

Investing in Integrity in an Increasingly Complex World: The Role of Anti-Corruption amid the ESG Revolution

COMMUNITY PAPER

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Executive summary

This paper makes the case for raising the profile and role of corruption risks within investor decision-making processes and corporate ratings. Whether focusing exclusively on financial prospects or embracing the growing trend of ESG (environmental, social and corporate governance) investing, corruption risks – including bribery, fraud, money laundering and other illicit financial activities – are a material concern.

This paper first discusses the various ways in which corruption can undermine both traditional and emerging aspects of the investment agenda, including financial growth, environmental sustainability and respect for human rights. Corruption heightens financial risk, distorts regulatory enforcement, siphons money and attention away from public priorities, and distracts public- and private-sector actors from building a sustainable and stakeholder-centred economy. Within the ESG framework, corporate corruption is therefore framed as both a vertical and a horizontal concern – directly measurable as a key factor within the “G”, while simultaneously affecting the “S” and “E”. Further, corporate integrity is essential to the ethical pursuit of ESG standards and the honest reporting of ESG metrics. In sum, integrity should be understood as the backbone of ESG and sustainable investing more broadly.

Despite the foundational role of corruption vis-à-vis investor (and global) priorities, it appears to be a relatively rare and inconsistent consideration among asset owners, investment managers and rating agencies. In particular, this paper highlights the role of existing ESG disclosure frameworks and

standards in shaping investors’ understanding of and priorities within ESG investing. It notes that individually and collectively these frameworks and standards contribute to the marginalization of corruption risks through: (1) inconsistent terminology; (2) inconsistent framing; (3) inconsistent reporting recommendations; and (4) the over-greening of ESG.

In order to more adequately and accurately incorporate corruption risks into investor decision-making processes and frameworks, this paper concludes with three recommendations. First, all actors within the investor universe should centre integrity within their own commitments, processes, policies and incentives. Second, corruption risks must be embedded into reporting and rating frameworks in a coherent, comprehensive and standardized manner. This should include verifiable disclosure requirements; process- and prevention-focused metrics; a critical and nuanced approach to corporate disclosures; and the adoption of a core, standardized set of indicators to promote cross-sectoral, cross-framework comparability and reflect the reality that some risks (and corruption risks in particular) are universally relevant. Finally, it advocates for increased investor-driven collective action on the mainstreaming of corruption risks within investor decision-making processes.

Centring integrity within investor priorities, and the ESG revolution more specifically, will increase the likelihood that the promises and policies of investors and investees translate into concrete action and the sustainable, inclusive future towards which we strive.

Introduction

As the momentum around ESG (environmental, social and corporate governance) investing translates into concrete metrics, actions and, at least in some jurisdictions, binding law, the role and significance of corruption are often sidelined. The world's attention has justifiably fixated on the existential threats of corporate-caused climate change and, increasingly, human rights abuses and inequity. However, investors and standard-setting organizations should not lose sight of the corrupt conduct that frequently enables environmentally and socially corrosive corporate behaviour. Corruption is intricately intertwined with financial, environmental, social and governance risks alike. Moreover, corporate integrity is fundamental to ethical ESG performance and reporting. Screening and mitigating corruption risks should therefore be integral to investor frameworks, metrics and ratings across the board.

ESG investing is now a widely offered and increasingly adopted investment strategy – an achievement that was at least partially propelled by the devastation caused and inequality exposed by the [COVID-19 pandemic](#), as well as growing concern about [climate change](#). Of maybe greatest

importance, however, is that many large ESG investment funds have begun to [outperform the broader market](#). This combination of factors has resulted in a surge of interest in ESG investing. In the United States, for example, the amount of net new money invested in ESG funds jumped from approximately [\\$21 billion in 2019](#) to an estimated [\\$120 billion in 2021](#). Worldwide, total ESG assets under management are predicted to reach [\\$50 trillion by 2025](#).

Against the backdrop of the pandemic, climate change and growing interest in sustainable finance, embracing a coherent and comprehensive approach to ESG investing is more important than ever. Although this paper was developed prior to the war in Ukraine, the conflict and the response from companies and investors add additional weight to the meaning and implications of ESG investing, divestment and the role of anti-corruption. Particularly as the nascent [International Sustainability Standards Board](#) sets out to create the new global baseline for sustainable investing, integrity must be placed at the heart of these conversations and investing frameworks.

1

Understanding and managing diverse corruption risks

1.1 Corruption and financial risk

Corruption – including bribery, fraud, money laundering and other illicit financial activity – is a material concern for all corporations and industry sectors. It can substantially affect the worth and future prospects of a company. Corruption encourages financially unsustainable business practices, promotes short-term thinking and often translates into dishonest reporting. If exposed, corruption can lead to massive financial loss, reputational damage, market exclusion and even bankruptcy.

