

Part 2

UNDERSTANDING ESG AND
HEALTHCARE INNOVATION:

**IMPLEMENTING ESG
IN EARLY- AND
GROWTH-STAGE
HEALTHCARE COMPANIES**



This is the second in a series of papers taking investors and healthcare leaders on an “ESG journey”: what it is, why it matters, and how to put ESG into practice.

Introduction

In [Part 1](#) of the series, we introduced the concept of ESG and explained why it is an increasingly important issue for companies of any size. With sustainable investing on the rise, professional investors and their clients are demanding evermore comprehensive ESG disclosures, and many will only invest in companies above a certain ESG rating. The extent to which a company is focused on ESG thus has a direct impact on its access to capital.

So, it is even in the interests of early- to growth-stage companies to improve both their ESG rating and the depth of ESG-related information they disclose. The best way to start refining ESG practices for an organisation is to conduct an ESG health

check — this reveals the company's compliance to ESG standards and demonstrates where it can make improvements.

Tackling ESG can be daunting. Even more so for start-up companies, which often lack the resources of more established organisations. This is why we support our portfolio companies in conducting ESG health checks, and why we are making these resources accessible to the wider industry.

In this paper, we explain how we conduct ESG health checks, along with our key recommendations for start-up healthcare companies looking to embark on their ESG journey.

Defining our approach

Last year, we set out to support our portfolio companies with their ESG reporting. The first step was to identify the best way to conduct an ESG health check that is rigorous, while being suitable for start-ups and early- to growth-stage companies.

We approached several ESG consulting firms and rating agencies to find that most focused only on public or large private companies, using approaches

that were too comprehensive and resource-hungry for start-ups. We eventually found an independent provider called Apex Group, which offers an ESG questionnaire and follow-up reports designed specifically for private companies and therefore well suited to our portfolio companies. Apex Group is one of the world's largest financial services providers with a global presence of 85 offices.

STANDARDS AND FRAMEWORKS REPRESENTED BY THE APEX GROUP ESG QUESTIONNAIRE:

- ESG Data Convergence Project¹
- The EU's Sustainable Finance Disclosure Regulation (SFDR)²
- Global Reporting Initiative (GRI)³
- International Labour Organization⁴
- International Organization for Standardization (ISO)⁵
- Sustainability Accounting Standards Board (SASB)⁶
- Task Force on Climate-related Financial Disclosures (TCFD)⁷
- UN Global Compact⁸
- UN Sustainable Development Goals (SDGs)⁹

We chose Apex Group's ESG Health Check because:

- ▶ It offers a "light" ESG questionnaire containing just 40–50 data points, making it relatively straightforward to complete
- ▶ It provides an industry benchmark, allowing companies to understand where they stand in relation to peers
- ▶ The questionnaire produces a dataset that is aligned with key international standards and frameworks, which define sustainable business practices and shape emerging regulations

¹ ESG Data Convergence Project. ILPA. 2022. https://ilpa.org/ilpa_esg_roadmap/esg_data_convergence_project/ (Accessed 17 June 2022) ² SFDR. Eurosif. <https://www.eurosif.org/policies/sfdr/> (Accessed 17 June 2022) ³ Global Reporting Initiative. <https://www.globalreporting.org> (Accessed 30 June 2022). ⁴ International Labour Organization. <https://www.ilo.org/> (Accessed 17 June 2022) ⁵ International Organization for Standardization. <https://www.iso.org/home.html> (Accessed 30 June 2022) ⁶ Sustainability Accounting Standards Board. <https://www.sasb.org> (Accessed 17 June 2022) ⁷ Task Force on Climate-related Financial Disclosures. <https://www.fsb-tcf.org> (Accessed 17 June 2022) ⁸ United Nations Global Compact. <https://www.unglobalcompact.org> (Accessed 17 June 2022) ⁹ United Nations Sustainable Development Goals. <https://www.un.org/sustainabledevelopment/sustainable-development-goals/> (Accessed 30 June 2022)

Completing the ESG Health Check

1 PORTFOLIO COMPANIES COMPLETE THE ESG QUESTIONNAIRE

The ESG questionnaire, which takes around three hours to complete, is filled in by the responsible individual(s) at the portfolio company. Several questions require supporting documents to authenticate answers, such as company policies or survey results.

