EXPERT CORPORATE COMPLIANCE

THE ESG IMPERATIVE

Katarzyna Saganowska, Risk and Compliance Director at TMF Group, explains why ESG is essential now more than ever.

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Recently, the term ESG (Environmental, Social, and Governance) has become very popular. However, many people still wonder why it is so. In a world where climate change and social injustice make headlines every day, the increasing significance of tackling these issues for business organizations may not seem surprising. After all, the business sector can exert pressure on legislators and regulators.

But what seems to be even more apparent is that while improving ESG performance is crucial both for creating the greater good and for managing organizations' reputation and performance, it can provide companies with valuable insights into their performance.

ESG evaluates the environmental, social and governance elements for focusing on conducting business ethically in all three areas. With this, ESG is tangibly related to corporate social responsibility (CSR), but easier to quantify, measure, and manage.

NEW STANDARDS

For multiple reasons, companies across different sectors embrace the philosophy that social and environmental issues should be of equal concern to profit generation. Consequently, ESG can hardly be of more importance and for a few good reasons.

First, climate concerns are accelerating a desire for sustainable finance, embedding this concept in corporate consciousness. Climate sustainable finance is driving businesses in all sectors to review their practices as well as their investment decisions. At the same time, companies recognize the need to build sustainable supply chains that embrace environmental risks.

Second, businesses' social concerns include issues such as workforce diversity—where performance is increasingly under the spotlight—and regulations, such as the prevention of modern-day slavery. The same goes for leadership—the benefits of inclusive and diverse policies are becoming apparent through various HR programs across many companies.

Third, organizations' governance is now about keeping the company honest and ethical in all areas of its operations. The scrutiny level is elevating to ensure proper performance and delivery.

And last but not least: not only investors are getting more involved in ESG issues but so are customers, clients, and suppliers. Thus, companies need to demonstrate strong ESG credentials for all stakeholders.

ESG REPORTING

It is arguably impossible to access the role of ESG without looking at the requirements of ESG reporting.

Many companies are now under an obligation to provide their ESG disclosures. The popularity of ESG scores and rankings for accessing a business as a potential investment, supplier, or employer is on the rise. This shifts the focus of companies' boards onto robust ESG metrics with which they can prove that they have a proactive ESG strategy in place.

With ESG principles becoming a new standard, companies face a risk that without having ESG strategies embedded in their broader risk assessment, they may be viewed as not being serious about the ESG principles and thus to be avoided.

BOARD'S ROLES

Typically, in the area of ethics and compliance, the example set by the top echelons within a company can be crucial in facilitating the implementation of ESG strategies into the organization's overall business strategy. The goals that the board sets forth are where the company focuses its attention. ESG risks are often conflated with broader business risks, which is why there are good reasons for the board and business to focus their energies to translate broad ESG aims into concrete strategies that give directors persuasive incentives to prioritize ESG management and measurement.

The board also has ultimate responsibility for corporate performance and reporting. When it comes to evidencing strong ESG credentials, the role of the board must not be underestimated.

FIRST THINGS FIRST

The essential first step for the board is to set quantifiable ESG goals, along with defining the ways to measure and report progress.

ESG measurement can be challenging, involving unwieldy systems and inconsistent processes, along with the lack of accurate data to build strategies for improvement. A structured framework with clear objectives and the inclusion of ESG in the mapping of the organization's risk seems to be the simplest and best way to start.