For example, as of May 2022, the [top 10 biggest US Foreign Corrupt Practices Act \(FCPA\) cases of all time](#), in terms of financial penalties and disgorgement, ranged between \$700 million and \$3.3 billion. Emblematic of the financial risks posed by corporate corruption, in 2019 the once industry-leading Brazilian construction giant Odebrecht (which now goes by Novonor) filed for bankruptcy protection to restructure [\\$13 billion in debt](#) following a transnational corruption scandal that was exposed in 2014. Company representatives referred to the situation as a financial and reputational crisis.

Almost two decades earlier, Enron Corporation, a US-based energy-trading company, experienced an even more dramatic fall from grace due to a large-scale fraud scheme. The company, which was once the seventh largest in the United States, filed for bankruptcy in 2001 and quickly [became synonymous with corporate corruption](#).

While some countries and industries appear to be more exposed to corruption risks than others, none has escaped the financial fallout associated with acts of corruption. As a key indicator of corporate financial health, it is essential that investors understand the corruption risks in their portfolio. If a high-performing company is built upon a corrupt foundation, it is only a matter of time before this reality comes to light – an outcome made increasingly inevitable by [recent digital advances](#). Asset owners and managers would be best served if such risks were assessed and avoided ex ante rather than waiting for enforcement action and a financial crisis.

1.2 Corruption and ESG risks

Essentially synonymous with socially responsible or sustainable investing, ESG investing considers environmental, social and corporate governance risks, as well as traditional financial risk, when making investment decisions. This more holistic approach to evaluating and investing in corporate prospects and potential is increasingly shaping

the investment universe. If the purpose of the global investment system is to enable the efficient allocation of capital to improve economic outcomes, ESG investing expressly acknowledges the reality that efficiency and economic improvement depend on more than financial metrics.

Corruption and corporate governance

Within the ESG framework, corruption risks are generally factored into the overarching category of “corporate governance” (the “G” in ESG), alongside other factors related to corporate structure, board composition and power allocation.

Moreover, corporate governance is evolving with the ESG revolution. For years, corporate governance has been centred on corporate leadership, shareholders, liability and profit. However, with the world’s attention turned towards the climate crisis, the pandemic, human rights abuses and other ESG factors, [corporate governance is increasingly understood to be a more holistic concept](#). In addition to the

inward lens of years past, corporate governance is beginning to encompass the external impact of corporations, as well, including factors such as responsible stewardship, stakeholder well-being and lobbying with integrity. As the definition of good corporate governance expands to embrace ethical and stakeholder-centred issues, so, too, does the significance of corruption risks vis-à-vis the “G” in ESG. Corruption not only affects a company’s exposure to legal risk and mismanagement, it also has an impact on the integrity of political partners and the welfare of surrounding communities. Further, corruption is intimately connected to relevant environmental and social factors.

Corruption and the environment

Both people and the planet suffer when corruption distorts markets, regulatory enforcement and legislative progress. A 2020 report by the [Brookings Institute](#) illustrates that:

“Even when regulations are strong on paper, they can be ineffectively and corruptly enforced, which undermines all ensuing environmental protections. At the national level, officials [have been known to accept or ask for bribes to issue licenses that open up land for extraction that would otherwise remain environmentally protected.](#) At the local level, corruption can take such forms as demanding [bribes](#) from companies to waive regulatory requirements and otherwise enforcing legal requirements in an ad hoc fashion based on kickbacks.”

Corruption can also affect assessments of and accurate reporting on corporate environmental impact. In the words of Delfin Ganapin, World Wide Fund for Nature (WWF) Governance Practice Leader, “[u]nless we tackle [environmental crime and corruption](#), our efforts to ensure the world’s natural systems flourish and benefit communities and economies for the long-term will come to naught”. From CO₂ emissions and water pollution to environmental degradation and ever-dwindling biodiversity, there is a clear link between corruption and all of the chart-topping items on the [global environmental agenda](#). For example, corruption has facilitated [deforestation](#), [abusive extractive practices](#), the illegal [poaching and trafficking of wildlife](#) and [ecosystem-altering dam projects](#).

Corruption and human rights

Similarly, social risks are exacerbated when corruption allows profit to take priority over regulatory enforcement and human well-being. Corruption siphons money away from a [broad range of basic necessities and essential services](#), including healthcare, education, clean water and housing. Corruption can inspire governments to turn a blind eye towards, or even contribute to, the silencing of speech, the stealing of land, the

poisoning of water and the killing of community leaders, all in the name of corporate interests. In a [2020 report](#) tallying the number of land and environmental defenders murdered the previous year, the non-profit Global Witness attributed many of the “world’s worst environmental and human rights abuses” to “corruption in the global political and economic system”. Further, corruption [negatively affects economic growth](#)

[and exacerbates global inequalities](#) by eroding political legitimacy, discouraging investment, distorting markets and stunting crucial public services – all of which have a particularly profound effect on developing economies, [small and medium-sized enterprises](#), and society’s most vulnerable populations.

