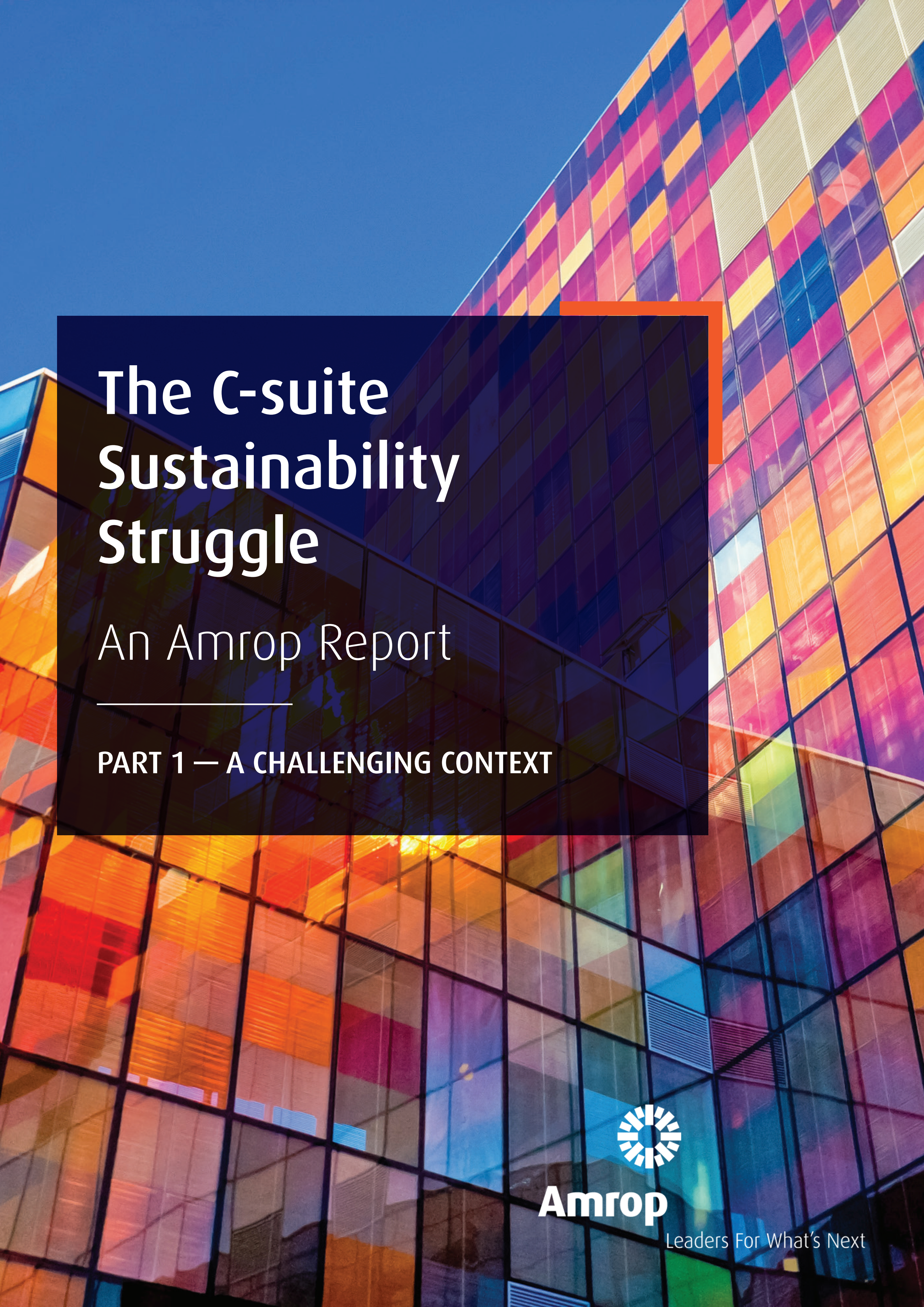


The C-suite Sustainability Struggle

An Amrop Report

PART 1 — A CHALLENGING CONTEXT

Amrop
Leaders For What's Next

The C-suite Sustainability Struggle

Environmental and social responsibility have been a feature of the business landscape for a surprisingly long time. For over a century now, investors have been considering a company's track record in making their decisions.[1]

And yet the place of sustainability on the corporate agenda, how it is addressed, and by whom, is in a state of revolution.

