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ESG: Why the UK is having to measure up

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Introduction

Environmental, Social and Governance or ESG for short was a term first used as a means by which investors could assess businesses across a wider range of criteria than the usual financial metrics:

Environmental - for a company's impact on the natural environment and vice versa.

Social - for how a company treats people whether in its workforce or externally and the values that it holds.

Governance - for how a company manages itself, including its organisational and operational controls and commitment to diversity and inclusion.

Although these factors were initially devised to help investors and other stakeholders to measure performance and accountability, they have slowly but surely gained traction, becoming a fact of life for UK businesses and also increasingly the subject of primary and secondary legislation as well as a plethora of codes of conduct and statements of best practice.

There are now tangible as well as ethical reasons why UK businesses have to act responsibly regarding ESG. Decision-makers are required to take account of more than just their shareholders and investors. They must consider the impact of their activities on the environment, employees (including equality, diversity and inclusion), local communities, the supply chain, privacy, security and so on.

Please read on to find out more about the legal landscape applicable to ESG in the UK.

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Environmental

Environmental reporting and the TCFD Recommendations

The Companies Act 2006 (Strategic Report and Directors' Report) Regulations 2013 created a new structure for UK companies to report their impact on the environment in their annual accounts.

The Financial Stability Board's (FSB) Taskforce on Climate-related Financial Disclosures (TCFD) final report and recommendations, published in June 2017 (TCFD Recommendations), expand upon the Regulations by setting out information that companies should disclose to allow investors, lenders and insurance underwriters to better understand how companies oversee and manage climate-related financial risks.

The TCFD Recommendations require companies to focus on the resilience of an organisation's strategy, taking into consideration different climate-related scenarios. They aim to strike a balance between the need to raise existing climate disclosure standards and the desire to achieve widespread adoption. They have emerged as the lead framework for climate change reporting amongst the G20 nations. The UK was the first G20 country to make the requirements into law.

As a consequence since 6 April 2022, over 1,300 of the UK's largest companies and financial institutions have been required to disclose climate-related risks and opportunities in line with the TCFD Recommendations. Those entities within the scope of the disclosure requirements include:

- UK companies who have more than 500 employees and have either transferable securities admitted to trading on a UK regulated market, or are banking or insurance companies (Relevant Public Interest Entities (PIEs)).
- UK companies with securities admitted to the AIM market of the London Stock Exchange and have more than 500 employees.
- UK companies and LLPs with more than 500 employees and a turnover of more than £500 million.

In addition companies admitted to the Official List of the London Stock Exchange are, regardless of size, also obliged to follow the TCFD Recommendations (see further below).

Carbon emissions and net zero

The Climate Change Act 2008, as amended in 2019, commits the UK to reducing the UK's greenhouse gas emissions in 2050 by at least 100% of the levels in the 1990s – net zero.

Although the Act does not directly affect UK businesses there is no doubt that it will have indirect consequences as a result of the legally binding emissions' targets to be set by the UK government every five years.

SECR (Streamlined Energy and Carbon Reporting) and greenhouse gas reporting

The Companies (Directors' Report) and Limited Liability Partnerships (Energy and Carbon Report) Regulations 2018 came into force on 1 April 2019 and impose obligations as to what must be included in the directors' report for quoted and large unquoted companies and LLPs.

SECR applies to any UK companies, LLPs and groups that exceed at least two of the following three thresholds in the financial year:

- £36m annual turnover.
- £18m balance sheet total.
- 250 employees.

For businesses meeting these criteria, company or group reporting is required regardless of whether an overseas parent company or group has published a similar report. A group may however exclude energy and carbon information relating to any subsidiaries not obliged to report individually by virtue of the thresholds and will be exempt from the disclosure requirements where less than 40MWh has been consumed in the financial year.

Energy Savings and Opportunities Scheme (ESOS)

ESOS is a mandatory energy assessment scheme for organisations in the UK that meet the qualification criteria. The Environment Agency is the UK scheme administrator. Organisations that qualify for ESOS must carry out ESOS assessments every 4 years.