Finally, the battle against COVID-19 has made the problematic role of corruption in emergency and crisis situations salient for the world.

Reports have exposed the various ways in which [corruption has interfered](#) with ventilator production, vaccine distribution, adequate medical care and access to life-saving personal protective equipment (PPE). However, the phenomenon of corrupt actors capitalizing on dire situations is nothing new. Humanitarian aid has long been plagued by the [corrosive impact of corruption](#), which can unnecessarily deepen human suffering and prolong recovery processes.

1.3 Integrity as the backbone of strategic, sustainable investing

Corporate integrity should be understood as the foundational element of ESG and sustainable investing more broadly. It is a cross-cutting material concern and fundamental to the realization of the ESG agenda. Not only does corruption erode ESG priorities, it can also distort ESG administration and reporting. These risks are exacerbated by the

novelty of ESG disclosure requirements and the qualitative nature of many ESG indicators, both of which make third-party verification relatively difficult. It is therefore impossible to achieve investors’ environmental, social, governance or financial goals without properly accounting for corruption risks.

FIGURE 1 The various ways in which corporate integrity impacts ESG performance and reporting



Source:
World Economic Forum

Corruption also affects the entire range of stakeholders, from shareholders and employees to community members and the planet. As such, realizing a sustainable and stakeholder-centred business agenda – the stated goal of the [Business Roundtable](#) and the World Economic Forum’s International [Business Council](#) – cannot be achieved without tackling corruption.

Some progress has been made towards making anti-corruption more of an investing priority. [International organizations](#) and leaders from

[civil society](#) and the [private sector](#) have developed guidance on why and how the issue of corruption risks should factor into investment analyses and decision-making processes. Nonetheless, much of the “G” in ESG, and corruption in particular, appears to have fallen through the cracks of many investor practices, investee engagement processes and prominent sustainable investing standards. While the “G” is part and parcel of ESG frameworks in name, there is little consensus on what it actually encompasses and where corporate corruption risks fit into ESG priorities, if at all.

2

The confusing and fragmented status quo

Despite the foundational role of corruption vis-à-vis investor (and global) priorities, corruption appears to be a relatively rare and inconsistent

consideration within investor practices and prominent ESG frameworks.

2.1 Key actors and current practices

It is widely recognized that 2020 was the year ESG matured into a [mainstream investment strategy](#). Although ESG investing was already on the rise, by the end of 2020 institutional investors and rating agencies had notably stepped up their ESG game by embedding ESG policies, metrics, funds, services and surveys into their business models.

It is illustrative of the proliferation of ESG within the investor universe that, as of May 2022, there were [4,946 companies](#) signed on to the voluntary [Principles for Responsible Investment](#), which advocate ESG investing. Signatories include asset owners, investment managers and investment service providers from around 80 different countries

and representing more than [\\$121 trillion](#) in assets under management. While [Europe dominates](#) the ESG investing landscape, the United States, Canada, Australia, New Zealand and Japan have all seen a massive rise in sustainable investing in recent years. At the close of 2020, sustainably invested assets accounted for [35.9% of total assets under management](#) across these regions. Despite the market enthusiasm, however, there is no clear definition of ESG – few institutions or professionals seem to agree on the qualifying or disqualifying criteria, and even fewer agree on the role of anti-corruption within ESG frameworks.

Asset owners

Asset owners are the primary decision-makers when it comes to asset allocation, though many asset owners delegate the management of their investments to investment managers. A variety of actors qualify as asset owners, including individuals, family offices, banks, insurers, pension funds, endowments and sovereign wealth funds. A [December 2020 survey](#) of asset owners around the world, representing a combined \$7 trillion in assets, revealed that

ESG factors are of increasing concern among investors. For example, the survey found that 60% of respondents felt strongly that ESG criteria are important when selecting investment managers and 28% map their portfolios against the UN Sustainable Development Goals (UN SDGs), up from 3% three years earlier. However, the extent to which ESG interest translates into ESG investing remains a little unclear – 84% of survey respondents reported challenges in

obtaining consistent ESG reporting from asset managers and various respondents expressed frustration with fragmented ESG standards and metrics. Notably, the survey report never mentions the issue of corruption risks.

