. Consistent with the Reporting Standards hierarchy which enables a balanced industry perspective, other stakeholder groups were added to the

Think Tank including consulting and public accounting firms.

Organizations included investors, investment managers and service providers including:

Investors: California Public Employees’ Retirement System (CalPERS), New York State Common Retirement Fund, New York State Teachers’ Retirement System (NYSTRS), and Oregon State Treasury.

Investment Managers: Ascendis Real Estate Private Equity, BentallGreenOak, Berkshire Residential Investments, Blackstone, Morgan Stanley Investment Management, Nuveen Real Estate, Principal Real Estate Investors, and QuadReal Property Group.

Service Providers: KPMG and Stepstone Group

*Not a blank slate*

Members of the Think Tank were well aware of the numerous existing domestic and global efforts to create standards, guidance, indices, and databases which focus on ESG reporting. Some of these important efforts, along with a brief statement of their scope, include:

- European Association for Investors in Non-Listed Real Estate Vehicles (“INREV”)
  - European-based guidelines endorsed and promoted in Asia Pacific by Asian Association for Investors in Non-Listed Real Estate Vehicles (“ANREV”)—substantial focus on environmental and governance issues
- Global Reporting Initiative (“GRI”)
  - Broad set of sustainability standards for all sectors and companies
- Global Real Estate Sustainability Benchmark (“GRESB”)
  - Membership-based; Fund-specific granular ESG metrics
- Principles for Responsible Investment (“PRI”)
  - Membership-based: Firm information at a high level
- Sustainability Accounting Standards Board (“SASB”)
  - A short list of specific environmental questions for real estate
- Task Force on Climate-related Financial Disclosures (“TCFD”)
  - Climate risk specific guidance

The overarching goal of The Principles was to collaborate across these disparate efforts. Although laudable and important initiatives, compliance with, or use of, these standards and guidance materials without targeted private real estate investment specific attributes may prove to be a daunting task. Eric Duchon, Global Head of Real Estate ESG at Blackstone and member of the Think Tank noted, “incorporating ESG into our investments has been a focus for a long time and is a critical component to making our investments stronger and more resilient. This approach aligns with our number one goal of generating long-term returns for our investors. We support the development of the ESG Principles and enhancing transparent communication of these important issues.”

Members of the Think Tank have a clear understanding of, and/or experience with, the existing ESG standards and guidance and appreciation for the diversity of styles, strategies, products, firms, etc., which represent the institutional private real estate investment industry. Accordingly, the Think Tank was well-positioned to create the Reporting Standards ESG mission:

*To facilitate the establishment, management, and promotion of transparent and consistent private real estate industry best practices related to ESG reporting in order to incorporate ESG as a part of global investment operations.*

*INREV Guidelines: creating collaborative opportunities*

NCREIF and PREA, as sponsors of the Reporting Standards, have successfully collaborated with INREV for a number of years on global reporting standards. INREV published and continues to enhance ESG Guidelines (the “Guidelines”) which has a European focus. Included in the Guidelines, INREV mapped standards and guidance produced by some of the other initiatives noted above.

It is well known that Europe is ahead on some ESG matters. Accordingly, the Think Tank relied heavily upon INREV’s ESG Guidelines to form the basis of the Principles. A Task Force of the Think Tank was formed to provide detailed feedback on the INREV ESG Guidelines, identifying which Guidelines are globally applicable and which Guidelines should be supplemented.

“INREV has long been focused on helping members understand and integrate climate and ESG considerations into their investment and portfolio decisions. Working closely with our members and our industry partners – especially through the ongoing global standards collaboration with the Reporting Standards – we remain committed to developing and embedding the most effective ways for the industry to measure progress, mitigate future risk, and contribute to the overall net-zero transition as we continue to support the Paris Agreement,” said Constantin Sorlescu, Director of Professional Standards, INREV.

During 2022, INREV will refresh its ESG Guidelines. As of this writing, the Reporting Standards and INREV are discussing how to move forward with the Principles and Guidelines collaboratively.

*The Reporting Standards ESG Principles for Reporting: a roadmap for the ESG journey, is a great place to start or advance on ESG reporting.*

In order to provide for scalability within the Principles, each of the four sections of the Principles consider environmental, social and governance elements.

The four sections of the Principles address the following:

- I. *Firm ESG information* includes firm policies, culture, DEI, training, goals, and thought leadership which are generally described in a Due Diligence Questionnaire (“DDQ”) and in periodic reporting as material changes occur.
- II. *Vehicle ESG overview* includes ESG targets, reporting considerations, and contractor/joint venture partner responsibilities which are generally described in vehicle formation documents and in periodic reporting as material changes occur.
- III. *Vehicle ESG strategy and objectives*: includes assessments of ESG within ongoing operations, management and exit strategies; identification of data elements to collect and report; and certifications/rating goals. These Principles are generally described within annual reporting to investors.
- IV. *Vehicle ESG Performance*: KPIs and rating scores, which would generally be updated at least annually.

Although investors and investment managers should be able to comply with Section I of the Principles regardless of where they are on their ESG journey, investors and investment managers should consider the following when assessing the scope of the minimum ESG information to request and provide:

- Firm size
- Fund structure
- Investment strategy
- Where firm is on its ESG journey and/or firm resources

This will encourage the investment manager to tell their own ESG story, which may not be afforded through other reporting frameworks.

*KPIs: Identified and prioritized to aid Principles implementation*

Currently, the Think Tank and Task Force are developing a set of key performance indicators (KPIs) which can be used to comply with the Principles, supplement DDQs, and generate periodic reporting to investors. The KPIs cover the whole of ESG and DEI for real estate and are recommended for use by managers and investors alike. The KPIs have been prioritized from ESG questions posed in industry benchmarks and Due Diligence Questionnaires. Definitions, formulas, and mapping to the Principles will also be developed to support and rank the KPIs. The KPIs will be published in the second quarter with broad-based industry feedback collected prior to publication

*It takes a village*

A collaborative, concentrated, and directed effort to achieve consistent, transparent, and scalable ESG information for the global real estate investment industry is no small task. Every association, standard-setter, and stakeholder bring a unique and valuable objective and perspective to the table. There is clearly no single solution, product, standard, or aspect of ESG most important to each stakeholder.

The Reporting Standards and its sponsorship intends to encourage the formation of a global ESG advisory board/think tank consisting of industry associations and their memberships to forge communication, prioritization, and collaboration of broad strategic plans for ESG within these groups.

The Reporting Standards ESG Task Force will be invited to actively participate in the newly formed NCREIF ESG Committee, which will kick off in March at the NCREIF Spring Conference in Phoenix. The Think Tank will remain as an advisory body, meeting regularly to ensure that the ESG Committee is up to date on the most relevant and important topics. “We are very eager to get the NCREIF ESG Committee off the ground. We will continue the work of the Reporting Standards’ Think Tank to facilitate and promote important discussions and prioritization of ESG in the institutional real estate community,” said Katie Milleville, Vice President of Ascentris, and vice-chair of the NCREIF ESG Committee. Committee participation is open to all NCREIF member firms, and participation of ESG staff within organizations is particularly encouraged. Please be sure to contact administrator@reportingstandards.info for further information.

<sup>1</sup>Environmental, Social (including Diversity, Equity, and Inclusion “DEI”), and Governance.