Currently ESOS applies to any UK registered entity that either:

- Employs 250 or more people; or
- Has an annual turnover in excess of £44 million and an annual balance sheet total in excess of £38 million.

Businesses must take part in ESOS if they are part of a corporate group which includes another UK undertaking or UK establishment which meets these criteria.

UK registered establishments of an overseas company must also take part (regardless of size) if any other part of their global corporate group activities in the UK meet the ESOS qualifying criteria.

FRC Lab

The Financial Reporting Council (FRC) was set up in 2011 to improve the effectiveness of corporate reporting.

On 20 July 2023, the FRC Lab published its report on ESG data distribution and consumption. The report considers how investors access, collect and use ESG data and also identifies what companies can do to facilitate this. The report highlights a strong connection between narrative and data reporting as being critical to avoid greenwashing and maintain credibility.

On 26 July 2023, the FRC published its review of TCFD disclosures in the annual reports of 20 listed companies across four sectors. The review assessed the quality and maturity of disclosures on climate-related metrics and targets in the companies' annual financial reports.

The FRC encourages companies to focus on clearer and more concise explanations about their targets, actions and any impacts on financial statements. To address concerns about greenwashing, the review emphasises that the FRC will challenge companies where it considers climate-related reporting is unclear or potentially misleading. It identifies key areas that companies should consider when reporting on climate-related metrics and targets, including the overall clarity and balance of reporting and the avoidance of undue emphasis on immaterial areas of a company's business that are greener compared to more material carbon-intensive business activities.

Environmental - what's coming next?

IOSCO Recommendations

The International Organization of Securities Commissions (IOSCO) is an association of organisations that regulate the world's securities and futures markets. In November 2021 IOSCO published its recommendations for securities markets' regulators, ESG ratings and data products' providers, users of these products and services and companies subject to these providers' review. The recommendations start with a proposal that regulators could consider focusing greater attention on the use of ESG ratings and data products and the activities of ESG rating and data products' providers in their jurisdictions.

Department for Energy Security and Net Zero

On 7 February 2023, the UK Government announced the creation of a new Department for Energy Security and Net Zero, which will focus on:

- The energy portfolio of the former Department for Business, Energy and Industrial Strategy.
- Maximising the UK's long-term energy supply.
- Reducing energy bills.
- Ensuring the UK is on track to meet its net zero commitments and support its carbon capture and hydrogen sectors.

UK's Green Finance Strategy and a Powering Up Britain strategy framework

On 'World Green Day' in March 2023, the UK Government published a series of policy statements, consultation responses, new consultations and guidance as part of its wider strategy to 'Power up Britain' and transition to net zero and energy security. These include:

- The introduction of Sustainability Disclosure Requirements (SDR), which are intended to comprise an overarching, economy-wide, ESG disclosure framework for financial institutions.
- The requirement for listed companies and large private companies to report on ESG risks, opportunities and impacts.
- A plan to require certain companies to report on net zero transition plans or provide an explanation for why they have not done so.
- The development of a green taxonomy for the UK, which is expected to take a similar approach to the EU taxonomy.

The Digital Markets, Competition and Consumer Bill

The Competition and Markets Authority in the UK (CMA) is cracking down on 'greenwashing'. "Greenwashing" is the label given to the practice of companies aiming to boost sales by making misleading environmental claims about their business, products or services.

The Digital Markets, Competition and Consumer Bill was published on 25 April 2023 and could become law later this year. The Bill proposes a raft of reforms to strengthen the enforcement of consumer protection laws by, for example, handing the CMA the ability to decide when consumer law has been infringed and to then directly fine companies up to 10% of their global turnover. The ability of the CMA to impose fines would also extend to "greenwashing".

ESOS

The new UK Energy Act 2023 brings some changes to ESOS that will be enabled through secondary legislation. The changes* will standardise, improve the quality of and strengthen audits, include a mandatory net zero aspect to audits and introduce a public disclosure requirement of high level recommendations by participants. In the longer term the Government plans to hold consultations before extending ESOS to smaller businesses than currently and take further action to improve energy efficiency.