Pension funds, endowments and sovereign wealth funds are among the largest asset owners, as well as some of the most actively engaged in ESG investing. These relatively socially minded asset owners tend to use ESG factors to [guide their investment decisions](#), and have recently grabbed headlines by choosing to [divest from the fossil fuel industry](#). However, Norges Bank Investment Management (NBIM), which manages the assets of the Norwegian Government Pension Fund, alone

Investment managers

Investment managers invest assets on behalf of asset owners. The world's largest investment managers now offer a variety of ESG-focused funds and highlight different strategies for ESG investing, such as negative screening, ESG integration and active stewardship. Investment managers have also begun to emphasize their commitment to the Principles for Responsible Investment, the UN SDGs and the Paris Climate Agreement, among other similar sustainability-oriented initiatives.

However, corporate corruption rarely makes it into the conversation. For example, in 2020, [Blackrock launched its first ever sustainable investment survey](#) in an effort to “make sustainability a key component of [its] investment approach”; however, corruption is never mentioned in the survey report. Similarly, UBS lists [“ten pivotal debates” on sustainable investing in 2021](#) without once mentioning corporate

Investment rating agencies

Investment rating agencies are companies that evaluate and rate corporate and sovereign investees. Ratings have traditionally focused on financial concerns – most prominently, loan default risk. However, like the other actors in the investor universe, rating agencies have begun to embrace the importance of ESG concerns, as well.

Among investment rating agencies, the materiality of corruption risk vis-à-vis [sovereign ratings](#) is broadly accepted, having gained significant traction since the 2008 global financial crisis. However, no similar consensus exists vis-à-

vis corporate ratings. While all major rating agencies have begun to produce ESG scores and sustainability reports, corruption does not seem to be a central or systematic consideration. Further, whereas corruption metrics for sovereign investees are largely based on externally conducted assessments, corporate integrity or corruption-related metrics (to the extent they exist) are overwhelmingly based on self-reporting. Following a [major corruption scandal](#), rating agencies do occasionally downgrade implicated companies; however, there is no indication that post-scandal demotions are systematic.

has set the standard in terms of commitment to [sustainable investing](#) and [anti-corruption specifically](#). Most notably, NBIM has published “expectation documents”, including one on [anti-corruption](#), that communicate the bank's investment priorities. It then actively engages and follows up with investee companies to ensure they are aligned with the bank's investment agenda. Finally, based on recommendations from an independent Council on Ethics, NBIM may choose to divest from companies that fail to uphold the bank's sustainability standards, including those related to [corruption risk](#). Although other asset owners appear to be catching up, NBIM's robust commitment to ESG investing, and to corruption in particular, remains the exception.

corruption. Investment managers have also begun to publicly pressure investees on environmental sustainability and human rights, but they have yet to amplify parallel concerns about anti-corruption.

Recent stewardship [reports](#) and [policies](#) published by the world's top investment managers similarly embrace ESG with little, if any, discussion of corruption risks. “Stewardship” involves purposeful engagement by investment managers with corporate investees towards the goal of ensuring sustainable performance and mitigating risks. Traditionally focused on financial value generation, stewardship has almost uniformly expanded to embrace ESG performance, as well. While stewardship reports and policies dedicate pages and subheadings to climate change, diversity and human rights-related risks, corruption risks are allotted no such coverage.

As illustrated in [The Use of Corruption Indicators in Sovereign Ratings](#) (2017), a report produced by the Inter-American Development Bank (IDB), corruption risks play a more significant and slightly more standardized role within sovereign-investor engagement as compared to corporate-investor engagement. According to the IDB, the major rating agencies already recognize that “corruption is an important indicator for evaluating sovereign creditworthiness”. The report outlines various third-party indices of sovereign corruption risk, each of which consists of multiple indicators aggregated into a single score, and some of which are incorporated into the rating schemes of investment rating agencies.

In a similar vein, in 2018, the International Monetary Fund released a revised Guidance Note on Governance that sets forth a proposed [Framework for Enhanced Fund Engagement](#). The framework

“is designed to promote more systematic, effective, and candid engagement with member countries regarding those governance vulnerabilities, including corruption, that are judged to be macroeconomically critical”. The guidance note outlines a multifaceted approach to assessing the existence and impact of corruption within member states, strategically engaging states (especially those that are particularly corruption-vulnerable) and evaluating existing policies and preventative measures adopted by states.

Although corruption risk could play a larger role in the sovereign-investor context, integrity-related engagement with sovereign investees is steps ahead of that which occurs with corporate investees. It could therefore provide a concrete model for more adequately accounting for corruption risk in the corporate context.

