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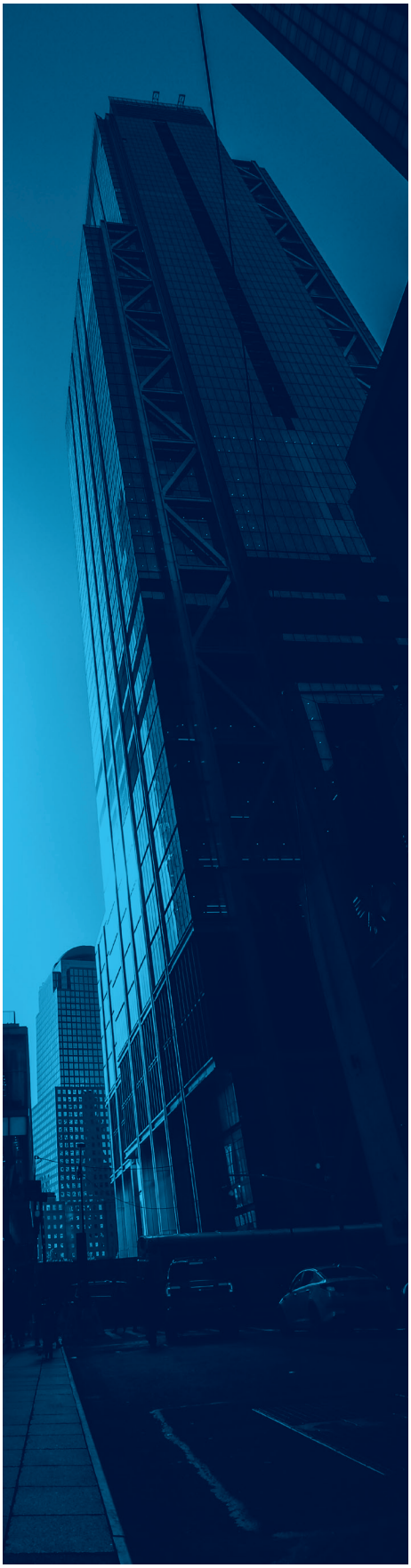
5 Ways to Normalize ESG into Operations & Reduce Reporting Burdens



There is no longer any doubt that environmental, social and governance (ESG) disclosure is necessary for every commercial real estate portfolio.

The challenge is clear. Owners and operators cannot continue to dedicate entire months to corralling vendors, gathering data, filling out surveys, and smoothing out edges to meet ever growing reporting requirements.

The solution is also clear. In order to continue to meet the demand for ESG disclosure, operations should be digitized so that reporting becomes a byproduct of routine workflows as opposed to a task in and of itself.

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The Current ESG Landscape

The Biden Administration has made its intentions clear. There have already been a broad range of policy changes around ESG disclosures, stricter regulations, incentivizing investors to price ESG criteria into decision-making, and reversing a Department of Labor rule that made it harder for retirement funds to invest in ESG-focused assets.

A similar political agenda is flowing up from the state and local level. According to Fifth Wall's **recent report**: "Policies such as Local Law 97 in New York City and the Green New Deal in Los Angeles are likely to set the standard across the nation. Conservative analysis estimates that New York City real estate asset owners could be on the hook for more than $10 billion in fines per year if they don't take action to reduce their carbon footprints — nearly an additional $9 per square foot above market rates."

In addition to public pressure, private investors are exerting significant influence. BlackRock, the world's largest asset manager, **published a document** laying out their specific expectations following CEO Larry Fink's letter in January calling on firms to align with global efforts to combat climate change, including voting against directors if the company fails to provide a credible plan. "We expect directors to have sufficient fluency in climate risk and the energy transition to enable the whole board — rather than a single director who is a 'climate expert' — to provide appropriate oversight of the company's plan and targets."

> "We expect directors to have sufficient fluency in climate risk and the energy transition to enable the whole board…

The growth of ESG-focused investment is likely driven by the studies that have shown a positive correlation between ESG and financial performance. Interestingly, according to a **report produced** by NYU and Rockefeller Asset Management, disclosure alone did not drive financial performance; companies that measured ESG metrics without an accompanying strategy tended to see a neutral or negative correlation with earnings.