*The Energy Act 2023 received royal assent on 26 October 2023. We refer to the changes as worded in the July 2023 draft Energy Bill.

Social

The UN Guiding Principles on Business and Human Rights (UNGPs)

The UK was the first country to produce an action plan to implement the UNGPs across all Government departments. Much of the UK's current and proposed legislation for the promotion and protection of human rights stems from these voluntary principles.

Human rights in this context include those identified by the International Bill of Human Rights such as:

- The prohibition of forced, compulsory and child labour.
- The right to a safe and healthy working environment.
- The right to be paid a fair salary and equal pay.
- The right to be treated equally without discrimination.

For businesses meeting the above criteria, company or group reporting is required regardless of whether an overseas parent company or group has published a similar report. A group may however exclude energy and carbon information relating to any subsidiaries which would not be obliged to report individually by virtue of the thresholds. After undertaking a calculation, where a company has consumed less than 40MWh in the financial year, a disclosure is not required.

The Health and Safety at Work Act 1974

The Health and Safety at Work Act 1974 is the key piece of health and safety legislation in the UK. It places employers under a duty "to ensure, so far as is reasonably practicable, the health, safety and welfare at work" of all employees – this duty encompasses mental health and wellbeing as well as physical health.

The Working Time Regulations 1998

The Working Time Regulations 1998 set out limits on an employee's working time and specify minimum rest periods, rest breaks and paid holidays although employees can opt out of their rights under the Regulations.

Equality Act 2010

In the UK certain characteristics are protected characteristics under the Equality Act 2010, namely: age, disability, gender reassignment, marriage and civil partnership, pregnancy and maternity, race, religion or belief, sex and sexual orientation. Broadly speaking, the Equality Act:

- Prohibits discrimination based on any of these protected characteristics. Discrimination can take many forms, including indirect discrimination, discrimination arising out of a disability, a failure to make reasonable adjustments, harassment and victimisation. The anti-discrimination laws also protect job applicants, workers and former workers. Individuals who believe they have suffered unlawful discrimination can bring a claim in the employment tribunal and there is no maximum award of compensation.
- Implements the principle that men and women should receive equal pay for equal work. Anyone employed under a contract personally to do work is entitled to contractual terms that are as favourable as those of a comparator in the "same employment" as the other gender, if they are employed on equal work (that is, like work, work rated as equivalent or work of equal value).
- Enables employers to take steps to provide a level playing field where a group of people with a particular protected characteristic suffer a disadvantage, have particular needs that are not being met or are disproportionately under-represented in the workplace. In such circumstances an employer may take action by treating that group more favourably than those without the protected characteristic without being in breach of the Act. This is a permissive power. There is no legal requirement for an employer to use positive action but it can be a helpful tool to improve diversity and inclusion in the workplace.

Modern Slavery Act 2015

The Modern Slavery Act 2015 makes it an offence for businesses supplying goods or services in the UK to hold someone in slavery or servitude, to require someone to perform forced or compulsory labour or to facilitate or arrange human trafficking.

The Act further requires businesses supplying goods or services in the UK with a turnover of £36 million or more to prepare an annual statement that demonstrates what they have done to make sure that modern slavery is not taking place in their business or supply chain. The Act explains that such corporate statements may include information about issues such as risk assessment, due diligence, steps taken to address identified risks, policies and procedures, training and the effectiveness in ensuring that modern slavery is not taking place. The UK Government has published guidance which expands on these issues.

The Equality Act 2010 (Gender Pay Gap Information) Regulations 2017 (SI 2017/172) (as amended)

Employers with 500 or more employees are required to publish information on their gender pay gaps each year. They must do this for each year they have 500 or more employees and for each separate 'legal entity', if part of an organisation or group comprising more than one legal entity.

Social - what's coming next?