Moreover, despite the gloss of objectivity, corporate ESG ratings are [notoriously inconsistent](#) from one agency to the next. Rating agencies include different metrics, define metrics differently and assign different weights to each metric when aggregating the data into a single ESG score. The divergence and opacity of rating methodologies make longitudinal or cross-corporate comparisons nearly impossible, send mixed messages to companies and leave investors with little guidance on what ESG really means.

As ESG investing gathers steam, a common thread throughout the investor universe is the relative inattention paid to corruption risks. This is not to say that corporate corruption is entirely forgotten – it has [occasionally risen to the top of ESG investing priorities](#). Overwhelmingly, however, the rhetoric, frameworks, policies and products within the investor universe do not seem to reflect the centrality of corporate integrity to environmental, social, governance and financial goals.

2.2 Corruption and ESG disclosure frameworks

The underwhelming attention to corruption risks likely stems from various factors, including the persistent fixation with short-term profit maximization and the inherent difficulties in developing accurate corruption risk indicators. Recent efforts to promote a more holistic and sustainable investing agenda have also contributed to the marginalization of corruption risks. The development of increasingly robust ESG indicators, corporate disclosure frameworks and binding regulation present a prime opportunity to incorporate corruption risks more adequately into investor decision-making processes. However, the inconsistent messaging around corruption to date has done little to bolster the relevance of corruption risks to ESG investing or investing more generally.

The most prominent ESG disclosure frameworks for investors and investees include the following:

1. The [EU Sustainable Finance Disclosure Regulation](#) (SFDR)
2. The Global Reporting Initiative (GRI)'s [Global Standards for Sustainability Reporting](#)

3. The Value Reporting Foundation's [SASB Standards](#)
4. Transparency International's [Transparency in Corporate Reporting](#)
5. PRI's [Principles for Responsible Investment](#)
6. The World Economic Forum's [Toward Common Metrics and Consistent Reporting of Sustainable Value Creation](#)
7. The anticipated standards of the [International Sustainability Standards Board](#) (ISSB)

Some of these frameworks seek to highlight the impact that ESG factors have on traditional metrics of investment performance – that is, environmental, social and corporate governance risks are material only to the extent that they affect financial outcomes. Others value ESG factors due to their impact on people, the planet and markets, apart from or in addition to their impact on corporate financial performance.

2.3 Mixed messaging on corruption

On the one hand, these frameworks concretely contribute to the future of sustainable investing. They increase attention on the importance of ESG risks, provide guidance on incorporating ESG into existing investor decision-making frameworks and distil metrics for previously unmeasurable non-financial factors. On the other hand, they

collectively create confusion around ESG investing and the role of corruption risks in particular. As widely embraced authorities on what it means to “be ESG”, these frameworks run the risk of creating an ESG investing universe with significant blind spots in relation to the issue of corruption.

Inconsistent terminology

Most ESG frameworks divide relevant risks into a small handful of overarching categories. While some use the categories of “environment”, “social” and “governance” (i.e. ESG), others use the categories of “social capital”, “human capital”, “business model and innovation”, “leadership and governance”,

“prosperity” and “economic”. Although the frameworks may share common goals and overlapping indicators, this lack of clarity regarding terminology can cause confusion among those seeking to use and implement the frameworks.

Inconsistent framing

Corruption is inconsistently housed within ESG disclosure frameworks. While most frameworks catalogue corruption risks under “governance”, some categorize it as an “economic” consideration or as an optional indicator distinct from ESG priorities. For example, the EU SFDR prescribes [18 core indicators](#), the integration of which investors are obligated to disclose. These 18 indicators include two that broadly or indirectly relate to corruption risks – violations of, or lack of compliance with, the [UN Global Compact principles](#) and the [OECD Guidelines for Multinational Enterprises](#). However, more obvious corruption risk indicators – including metrics pertaining to anti-corruption and anti-bribery policies, responses to breaches of said policies and convictions for violations of anti-corruption or anti-bribery laws – are left as optional. While corruption risks are arguably captured by both the mandatory and the optional reporting requirements, as both the UN Global Compact and OECD Guidelines for Multinational Enterprises address the issue of

corruption, they are most clearly and concretely categorized as optional. Such inconsistent framing of corruption risks may actively encourage investors, rating agencies and corporate investees to address them as a second-tier consideration.

Relatedly, existing ESG frameworks are collectively unclear as to whether “governance” and its sub-metrics are intended to measure state governance or corporate governance indicators. For example, within its list of optional indicators, the EU SFDR includes a “governance” indicator, defined as “average corruption score”, which applies only to sovereign investees. While there appears to be increasing consensus that the “G” in ESG refers to corporate (rather than state) governance, persistent mixed messaging within some of the most authoritative ESG frameworks perpetuates confusion about what, if anything, investors should be measuring when it comes to corporate corruption risk.

