Defining the 'G' in ESG
Governance Factors at the Heart of Sustainable Business

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Growing concerns about sustainability have catapulted corporate ESG (environmental, social and governance) performance into the spotlight. By 2020, ESG investment funds had officially gone mainstream and had even started to outperform the broader market. In the meantime, various jurisdictions have begun to contemplate binding ESG corporate disclosure regulations. The influx of money and attention around ESG has rapidly raised the stakes of non-financial corporate performance, produced a web of ESG reporting and rating frameworks, and led to a barrage of ESG-related pledges and promises from corporate actors worldwide.

While much of the momentum has focused on environmental performance and certain social indicators – such as diversity, inclusion and modern slavery – there has been comparatively little emphasis on corporate governance, the "G" in ESG. Corporate governance includes factors such as corporate structure, board composition, business ethics and anti-corruption. Although our understanding of corporate governance is evolving alongside the rise of ESG, it generally predates environmental and social risks as a corporate priority. Consequently, many key governance indicators cover information that readily exists and may already be included in corporate disclosures. However, the comparative lack of attention on the G in ESG has led to confusion about the nature and role of corporate governance within ESG frameworks.

In addition to being one-third of the ESG equation, the G is also foundational to the realization of both the E and S. Behind each breach of a company's environmental or social commitments lies ineffective corporate governance, be it inadequate anti-corruption practices, perverse incentive structures, contradictory lobbying activity, or ill-equipped leadership. Further, corporate governance affects the integrity of ESG disclosures, determining whether ESG indicators are ethically pursued and reported. Although corporate governance attracted public attention during the first waves of the anti-corruption movement, climate change and human rights have dominated the ESG stage. Nonetheless, effective corporate governance is essential to ensuring that ESG enthusiasm translates into concrete action and systemic change.

To this end, the World Economic Forum Global Future Council on Transparency and Anti-Corruption has developed the following basic list of factors that should be included within the G in ESG. This list builds on recent reports on the rise and role of the chief integrity officer, the role of anti-corruption within ESG investing and the need to develop common metrics and consistent reporting on sustainable value creation, as well as other prominent ESG disclosure frameworks.

Although presented in list form, treating the factors below as a checklist will render the exercise meaningless. For example, it is not the mere existence of "whistle-blower protocols" that matters but how they are executed in practice. In a similar vein, the nature and deployment of governance factors will vary based on industry. For example, those in mining must consider the issue of conflict minerals while those in consumer goods must consider the importance of responsible advertising. Adaptations may also be necessary to accommodate institutional capacities and the particular needs of, and limitations imposed by, the local context.

If thoughtfully deployed, however, the enumerated factors will help ensure that the G in ESG is adequately represented in rating and reporting frameworks while simultaneously increasing the likelihood that companies are delivering on their environmental and social commitments as well.

Factors	Example sub-factors, key indicators
Business ethics	Purpose, values, culture, integrity beyond compliance, ESG integration, pursuit of and reporting on KPIs
Board composition	Competencies, diversity, structure, committees, oversight capacity, independence
Corporate leadership	Tone, knowledge, experience, power allocation, compensation, decision-making processes, independence and empowerment of compliance function
Risk and crisis management	Preparedness, mitigation, past performance, regulatory compliance, segregation of duties, audit independence, shareholder rights, information governance, cybersecurity
Resource allocation	Capital allocation, personnel allocation, mergers and acquisitions
Incentive structures	Compensation, promotion, reporting structures, defined prohibited misconduct, disciplinary measures
Political responsibility	Lobbying, amicus briefs, campaign finance, political contributions
Transparency	Ownership, subsidiaries/holdings, open contracting, lobbying, charitable donations, countries of operation, verifiability of disclosures
Anti-corruption and integrity	Training and communications, whistle-blower protocols, due diligence, risk assessments, public procurement, government relations, gifts and entertainment, conflicts of interest, remuneration and payment procedures, record-keeping, financial controls, reporting and accounting, contractual obligations, public commitments, past incidents, internal investigation and remediation
Tax strategy	Tax compliance, anti-tax avoidance, tax disclosures
Fair competitive practices	Anti-collusion, anti-exclusion, anti-monopoly, anti-coercion, market-based pricing
Stakeholder engagement	Understanding corporate impact and stakeholder priorities, pursuing stakeholder-centred practices
Supply/value chain management	ESG integration, transparency, contractual obligations, countries of operation