Modern Slavery Bill

The Queen's Speech 2022 outlined the Government's intention to bring forward a Modern Slavery Bill, which would propose a number of changes including mandated areas to be covered in modern slavery statements, require these statements to be published on a Government-run registry and introduce civil penalties for non-compliance. The Bill has not yet been published.

Proposals have been announced to amend and strengthen the provisions within the Modern Slavery Act 2015 including, for example, the introduction of civil penalties for organisations that do not comply with the requirements of the Act and mandating the topics to be included in modern slavery statements. These proposals have not yet made their way through the parliamentary process.

Neonatal Care (Leave and Pay) Act 2023

This Act received royal assent on 24 May 2023 and is due to come into force in April 2025. The Act will allow parents to take up to 12 weeks leave each to spend time out with a baby receiving neonatal care. Leave will be available to all employees from day one of employment but statutory neonatal pay, which will be paid at the same rate as other statutory family leave will only be available to employees with over 26 weeks' service.

Carer's Leave Act 2023

This Act received royal assent on 24 May 2023 and subject to implementation regulations will introduce a new statutory right of up to one week of unpaid carer's leave per year for employees who are providing or arranging care. No qualifying period of service will be required. Employees will not need to provide evidence of how the leave is used or who it will be used for. Employees taking carer's leave will be protected from dismissal or detriment as a result of taking time off.

Protection from Redundancy (Pregnancy and Family Leave) Act 2023

This Act will give pregnant women and new parents greater protection against redundancy by extending the time during which an employee, who is facing redundancy, has the right to be offered alternative suitable available employment. The extension of time is yet to be decided but could be up to 18 months after the birth or adoption. This will apply to maternity leave, adoption leave and shared parental leave and is expected to come into force in April 2024.

Employment Relations (Flexible Working) Act 2023

This Act received royal assent on 20 July 2023 and is expected to come into force in mid-2024. The Act will amend the application process for making a flexible working request. The employer will have to consult the employee before rejecting a request, an employee will be able to make two applications in 12 months (rather than one), the employer's decision period will be reduced from three months to two months and the employee will not have to state in their request what impact the change would have on the employer's business.

Workers (Predictable Terms and Conditions) Act 2023

This Act received royal assent in September 2023 and is expected to come into force in autumn 2024. It will give workers (including agency workers) the right to request a predictable working pattern where their existing working pattern lacks certainty in terms of hours or times of work or where they have a fixed term contract of less than 12 months. Workers have to have worked for their employer for 26 weeks before making an application. Employers will be able to refuse a request on specific grounds, such as the burden of additional costs to make changes or if there is insufficient work at times when the employee proposes to work. Workers will be able to make up to two requests a year.

Worker Protection (Amendment of Equality Act 2010) Bill

This Bill proposes to reintroduce employers' liability for harassment of employees by third parties at work, such as clients or customers. It will also introduce a new duty on employers to take all reasonable steps to prevent workplace sexual harassment.

Ethnic pay gap reporting

On 17 April 2023, the Department for Business & Trade (DBT) published new guidance for employers on ethnicity pay reporting. There is as yet no obligation in the UK to report on the ethnicity pay gap but the DBT explains that it can help to build transparency and trust among employees. It states that providing a consistent approach to measuring pay differences will enable meaningful comparisons to be made between different periods of time at the same organisation and between different employers. The recommendation was "to support employers and industry sectors to create opportunity for groups that are underrepresented in their workforce".

Governance

Section 172 of the Companies Act 2006

For all companies incorporated in England and Wales the overarching legislation in relation to governance is found in the Companies Act 2006. The duties of company directors are codified pursuant to Section 172 to promote the success of the company for the benefit of the members as a whole having regard to:

- The likely long-term consequences of decisions.
- The interests of the company's employees.
- The need to foster the company's business relationships with suppliers, customers and others.
- The impact of the company's operations on the community and the environment.
- The desirability of the company maintaining a reputation for high standards of business conduct.
- The need to act fairly as between members of the company.