Inconsistent reporting recommendations

Industry-specific ESG reporting frameworks, most notably those put forth by the highly regarded SASB Standards, exclude entire industries from corruption-related reporting recommendations. In fact, according to SASB’s materiality map, only 18 of SASB’s 77 industry categories contain corruption-related reporting recommendations. Among the 59 industries that contain no such recommendations are industries that are closely tied to natural resources and government procurement, such as the utilities and renewable or alternative energy industries, which generally face a high

level of corruption risk. Moreover, no industry is entirely free from the risk of corruption. The present patchwork of recommended red flags may lead companies and investors to mistakenly assume that corruption risks are not universally material.

Further, among industries that SASB flags as corruption-vulnerable, the recommended corruption-related indicators vary from one industry to the next, with various inexplicable inconsistencies. For example, while those in finance are asked to provide a description of whistle-blower protection

policies and procedures, no such indicator exists for those in healthcare. Similarly, those in healthcare are asked to describe their code of ethics, while no such requirement exists for those in finance. Various indicators in the SASB framework are universally applicable and should be universally applied. This includes, but is not limited to the following:

- “Description of codes of ethics”
- “Discussion of process to manage business ethics risk throughout the value chain”
- “Description of policies and practices for the prevention of bribery and corruption, and anti-competitive behavior”

The over-greening of ESG

Finally, the “E” in ESG has come to predominate in ESG frameworks at the expense of other equally important factors, including corruption. Much of the above inconsistency and ambiguity may be a function of the fact that the “G” in ESG is not always a top priority. The ESG wave has grown in conjunction with global momentum on combating climate change. While human rights, or social concerns, have recently begun to grab the attention of regulators and international organizations, there

- “Total amount of monetary losses as a result of legal proceedings associated with corruption, bribery, illicit international trade, or anti-competitive behavior”

There is certainly substantial value in embracing sector-specific reporting guidance, but the present fragmented approach to accounting for corporate integrity and anti-corruption policies, practices and performance could unintentionally create complacency or blind spots within industries that are, in reality, vulnerable to various corruption risks.

is no comparable push behind governance risks. The EU SFDR explicitly acknowledges its heavy emphasis on climate – even adopting a tiered investor rating approach using [shades of green](#). However, because these frameworks are marketed and celebrated as “ESG”, the urgent need to simultaneously develop and mobilize metrics related to “S” and, to a greater extent, “G” is at risk of being neglected.

3

Recommendations for action

As an essential ingredient to achieving the financial and ESG goals of investors and investees alike, corruption risks cannot be an afterthought or fragmented consideration. Within ESG, corporate corruption is both a vertical and horizontal concern – directly measurable as an important factor within the “G”, while simultaneously affecting the “S” and “E”. The growing global consensus around the

significant role companies can play in combating (or, at least, not exacerbating) inequity, human rights violations and climate change will prove futile if corruption is not simultaneously reined in. To this end, various recommendations are outlined below for more adequately and accurately capturing corruption risks within investor decision-making processes and frameworks.

3.1 Prioritize corporate integrity through internal commitments, processes, policies and incentives

As key financial gatekeepers, all actors within the investor universe – including institutional asset owners, investment managers, rating agencies, ESG data providers, regulatory bodies and transnational standard-setting organizations – should prioritize integrity within their own commitments, processes, policies and incentives.

This means that these institutions should themselves embrace a broader definition of good corporate governance, one that builds upon and expands traditional considerations such as corporate structure and board composition to include corporate accountability and transparency at its centre. While imposing ESG standards on investees is important, it is equally essential that those who evaluate, enforce and allocate capital in accordance with these standards embrace ESG themselves.

Institutional integrity is where ESG commitments are put to the test. To ensure that sustainability is substantively, rather than just nominally, promoted by rapidly developing ESG criteria and tools, actors

within the investor universe should embed integrity, transparency and accountability into their own public commitments, decision-making processes, internal incentives, hiring practices, lobbying activities and other areas of corporate governance that shape the culture of an organization. Institutions should also establish monitoring structures to enforce and update policies and practices and to minimize instances of tick-boxing or ESG-washing that might endanger institutional integrity. Further, boards and other leadership bodies should include individuals who are well versed in the field of anti-corruption – people who know the vocabulary, red flags and best practices, and who can “connect the dots” between corruption risks and other intertwined ESG-related risks. In sum, internal priorities should align with the robust ESG commitments that investors increasingly expect from investees.

Integrity should also be prioritized within all investee-facing initiatives. For example, anti-corruption indicators should play a significant role within

investment managers' stewardship efforts, products and services. Rating agencies, ESG data providers and standard-setting bodies should also critically assess whether their ESG metrics meaningfully capture corporate corruption risks and vulnerabilities.

