EDGE EMPOWER

A clean bill of health

How organizations can build trust with their stakeholder community and avoid accusations of 'pinkwashing'.

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It's very easy for an organization to publicly state that it subscribes to best practices in its Environmental, Social and Governance (ESG) and Diversity, Equity and Inclusion (DE&I) methodologies and policies.

However, just because an organization claims to adhere to these methodologies doesn't mean that they hold themselves accountable towards them, neither does it mean they have taken positive steps to implement meaningful change. For some, they're just a medium with which to improve their corporate image to enhance perceptions of the organization in the eyes of investors, future talent, or society at large.

In fact, 'greenwashing' – once a phrase that simply related to an organization's environmental (i.e 'green') credentials – has now largely become a generic term in relation to ESG, in the same way that 'pinkwashing' has become generic in the context of gender equity. Either way, the actions of these organizations are just a veneer toward respectability.

But regardless of the colour of the wash, organizations need to be aware that they're being closely observed by not only investors and the market, but also by regulators who are starting to pay greater levels of attention to anything labelled as delivering an ESG benefit. The conversation now needs to change and talk about removing the opportunity for 'washing' so that stakeholders are no longer misled about an organization and its activities, goods and services.

The only valid way to do this is to use independent verification and third-party certification to measure change so that those organizations that act with integrity reap the rewards from being ethically responsible.

Why washing happens

As to why the subject is so topical, the growth of investor interest in ESG is one of the main drivers.

Such interest reflects the view that various issues – including risk and opportunity – can affect the long-term performance of organizations and so should be given appropriate consideration in investment decisions.

But there is, presently, some inconsistency in the process. ESG ratings can vary. Scoring too can differ because of variations in how elements are measured. And bias can be exhibited. We need standardization.

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Looking forward positively

Counterintuitively, instances of 'washing' should be looked upon with a positive twist. Not for the action of washing itself, but for the fact that organizations are starting to feel the need to comply with the demands for change even if they themselves are not yet properly engaged with the change.

This pressure for change is coming from several directions.

- First, there is an increased societal attention of ESG-related issues. Allied to this is growing momentum for corporations and financial institutions to show more of a long-term perspective while moving away from short-term views of risk and return.
- Second, society is focusing attention on climate change issues, calling for more responsible business conduct, and greater diversity in the workplace and on boards. Society's new values are increasingly influencing investors and consumer choice; they can no longer be ignored.
- Third, societies which influence investors, who in turn influence corporations, are leading to more products and services being labelled as being ESG-compliant. Organizations are having to change their mix of goods and services to meet the demand.

That's the good news

But there is a mismatch between the appetite and the desire for change, and the tools that determine what defines or constitutes something that carries an ESG label. This follows from an evolving process where the response to new demand – for ESG – is imperfect because organizations are rushing to respond to the market but without the appropriate processes in place.

Organizations should lead the charge

Proper change needs the public and corporate investors to speak up; they need to demand the continual raising of the bar so that whatever is labelled as ESG – be it a product, a service or an investment – becomes ever more compliant with standards that themselves become better defined, more accurate, and stringent.

Naturally, in finding a new equilibrium, organizations will find themselves disclosing ever greater levels of ESG-related information. This data needs to be categorized and assessed from a quality perspective; onlookers need to be able to distinguish a difference between the compliant and non-compliant, reliable and unreliable.

But this leads us to another set of challenges that need to be resolved.

First, how do organizations decide on the data that matters? Once this question is settled the methodology will become more transparent. Then there's the matter of scoring – how is relevant data selected, combined, and compiled into an ultimate score that leads to a reliable ESG rating that the market can trust?

Beyond that is the challenge of ensuring that data and the subsequent scores lead to relevance and consistency in reporting frameworks. This means ensuring that the whole process is as objective and measurable as possible in line with materiality thresholds and the performance of the organization.

Lastly, any inherent biases associated with the data and process need to be eliminated so that results become universally acceptable and aligned with the public and regulators, regardless of the size of the organization.

The solution to all these problems? Independent verification and credible certification.

The goal

To avoid future 'washing' requires improved transparency, international consistency and comparability, alignment with materiality, and clarity on how this information can be trusted. Global standards and independent third-party certification are the answer.

Ultimately, getting this right will create robust assessment methodologies and scoring frameworks that organizations can use, which are transparent and can be objectively verified and certified and therefore trusted to be accurate.

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