The road to sustainability is still under construction. But how durably is it being built? What forces are shaping it? Is it even headed in the right direction?

In this report we take a hard look at the current context of sustainability in business and why it is such a headache for hard-working organizations.

We open the box on why the ever-expanding function of the Chief Sustainability Officer (CSO) is only a partial answer to these challenges.

We set the scene for Part 2 of our report: the attitudes, behaviors and skills needed for leaders to not only maintain the relevance of sustainability in an organization but to ensure it has the momentum to meet future needs.

The C-suite Sustainability Struggle

Topline messages

There is persistent confusion about the concepts of CSR, ESG and sustainability.

Boards must ensure that stakeholders understand the terminology used in the design, implementation and communication of sustainability endeavors. This clarity also needs to extend to hiring processes surrounding the CSO and related functions.

Sustainability efforts are backfiring and accusations go deeper than greenwashing.

As the authors put it in a recent HBR article, CSOs must "change their focus from public communication and outreach to more direct interactions with key stakeholders and investors."

Compliance is no longer enough — organizations can raise the moral bar.

We invite Boards and CEOs to position their organization on a 4-level moral scale. From legal risk, to legal compliance, through to moral responsibility and ultimately, moral excellence. Where does your company currently stand, and what is its ambition?

Drowning by numbers — ESG reporting has exploded but may get easier.

In a context of inconsistent reporting methodologies and standards, successful Boards and CSOs decide on priority ESG reporting areas, ensure access to accurate and relevant data and secure the manpower needed to synthesize it. This demands a realistic allocation of resources.

Many leaders are still navigating in a fog of dilemmas.

Dilemmas and paradoxes are an integral part of the sustainability landscape. Wise and purposeful leaders are adept at identifying and resolving them. It involves combining seemingly opposite demands in innovative and agile ways, allowing the leader to move beyond the tension and get the best of both worlds. Moving from 'either/or' to 'and/and' thinking

The rise of the CSO is generating as many questions as answers.

Sustainability is wide-ranging, shifting and ambiguous. As the role becomes pivotal, CSOs face fuzzy mandates, crossed reporting lines and multiple demands. For the movement to be sustainable, Boards must set the focus of their organization as best they can. They need to be clear on the ESG targets to prioritize. The mandate and reporting lines for the CSO must align with these.

How Did We Get Here?

Setting a clear starting point

"When we're recruiting sustainability executives, we still see elements of a 'save the world' attitude," says Amrop Partner Pernilla Engwall. "We need to ensure that candidates' motivation and drive are linked to the business, and how it can become more sustainable over time."

'CSR', 'ESG', 'sustainability' — today, they're part of everyday business language. Yet many executives use them interchangeably. The confusion is understandable.

CSR[2] (Corporate Social Responsibility) is a self-regulating business model that aims to position companies as responsible citizens. In its early days, initiatives included recycling, waste reduction, environmentally friendly energy consumption and employee volunteer programs. It was hard to tell where CSR ended and philanthropy began. Measurement remains mainly qualitative, although the ISO 26000 voluntary standard can help companies define social responsibility and achieve it via practical guidelines.

This brings us to ESG and sustainability. Why do we so often mix them up? Bill Zujewski, writing for the Green Business Bureau[3], points out that the Sustainability Framework has three pillars: Environmental (Planet) Social (People) and Economic (Profit). "The letters ESG map almost exactly to the three pillars of sustainability."