2 THE ESG ANALYSTS SCORE THE COMPLETED QUESTIONNAIRE

The Apex Group analysts review the questionnaire and supporting evidence. The analysts score the company's practices, abiding by clearly defined scoring criteria aligned with global standards to ensure rigour, objectivity and credibility — thereby mitigating accusations of greenwashing. The scores provided for each aspect of ESG are binary, either receiving a pass or fail; the overall ESG score is then provided as a percentage of questions which received a positive response.

Example of questions from the ESG questionnaire:

Environmental:

- Does your organisation have a formal environmental policy or related documents that cover environmental issues?
- Does your organisation measure and monitor its total annual energy consumption?
- Does your organisation report on its annual greenhouse gas (GHG) emissions?

Social:

- Does your organisation perform regular employee engagement surveys?
- At which levels of your organisation (if any) do you measure and monitor gender diversity?

Governance:

- Does your organisation have a formal code of business conduct in place, which includes anti-corruption, bribery, and other business ethics?
- When was the most recent formal cybersecurity assessment completed?



3 APEX GROUP PRODUCES TWO ESG REPORTS

I. ESG HEALTH CHECK REPORT

The ESG Health Check report presents the company's overall ESG score as a rating out of 100 (Figure 1). Individual scores are provided for each of the three dimensions, in addition to sector benchmarks, which are the average scores of companies that have completed the Apex Group ESG Health Check to date. A scorecard highlights every question for which the company provided both a positive response and, if required, supporting evidence (Figure 2).

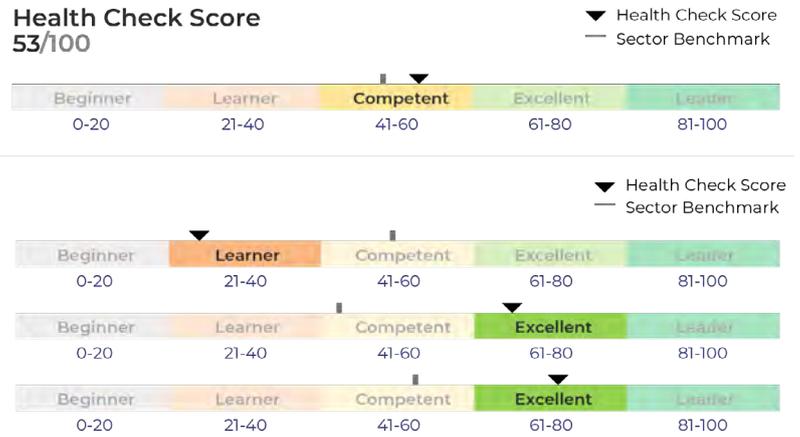


Figure 1: Apex Group ESG Health Check Score for a growth-stage company in Endeavour Vision's portfolio. The Health Check Score (arrow) is shown in relation to the sector benchmark (line).

Health Check ESG Scorecard

Environment	24%	Social	65%	Governance	71%
Environmental Policy		Employee Development Opportunities		ESG Strategy	
Environmental Impact Identification		Employee Engagement Survey		ESG Materiality Assessment	
Environmental Breach Management		Living Wage Guarantee		Corporate Governance Policy	
Climate Change Governance		Employee Benefits Plan		Independent Board Members	
Climate Change Risks Identification		Employee Turnover 2020		Code of Business Conduct	
Climate Change Opportunities Identification		Female Board Members		Whistleblowing Policy	
Climate Change Targets		Gender Diversity Management		Business Ethics Breach Management	
Energy Consumption 2020		Gender Diversity All Employees		Data Protection and Privacy Policy	
Renewable Energy Consumption 2020		Mean Gender Pay Gap		Cybersecurity Policy	
Scope 1 GHG Emissions 2020		Median Gender Pay Gap		Cybersecurity Assessment	
Scope 2 GHG Emissions 2020		Diversity and Inclusion Initiative		Risk Management Training	
Scope 3 GHG Emissions 2020		Health and Safety Indicators 2020		Product/Service with ESG Benefits	
Water Use 2020		Employee Health Care Guarantee		Product/Service UN SDG Alignment	
Emissions to Water 2020		Charitable Donations 2020		R&D Spend 2020	
Waste Generation 2020		Volunteering Hours 2020		Supplier Code of Conduct	
Hazardous Waste 2020		Human and Labor Rights Policy		Sustainability Certification Procurement	
Biodiversity Assessment		Human and Labor Rights Breach Management		Sustainability Certification Sales	