The Companies (Miscellaneous Reporting) Regulations 2018 (SI 2018/860)

The Miscellaneous Reporting Regulations 2018 require UK companies that meet specific qualifying conditions (predominantly quoted companies and large private companies) to include a statement of corporate governance arrangements in their directors' report. Such a statement must include:

- Which (if any) corporate governance code the company applies and the reasons for any departure from that corporate governance code.
- If the directors have decided not to apply any corporate governance code, the reasons for that decision and an explanation of what corporate governance arrangements have been applied for the financial year.

Large private companies may choose to adopt the Wates Corporate Governance Principles for Large Private Companies to comply with the Regulations.

Listing Rules

The rules relating to admission to the London Stock Exchange Official List (Listing Rules) require companies admitted to both the premium and standard lists to contain detailed information about their commitment to ESG in their annual financial report. Such information must include:

- Whether the company has made climate-related financial disclosures consistent with the TCFD Recommendations. In providing such information the company is required to consider whether those disclosures provide sufficient detail to enable users to assess the company's exposure to and approach to addressing climate-related issues taking into account factors such as:
  - The level of its exposure to climate-related risks and opportunities.
  - The scope and objectives of its climate-related strategy.
- Whether the company has met certain targets on board diversity including:
  - At least 40% female directors.
  - At least one senior position on the board being held by a woman.
  - At least one director being from a minority ethnic background.

In addition listed companies are required to set out numerical data in a prescribed tabular form on the ethnic background and the gender identity or sex of the individuals on the company's board and in its executive management.

Companies with a premium listing are also required by the Listing Rules to comply with the UK Corporate Governance Code (UK Code) and to include in their annual report a statement of how they have applied the main principles of the UK Code in a manner that would enable shareholders to evaluate how the principles have been applied and where they have failed to comply with the UK Code to explain any non-compliance – the 'comply or explain' approach.

The UK Corporate Governance Code

The first version of the UK Code was produced by the Cadbury Committee in 1992 and contained what is still regarded today as the classic definition of corporate governance for UK companies.

The UK Code focusses on five core principles of governance:

- A successful company is led by an effective and entrepreneurial board, whose role is to:

- Promote the long-term sustainable success of the company, generating value for shareholders and contributing to wider society.
- The board should establish the company's purpose, values and strategy, and satisfy itself that these and its culture are aligned. All directors must act with integrity, lead by example and promote the desired culture.
- The board should ensure that the necessary resources are in place for the company to meet its objectives and measure performance against them. The board should also establish a framework of prudent and effective controls, which enable risk to be assessed and managed.
- In order for the company to meet its responsibilities to shareholders and stakeholders, the board should ensure effective engagement with, and encourage participation from, these parties.
- The board should ensure that workforce policies and practices are consistent with the company's values and support its long-term sustainable success. The workforce should be able to raise any matters of concern.

The UK Code also contains a number of principles that feed more directly into the principles of ESG, such as the requirements that:

- The company's annual report:
  - Includes an explanation of the company's approach to investing in and rewarding its workforce (Principle 2).
  - Describes the work of the company's nomination committee including:
    - The process used in relation to appointments, its approach to succession planning and how both support developing a diverse workforce.
    - The policy on diversity and inclusion, its objectives and linkage to company strategy, how it has been implemented and progress on achieving the objectives.
    - The gender balance of those in senior management and their direct reports.
- The board should understand the views of the company's other key stakeholders and describe how their interests have been considered in accordance with section 172 of the Companies Act 2006 (Principle 5).

AIM Rules

Companies admitted to the AIM market must provide to the London Stock Exchange and disclose on their website details of a recognised corporate governance code that they will apply, how they comply with that code and if they depart from their chosen code, an explanation of the reasons for doing so. This information is to be reviewed annually. AIM companies are not required to adopt the UK Code and instead most AIM companies choose to adopt the Quoted Companies Alliance Corporate Governance Code which is considered to be more appropriate for small to medium sized corporate entities or SMEs.