Elevating the calls for, and consequences of, corporate integrity-related ESG factors will better reflect their foundational role within ESG investing and financial sustainability more broadly.

3.2 Effectively embed corruption risks into ESG reporting and rating frameworks

Corruption risks should be embedded into ESG reporting and rating frameworks in a coherent, comprehensive and standardized manner. Corruption also needs to be a consistently applied governance risk across all industries and regions worldwide.

Corporate ESG reporting and rating frameworks play a fundamental role in the creation of ESG portfolios, the distribution of investment capital and

perceptions of a corporation's ESG performance. Consequently, the accuracy of the metrics that underlie rating and disclosure frameworks is crucial to ESG investing delivering on its promise. These considerations are of particular importance as the International Sustainability Standards Board drafts its forthcoming disclosure standards.

Verify disclosures with reliable third-party sources

Corruption risk indicators should, to the greatest extent possible, be externally verifiable. At present, rating agencies and data providers rely almost exclusively on self-reporting by corporations. Self-reporting has traditionally been a pillar of financial rating and regulation and should play a role within ESG rating and regulation, as well. However, when relevant information bears potential legal consequences or stigmatization, as is often the case with corruption-related indicators (as well as

those relating to environmental sustainability and social inequity), rating agencies and data providers would be well served to verify information with reliable stakeholder data sources. Not only will this increase confidence in ESG metrics by establishing whether companies are really "walking the talk", but it will also emphasize the importance of transparency regarding ESG performance.

Expand metrics to include process, implementation and prevention

ESG metrics must also expand to capture the various manifestations of corruption risk more accurately. At present, there exists a range of ESG reporting or disclosure frameworks, each offering its own equation for calculating ESG performance. Most of these frameworks focus on country context, past litigation and the existence of general anti-corruption policies and training programmes. These metrics reflect inputs, short-term outputs and past incidents, rather than process, policy implementation and prevention. To obtain a more holistic and accurate picture of investee corruption risks, rating and disclosure frameworks should include the following indicators:

- Internal incentive structures
- The degree to which corporate leadership understands and promotes corporate integrity
- The degree to which management and employees possess anti-corruption vocabulary

- The degree to which compliance and ethics personnel collaborate
- The role of compliance personnel
- The degree to which corporate integrity is siloed or centred
- The actual implementation of anti-corruption policies
- The extent and quality of corruption due diligence
- The extent and quality of internal enforcement mechanisms
- The degree to which anti-corruption policies apply throughout a company's value chain
- The nature and extent of stakeholder engagement

- The extent to which corruption risks are mapped in connection with other material ESG risks for the company and the sector in which it operates
- The nature, extent and effect of corporate lobbying activity

While this list of additional metrics is not exhaustive, it provides a productive starting point for developing a more comprehensive, representative and forward-looking approach to measuring corruption risk.

Embrace nuance

Accurately capturing corruption risk also requires rating and disclosure frameworks to embrace a nuanced and critical approach to relevant metrics. The implications of a given metric may vary depending on the country context, industry and corporate structure. This means that in addition to asking “what is your anti-corruption policy?” and “what are the responsibilities of your compliance officers?”, rating and disclosure frameworks must

add “why?” Understanding the rationale behind a company’s past decisions and relevant policies will help educate investors and regulators on the particular risks faced by a given company. It will also provide additional data on how intimately the company understands and how seriously it takes those risks. Further, requiring greater detail and introspection from corporate investees may result in more robust corporate anti-corruption initiatives.

BOX 2 Existing guidance on investing with integrity

- The International Corporate Governance Network’s [Guidance on Anti-Corruption Practices](#) (2020) seeks to help investors make better-informed decisions regarding the anti-corruption practices of corporate investees. It highlights key areas for investors to consider when raising the subject of anti-corruption with companies and includes questions to guide investor stewardship.
- The OECD’s [Responsible Business Conduct for Institutional Investors: Key Considerations for Due Diligence under the OECD Guidelines for Multinational Enterprises](#) (2017) aims to help asset owners and managers prevent and address issues related to human/labour rights, the environment and corruption within their investment portfolios. It identifies relevant policies, management systems and essential due diligence activities.

- [Engaging on Anti-Bribery and Corruption](#) (2016), published by the Principles for Responsible Investment and the UN Global Compact, is a guide on company-investor engagement regarding corporate and public corruption. It distils lessons learned from investor initiatives, investor interviews and company feedback into evidence-based recommendations for investors and corporate investees. It also provides corruption-related indicators, information on the different phases of company-investor engagement and various case studies.
- EY’s [Anti-Corruption Considerations for Private Equity Firms](#) (2013) provides investor-focused guidance within the context of the US Foreign Corrupt Practices Act and the UK Bribery Act. It advocates and outlines a multiphased approach to due diligence and risk assessments and provides a list of relevant risk questions.

