

# The Complete Compliance and Ethics Manual 2024 Compliance Professionals as the New Face of ESG Leadership

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Environmental, social, and governance (ESG) concerns make up a broad area of investor and stakeholder interest. There are many different specific definitions, but generally:

- “E” covers a wide spectrum of **environmental** initiatives aimed at minimizing an entity’s harm to the environment, including climate change, pollution, biodiversity, deforestation, and greenhouse gas emissions; doing business with ecofriendly practices in mind, such as having energy efficiencies and goals; and practicing pollution mitigation, reducing-reusing-recycling product lifecycle management, waste management, and water usage reduction.
- “S” focuses on the many aspects of **social** interactions and human capital, including justice, equity, diversity, and inclusion; compliance and ethics matters, including reporting hotlines, labor standards, wages, and benefits; workplace and board diversity; racial, social, and organizational justice; and stakeholder and community relations.
- “G” is the **governance** and oversight of this area, such as board composition and structure, board diversity, oversight and compliance, executive compensation, political contributions and lobbying, and bribery and corruption.

Prior to 2019, the general thought was that a company’s primary purpose was to make money for its shareholders, but interest in ESG matters on the part of investors and other corporate stakeholders has intensified, and the current economic, public health, and social justice crises have made this focus acute. ESG is now a critical way in which companies are being evaluated beyond the financial reports, and there is active consideration by organizations, such as the United States Securities and Exchange Commission, and additional regulation, such as the European Commission Non-Financial Reporting Directive (NFRD).<sup>[2]</sup> The NFRD lays down the rules on disclosure of nonfinancial and diversity information by certain large companies, and in November 2022, the Council for the European Commission adopted, as part of the European Green Deal and the Sustainable Finance Agenda, the new Corporate Sustainability Report Directive (CSRD). The CSRD begins to apply to companies on a rolling basis in 2025.

## How Did We Get Here, and Why Does ESG Matter Today?

The 1990s saw the creation of what is now called the MSCI KLD 400 Social Index, the first index to track sustainable investment through a capitalization-weighted methodology.<sup>[3]</sup> Today, there are more than 1,500 indexes that measure ESG, and the number of ESG-specific exchange-traded funds has grown exponentially.

In the past 30+ years, a number of events have continued to shape ESG and investor interest in ensuring companies are focused on how they show up when it comes to ESG. The 2000s saw scandals from Enron, Tyco International, and WorldCom; the Sarbanes-Oxley Act went into effect to protect investors from fraudulent financial reporting by corporations; and the Dodd-Frank Wall Street Reform and Consumer Protection Act sought to protect consumers and the economy from risky behavior from banks and insurance companies. Further events,

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such as the Equifax data breach, Wells Fargo banking scandal, and Theranos fraud occurred in 2017 and 2018, with these companies and individuals facing significant backlash from customers, investors, and the government. The social side of ESG was also bolstered by movements, such as #MeToo, #TimesUp, and Black Lives Matter, and 2019 saw California mandate that women be included in boards of directors.

Today, as global challenges continue to converge with social issues like racism and environmental issues like global warming, your investors, customers, and employees have never cared more about how you're tackling ESG. This means the opportunity is real—as are the risks if your company misses the opportunity or gets it wrong.

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