Institutional investor guidelines

Certain institutional investor bodies, such as the Investment Association (IA), The Pensions and Lifetime Savings Association (PLSA) and the Institutional Shareholder Services (ISS) have published corporate governance guidelines which are designed to assist shareholders and others in interpreting the UK Code and the adherence by premium list companies with statements of best practice when considering voting decisions at company meetings. Although not directly applicable to companies outside the premium list many smaller listed companies nevertheless chose to comply with institution-led statements of best practice.

UK Stewardship Code

The UK also has a Stewardship Code setting out good practice for institutional investors when engaging with UK listed companies.

As may be seen from the requirements of the Listing Rules in particular, ESG has become more prevalent in the initial public offering (IPO) process, with companies and investors undertaking extensive diligence to ensure they do not lose value as a result of ESG issues. Such enhanced reporting requirements have enabled investors to better understand the risks associated with their investments.

Governance - what's coming next?

Significant corporate governance reforms are outlined in the Government response (published on 31 May 2022) to the Department for Business, Enterprise and Industrial Strategy's (BEIS) March 2021 consultation paper: Restoring trust in audit and corporate governance.

These include (among other things) changes to reporting on internal controls and reporting on anti-fraud measures, claw-back of director bonuses, publication of an annual resilience statement on the company's mitigation of risks, publication of a triennial audit and assurance policy and annual implementation report, stronger disclosure and attestation requirements on directors in relation to dividends and capital maintenance, new standards for audit committees in relation to appointment and oversight of auditors and shareholder engagement and in relation to directors' breach of duty and misconduct.

On 30 January 2023, the Financial Reporting Council (FRC) updated its first statement of intent on ESG from 2021. The FRC has proposed changes to the UK Code to implement its reforms with its stated intention being that a revised UK Code will apply to accounting years commencing on or after 1 January 2025.

As part of the FCA's proposals to reform the existing UK listing regime for equity shares the FCA is also expected to consult on moving away from the current 'comply or explain' approach to corporate governance in favour of mandatory disclosures for listed companies. The FCA is also expected to seek views on proposed guidance for disclosures relating to listed companies' transition plans, which describe a company's targets and actions (such as reducing greenhouse gas emissions) for transitioning to a lower-carbon economy.

Governance by sector

Depending on their sector of operation UK businesses may face other governance requirements and challenges.

In the financial services sector for example there have been various initiatives to strengthen corporate governance. These have included increasing focus on sustainable finance, senior managers' responsibility and individuals performing significant influence functions in regulated firms and measures to control remuneration policies and arrangements.

In the legal profession, solicitors and law firms are required to publish their diversity data on their websites.

A comprehensive review of sector-specific requirements is beyond the scope of this paper but for more information about the impact of ESG on the Construction and Hospitality Sectors please see:

New report: How ESG principles are impacting on companies in the UK built environment | Womble Bond Dickinson

The "S" in ESG for the hospitality sector | Womble Bond Dickinson

What's happening elsewhere?

EU

Transitioning to a net zero economy and channelling investment accordingly has been one of the key policy aims for the European Commission over recent years, reflected in its overarching Green Deal policy framework. As a result, a number of specific policies and regulatory initiatives have been developed in the ESG space.

The package of EU sustainable finance regulations seeks to integrate ESG considerations into the investment and advisory process in a consistent manner across sectors. As one of the key pillars of the EU Action Plan on Sustainable Finance, the Taxonomy establishes a classification system for "environmentally sustainable activities". The EU regime for ESG disclosures in the financial services sector has grown more rapidly than elsewhere in the world and is continuing to grow at pace.

In addition, in February 2023, the European Parliament and Council reached political agreement on a European Green Bond Standard, laying out the basis of a framework of rules that issuers worldwide can use to achieve the designation "European Green Bond". The Green Bond Standard will be aligned with the Taxonomy (with 85% of the proceeds of the issuance to be channelled toward Taxonomy-aligned investments) in order to provide consistency of usage of the term "green" within European financial markets.

