Item 03 – Sector Program Description

For GSSB discussion

Date	13 November 2018
Meeting	29 November 2018
Program	Sector Program
Description	This document describes objectives, scope and process of GRI's Sector Program, for discussion by the GSSB.

Program Purpose

As reported by the Sustainable Development Goals Report 2018, urgent and accelerated actions are needed to address global challenges facing the economy, the environment and society.[1] More clarity is needed on which issues constitute the sector's most significant impacts from a sustainable development perspective and how these might be addressed in sustainability reporting and in company strategies.[2] A firm foundation providing authoritative information on sectoral impacts can:

- focus corporate reporting toward organizations' most significant impacts;
- support existing corporate reporters;
- encourage new reporters to participate in sustainability reporting;
- support stakeholders that use sustainability reporting in their decision-making, such as investors, regulators or mediating institutions;
- support civil discourse on sustainability issues, providing information to civil society or media;
- meet demand for up-to-date and authoritative Sector Standards.

The Sector Program aligns with GRI's mission to empower decisions that create social, environmental and economic benefits for everyone. Providing Sector Standards will help to focus sustainability reporting on the issues that matter most from a sustainable development perspective, leading to a stronger foundation for sustainable decision-making. The Sector Program can help stakeholders speak a common language, build a common understanding of sustainability priorities for covered sectors, and inform stakeholder engagement with companies.

Furthermore, the Sector Program can help surface emerging issues for future development in the Standards, which will help the GSSB deliver on its commitment to continuously improve the GRI Standards. The Sector Program will help to complete the reporting framework provided by the GRI Standards.

High-Level Requirements

The GSSB will approve high-level requirements for the Sector Program. The Standards Division has identified the following high-level requirements:

- **Process**: The Sector Program is to follow the Due Process Protocol, including a multi-stakeholder process for content development as well as exposure to public comment.

- **Deliverables:** The Sector Program intends to produce regular releases of Sector Standards, beginning with the commencement of a pilot project in 2019 (see Item 04 – Sector Program Pilot Project Proposal). The Standards Division will propose the number and sequencing of sectors to be covered in the Sector Program for the approval of the GSSB.

- **Quality**: Publications are to be well evidenced, and to have excellent technical quality and clear definitions. Sector Standards are intended to be clear and user friendly to promote uptake among corporate reporters, as well as other stakeholders that use sustainability reporting to empower sustainable decision-making.

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[1] United Nations, *The Sustainable Development Goals Report 2018*, accessed on 23 October 2018.
[2] For example, the World Business Council for Sustainable Development's (WBCSD's), *Materiality in Corporate Reporting – A White Paper focusing on the food and agriculture sector 2017*, accessed on 23 October 2018, has highlighted inconsistencies in identified material issues in sustainability reporting in the food sector.

40 • **Authority and Credibility:** Sector Standards should be perceived as authoritative and credible.

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42 • **Enhancement of the technical features of the GRI Reporting Framework**: The Sector
43 Program is to support the enhancement and expansion of the GRI reporting by explaining a sector's
44 impacts and stakeholder expectations, including surfacing issues not previously covered in the GRI
45 Standards.

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Sector Program Process

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49 The process for developing Sector Standards is expected to involve:

50 • conducting preliminary desktop research on issues of relevance to a given sector;

51 • forming a multi-stakeholder, expert Project Working Group;

52 • surveying the Group for identification of significant impacts and stakeholder expectations and analyzing
53 survey results;

54 • vetting identified issues and their descriptions through a multi-stakeholder process (draft development),
55 using a combination of virtual and in-person group meetings as well as one-on-one meetings, as
56 warranted;

57 • exposure of draft Sector Standards to public comment and incorporation of public feedback;

58 • finalization and release of the Sector Standard.

59 It is currently anticipated that an average sector project lifecycle is approximately 15 months. The process and
60 timelines will be field tested during the pilot project. Learnings from the pilot project may cause changes in
61 scope or process that may impact the project lifecycle.