Figure 2: Apex Group ESG Health Check Scorecard for a growth-stage company in Endeavour Vision's portfolio. The scorecard highlights in colour every ESG topic for which the company provided a positive response along with supporting evidence.

II. ESG GAP ANALYSIS AND RECOMMENDATIONS REPORT

The Gap Analysis Report highlights the priority areas for ESG improvement and provides expert recommendations for a long-term strategy to address these. Each recommendation is tailored to the company's size, sector, geography, and experience with ESG, to ensure that they focus on the most material areas for improvement.

4 COMPANIES RECEIVE THEIR INDIVIDUAL REPORTS

When we, at Endeavour Vision, receive the two ESG reports, we share these with the management team of each portfolio company. We recommend that they discuss these reports with executive management, the board of directors, and other interested stakeholders, so they can devise a strategy to address the gaps and implement the recommendations within a given timeframe. Furthermore, we provide practical support and help them track their ESG progress over time.



ESG priorities for healthcare start-ups

Aside from the maturity of the business, there are several other factors that influence whether ESG is considered a priority for a company and which dimensions (E, S or G) the company should focus on. For example, geography plays a role, with ESG differing in prominence and regulation in the US, UK and Europe. Certain reporting practices are subject to voluntary disclosure in some countries, while in others it is a matter of law. Additionally, some countries are more sensitive to ethnic diversity,

while others might be relatively ethnically uniform.

Despite these challenges, there is a trend towards what we can define as emerging best practice. Based on research and the observations from our portfolio companies' ESG scorecards and gap analyses, we have outlined some key priorities, quick wins, and resources that can be used and adapted by any start-up healthcare company embarking on its ESG journey.

Environmental

In general, growth-stage healthcare companies can make the most significant improvements within the environmental aspects of ESG, as the sector benchmark score for this dimension lags behind the other two. Below we briefly highlight three environmental factors that are material for investors and regulators. We will elaborate further on this topic in Part 3 of this whitepaper series.

1 ENVIRONMENTAL POLICY

Documenting the company's environmental policy is a great place to start, especially if environmental data is scarce. An environmental policy should set out the company's commitment to minimising its environmental footprint with respect to climate change, biodiversity loss, and pollution. [An environmental policy template](#) is available on our website, which can be used as a basis when preparing this document.

2 ENERGY CONSUMPTION TRACKING

Energy consumption is typically the most immediate and quantifiable environmental impact of any company. The best sources of data to track energy consumption include utility bills, invoices, and meter readings. Companies may estimate their annual consumption by measuring it over a quarter and then extrapolating it, building assumptions into the equation to account for variability in energy use throughout the year.

3 CALCULATING GREENHOUSE GAS (GHG) EMISSIONS

The GHG emissions of an organisation encompass all emissions that are directly and indirectly derived from a company's activities. This includes emissions from sources that the company has a large degree of control over, such as business travel and energy consumption, but it also includes upstream and downstream sources, which are more complicated to calculate, such as the supply chain and the lifecycle of goods following manufacture. There are many GHG emission calculators available online that can help, such as the [US EPA Simplified GHG Emissions Calculator](#).

Social

Healthcare companies typically perform well on the social aspect of ESG, as a result of their socially oriented mission to deliver better patient care. Nevertheless, there are a couple of easy wins that could improve a company's social scores even further.

