Why corporate boards need sustainability experts

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Demands for corporate sustainability now come from a full range of stakeholders: investors, consumers, supply chain partners, government regulators, and employees. Given the importance of environmental, social, and governance aspects for a company, ***Talal Rafi*** *asks: why aren't all companies making sure to have at least one sustainability expert sitting on its board of directors?*

Sustainability is the number one topic on which investors want to engage the board of directors during shareholder meetings. Investors are the most powerful stakeholders. When they want priority to be given to ESG (environment, social, and governance), should not the corporate board have members who have at least some form of expertise in ESG? Unfortunately, about 70% of board directors in a BCG-INSEAD Survey said their board was ineffective at integrating sustainability into governance and strategy building. Demands for sustainability coming not only from investors, but also from consumers, supply chain partners, government regulators, and employees are increasing year by year. It is only logical to have sustainability experts sitting on the board of directors of a company.

Rising importance of sustainability

A decade ago, a company focusing on sustainability would have a competitive marketing edge, but today it is more than that. It has become imperative for all companies to integrate ESG due to increasing demand by all stakeholders. Younger generations of consumers, especially millennials and Gen Z, are increasingly particular on consuming sustainable products, with 73% of Gen Z consumers saying they are even willing to pay more for them. Gen Z are also particular on working for companies adhering to sustainability: a Deloitte survey shows that 49% of Gen Z had made career choices based on personal ethics.

Many governments have become stricter after the Paris Climate Agreement, with many setting legally binding net zero emissions targets. The EU's taxonomy, for example, will force change in companies operating not only in the EU but also in other countries around the world that have businesses in or trade with the EU. When making investment decisions, 85% of investors in 2020 looked at ESG factors. Sustainability is also about increasing financial returns as companies with an inclusive culture show a 22% increase in productivity and a 27% higher profitability.

Why sustainability experts are essential to corporate boards

Boards lack knowledge on ESG factors – Only 25% of board directors say boards understand ESG risks, which is disturbing when the world is shifting heavily towards sustainability. This year, the board directors of the oil giant Shell were sued for failing to prepare for a net-zero future. With so much on the line, the board needs to have the expertise on ESG. Unfortunately, in an INSEAD survey, only 47% of board directors felt that they have the required ESG expertise and competence to exercise board oversight on execution. Even having an ESG expert at the C-suite as a chief sustainability officer is not enough as ESG requires board-level attention and authority.

Fulfilling stakeholder demand – The calls for ESG have become louder and more proactive, fuelling stakeholder demand. Apple's 2022 shareholder meeting saw Apple giving in to pressure by shareholders to do a civil rights audit. The world's largest asset manager Blackrock backing climate activists to join the ExxonMobil board last year was another clear sign of the need for sustainability as a strategy at the highest decision-making authority in a business, which is the board. The voice for prioritising ESG also comes from supply chain partners, regulators, employees, and consumers. Not having an expert on the board and relying on the C-suite or outside consultants is clearly not enough in an evolving world demanding change on the environmental, social, and governance fronts.

Accountability requirements – Recent regulations by the US Securities and Exchange Commission regarding ESG information shows that there will be a need for aligning financial statements with ESG disclosures. At least one ESG expert at the board will need to be up to date with present and future regulations to oversee management's fulfilment of compliance needs. Also, independent ESG auditors giving assurance is likely to increase with many standards converging under the International Sustainability Standards Board through which companies are looking to guide their policies.

Building strategy around sustainability – Like digital transformation, sustainability is embedded into all parts of an organisation. To stay relevant, the board needs to integrate sustainability into the company's overall strategy. A report shows that 81% of board members prioritise strategic and operational ESG integration. To make long-term investments and strategic partnerships, a strategy is needed. More experts can shift the focus of the board towards integrating ESG into strategic planning and execution.

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Notes:

- *This blog post represents the views of its author(s), not the position of the European Commission, LSE Business Review, or the London School of Economics.*

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