These factors combined have essentially created a self fulfilling prophecy. The companies that perform well on ESG metrics will avoid fines and attract investment, increasing their relative competitiveness and allowing them to attract more investment.

The only question left is, how can more focus be dedicated to improving performance and less focus dedicated to data collection and entry?

The Reporting Burden

If there's anything that private investors and public regulators have in common, it's the desire for standardization in metrics and reporting. This aspiration has led to a growing number of reporting frameworks and benchmarking laws.

GRESB has become the gold standard for voluntary ESG reporting in commercial real estate. On the regulatory side, as of January 2021, there are nearly 40 state and local governments across the US that require some segment of commercial building owners to benchmark the energy performance of their buildings.

Unfortunately, these reporting frameworks and regulatory requirements have created a huge reporting burden for owners and operators of commercial real estate.

Many portfolios claim spending an entire month on GRESB reporting. The survey itself is long and the sources of data are siloed, manually extracted, and often only looked at once a year for reporting purposes. Real estate is notoriously fragmented, not only between different portfolios but within them.

This burden is a drag on performance and has significant opportunity costs for the operators, asset managers and sustainability teams involved.

Not to mention, reporting requirements are constantly getting more stringent.

For example, asset-level reporting is now mandatory in GRESB. Performance indicators, including energy, water, GHG emissions, and waste, must be monitored and reported in both landlord and tenant-controlled spaces. Efficiency Measures (Projects), Technical Assessments (Audits), Ratings, and Certifications are also now reportable on the asset-level.

All of this asset-level information is submitted through a spreadsheet that carries with it common issues such as versioning and lack of transparency into progress.

There are software solutions to help with reporting, but ultimately this is another "point solution" that services one narrow purpose on top of an already bloated tech stack.

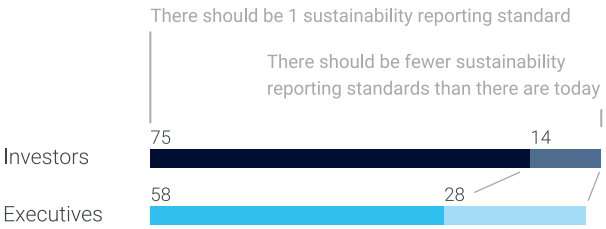
In order to improve this process, it's important to break it down into its component parts.

The truth is, ESG is a bit of a mixed concept. Environmental (E) performance is quantifiable in a way that Social (S) and Governance (G) metrics will never be.

Given this, while social and governance performance will continue to be measured through long qualitative surveys, there are big opportunities to streamline reporting of environmental performance as a byproduct of digitizing and improving operations overall.

Investors and executives say that reducing the number of sustainability reporting standards would be beneficial — and even that there should be legal mandates for reporting.

Respondents who agree with statement, %[1]



Companies should be required by law to issue sustainability reports

% of investors who agree or strongly agree that more standardization of sustainability reporting would do the following[1]