1 GENDER PAY GAP

The gender pay gap is a crucial metric, especially as it is now a regulatory reporting requirement in many jurisdictions, including the UK and the EU. While increasing transparency of gender equality within the business, it also enhances employee recruitment and retention. We recommend analysing and publishing aggregate gender differences in salary across all levels of the organisation.

2 HUMAN AND LABOUR RIGHTS POLICY

A human and labour rights policy should describe the company's commitments to ensuring fair working conditions, equal opportunities, and freedom of association. It should also cover its commitment to fighting discrimination, bullying, harassment, physical and mental health risks, forced labour, child labour, modern slavery, and human trafficking. It should outline the grievance procedures to be followed in the event of a complaint — both within the company and throughout its supply chain. A [human and labour rights policy template](#) is available on our website.

Companies with a diverse workforce are more likely to excel financially than those who lag behind.

Companies in the top quartile for gender and ethnic diversity in leadership see a +12% increase in financial outperformance vs. the industry average. Meanwhile, the lowest quartile sees a -27% underperformance.¹⁰

¹⁰ McKinsey & Company. Diversity wins: How inclusion matters. 2020. <https://www.mckinsey.com/-/media/mckinsey/featured%20insights/diversity%20and%20inclusion/diversity%20wins%20how%20inclusion%20matters/diversity-wins-how-inclusion-matters-vf.pdf> (Accessed 26 July 2022)

Governance

The governance aspect of ESG refers to corporate governance processes and decision-making, which have a bearing on how a company is directed and controlled. This includes the composition of the organisation and responsibilities at the leadership and board levels.

1 ESG MATERIALITY ASSESSMENT

An ESG materiality assessment is a tool that identifies and prioritises the ESG issues that are the most impactful for an organisation and most important to the company's stakeholders. It is best to start by compiling a list of material ESG issues; frameworks such as the SASB standards⁶ are a useful source of topics, and companies can filter results by industry to understand which are likely to be relevant. For instance, medical device companies should consider disclosures for topics including affordability and pricing, product safety, ethical marketing, product design and lifecycle management, supply chain management, and business ethics.¹¹ Other topics, which are applicable to any industry, include employee wellbeing, data privacy and cybersecurity, and diversity and inclusion.

A company should then consult with its key stakeholders (company leadership, staff, investors, customers, and key suppliers), using surveys or interviews to understand which topics are most important to them. Following that, it can finalise its list of material topics by evaluating each issue's business impact, enabling the company to rank its ESG efforts. Once ranked, the ESG material topics can be visualised by means of a materiality matrix, such as in Figure 1 below. This visualisation can assist in determining which priorities to focus on for the highest impact and stakeholder satisfaction.