ESG was originally designed as a reporting framework for investors to measure and evaluate target companies and this continues to be the case. For companies in line for evaluation by investors and regulators, ESG therefore has an external focus. It is explicit and quantifiable: rating agencies such as Bloomberg assign ESG scores to companies using different sets of criteria.

Sustainability is defined as meeting present needs without compromising future generations. Taking a long-term perspective, it holistically (and more broadly) encompasses responsible and ethical business practices. It has an internal focus and helps companies decide where to invest their own resources.

"ESG which has been historically used to reference an investment rating and framework, is now being used as a shortcut acronym for corporate sustainability," says Zujewski. "When you hear "ESG" being used in a discussion or communication, it might just make sense to get clarity on what the user meant."

IMPLICATION 1

The best Boards ensure that stakeholders understand the terminology used in the design, implementation and communication of sustainability endeavors. This clarity also needs to extend to hiring processes surrounding the CSO and related functions.

The Road to Sustainability

Milestones through the years

2024 — EUROPEAN UNION: EU Corporate Sustainability Directive requires large companies operating in the EU to disclose information about their human and environmental impact.

2020 — EUROPEAN UNION: Introduces the EU Taxonomy for Sustainable Activities to clarify environmentally sustainable investments (vs greenwashing).

2006 — UNITED NATIONS: Introduces the acronym 'ESG' in its Principles for Responsible Investment report, giving birth to the Global Compact.

1994 — JOHN ELKINGTON: Develops a 'Triple Bottom Line' concept with 3 categories of sustainable development: Environmental, Social and Economic.

1984 — R. EDWARD FREEMAN: Signals the importance of considering ALL stakeholders in strategic business management.

1970 — MILTON FRIEDMAN: Landmark declaration in the New York Times that a firm's primary aim is to maximise profits and prioritize shareholder interests.

1953 — HOWARD R. BOWEN: First scrutiny of the relationship between CSR and financial performance.

The current backlash against organizations' sustainability statements goes deeper than accusations of PR laundry.

Counter-revolution

How sustainability efforts are backfiring

Accusations of greenwashing are nothing new. They have haunted organizations' sustainability efforts for decades.

The term dates to 1986 when environmentalist Jay Westerveld called out appeals to hotel guests to allow towels to be re-used for the sake of the environment as a profit-seeking Trojan horse.[4]

Greenwashing now has a sibling: bluewashing. If greenwashing has an environmental focus, bluewashing (its color echoing the UN flag) is more about social and economic responsibility and the way companies may (mis)use the Global Compact to improve their public profile without taking real action.

But the current backlash goes deeper than accusations of PR laundry, whatever the color.

In their article for the Harvard Business Review, Robert G. Eccles and Alison Taylor warn that sustainability endeavors are polarizing people.[5] "A rising political backlash in the United States against investors who incorporate ESG into their decision-making processes has emerged, with some on the right framing this practice as woke capitalism and some on the left as an insufficient response to global challenges."

The trend is echoed by the US Sustainable Investment Forum (US SIF Foundation). In a 2022 report[6] it alerts us to "multiple regulatory proposals put forward as well as accusations of greenwashing and political attacks by some policy makers."

In May it released two proposals to prevent misleading or deceptive fund names and a requirement for more detailed ESG disclosure by funds and advisors — mirroring the EU pattern.

IMPLICATION 2

As the authors of a recent HBR article put it, CSOs must "change their focus from public communication and outreach to more direct interactions with key stakeholders and investors."

Compliance is Not Enough

The moral bar - and why organizations can still raise it

The 2023 Edelman Trust Barometer surveyed 32,000 people across 28 countries. It delivers clear messages for hard-pressed business leaders. Around 50% of people still don't believe that firms are doing enough to combat climate change, economic inequality, energy shortages and healthcare access.