In February 2022, the Commission adopted a proposal for a Corporate Sustainability Due Diligence Directive. The proposal includes:

- A new due diligence duty to be integrated into corporate policies and which requires companies to identify, prevent, mitigate, minimise and end adverse human rights and environmental impacts in their own operations, in their subsidiaries and in their established direct or indirect business relationships.
- A requirement for large companies to have a climate transition action plan to ensure that their business model and strategy are compatible with the transition to a sustainable economy and with limiting global warming to 1.5°C.
- Clarification of the duty of directors to act in the best interests of the company, which requires them to take into account the human rights, climate and environmental consequences of their decisions and the likely consequences of any decision in the long term.

Victims of breaches will be able to bring a civil liability claim for damages before the national courts.

The new due diligence duty will apply to EU companies with more than 500 employees and a net worldwide turnover of over €150 million and to EU companies operating in high risk sectors (agriculture, textiles or extraction of minerals) with more than 250 employees and a net worldwide turnover of over €40 million. Non-EU companies that meet the same criteria in respect of their net turnover generated in the EU will also be covered. The Directive is set to be negotiated between the EU political institutions and will likely not come into force before 2030.

US

The US does not have such an advanced regulatory process for addressing ESG-related issues as the UK or EU and there are particular reasons for this:

- The differentials between the federal and state legislatures, with current legislation often making it difficult for businesses to voluntarily implement ESG favourable policies. For example under Delaware law a company's sole purpose is to maximise shareholder value and whilst the board and management of a Delaware company are permitted some latitude to consider other stakeholders such as the company's employees, its community and even the planet, this must all be done in furtherance of the long term interests of the company's shareholders.
- Whilst the core political parties in the UK and EU are broadly in line when it comes to the importance of devising and implementing sound ESG principles and policies supported by appropriate legislative measures, in the US the legislature is somewhat divided not only on federal and state lines but also on party political grounds with some republican politicians volubly campaigning in favour of anti-ESG legislation and a significant cohort of democrats campaigning for an expansion of pro-ESG legislation. As a consequence both pro- and anti- ESG proposals are trending up; with anti-ESG proposals trending ahead of pro-ESG proposals in numerical terms (as of July 2023).

That said ESG is becoming an increasingly more significant and consistent area of focus for US institutional investors and for the boards of large US companies, particularly those with an international footprint, than ever before.

Finally, the challenges to the legislature

There is no doubt that over the past few years there has been a considerable rise in public concern for environmental and social equity as well as sound governance in the UK and amongst UK-based investors.

ESG considerations have become more prevalent in IPOs and also in the private equity arena.

It is these investor-led sentiments which have driven the growth of ESG-related laws and regulations, codes of conduct and statements of best practice.

However devising a framework whereby companies may be judged on a like for like basis is not without its challenges. In 2021, BNP Paribas Securities Services published The ESG Global Survey 2021, which identified the key challenges to ESG integration as being:

- Inconsistency of data across different classes of asset, conflicting ESG ratings or indices, challenges with quality and effectiveness of data.
- The complexity of social factors and the lack of a definite, industry-wide definition of what social factors are, exacerbated by the increased focus of investors on the social pillar of ESG.
- The differing views of voluntary frameworks and regulatory systems.

Providers of ESG data and ESG ratings are largely unregulated. However, plans have been proposed in the UK and EU to introduce additional regulation in this area, in light of the increasing role that these organisations are playing in investment decision-making and companies' public ESG disclosures.

Greenwashing, is a cause for concern. The complexity of ESG issues and measurement and the lack of unified frameworks for assessing and comparing risks and opportunities bring significant challenges. The UK and EU have both proposed additional regulation in relation to the labelling of financial products and we expect to continue to see such initiatives gain traction over the coming years.