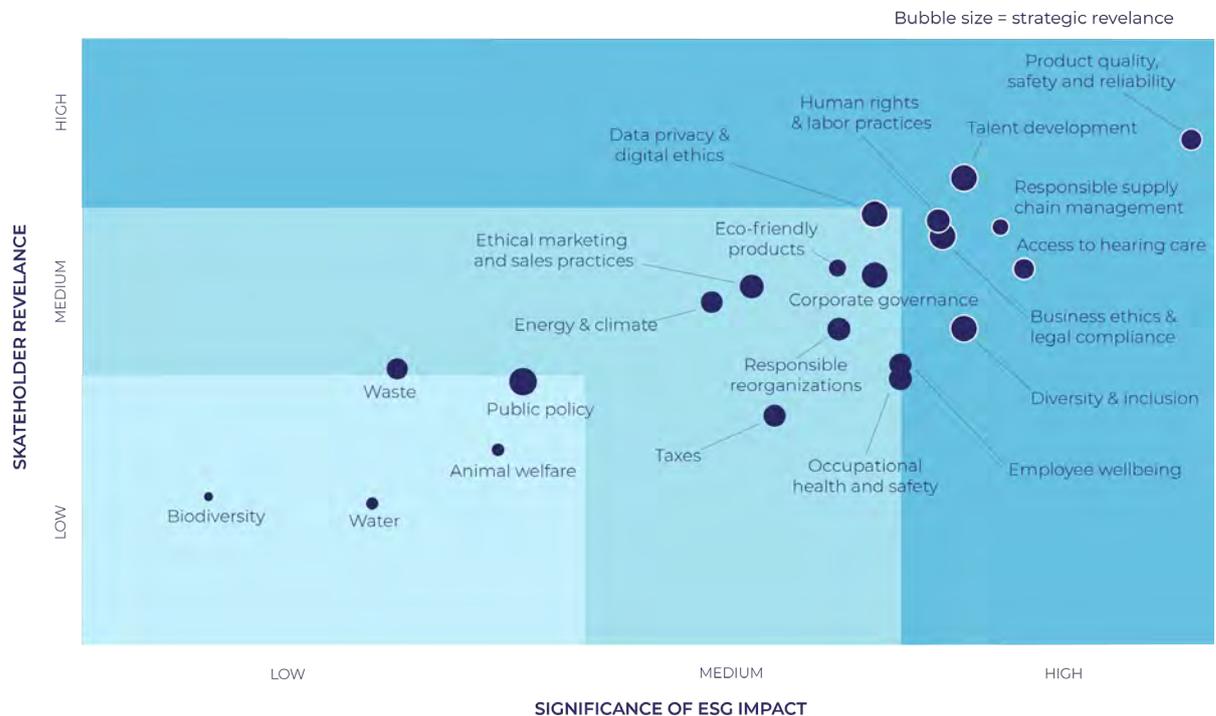


Figure 3: ESG Materiality Matrix, featuring topics which are ranked by the significance of ESG impact to the organisation (x axis), in addition to the relevance to stakeholders (y axis). The topics in the top right area, which have the highest values for both relevance and impact, are deemed the highest priority. Source: Sonova. IntACT.¹²

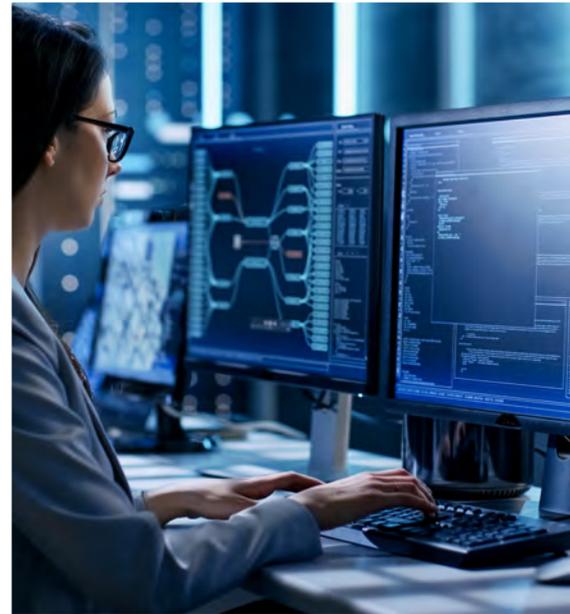
¹¹ Sustainability Accounting Standards Board. Medical Equipment & Supplies. 2018. https://www.sasb.org/wp-content/uploads/2018/11/Medical_Equipment_Supplies_Standard_2018.pdf (Accessed 30 June 2022) ¹² Sonova. IntACT — Sonova's ESG Strategy. <https://report.sonova.com/2021/en/intact-sonovas-esg-strategy/> (Accessed 30 June 2022)

2 CORPORATE GOVERNANCE POLICY

Implementing and maintaining strong corporate governance practices is crucial for the operation of any company. A corporate governance policy outlines how the company intends to act in the best interests of its stakeholders and promote integrity and ethical behaviour across the organisation. The procedures outlined by the policy help to reduce risks (e.g. risk to corporate reputation) and provide clear guidelines for company growth.

A robust corporate governance policy should document the company's governance structure and define the roles and responsibilities of its board (including their obligations to shareholders). It should define committee structures, board nomination processes, diversity and independence commitments, compensation guidelines, and any conflicts of interest. For guidance on best practices, we suggest referring to the Organisation for Economic Co-operation and Development's (OECD) Principles of Corporate Governance.¹³

Next, companies should develop a code of conduct covering important topics like corruption and bribery, gift policy, antitrust and competition, conflict of interest, data protection and privacy, and whistleblowing. Finally, we recommend that companies seek legal counsel to ensure that their corporate governance policies are in line with local laws and regulations.