85
Help my firm allocate capital more effectively

83
Help my firm manage risk more effectively

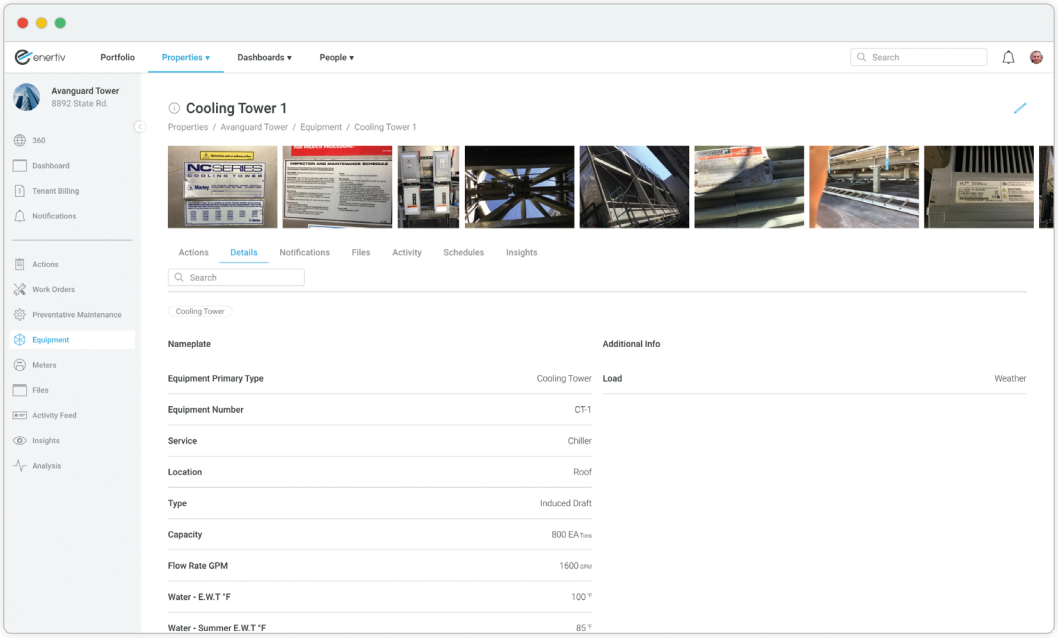
% of executives who agree or strongly agree that more standardization of sustainability reporting would do the following[1]

80
Help my company benchmark itself against its peers

68
Enhance my company's ability to create value or mitigate risk

[1]Repondents who answered "agree" or "strongly agree." For investors, n = 57; for executives, n = 50.

Source: McKinsey Sustainability Reporting Survey



1 | Asset & Reporting Characteristics

The GRESB Asset Spreadsheet for 2020 requires some basic information about the building before diving into performance metrics.

Currently, this includes "Asset Characteristics" such as each building's location, square footage, and property type. This also includes Building Certifications and "Reporting Characteristics" such as whether the building is tenant-controlled, the vacancy rate, the ownership period, and investment status.

While this high-level information can likely be pulled relatively quickly from another spreadsheet or a software like VTS, it can almost be guaranteed that the requirements around the "characteristics" of properties are only going to get more granular over time.

What happens when in a couple years, the survey inevitably asks how the building is heated and cooled, and then a couple years later, for an equipment inventory and capital plan?

> "...streamline data transfer during things like hand-off from developer to owner and during due diligence.

When these do become requirements, the reporting burden will increase exponentially.

On the other hand, digitizing this information today can improve the routine capital planning process and streamline data transfer during things like hand-off from developer to owner and during due diligence.

Then, when reporting requirements do increase, it will all be easily exported from a centralized place.

2 | Utility Consumption

The next step in the GRESB Asset Spreadsheet is to input the whole building utility consumption.

As simple as this would seem (after all, it's only 12 data points per building per utility), many portfolios struggle with this.

To be fair, there are a lot of moving parts. Digesting utility bills often requires understanding the context across different providers. There are a lot of moving parts and the utilities don't make it any easier to generalize.

All that being said, the primary reason that it's difficult to corral all of the utility data for GRESB reporting is that this information remains siloed and unused until it's time to submit.

> "…brough into a tool that only de-silos the information, but makes the budgeting process faster and more accurate…