Furthermore, in a world of digitization and rising threats from AI to job security, almost as many (44%) believe that business is under-performing on workforce re-skilling. And when it comes to consumer behavior, 63% buy or advocate for brands based on their beliefs and values, and 68% believe the social fabric would be strengthened by brands that celebrate what brings us together and emphasize our common interest. Such is the power of sustainability.

Organizations are under scrutiny by potential senior hires

Senior executives take sustainability very seriously when they are thinking about a potential employer. A recent Amrop global study[7] surveyed the factors motivating leaders to join one kind of organization and avoid another.

Our findings reveal that senior executives are even more demanding than the general population.

Regarding sustainable behaviors, 91% want an ethically intact player and a serious negative fallout would dissuade 84% from joining. Over 80% seek ethics and purpose from their organization; 94% say it is very important that they are aligned with its ethical values and principles. When it comes to ESG, 74% say this is very important.

Talent has antennae

Senior executives consult multiple channels prior to an interview and many fall outside an organization's direct control. If 96% consult company websites, only 33% seek further data and facts directly from the organization. 74% prefer to talk with current (and ex) employees, and 67% read press coverage. If social media is less widely visited by senior executives, it is still an information source for 40-50%.

When it comes to quitting, a bouquet of reasons contributed to the departure of around 40% of senior executives: neglected learning, a disconnect with their personal mission, vision, values or ethics.

This means that factors related to support, growth, beliefs and values are more common reasons for executives to defect than 'hard' compensation or contracts. Far fewer cite working conditions as a reason to leave, (stability, work/life balance, or where the work gets done). Sustainability is a critical element of an employer value proposition, and not just for the supposedly 'woke' generation.

Advocacy organizations are publicizing shortfalls

Ceres, a nonprofit organization, works with capital market leaders to solve sustainability challenges. It recently published a report[8] examining "How Companies are — and are Not — Leading on US Climate Policy."

They benchmark S&P 100 companies against the expectations set out in the Ceres Blueprint for Responsible Policy Engagement on Climate Change. Published in 2020, the Blueprint outlines tactics for companies to assess their climate-related business risks, systematize decision-making for climate risks, advocate in support of Paris-aligned policy, and engage trade associations.

Not simply complying with ESG frameworks, in other words, but changing the game.

After a dismal picture in the previous year's exercise, 2022 brought significant progress, say Ceres: "Half of the benchmarked companies lobbied in support of at least one Paris-aligned climate policy during the last three years."

Yet almost twice as many (93%) say that climate change represents a material risk to their businesses. In other words, a large proportion of companies are failing to support policies that would protect their own interests. And 29% even lobbied *against* certain Paris-aligned policies in recent years.

This is particularly significant when we consider that over 80% of people want CEOs to take a public stand on the treatment of employees, climate change and discrimination, according to the 2023 Edelman Trust Barometer.

It all leads to a fundamental challenge for hiring organizations. Compliance is not enough.

"Greenwashing" roles using arbitrary sustainability titles won't suffice" Altrata, a data-driven business intelligence organization, confirm. Instead, "understanding where you are in your sustainability journey determines what roles you need."[9]

At what level does a business earn legitimacy?