62 The project cycle is expected to repeat, incorporating lessons learned, for subsequent sectors. After the desired
63 sector coverage is achieved, the Sector Program will transition to a recurring maintenance cycle. Sector
64 Standards will continue to evolve to align with the GRI Standards and to reflect developments and emerging
65 issues within sectors.

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Program scope

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68 The Standards Division has conducted preliminary analysis on sector coverage and will propose the number and
69 sequencing of sectors to be covered in the Sector Program for the GSSB's approval. The GSSB will decide the
70 sectors to be covered by the program and the order of these sectors within the GSSB Work Program,
71 incorporating public feedback on the Work Program.

72 The Standards Division will include the following criteria to prioritize sectors:

73 • the number of existing GRI reports on the sector;

74 • the economic, environmental and social impacts of the sector; and

75 • the strength of the literature on the sector's impacts and role in sustainable development.

76 In addition, the Standards Division has reviewed several sector classification systems in its analysis of sector
77 coverage, to determine whether adopting an existing external sector classification system would be beneficial for
78 the Sector Program. The Standards Division has also reviewed documentation and stakeholder feedback gathered
79 by GRI in previous years on this issue. (More detail on external sector classification systems and stakeholder
80 feedback related to these in provided in Annex I: Sector Classifications.)

81 The main observations drawn from this review are as follows:

82 • Interviewed stakeholders did not agree on whether an external sector classification system was suited
83   for the Sector Program, and if so, which one;

84 • Some stakeholders noted that external classification systems were not designed for GRI's needs in the
85   sector program, and only partially align with those needs;

86 • External sector classification systems are not recognized or understood by some stakeholders.

87 In light of these observations, the Standards Division recommends against adopting an external sector
88 classification system for the Sector Program. The Standards Division has developed a preliminary naming system
89 that uses 'common denominator' names (e.g. mining, oil and gas, agriculture) that are intended to be
90 recognizable to all stakeholders, regardless of the classification systems they use, to avoid privileging some
91 stakeholders while creating barriers or challenges for others.

92 The Standards Division will recommend a sector name and the desired constituents of a sector project at the
93 project proposal stage (e.g. Item 04 – Sector Program Pilot Project Proposal). The Standards Division further
94 proposes to include a key to predominant external sector classification systems within each sector project
95 proposal for the GSSB's consideration. The GSSB can approve the draft name and key when approving a draft
96 standard for public comment, taking into account feedback from the Project Working Group, and can consider
97 public feedback on the name and key when approving a Sector Standard for final release.

98 An example of a key for two sectors is provided in the table below.

99 Table 3: Key linking sectors within the Sector Program to GICS, ICB and ISIC equivalents

Sector Standard Name	GICS No.	GICS Name	ICB No.	ICB Name	ISIC No.	ISIC Name
Mining	151040	Metals & Mining	551020	Industrial Metals & Mining	Division 05	Mining of Coal and Lignite
	151040	Coal & Consumable Fuels	551030	Precious Metals & Mining	Division 07	Mining of Metal Ores
			60101040	Coal	Division 24	Manufacture of Basic Metals
			60102010	Alternative Fuels		
Oil and gas	101020	Oil, Gas & Consumable Fuels	601010	Non-Renewable Energy	Division 06	Extraction of crude petroleum and natural gas
					Division 19	Manufacture of coke and refined petroleum products

Next Steps – Pilot Project

The Sector Program will begin with a pilot project to field test the sector strategy, streamline processes and build team capacity (e.g. Item 04 – Sector Program Pilot Project Proposal).

After the pilot is completed and lessons learned, the intention is to scale up to running multiple projects concurrently to allow completion of desired sector coverage. Scale-up depends on securing additional resources.

