



ESG in treasury

ACTA – Essential Treasurer Day

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Agenda

1. ESG definition and drivers
2. ESG hot topics and trends
3. Corporate treasurers ESG agenda
4. Bank treasury products
5. ESG products – Accounting implications

Key takeaways

1. There is significant momentum across the business towards 'greener' and more ESG-centric activities aimed at addressing ESG risks and opportunities.
2. Commitment of corporate treasurers to ESG agenda is steadily increasing as the expectations from the shareholders, regulatory bodies, clients/vendors and employees also increase.
3. Banks are providing a wide range of treasury products that adapted the ESG product framework and may help accelerate the broader revenue and growth goals of the business. It is important to understand how those products operate and what accounting consequences they might have.



Stefanija Cubelic

Director

ESG definition and drivers

The **CFA Institute** believes that **ESG factoring** (i.e., material ESG information and considerations) *is an important component of a complete and thorough financial analysis* for any actively managed fundamental investment portfolio.

Environmental	Social	Governance
<ul style="list-style-type: none">• Climate risk• Carbon emission• Energy efficiency• Pollution and waste management• Use of natural resources• Clean energy and technologies• Biodiversity	<ul style="list-style-type: none">• Human capital• Labour relations and working conditions• Diversity agenda• Employee safety• Product safety• Human rights• Child labour• Corruption and bribery• Anti-money laundering	<ul style="list-style-type: none">• Board diversity• Business ethics• Risk tolerance• Compensation policies• Escalation protocols

ESG definition and drivers

Shareholder pressure

Record support for environmental and social topics in 2021: 20% of proposals that went to a vote received more than 50% support. ¹

Regulatory developments

Jurisdictions around the world are developing guidance on ESG disclosures.

Clients/Vendors

B2B customers are increasing their ESG requirements for suppliers. Consumers continue socially conscious buying.

Social license to operate

Communities are requiring engagement and increased transparency.

Employee demands

Millennials identify corporate sustainable strategies as a crucial consideration for career decisions. ²

ESG hot topics and trends

Climate change and net zero

- Address and disclose risks and opportunities associated with climate change
- Achieve net-zero emissions in lending/investments

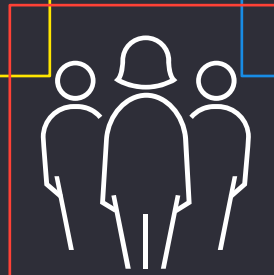
Human rights

- Demonstration of protection of basic human rights e.g., related to child labour and forced labour, fair wages and freedom of association



Underserved groups and equity

- Demonstration of deployment of capital towards ESG opportunities benefiting vulnerable people/communications



Sustainable finance

- Demonstration of deployment of capital towards ESG opportunities

Corporate treasurer ESG agenda

Treasury governance

- Business relation partners
- Green treasury policy

Investments

- Strategic asset allocation

Financing

- Green bond
- Green loan

Operations

- Digital payments
- Online bank statements
- Other paper products

Reporting

- Impact reporting

Based on a survey (finance and treasury professionals of top 80 large UK corporates), more than two-thirds (71%) of respondents expect to include ESG or sustainability features in their next financing.

71%

The latest finding follows a steady increase in treasurer commitment to ESG and sustainability over the past two years (50% in 2020 and 65% in 2021, respectively).

65%

At 47%, sustainability-linked loans are the most likely to be implemented by firms surveyed, followed by sustainability-linked bonds and green bonds, each at 28%, respectively. *