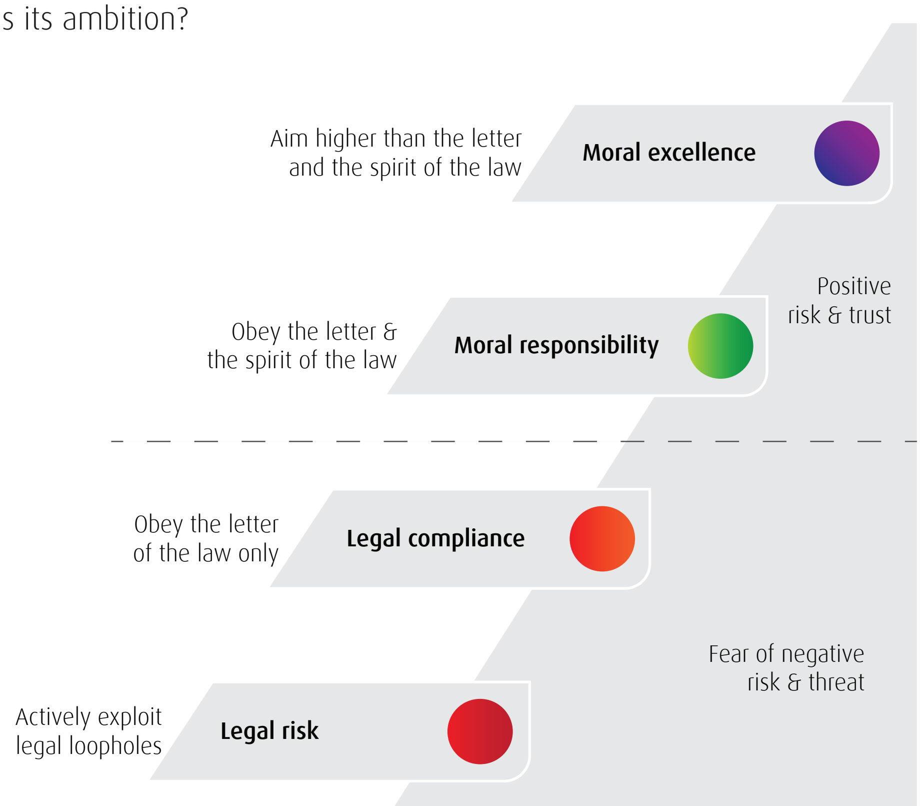
Is it enough for a firm to comply with the letter of the law and practice minimal disclosure, (even exposing itself to legal risk by exploiting loopholes?)

We argue that, below a certain moral line, the operating climate will likely be characterized by a fear of negative risk and threat.

Should businesses rise higher and take moral responsibility? Or should they take a more visionary approach still, aligning KPIs with socio-ethical concerns and values, based on a clearly communicated and facilitated purpose? In this way the operating atmosphere will more likely be one of positive risk-taking and trust.[10]

IMPLICATION 3

We invite Boards and CEOs to position their organization on a 4-level scale of moral excellence. Where does your company currently stand, and what is its ambition?



50%

of people still believe business is underperforming on ESG indicators.

44%

say it is underperforming on workforce re-skilling.

84%

of senior executives would not join an organization that had had a serious reputational fallout.

74%

of senior executives say ESG is a very important joining factor.

93%

S&P 100 companies say climate change is a material risk to their business.

29%

S&P 100 companies lobbied against some Paris-aligned climate policy in the last three years.

Drowning by Numbers

How reporting has exploded (and why it may get easier)

Organizations have a sincere desire to do more and better, and are under pressure to quantifiably demonstrate their progress. But for some, the demands of reporting are becoming overwhelming.

Ben Goodare is Head of Sustainability of Renishaw, a British engineering company. He recently told The Manufacturer Magazine: "Just to comply with our annual report, we collect around 15,000 pieces of data every year. So, being able to monitor that level of granularity and understanding the energy required for manufacturing every single part or component you're making is essential."[11]

Vote of no confidence

A recent Deloitte poll[12] revealed that less than half of professionals (46%) were confident in the ability of their organizations' financial reporting teams to gather and report on ESG financial metrics for regulatory compliance. (Confidence rose to 75% when the organization had an ESG controller). The poll also uncovered the rising involvement of finance functions in reporting — and the case for this. It found that professionals whose organizations' finance teams influenced ESG metrics had more than double the confidence levels (61%) of those whose finance teams did not (27%).