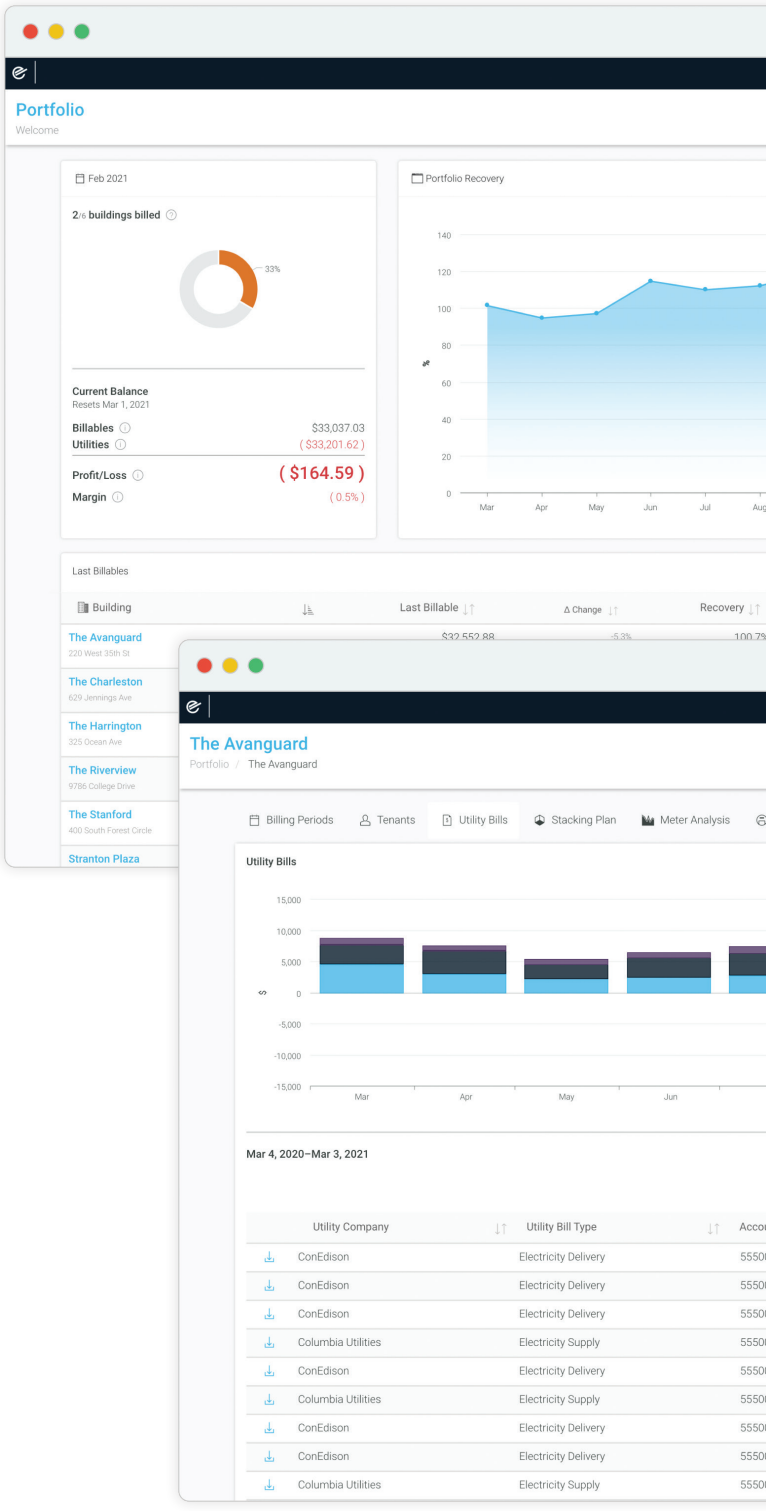
But there's a case for making this information available year-round.