Standardize core metrics and disclosure requirements across all industries worldwide

The existence of geographic and industry nuance does not mean that rating agencies or standard-setting bodies should deploy ESG criteria selectively. Rather, every company should be subjected to the same core set of standardized metrics and disclosure requirements, regardless of industry or region of operation. The present trend, in which each rating agency and new disclosure framework presents a unique formula for measuring ESG, has resulted in corporate ratings and evaluations that are impossible to compare. Industry-specific disclosure frameworks that recommend a different set of metrics from one industry to the next only complicate things further.

If the goal of ESG ratings and disclosure requirements is to accurately assess and portray corporate performance, divergent approaches to evaluation and the present lack of comparability seriously erode the value of such initiatives. Moreover, to the extent that ESG frameworks aim to guide corporate practices and priorities, adopting a standardized approach to corruption-related metrics and disclosure requirements would more effectively communicate the fact that all companies face corruption risks and should act accordingly.

This is not to say that metric or disclosure variation must cease to exist or that it serves no productive purpose – certain corruption risks, as well as other

ESG risks, do vary from one industry or country to another. Rather, variation should exist alongside and complement a standardized set of core metrics and disclosure requirements to promote comparability and the prioritization of across-the-board ESG risks.

Further, standard should not equate to static. As the nature of core ESG risks or our understanding of those risks evolve so, too, should the corresponding metrics and disclosure requirements.

3.3 Collectively mobilize to place integrity at the heart of ESG

Like climate change and inequity, corporate corruption is a systemic issue that plagues nations worldwide and impedes sustainable development. The ESG agenda and all of its underlying sustainability goals demand corporate attention, resources and transparency, none of which can be assured in the absence of corporate integrity. In order to realize the ESG commitments of asset owners and investment managers and, most importantly, to achieve the sustainable and inclusive future that ESG standards aspire to facilitate, corporate corruption must be more effectively captured within investing frameworks.

To this end, actors within the investor universe should join forces in the fight against corruption. While such initiatives exist in the context of human rights and environmental sustainability, no comparable alliance is focused on the issue of corruption and its mainstreaming within ESG investing. As the saying goes, there is strength in numbers. Collectively mobilizing for corporate integrity would reduce the cost of engagement for each individual actor and simultaneously increase the likelihood of meaningful impact.

BOX 3

Promising practices in the healthcare sector: Norges Bank, Basel Institute and industry leaders develop and deploy anti-corruption indicators

In 2020, Norges Bank Investment Management (NBIM) published a set of recommended metrics for [measuring the effectiveness of anti-corruption programmes](#) within the healthcare sector. The framework contains five themes – (1) culture; (2) risk management; (3) third parties; (4) compliance function; and (5) oversight – and 17 indicators. It was developed in collaboration with eight leading healthcare companies under the guidance of the Basel Institute on Governance.

This initiative provides one promising model for investor-driven, cross-sectoral collective action. The recommended indicators also present a compelling step towards a more nuanced and process-focused approach to anti-corruption

reporting. It asks for qualitative and quantitative responses, clear definitions of corporate structures and procedures, and thorough descriptions of how integrity and compliance fit into a company's DNA. In January 2022, one of the participating healthcare companies, Novartis, released its first [Anti-Bribery Report](#) based upon NBIM's recommended indicators.

Crucially, this type of collective action initiative should not end here. If embraced by a more comprehensive array of industries, investors and anti-corruption organizations, such collaborative models could lead to a more realistic and complete anti-corruption reporting framework.

Investor-driven collective action could help promote broader discussions on the importance of anti-corruption and corporate integrity, build depth and uniformity into existing corruption risk metrics and disclosure recommendations, and propel integrity-centred practices among investors and investees. By working together, asset owners, investment managers, investment rating agencies, ESG data providers and standard-setting institutions could replace the present patchwork of corruption risk metrics with a more coherent and representative framework for assessing and ensuring corporate integrity. Moreover, such an alliance would create a platform for continued dialogue, as well as a format for engaging new voices – including consumers and affected communities – towards systems-level change.

As an initial step, existing industry-shaping fora – such as the International Corporate Governance Network, the International Forum of Sovereign Wealth Funds, the International Platform on Sustainable Finance, UNCTAD's World Investment Forum and the World Economic Forum's Partnering Against Corruption Initiative – can more forcefully take up corporate integrity as an ESG priority. Particularly as ESG investing begins to solidify as a widely offered, regulated and even mandated approach to investing, all actors within the investor universe should ensure that corporate integrity lies at the heart of the ESG revolution.

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