In recent times however, there has been a notable consolidation of standards, and this looks set to continue moving forward. During the COP 26 summit in November 2021, the International Financial Reporting Standards (IFRS) Foundation announced the formation of the International Sustainability Standards Board (ISSB). The ISSB issued its inaugural standards—IFRS S1 and IFRS S2— in June 2023 ushering in a new era of sustainability-related disclosures in capital markets worldwide. IFRS S1 provides a set of disclosure requirements designed to enable companies to communicate to investors about the sustainability-related risks and opportunities they face over the short, medium and long term. IFRS S2 sets out specific climate-related disclosures. Both fully incorporate the recommendations of the Task Force on Climate-related Financial Disclosures (TCFD).

For the first time, the standards create a common language for disclosing the effect of climate-related risks and opportunities on a company's prospects.

Investment funds that focus on ESG issues are growing in popularity and requirements in relation to ESG issues are increasingly becoming mandatory in a number of jurisdictions. Companies expect climate and ESG issues to continue to gain traction and are addressing pressure from investors through a range of measures, including their governance structures, stakeholder engagement, public disclosures and specific targets and strategies.

This article was written by Rebecca Ferguson (Partner) and Krish Dholakia (Managing Associate) in the Womble Bond Dickinson London office.

About Womble Bond Dickinson

Womble Bond Dickinson (WBD) is a full-service international law firm sitting amongst the Top 20 UK law firms and ranking 109th globally.

We have eight offices in the UK and 24 in the US. Our international reach also extends to Europe where we have strategic partnerships with law firms in Germany and France. Through our membership of the Lex Mundi network we can offer clients access to legal counsel in more than 120 countries.

Advising businesses across eleven key sectors of expertise, our clients range from FTSE 100 companies, to private clients, family offices, charities and both local and central government authorities.

WBD has a strong focus on innovation and has consistently ranked in the Top 30 most innovative law firms in Europe by the Financial Times. Our Innovation Group works with lawyers and clients to help identify new opportunities to deliver the best value and coordinate initiatives and projects across the firm that will help drive our business – and our clients – forward.

Corporate Services at Womble Bond Dickinson

The legal and regulatory complexities of setting up and running a business successfully may seem challenging to most and off-putting to many. We provide our clients with a team of top-tier, high profile lawyers deeply familiar with the many and various issues which businesses and those seeking to start or invest in a business may face.

Our diverse client range means that we have a breadth of experience providing assistance to a range of businesses across different sectors. We act for a number of private and listed companies from single entities to corporate groups in addition to entrepreneurs and family offices across the UK and the US.

We specialise in tailoring our full corporate service offering to suit the specific business needs of our clients.

Our corporate services team includes:

- Transactional lawyers experienced in advising on public and private mergers and acquisitions and restructurings, private equity, corporate finance, IPOs and RTOs.
- Compliance lawyers expert on advising on, devising and implementing corporate governance structures and regimes for all types of businesses and at all stages of their evolution.
- Employment and pensions lawyers who work with business owners across a wide range of employment and employment-related matters and issues.
- Regulatory lawyers who advise on health & safety, fire safety and environmental regulations.

Womble Bond Dickinson & ESG

Being a responsible business is integral to who we are. From our commitment to reaching net zero by 2030 and our Sustainable Procurement Policy, to giving all of our people 14 volunteering hours every year, and achieving Stonewall Top 100 and 11th place on the Social Mobility Employer Index, we are focused on becoming a truly responsible business.

Our Gold sustainability rating from EcoVadis, which assesses us across four key areas: labour and human rights, ethics, procurement and environment, ranks us in the top two percent of the 100,000 companies submitting annually. We have also achieved the Gold Investors in People 'We Invest in People' standard demonstrating our commitment to putting responsible business at the heart of all we do.

We are a Disability Confident Employer and an accredited Living Wage employer. We are signatories to the Mindful Business Charter and Halo Code and achieved the Silver Investors in People 'We Invest in Wellbeing' standard. We are also founding and executive members of the Legal Sustainability Alliance and are ISO 14001 accredited recognising that we have an effective environmental management system in place.

We are proud of our achievements to date, and know that by embracing innovation and collaboration, we can continue to strive for a more sustainable and inclusive future for us all. To find out more about our responsible business work, please read our latest Responsible Business Report.

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