The member of a leading global bank's Group Management Committee recently spoke to Amrop about the bank's reporting on the UNEP FI Principles for Responsible Banking. "To follow all the kinds of ratings, regulatory reporting and whatever it takes, we have an army of people working. As you can imagine, we want to do it. And the different associations want to know what we are doing on ESG — the International Energy Agency, the NGO's, the ECB…"

In a drive to make Europe the first climate-neutral continent by 2050, large companies operating in the EU must from 2024 disclose information about their impact on people and the environment.

The Corporate Sustainability Reporting Directive (CSRD) elevates the existing Non-Financial Reporting Directive (NFRD) with more detailed reporting requirements.

The rules will apply to all large companies (with over 250 employees), listed or not, including non-EU companies making more than €150 million in the EU. Nearly 50,000 companies in the EU are expected to fall under the new scope, (versus 11,000 companies covered by the NFRD).

Business leaders, investors and regulators appreciate the (apparent) rationality of numbers. But not only is reporting an arduous task, reporting standards are still all over the place. Comparing apples with apples is still difficult and getting hold of the data is no easy task.

Even investors are struggling: private equity firms are in the dark regarding their investments and the value creation chains of their portfolio companies, according to a recent Amrop study. Say the authors: "It is vital to implement data driven, corporate ESG controlling systems. Getting access to ESG data processing knowledge will be a difficult but necessary first step."[13]

In its 2022 Report on US Sustainable Investing Trends, the US Sustainable Investment Forum (US SIF) signaled a change in its methodology. "ESG research and integration have become mainstream and are applied across trillions of dollars," they say, "but disclosure on specifics has remained limited across a large portion of those assets." The 2022 upgrade required "more granular information for ESG issues to be included in the tally of sustainable investment assets under management."

As a consequence, 53% of total assets reported by 135 money managers using specific ESG criteria remained uncategorized by investment vehicle type, (such as mutual or private equity fund) due to their inadequate disclosures.

This created a $3 trillion pool of undisclosed ESG vehicles.

Fortunately, a drive is underway to improve and standardize reporting: it is recognized that organizations need help to identify and communicate the ESG domains that matter most for performance. And investors need to directly compare the performance of different companies in the same sector.[14]

The IFRS (International Financial Reporting Standards Foundation) recently created an International Sustainability Standards Board. This, the European Financial Reporting Advisory Group and the U.S. Securities and Exchange Commission are all working towards clarity and coherence.

And the need for clarity and coherence is growing exponentially: when the UN launched its framework to incorporate ESG criteria in the financial evaluations of companies, 63 investment companies composed of asset owners, asset managers and service providers, signed with $6 trillion in assets under management incorporating ESG issues. Today 2500 signatories represent over $80 trillion in assets.[15]

IMPLICATION 4

In a context of inconsistent reporting methodologies and standards, successful Boards and CSOs decide on priority ESG reporting areas, ensure access to accurate and relevant data and secure the manpower needed to synthesize it. This demands a realistic allocation of resources.

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Navigating in the Fog

Why leaders need to move from 'either/or' to 'and/and'

Your consumers are demanding low cost, 'fast' fashion. Your factory, like those of your competitors, is in a location with zero environmental regulation and it is polluting the local river. Should you invest in a cleaning system, even if this slows production and hits the share price?

How well are leaders conducting subtle discussions around tensions such as these? Not very well, according to a 2022 review of 200 sustainability reports. Whilst many contain a 'materiality' matrix to identify critical ESG issues, most fail to distinguish between value creating and ethical concerns. Or between risk reduction measures and strategic opportunities. Especially given the current cost-of-living crisis, and as the effects of global warming become more painfully evident, how can companies keep prices down whilst protecting the planet as well as the human beings serving their supply chains?

Under pressure in an ambiguous and shifting environment, executives understandably fail to see the wood for the trees. They pay the same attention to minor issues as to existential threats — the symptoms of problems, rather than the underlying causes. This results in a "laundry list of ESG issues and inspirational goals" with "little credibility on the specifics of execution."[16]

From smart, to wise and purposeful decision-making

Strategic tensions are defined as asking leaders to do two contradictory things at once. They can be viewed as a dilemma, which may require an 'either/or' choice, or as a trade-off between opposite demands. Breaking through tensions takes pragmatism and realism — paradoxes can't always be resolved. Hard choices must be made and justified.