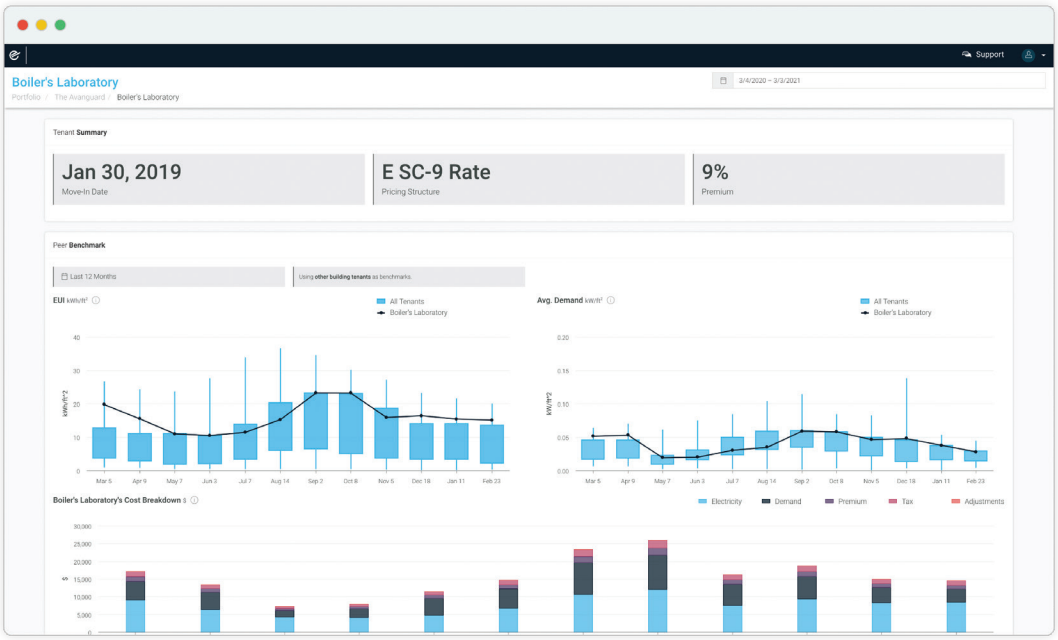
For example, many asset managers often do utility budgeting in spreadsheets and use basic assumptions, such as a flat 3% year-over-year increase, to forecast costs in the future.

This process could be brought into a tool that not only de-silos the information, but makes the budgeting process faster and more accurate based on a broad range of inputs.

This same tool could also connect to ENERGY STAR Portfolio Manager to push data to streamline benchmarking as well as pull data to create dashboards that live in a more accessible platform for team members who don't often login to the Portfolio Manager tool.

Again, as a byproduct of improving the budgeting, benchmarking and reporting process, a major aspect of ESG reporting becomes greatly simplified.





3 | Tenant Consumption

In addition to reporting on utility consumption, the GRESB Asset Spreadsheet has a section to submit base load and tenant consumption.

This is a level of granularity that many portfolios are simply not setup to report on. As far as tenant consumption, to get the aggregate number from an entire year, someone would have to manually compile a huge number of submetering spreadsheets and/or PDF documents.

To make matters worse, there is likely no portfolio today that has a standardized and up-to-date submetering infrastructure.

> "…tenant submetering in a software that not only generates bills, but is designed to report on analytics and easily aggregate and export data across a portfolio.

The sheer amount of effort required to do this is daunting for anyone, let alone operations and property management teams that are usually already stretched thin.

The solution is to digitize tenant submetering in a software that not only generates bills, but is designed to report on analytics and easily aggregate and export data across a portfolio.

In addition, many office tenants are looking towards getting ENERGY STAR certified, which requires metering what they are responsible for in the building. Providing this service, along with a tenant portal to view consumption, will be increasingly important.

4 | Efficiency Measures

Of all the sections of the GRESB Asset Spreadsheet that could be improved, it's the Efficiency Measures.

Currently, the survey asks true / false for whether a range of efficiency measures, such as automatic meter readings, automation or management systems upgrades, installation of high-efficiency equipment or renewable energy, occupier engagement, smart building technologies, systems commissioning, insulation or window replacements have been implemented in the last three years.

First of all, this presents a challenging fact-finding exercise for owners and operators. The answers to these true/false questions are generally not known at the portfolio level. They are only known by on-site teams, who likely have to rely on their memory to provide answers.

Secondly, true/false questions do not nearly capture the level of nuance that each of these categories have.

It's understandable that GRESB is starting here, but it can be guaranteed that as investors get more sophisticated and start to use this data to underwrite their decisions, they are going to demand more details.

