BRIGHAM YOUNG UNIVERSITY
FOUNDED
BYU
1875
PROVO, UTAH

J. Reuben Clark Law School

"ESG Transparency of Private Equity and Debt Firms"

by

Pascal Böni, Jurian Hendrikse & Philip Joos

Comments by
William W. Clayton

Overview of Paper

- Examines ESG transparency in private equity and private debt funds
- Preqin dataset contains 37 ESG disclosure indicators "most relevant to the setting of private capital markets"
- Paper finds that:
  - ESG disclosure by GPs is low compared to public firms
  - Larger, listed, older, and more recently fund-raising GPs, as well as GPs in Europe, are more transparent, and those following VC strategy are less transparent
  - GP's region of headquarters and investor base were also significant drivers of GP disclosures
- The findings "may support the need for further private market ESG disclosure regulations" and "simultaneously provide nuance to claims that private markets are completely opaque"

Overview of Comments

1. How concerned should we be if there's weak ESG transparency in private funds?

2. A closer look at the 37 indicators and the comparison with public firms

3. Some concluding questions

→Great topic, shining light on an important blind spot in an extremely large and consequential market

How concerned should we be if there's weak ESG transparency in private funds?

Maybe a policy response could be worth considering:

- Cancels out the benefits of public market ESG?
- Lost potential – could ESG work even *better* in private funds?

Some problems with ESG in public settings could theoretically be improved in private funds

Divestment versus engagement

Greenwashing concerns

How concerned should we be if there's weak ESG transparency in private funds?

Maybe a policy response could be worth considering:

- Cancels out the benefits of public market ESG?
- Lost potential – could ESG work even *better* in private funds?

Maybe not:

- Are GPs just providing the level of ESG disclosure that LPs actually want?
- Maybe weak ESG transparency is a feature, not a bug?

A closer look at the 37 indicators

Environmental (all factors)

Does the firm disclose any policy related to climate change, carbon or emissions?

Does the firm disclose their carbon or greenhouse gas (GHG) emmisions?

Does the firm track the emissions of portfolio companies/ assets?

Does the Firm obtain environmental impact studies for each of its portfolio company and property investments?

A closer look at the 37 indicators

Social (all factors)

Does the firm have a modern slavery policy?

Does the firm mention that it adheres to any ISO standards?

Does the firm have a privacy policy?

Does the firm have a diversity and inclusion policy?

Does the firm provide education to portfolio companies about ESG issues?

What is the firm's AUM for ESG specific funds?

Does the firm disclose their AUM targeting impact or SDG-related investments?

A closer look at the 37 indicators

Governance (selected factors)

Does the firm mention consideration of ESG factors in its investment process?

Does the firm consider ESG factors before making an investment?

Does the firm disclose who is responsible for ESG at the firm at executive level?

Does the firm mention the types of investors they work with?

Does the firm mention any consideration of ESG?

Does the firm consider ESG factors after making an investment?

Does the firm have a dedicated ESG team?

Does the firm monitor ESG performance in their portfolio companies?

Potential for opportunism by GPs? It wouldn't be the first time…

"***Many limited partnership agreements are broad*** in their characterization of the types of fees and expenses that can be charged to portfolio companies. This has created an enormous grey area, ***allowing advisers to charge fees and pass along expenses that are not reasonably contemplated by investors***."

"When we have examined how fees and expenses are handled by advisers to private equity funds, we have identified what we believe are ***violations of law or material weaknesses in controls over 50% of the time***."

Head of SEC Exams Unit (Mar. 2014)

If the bar is low, why aren't GPs' ESG scores higher?

Maybe LPs *really* don't care about ESG (and the political and social pressure to have good ESG practices isn't very strong either)?

Maybe these kinds of policies and procedures are too costly to produce unless done at scale?

Maybe there are *other* important ESG disclosures not captured by the Preqin data?
→The 37 indicators are drawn primarily from publicly available data. But maybe GPs are also providing valuable disclosures to LPs privately?

The comparison with public firms

The Preqin ESG score for PE and PD firms is based on a total of **37 indicators**.

The Refinitiv ESG score for public firms is based on a total of **156 indicators**.

But the authors found only **7 indicators** that overlapped between the two.

If there are only 7 overlapping indicators, how strong is this comparison? Can we draw firm conclusions about how transparent private funds are compared to public firms based on this limited set of data points?

Conclusion

Great topic in an important, understudied area

Provides a useful descriptive account and also raises some important questions about what exactly the data says about ESG transparency in private funds and the policy implications