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ESG Initiatives Can Benefit Companies Without Political Fallout

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If you are leading a business in America, it's hard to ignore the political push and pull around environmental, social, and governance practices and investing.

With a divided Congress, there is disagreement in the House over financial emphasis on ESG issues, even as the Senate entertains bills requiring greater disclosure regarding the effects of climate change on a company's business.

State and Federal Efforts

The unofficial kickoff of the 2024 presidential campaign holds the prospect of yet another potential reversal of federal policy around ESG issues.

The Biden administration's signature ESG action—the Securities and Exchange Commission rule on greenhouse gas reporting—remains in gestational limbo, but has potential to reshape the way companies address ESG issues if it survives the inevitable courtroom brawl that awaits.

Meanwhile, states on both sides of the political divide are exploring means to either promote or stifle ESG initiatives. Many of these state initiatives rely on state market power, leveraging the investment of state funds (including pension funds) by requiring, or prohibiting, the reliance on or use of ESG investing criteria.

However, other measures go farther, requiring divestiture of investments in certain industries—oil and gas, firearms—or banning firms that impose such boycotts on ESG grounds.

Some states have even exercised their regulatory power to impose their own requirements for disclosure, as California is poised to require greenhouse gas disclosures and risk assessments beginning in 2026.

Corporate Response

Amid these shifting sands, American companies find it challenging to develop a firm, principled position on ESG issues that advances the company's business and avoids adverse political and market fallout. Should leadership lean in, convinced that a focus on ESG principles is essential to being regarded as a good corporate citizen today?

Should leadership focus only on traditional financial metrics until federal or state laws provide an actionable mandate to prioritize ESG principles? Is there a middle course, and how will the company's customers, shareholders, employees, and other relevant stakeholders judge the path ultimately chosen?

A successful ESG program is authentic, grounded in data, proven through metrics, and aligned with a company's overarching strategy and stakeholder priorities. Each pillar—environmental, social, and governance—must be individually evaluated, and may offer very different risks and opportunities.

Governance initiatives tend to draw the least political fire, but environmental and social initiatives that in the abstract might be derided as "woke capitalism" can be completely appropriate when contextualized with business need.

Workforce and Production

Social initiatives often reflect savvy human resource policies. Today many businesses are struggling to expand (or even to maintain) their workforces. Initiatives like diversity programs can be useful as a means to increase the applicant pool through outreach to underrepresented populations.

Progress in this area is measureable using data on new hires, vacancies, and applications. Equitable supply chain policies can serve to harden fragile supply chains, as well as respond to mandatory legal constraints like those on conflict minerals or Uyghur cotton. When the elements of its ESG program are tethered to business needs, a company can stay true to its business goals and steer clear of the ideological fray.

Environmental initiatives can similarly be tied to business goals, particularly when a holistic view of environmental stewardship is applied, instead of a hyper-narrow focus on climate change and greenhouse gas emissions.

Initiatives designed to cut energy and water usage, to reduce waste and increase recycling, and generally to emit less air and water pollution may all lower both production costs and regulatory and litigation risk.

Often such initiatives also reduce GHG emissions, but may fail to satisfy stakeholders who prioritize climate change over other environmental concerns. This is where the temptation to stray from granular business justifications is highest.

Most US businesses aren't subject to direct GHG regulation or to a meaningful risk of climate change litigation claims by governmental or private actors. That doesn't mean, however, that efforts to reduce GHG emissions don't have strong business justification.

At a minimum, it's reasonable to conclude that constraints on GHG emissions will increase in the future in a way that increases business costs and risk.

Much like companies pay down variable rate debt in anticipation of rising interest rates, it's prudent to plan for reduced exposure to rising GHG costs.

However, before adopting an internal cost of carbon or setting a long-term GHG reduction goal, each company should carefully evaluate both the business and legal environment that will inform how the company tailors its GHG policies and goals to the likely risks it will face in the future.

This analysis distinguishes data-grounded business choices from the sort of ill-considered bandwagon jumping that risks misalignment and greenwashing claims.

Sound Enterprise

Ideally, a company's ESG policies will be designed to contribute to a successful and resilient business enterprise. The process begins with data collection, evaluating current ESG initiatives, communications, the relevant peer landscape, and industry best practices.

Leadership must then identify the best way to align ESG objectives with the business goals of the company, a process that may include a fulsome stakeholder engagement program.

A rigorous review of company policies, practices, and communications should precede rollout to ensure alignment and guard against greenwashing claims. And the program should include some means of measuring progress to identify how successfully the program achieves its objectives, and how to evolve to become a more resilient company.

ESG programs developed in this way focus on creating value for shareholders, employees, and customers alike, and demonstrate investment potential over the long term, whichever way the political winds may blow.

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