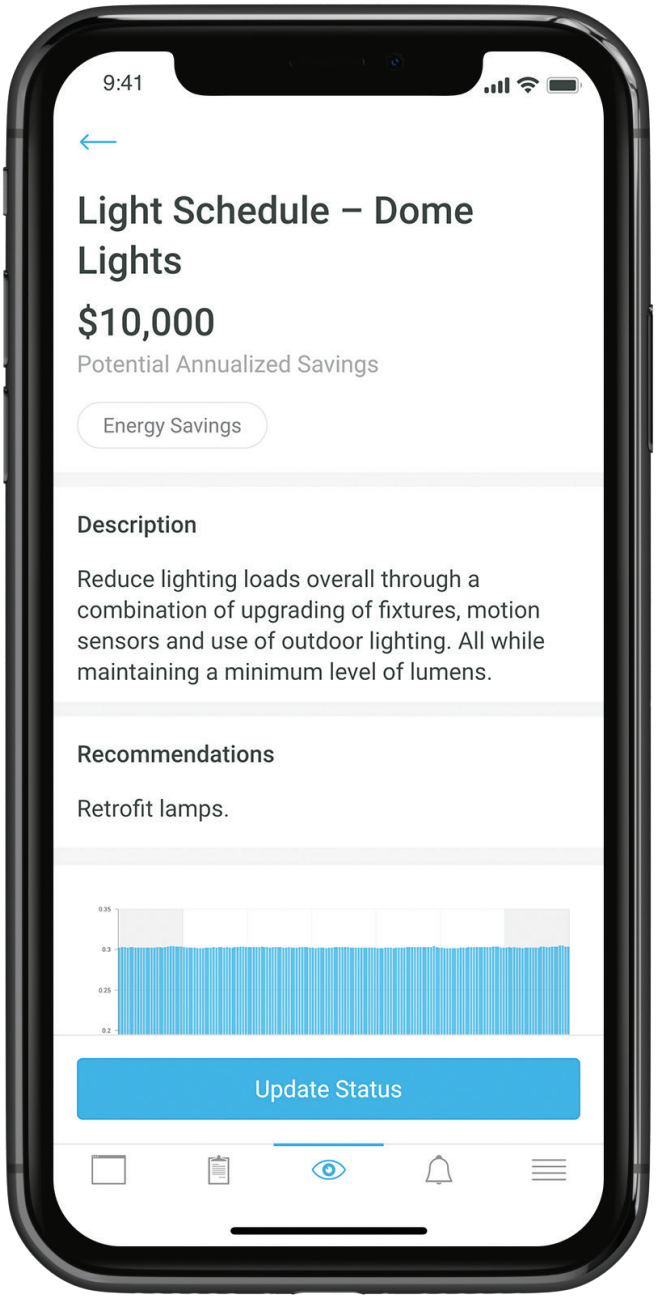
Specifically, what was done, when, and what were the expected vs actual results.

Ideally, this reporting, whether true/false or in a more detailed fashion flows directly from a platform designed to identify opportunities for efficiency measures, track implementation and measure results.

Simply tracking projects can be achieved with the same digitization used to improve capital planning mentioned above.

Once there is an equipment inventory in software, real-time monitoring can be deployed as needed to track the assets that are causing the biggest problems or using the most energy. With analytics applied to this monitoring, not only can efficiency measures be identified and prioritized, their results can be measured and verified.

With this setup, there will be no updates to reporting requirements that wouldn't be easily exportable from the platform.



5 | Waste Streams

Of all the quantifiable environmental metrics, waste is the most difficult to digitize. Generally, there is no utility or ENERGY STAR Portfolio Manager to pull the data from.

It must be collected from a variety of sources, all of which change dramatically depending on the region and market.

Worse, it is often not tracked in real-time and all the information must be manually compiled when reporting season comes around.

One way to fix this is treating waste disposal / removal just like a routine inspection. Operators are used to checking on temperatures, flow rates, and many other measures throughout the day.

So, using that same framework, a mobile app can be used to digitize information about waste removal as it happens. From there, it can be rolled up to the asset and portfolio level, monitored in real-time and easily exported when it's time to submit reporting.

Interested in Digitizing Operations to Reduce ESG Reporting Burdens?

Demo the Enertiv Platform

enertiv.com/get-started