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How compliance can impact ESG

by Nakis Urfi

Environmental, social, and governance (ESG) programs are becoming more embedded within a company's overall strategy; compliance has an opportunity to inform and shape the development within this area.

By paying attention to ESG, one starts to notice it is hard to keep track of all the various ESG information and trends that are rapidly evolving and generating an overload of content. Spanning across various media and perspectives—the news, reports, and individual opinions—ESG content has ranged from "It will save the world" to Elon Musk calling it a scam to academic and financial institutions theorizing on the future states of ESG to anti-ESG movements evolving—and everything in between.

What is ESG?

ESG are nonfinancial factors investors use to measure investments and companies and their overall sustainability impact.

ESG's near-term goal is identifying relevant material issues important to a company's stakeholders, developing targets to positively address these issues, and sharing public reporting metrics on a company's progress toward these targets.

ESG's long-term goal is for industries to use consistent standards so rating agencies and investors can assess the value and risks of companies for investment purposes when comparing companies of interest. Currently, it is unclear whether companies will adopt the same standards for reporting, as they have options on what standards to use with so many different countries, industries, and entities involved.

Looking back at history, the first big multinational corporation was the Dutch East India Company in the 1600s. Then eventually came Milton Friedman's concept that corporations' main purpose was to maximize revenue for shareholders. From there came the ideas of corporate social responsibility and the "triple bottom line" focusing on "people, planet, and profit."[1] Fast forward to today, industry commentators state that shareholder capitalism is moving to stakeholder capitalism. Corporations have shifted from focusing only on shareholders' interests to now focusing on the interests of all stakeholders.[2] Stakeholders include investors, members and patients, employees, clients, partners, regulators, communities, etc.

Depending on where one is on the ESG maturity curve, it is helpful to understand that one's organization has some form of ESG program and activities inflight; however, it may yet not have categorized them under "ESG." The following is a deeper dive into the various ESG categories.

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Environmental

Some people confuse ESG with being strictly focused on climate change and carbon emissions. The environmental component of ESG is in high focus; however, as discussed later, only when the "S" and "G" are combined will you get a holistic view of one's organization's overall ESG standing.

Governments have committed to reducing a country's carbon emissions by a certain date, typically 2030, and reaching net-zero by 2050. The United States and European Union are pouring billions of dollars into helping reduce carbon emissions, most recently through legislation passed from the Inflation Reduction Act and REPowerEU plan.[3] Subsequently, organizations of all varieties made public commitments to do the same or similar in reducing carbon emissions. There are three primary categories for tracking carbon emissions, including Scope 1 (direct emissions), Scope 2 (indirect emissions – owned), and Scope 3 (indirect emissions – not owned).[4]

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