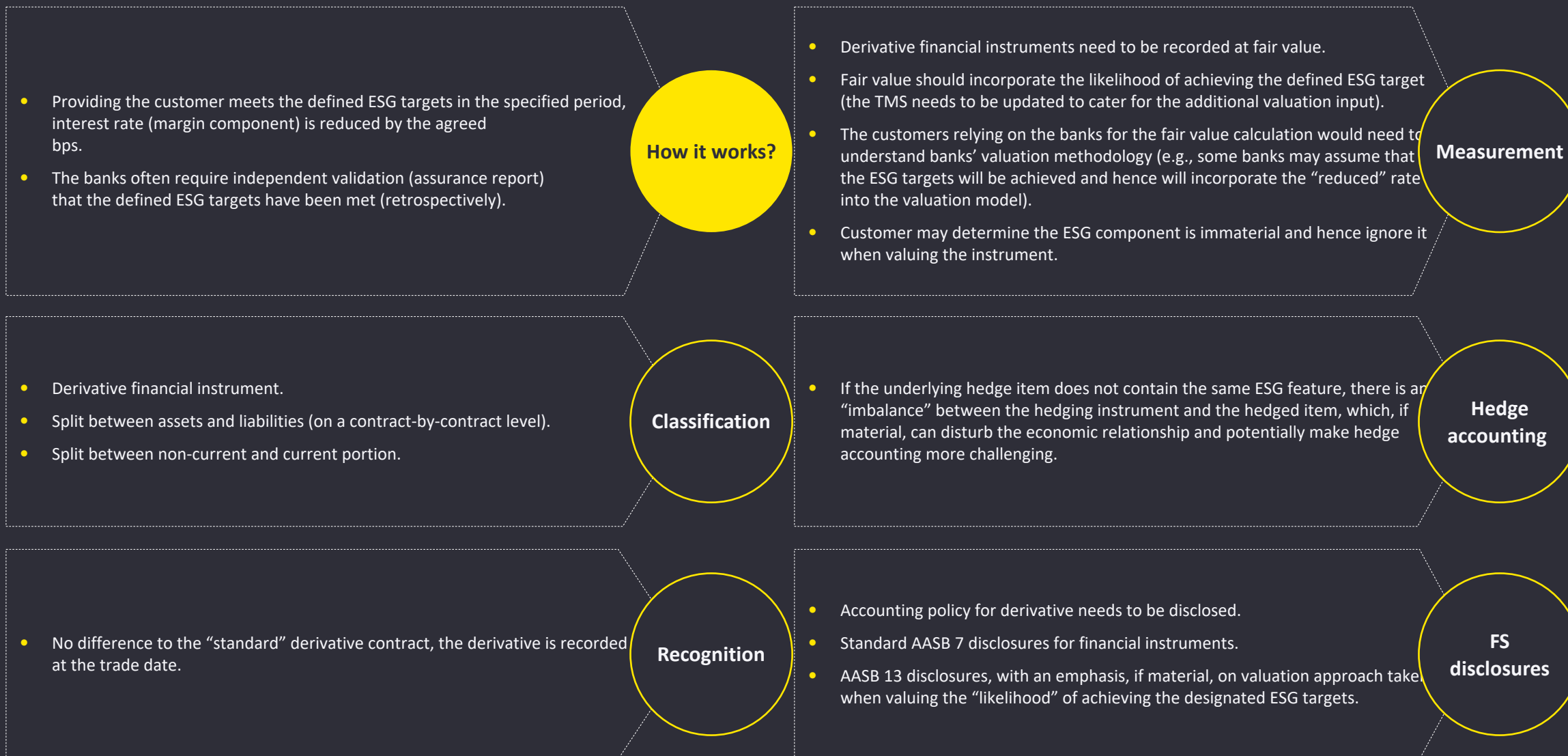
47%

Bank ESG products



ESG Products – Accounting implications

ESG-linked derivative financial instruments (IRS)



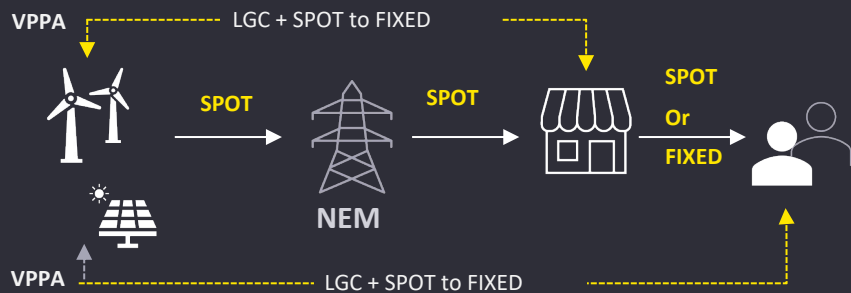
ESG Products – Accounting implications

ESG-linked loan (holder/borrower)



ESG Products – Accounting implications

Power Purchase Agreements (synthetic or VPPA)



How it works?

- Electricity derivative is measured at fair value with the changes in the fair value recognised in the PL, unless hedge accounting is applied.
- EC measurement depends on the chosen accounting policy and business model
 - Inventories (cost vs NRV or fair value less cost to sell) or
 - Intangibles (cost less any impairment vs revaluation model).

Measurement

- VPPA is considered a host environmental certificate (EC) contract (“green component”) with an embedded electricity derivative (“black component”).
- The embedded electricity derivative needs to be bifurcated from the host contract and accounted separately (at day one).
- Energy certificates are classified as:
 - Inventories or
 - Intangible assets.

Classification

- It is possible to designate the electricity derivative into a hedge relationship, providing that all the AASB 9 hedge accounting requirements are met (economic relationship, impact of the credit risk, eligible hedged item, highly probable forecast of electricity purchase, hedge accounting documentation, etc.).
- Detailed analysis is required before hedge accounting designation to assess all the criteria.

Hedge accounting

- Electricity component classified as a derivative financial instrument is recognised at the trade date.
- Environmental certificate (e.g., LGC) are recognised when purchased (at cost).

Recognition

- Accounting policies for embedded derivative and EC need to be disclosed.
- Standard AASB 102 or AASB 138 disclosure requirements for EC, depending on the chosen accounting policy.
- Standard AASB 7 disclosures for financial instruments.
- AASB 13 disclosures, with an emphasis on the Level 3 hierarchy related disclosures.

FS disclosures

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