The GSSB will approve sector projects before commencement, will approve the membership of project working groups, will provide feedback on content development, will approve draft Sector Standards for public exposure, and will approve all final Sector Standards.

Summary Milestones *Significant events in the project e.g., the completion of key deliverables or beginning/completion of a project.*	Due Date
GSSB approval of Program Charter	Jan 31 2019
GSSB approval of Sector Pilot Project Proposal	Jan 31 2019
GSSB subcommittee convenes as needed to guide direction of program	December 1 2018 – February 21 2019
Commencement of Pilot Project: Appointment of Project Working Group	Call for nominations for Project Working Group in February 2019
GSSB approves Project Working Group membership via electronic vote	April 2019
GSSB approves draft Sector Standard for public exposure (pilot project)	Anticipated in October 2019
Public comment period	November 1 2019 – January 15 2020
GSSB approves final draft of Sector Standard (pilot project)	Anticipated in April 2020
Launch of Sector Standard (pilot project)	June 2020
Commencement of Subsequent Sector Projects	Project lifecycle anticipated to be 18 months; how many projects can be run concurrently depends on resources

115   *Input requested from the GSSB*

Comments are invited on:

1. The program **objectives, scope and process** outlined in this draft proposal.

2. The Standards Division proposes to organize a GSSB subcommittee of three members to advise on the direction of the Sector Program. Please indicate which members would like to volunteer to be on a **Sector Program Subcommittee**.

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Annex 1 Sector classifications

The GSSB discussed the workplan for the GRI Sector Program in November 2015 and April 2016 meetings, including the potential selection of an external sector classification system for GRI's Sector Program.

In 2015, the Standards Division conducted a limited initial stakeholder consultation with 25 stakeholders to determine the suitability of using an external sector classification system within GRI's Sector Program. Stakeholders were not asked to gauge cost or feasibility.

The consultation focused on three options deemed likely to be most suitable for the Sector Program:

- the Global Industry Classification Standard (GICS), a proprietary classification developed by Standard & Poor's and MSCI;

- the Industry Classification Benchmark (ICB), a proprietary classification developed by Dow Jones and FTSE Russell;

- the International Standard Industrial Classification of All Economic Activities (ISIC), a public classification developed by the United Nations.

Stakeholder feedback received in 2015 revealed three predominant viewpoints. Stakeholders either:

- exhibited a strong preference for classification systems commonly used by investors such as GICS or ICB, which were designed for investment purposes;

- exhibited a preference for the United Nations sector classification ISIC, which is non-proprietary and designed to enable international statistical analysis; or,

- had no knowledge of the classification systems in question, recommended alternative classification systems, or questioned the benefit of selecting an external sector classification system for use in the Sector Program.

Characteristics of sector classification systems

Sector classification systems organize and classify companies hierarchically, with larger groups of companies containing aggregations of smaller groups. For example:

- GICS includes sectors>industry groups>industries>sub-industries;
- ICB includes industries>supersectors>sectors>subsectors; and
- ISIC includes sections>divisions>groups>classes.

Individual corporate entities are assigned to GICS and ICB by those who maintain the classifications. ISIC, on the other hand, does not assign individual corporate entities, though entities may be assigned by nations or governments to classes or groups within ISIC for the purposes of statistical analysis.

Investment-based classification systems

Investment-based sector classification systems such as GICS and ICB group companies together based on market or production-related characteristics. An investment-based sector classification system groups together companies that are expected to more tightly correlate in terms of financial performance rather than the overall market.[3] These groupings are used in investment strategies. For example, an asset manager might decide to

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[3] See, for example, Investopedia, _GICS Vs. ICB: Systems For Classifying Stocks_ 2018, accessed 23 October 2018 and ETF.com, _Test-Driving Industry Classifications_ 2009, accessed 23 October 2018.

