(E)ESG - WHY IT MATTERS TO EMPLOYMENT EXPERTS

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In our hyper-transparent and increasingly joined up world, the concepts of corporate social responsibility and socially responsible investing are gaining greater currency. Over the last decade, and catalysed by COVID-19 over the last year, Boards and General Counsel have focused on the role of ESG in driving responsible and sustainable business conduct approaches which acknowledge that the purpose of a company should be amplified beyond just shareholders to also explicitly include their employees, clients and the communities in which they operate. In fact, the Chief Justice of the Delaware Supreme Court, the Honourable Judge Leo Strine in a piece he wrote for the Financial Times, has already suggested the next generation acronym – EESG: Employees, Environment, Social and Governance.

So, what does this mean and why is it important for employment professionals? Hopefully the first E is a clear hint (it's not a typo)!

What is ESG?

ESG is the umbrella term for broad range of **E**nvironmental, **S**ocial and **G**overnance factors against which a company's stakeholders can holistically assess the performance, value (risk/opportunity), investment in respect of the company. Many ESG factors contribute to a company's "social licence to operate" and responsibility to its stakeholders and the creation of long-term holistic value for a company – both financial and in terms of reputation.

Even pre-pandemic, there was a rise in "responsible investment", essentially investors looking for companies with an explicit objective of making a positive impact on the environment and society as well as a financial return. The pandemic, with its unprecedented impact on the workplace and business value chains, has clearly highlighted the critical importance of the social element of ESG. Statistics show that "millennials", or the up and coming investors, are twice as likely as other generations to invest in companies targeting social or environmental goals. As such, ESG is no longer something that companies can ignore – either as part of their approach to addressing risk or creating long-term value.

How does ESG impact business?

"ESG" has emerged as a key driver behind:

- pivoting and transitioning business models and assets to build resilience and improve performance around issues such as climate, deforestation, natural capital, human rights – modern slavery and child labour, corruption, fair taxation, and transparent and inclusive governance and executive remuneration;
- overhaul and redesign of value/supply chains to achieve greater resilience;
- new "green", "social" & "sustainable" goods, services & businesses;
- new laws and evolving performance standards, obligations, reporting;
- evolving "legal compliance" to include holistic ESG risk governance; and
- development and use of multi-stakeholder sectoral collaboration to address complex issues across industries, such as the Bangladesh Accord in 2013 regarding safety and labour standards in the textile / garment industry.

So what does this mean in practice for in-house legal teams and their companies? Addressing ESG related issues and risks requires legal (including employment experts), risk, compliance and ethics, environment and social risk teams (with other business stakeholders) to develop an integrated and interdependent legal and risk governance approach and framework across 3 key areas

- legal and regulatory compliance;
- social accountability risk governance; and
- alignment with stakeholder expectations and trust

Why – ESG related issues often complex and arise in situations that are driven by the interdependence between all 3 of above factors – such as the collapse of garment factory in Bangladesh with no or poor safety, labour conditions and using female and child workers. A singular and/or primary focus on legal compliance alone may not fully account for or provide resilient business decisions / position when the interests of a company's stakeholders are also considered – especially over time, in complex business environments, or where law is absent or contrary to international standards or a fundamental breach of ethics, public or stakeholder trust has occurred. As a result, local legal compliance may not be sufficient holistic legal risk governance for the company opposite its stakeholders and their interests in the company. Using an ESG framework, informed by authoritative international standards, industry best practice and stakeholder engagement (shareholders, investors, employees or the wider community), can provide:

- business resilience, agility and growth

- holistic understanding of value – mitigate risk and maximise opportunity
- regulatory and legal risk benefits – especially where national law is unclear, developing or contradictory when assessed against authoritative international standards
- reduce operational disruption and costs
- positive stakeholder and managerial interest
- increase employee productivity
- attract and retain employees, clients, business partners, suppliers and customers

As the "social" and "governance" aspects of ESG are particularly significant in an HR or employment law context, employment specialists are increasingly central to supporting their businesses manage legal / regulatory compliance issues in a manner that also supports and promotes ESG goals and standards.

What are the employment-specific aspects of ESG

There are a number of key themes emerging in ESG which relate to a company's and employer's relationship with its workforce and social capital. These include:

- Diversity and equality – how diverse is your workforce? How fair are your remuneration structures?
- Do you have a human rights policy and due diligence approach – that goes beyond dealing with safety and labour standards? Do you have a structured and dynamic risk management approach to address modern slavery and child labour issues associated with your business and your entire value chain?
- Do you pay Living Wages and/or fair wages? Do you have approaches for dealing with local and/or indigenous communities that are consistent with international standards?
- Health and well-being – what is your health and safety record? Do you look after the physical and mental health of your employees?
- Training – do you invest in people and in skills training?
- How do you undertake stakeholder engagement and diligence to identify social and/or governance issues or risks, including with civil society organisations? In what circumstances do you use NDAs?

We are already seeing a sharp focus on these issues, both to comply with current and developing regulatory obligations and address pressure from investors, consumers, the media and other stakeholders. For example, a lack of diversity at board level, or poor reputation regarding how certain behaviours are dealt with, could deter investment or funding. Inclusion and diversity – embedded through a company's governance structure has also become a matter of interest to the FCA, and is of increasing importance to regulated firms. As set out in the speech by Sheldon Mills, FCA Executive Director, the FCA is encouraging firms to improve in this area, and is considering how best to use its supervisory powers, such as requiring firms to explain a lack of diversity or their hiring strategy.

As such, HR's approach and relevant policies and procedures (particularly in relation to discrimination or equality) will be instrumental in ensuring that companies remain appealing to senior managers and employees, for investment and to comply with the requirements of the FCA. It is no longer enough simply to have the policies in place – companies must ensure that there is an aligned approach to build ESG leadership and competence, support multi-disciplinary engagement (across key functions including legal, compliance, risk, sustainability and CSR) around developing governance structures, incentives, management systems, procedures, reporting, and a culture that fosters integrating ESG issues and value.

As company's continue to engage with I&D and broader social and governance issues, HR specialists and in house-employment counsel are key contributors to a company's successful implementation of its (E)ESG strategy.

Practical Tips for Employment Experts

- Consider your recruitment practices. Do you recruit from a diverse range of people? What can you do to increase the diversity of your workforce?
- Take time to consider potential issues now to resolve them quickly. Consider running surveys regarding inclusion and diversity and employee engagement, and identify potential concerns around the employee experience.
- Take an integrated approach with other internal specialists. What are your wider ESG goals as a business and how can you use employment practices to support them? For example, consider the environmental impact of business travel and whether ESG targets can be linked to appraisals or to remuneration structures.
- Make sure that you have adequate systems for supporting the health and safety of your employees. This is not limited to physical health – focusing on healthy working practices, work-life balance and mental well-being is increasingly important.

Review your existing complaints procedures, including both grievance procedures and whistleblowing procedures – make sure that they comply with current legal requirements including higher standards imposed at a sector level, for example in financial services.

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