Wise and purposeful leaders are especially good at transforming 'win-lose' into 'win-win' situations.

Rather than taking an 'either/or' approach to solving tensions, they treat them as paradoxes. Resolving paradoxes is a skill. It involves combining seemingly opposite demands in innovative and agile ways, allowing the leader to move beyond the tension and get the best of both worlds.[17]

In our next article we'll discuss how CSOs and leaders in general need to shift from commercially smart, to wise and purposeful decision-making. We'll see how this can help them resolve tricky paradoxes. But for now, let's stay with the context.

IMPLICATION 5

Dilemmas and paradoxes are an integral part of the sustainability landscape. Wise and purposeful leaders are adept at identifying and resolving them. In our next article we'll dive more deeply into why and how.

A 2022 review of 200 sustainability reports reveals that many organizations fail to see the wood for the trees. They pay the same attention to minor issues as they do to existential threats.

The Rise of the CSO

As many questions as answers

The business case for sustainability is clear and the heat is on. Stakeholders and investors are relentless in their demands for measurable performance. Sustainability is a struggle. Unsurprisingly, CSOs are in hot demand. BoardEx data reveals that 27.2% of S&P 500 companies had a CSO in 2022, rising from 19.1% in 2017.[18] In 2021, more CSOs were hired than in the previous five years combined.[19] Amrop saw a 211% global increase in client demand for sustainability hires between 2019 and 2022.

The trend looks set to continue: "Given the new directives and reporting requirements at play — especially in Europe — we foresee a rise in demand for CFO and finance functions, executives with direct oversight and responsibility for sustainability and ESG initiatives, or adjacent roles with sustainability as a main functional imperative." says Amrop Partner Caroline Søeborg Ahlefeldt.

Inevitably, the scope and weight of the CSO role is changing. Once a lone evangelist, the CSO operated in an isolated and under-resourced silo, overseeing tactical CSR initiatives, and frequently linked to HR or communications departments. Their most visible output was a glossy annual report.

Today, the CSO is more likely a strategic and high priority hub. One that works closely with the board, senior leadership team, customers and investors, hot-wired into corporate strategy and operations. In short, a pivotal role.

Whilst this is a positive development, it brings more difficulties for boards and hiring organizations. Unlike legacy functions such as the CFO, the CMO or the CHRO, the CSO is a relatively recent arrival, and consistent role benchmarks have yet to be developed.

We believe that this inconsistency is a symptom of an underlying problem: the CSO is becoming a panacea, with an impossible task. Why?

Fuzzy mandates, crossed reporting lines and multiple demands

Reporting lines for the CSO depend on the level and focus of the role in the organization. In our experience, and as confirmed by a recent Harvard Business Review article, if the focus is on efficiency, the CSO will likely report to the COO. If compliance, they will report to the legal counsel. If financing and investor relations, (a growing trend, given the demands of reporting) then the boss will be the CFO. If the spotlight is (still) on public relations, s/he'll report to the corporate communications head or CMO.