152	underweight or overweight a particular sector as part of an investment strategy. Where a company is grouped
153	may impact how its shares are bought, sold or traded. For example, planned movement of telecom companies
154	within the GICS classification system to Communications Services in 2019 is anticipated affect the weight of
155	these companies within certain indices.[4]

156 Investment-based classification systems are:

157 • proprietary and cannot be used without licensing fees;
158 • complex and difficult to develop and maintain, as they assign individual entities to groupings;
159 • hardwired into databases and IT infrastructure;
160 • ingrained within investment organizations, habituating frequent users to certain terminologies.

161 These factors drive stakeholder affiliation with a classification system. Stakeholders within research and
162 investment institutions are strongly attached to the classification system used in their daily work.

163 The investment-based sector classification landscape is evolving and changing. Updates to classification systems
164 as business evolves also mean that it is more difficult to anticipate which sector nomenclature will remain valid in
165 3-5 years. For example, both GICS and ICB are undergoing revisions within the next 1-2 years.[5] Predetermining
166 a sector classification for a Sector Program intended to run for multiple years would have unforeseen
167 implications as these shifts occur.

United Nations-based classification system (ISIC)

169 The United Nations International Standard Industrial Classification of All Economic Activities (ISIC) is non-
170 proprietary. It is designed and maintained by the United Nations Statistics Division for the public good. The
171 development and maintenance is governed by the Committee for the Coordination of Statistical Activities,
172 including 45 international and supranational organizations, by the Principles governing international statistics
173 activities. ISIC is available free of charge on the ISIC webpages of the UN Statistics Division.

174 ISIC is designed for economic analysis and policy-making and is used by governments as a framework for
175 statistical analysis. The fourth revision of ISIC occurred in 2008, adding more granularity to allow stakeholders
176 to be more specific in statistical analysis. For example, ISIC's Manufacturing section has 28 separate divisions,
177 which are further broken down into groups and classes: Division 33 (Repair and installation of machinery and
178 equipment) is further subdivided into two groups (Repair of fabricated metal products, machinery and
179 equipment; and Installation of industrial machinery and equipment), and the Repair group is further divided into
180 six classes. ISIC's granularity in some sense treats business entities as 'pure plays' engaged in a single business
181 activity, which is becoming a rarity in the corporate landscape.

182 Most nations worldwide have adapted ISIC to their national statistics systems, though some nations may also use
183 their own classifications systems for statistical analysis (e.g., SIC codes in the UK, SIC/NAICS Code in the USA,
184 and GB/T 4754-2011 in China).
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186 In terms of updates, ISIC is considerably more stable (i.e., has fewer updates) than investment-based
187 classifications. However, this means that ISIC may diverge significantly from investment-based classification
188 systems over time, increasing a sense of unfamiliarity among reporters or report users that are accustomed to
189 investment-based classifications.
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[4] See Business Insider Netherland, *GICS Sector Reclassification 2018*, accessed 23 October 2018 and Fidelity, Know your sectors and industries. Available at: https://tinyurl.com/ybfcbhl4. [Accessed See Business Insider Netherland, *GICS Sector Reclassification 2018*, accessed 23 October 2018 and Fidelity, *Know your sectors and industries 2018*, accessed 23 October 2018.

[5] GICS – MSCI, *GCIS Structure Change 2018*, accessed 09/11/18 and FTSE Russell, *Industry Classification Benchmark 2017*, accessed 23 October 2018]

191 Generally speaking, corporate reporters as well as investors who commonly use information from sustainability
192 reporting in decision-making are less accustomed to working with ISIC. Governments and international agencies,
193 on the other hand, are less accustomed to working with GICS and ICB. Selecting one external classification
194 system may therefore add confusion for stakeholders accustomed to other classification systems.

Stakeholder feedback summary
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197 Sector classification systems were discussed informally in individual meetings with 25 stakeholders in 2015. The
198 stakeholders included labor, investors, ratings agencies, companies, civil society, as well as two internal
199 stakeholders within GRI who actively engage with governments and international organizations.

