

## ESG EXPERTISE A MUST-HAVE IN THE BOARDROOM

By Andy Davies

### ESG IN THE BOARDROOM

In some sectors, such as oil and gas and global manufacturing, ESG (Environmental-Social-Governance) has been a boardroom priority for a while, largely driven by the growth in sustainable investing. Now, though, the concept seems to have reached critical mass. Visible action on ESG has become a must-do for listed companies in all sectors as they seek to assert their sustainability credentials.

As ESG moves up the corporate agenda it creates a challenge for Chairs who need to recruit scarce ESG expertise to the boardroom to complement knowledge at the executive level. It also creates a valuable opportunity for individuals with the right experience and skills to contribute as non-executive directors (non-execs), helping organisations to establish their ESG strategy and credentials.

There are several reasons for the rising demand for ESG expertise in the boardroom. For a start, companies are under pressure to demonstrate action on ESG factors from a range of stakeholders, including consumers, employees and investors. Another key driver is the increasingly onerous responsibilities set by the evolving regulatory, legislative and case law environment<sup>1</sup>. Studies reveal that failing to meet ESG targets exposes companies to greater operational and financial risk<sup>2</sup>. Organisations and boards must show that they are up to speed on ESG issues and implementing measures that are meaningful – thus avoiding damaging accusations of greenwashing.

As one FTSE Chair highlighted to me: ‘The debate has moved on from something which is just another layer of regulation and cost to viewing it as an opportunity to differentiate ourselves. A lot of the matters discussed on the board will be seen through the prism of ESG, whatever the conversation is’.

Board Chairs are also saying that ESG expertise is being incorporated into companies in three main ways. The step that possibly sends the strongest message is recruiting an additional non-execs to the main board to take responsibility for ESG. This person will feed into ESG reporting, working with the audit committee, but also examine how the organisation operates in the context of ESG requirements and make recommendations accordingly. Those recommendations might be about hiring, health and safety, carbon footprint or product sustainability, for example.

Alternatively, the responsibility for ESG and its reporting may be added to the audit committee’s tasks or in some cases boards are creating a separate ESG subcommittee that reports independently into the audit committee.

1. <https://www.clientearth.org/latest/latest-updates/opinions/six-reasons-the-shell-ruling-made-history-for-climate-litigation>

2. <https://www.businesswire.com/news/home/20220606005403/en/Failing-to-Meet-ESG-Goals-Exposes-Companies-to-Increased-Operational-and-Financial-Risks-Study-Finds>

## THE ESG EDGE

The non-execs best able to add value on ESG in the boardroom share certain characteristics. As a CEO of a FTSE firm told me: 'These non-execs need to have lived experience of dealing with ESG at a senior level in a corporate environment. For example, on the environmental side that might mean a person who has been working in the extractive industries and closely concerned with environmental issues. They might have been co-ordinating ESG activity at a very senior level or implementing and being responsible for climate change strategies. And probably doing this across a number of countries'.

Similarly on the social side a suitable candidate might have worked in a manufacturing business that operates in developing economies, across parts of Asia for example, that have issues around human rights and labour practices. This could be in textiles, fast moving consumer goods or electronic products. It might be someone who had responsibility for activities such as implementing and leading the health and safety plan or the human rights charter, ensuring appropriate labour policies were in place, and promoting equal opportunities.

One non-exec I spoke to stressed that it's not just about lived experience. An ESG focused role on the board requires an unusual combination of skills. 'On the one hand you need the deep analytical skills and ability to pull together a regulatory report and lead a team of people to comb through the company generating the right reporting information. But to be an evangelist for ESG and get the message across about the action the company's taking and its performance, internally and externally, you also need to be a first-class communicator.'

A useful exercise for executives who want to evaluate their potential as an ESG focused non-execs is to map their experience against the different dimensions of ESG. For example, we use a framework for ESG which includes six dimensions for each of the three elements.

Setting non-execs with ESG expertise to one side, there is a general responsibility for other board members to be comfortable around ESG. At the very least they must be aware of the ESG factors and their different dimensions and the relevant responsibilities and regulatory requirements relating to these.

## CHANGING PERSPECTIVES

Even when companies have appointed a Chief Sustainability Officer (CSO) or equivalent the board will have an important role to play in shaping ESG performance and its reporting. But with a recent study by PwC revealing that just 30 per cent of listed companies had a formal CSO in 2021, the board's input on ESG matters is likely to be particularly critical to the company's financial performance<sup>3</sup>.

For non-execs with the right background, the lack of ESG expertise on boards provides an opportunity to step up and guide companies beyond a view of ESG as just a regulatory, reporting and compliance exercise. Instead, they can help companies make ESG a clear differentiator and source of competitive advantage.

3. <https://www.strategyand.pwc.com/de/en/cso2022.html>