3 CYBERSECURITY ASSESSMENT

Cyber risk presents a major threat to the value of an organisation. Sensitive digital information may include proprietary knowledge, confidential patient data, financial information, or behavioural data from users. The implications of cybersecurity breaches could therefore be potentially devastating for companies operating in the medtech, digital health, and diagnostics sectors, especially considering growing cybersecurity threats¹⁴ and regulations designed to protect personal information held by organisations.¹⁵

To mitigate this risk, we recommend conducting cybersecurity assessments. These tests should determine the robustness of the company's systems and protocols, highlight any gaps, and check whether previously identified gaps have been addressed.

¹³ Organisation for Economic Co-operation and Development. G20/OECD Principles of Corporate Governance. <https://www.oecd.org/corporate/principles-corporate-governance/>. (Accessed 30 June 2022) ¹⁴ Palandrani P and Lucas A. Rising Cybersecurity Threats Expected to Continue in 2022. Global X. 2022. <https://www.globalxetfs.com/rising-cybersecurity-threats-expected-to-continue-in-2022/>. (Accessed 30 June 2022) ¹⁵ EU data protection rules. European Commission. https://ec.europa.eu/info/law/law-topic/data-protection/eu-data-protection-rules_en (Accessed 14 July 2022)

Three general recommendations for implementing ESG changes

To implement the specific recommendations listed in this paper and to initiate the development of more robust ESG practices, we have three general recommendations for early- and growth-stage companies:

1 MAKE ESG A LEADERSHIP PRIORITY

We encourage companies to appoint an ESG officer to oversee their ESG activities and reporting requirements. Since every aspect of a business has an impact on their ESG reporting, we also recommend that companies establish an ESG committee consisting of representatives from every department. The committee should be led by a member of the company's leadership team.

2 DEVELOP AN ESG STRATEGY AND ACTION PLAN

The ESG committee should develop an ESG strategy and action plan and obtain approval from the board and audit committee. This will enable the company to have clear goals, implementation mechanisms and the necessary resources for this effort. These goals could include the specific recommendations covered in this paper (if relevant) as well as any company-specific issues identified. We also suggest setting longer-term ESG goals, so companies can continue to develop their ESG policies and processes as their business grows and new regulations come into force. The ESG committee should monitor and review progress on a regular basis and report at least annually to the audit committee and the board.

3 LEVERAGE YOUR INVESTORS AND PEER COMPANIES TO ACCELERATE YOUR PROGRESS

At Endeavour Vision, we actively support our portfolio companies in this process. We advise that, wherever possible, co-investors use the same ESG assessment, as this reduces the portfolio companies' reporting burden and saves them valuable time.

An acceleration in progress on ESG across the industry is needed, as our collective actions have a more substantial impact than our individual efforts. To support this, we are developing a range of frameworks, policies, tools, and templates for inclusion in a public library of resources on our website,¹⁶ which are designed to help any company improve its ESG performance.

¹⁶ ESG & Impact. Endeavour Vision. <https://www.endeavourvision.com/impact/> (Accessed 22 July 2022)

Conclusion

The importance of focusing on ESG sooner rather than later is underscored by the increasing depth and complexity of ESG assessments. Like quality, ESG is an ongoing process. Even as companies continue to improve, key stakeholders will raise their expectations. So, it is crucial that companies maintain their focus on ESG by conducting regular assessments on how they are progressing towards their shorter- and longer-term strategic goals. It is also vital that they compare with industry peers and make the necessary adjustments to stay the course.

Our next paper will focus on the “E” of Environment, which is where healthcare companies show the most potential for improvements across the ESG dimensions. We will cover why it is essential for companies to take responsibility for environmental stewardship. We will also provide recommendations for first steps and provide access to relevant frameworks, templates, tools and other resources to give companies a head start.

Stay up to date with our news and be the first to hear when the next issue of our ESG whitepaper series is released. Sign up to our newsletter [here](#).

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