200 The feedback reflects three different stances: pro-investment-oriented classifications; pro-internationally
201 oriented classification; and unfamiliarity or uncertainty that the Sector Program requires an external classification
202 to fulfill its purpose and to serve the public interest.

Feedback in favor of investment-based classification systems

204 Below are representative quotations from stakeholder feedback in favor of investment-based classification
205 systems. The feedback notes the importance of investors as sustainability report users, and notes that reporting
206 organizations may be more comfortable with an investment-based classification. The feedback also sees frequent
207 updating on investment-based classifications as a benefit.

208   "The language used by GICS and ICB might be closer to how companies speak about themselves."

209   "Strong preference for GICS because it is focused on investors and adopts a market-oriented
210   approach."

211   "GICS is updated more frequently, for the last time in 2014. The business world is changing often and
212   new sectors are being created as we speak. ICB was last updated in 2007 and ISIC in 2008, which is a
213   very long time ago."

214   "The system should have a relation to investors and analysts, as they are the main driver of
215   sustainability reporting."

216   "GRI should consider the system that is currently most widely used for investors."

217   "GICS or ICB is preferable as it is easy for companies to relate to."

218   "The link to integrated reporting may be easier if a system is chosen that is used for financial
219   reporting."

Feedback in favor of UN-based classification system (ISIC)

221 Below is a sample of feedback in favor of the United Nations-based classification system ISIC. The feedback
222 responds favorably to ISIC as non-commercial and promoting the public interest, and notes that the choice of an
223 investment-based classification system might be seen as problematic by non-investor stakeholders.

224   "The UN ISIC system seems the most neutral for GRI to base its sector standards on. It is expected
225   that stakeholders in the Labor constituency find this classification acceptable for GRI to use."

226   "It seems important to recognize that ISIC was developed for the public interest and not so much for a
227   commercial purpose. A system that is designed for stock exchanges and investors might have a negative
228   connotation for some target groups."

229   "The preference is for ISIC. It is designed in the interest of the public (rather than) revenue
230   generation."

231 Feedback expressing unfamiliarity/uncertainty with the proposed classification
232 systems

233 Below is a sample of feedback suggesting lack of familiarity or uncertainty regarding the usefulness of selecting a
234 classification system. The feedback suggests that for some stakeholders, classification systems are not within
235 their frame of reference, and that adopting a single classification system may not be helpful or necessary for the
236 Sector Program.

237   "(We were) not familiar with ICB, GICS, or ISIC before."

238   "The ideal approach would be to ask each company who their competitors are and to compare them
239   with those."

240   "Often sectors are difficult to assign and there is much overlap and differences between one sector."

241   "Perhaps it is possible to use GICS and ISIC at the same time?"

242   "The choice of classification depends on what you are going to use it for."

243   "It is doubtful whether any of these systems is suitable for GRI purposes, as these are designed for
244   other purposes."

245   "It is important that GRI clarifies the problem that we are trying to solve."

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247 *Proposal: A more flexible approach*
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249 Proprietary classification systems are important for investment purposes, and a non-proprietary international
250 framework is important for statistical and economic analysis. However, the purposes served by both types of
251 classification system are different from and the purpose of GRI's Sector Program.

252 GRI's sector program needs to name and define particular groups of businesses that are similar in terms of
253 business activities and sustainability impacts, in order to develop contents for these businesses. GRI's sector
254 program also needs to identify and define sectors in a way that resonates with corporate reporters and those
255 who use sustainability reporters for decision-making. Finally, GRI's sector program may need to name and define
256 entities that are not usually covered in sector classification systems, such as universities, public agencies or non-
257 governmental organizations.

258 It is pragmatic to be able to make decisions on naming and definition of sectors when needed (at project
259 proposal stage), rather than years in advance of a particular project. A flexible approach will ensure that Sector
260 Standards are named and structured in a way that is appropriate when the project occurs.