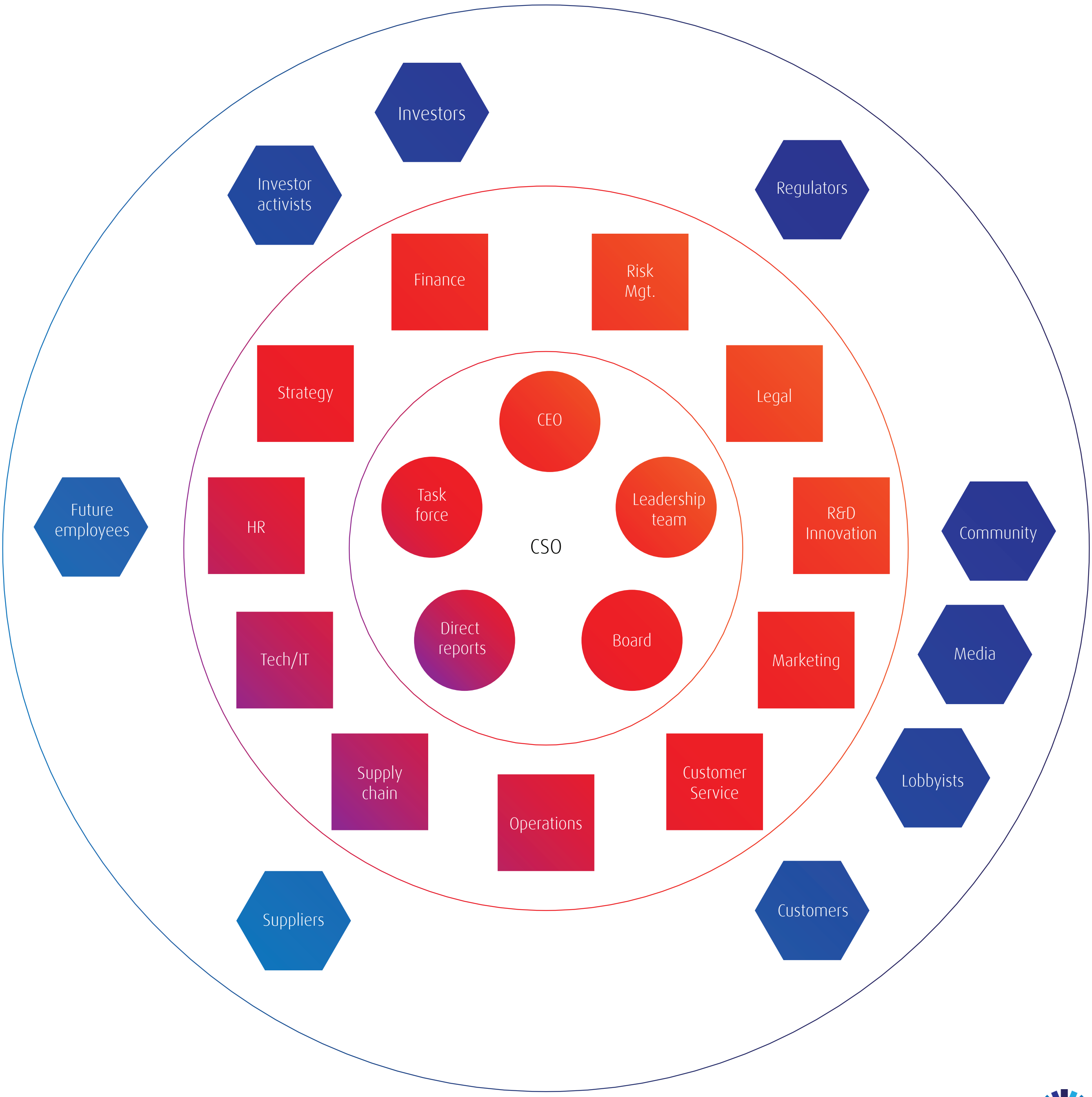
The CSO may even report to *multiple* departments in a confusing matrix: "ESG separation is not uncommon: the "E" of environmental under the COO, the "S" of social under the CHRO, and the "G" of governance under corporate legal." [20]

Only around a third of CSOs report directly to the CEO. [21]

Instead of fighting to be heard, the CSO now faces the opposite battle: juggling the demands of multiple stakeholders. As Olivia Whitlam, Head of Sustainability at Siemens PLC recently told The Manufacturer: "The sustainability team has traditionally been the ones challenging the rest of the company. That's now flipped… to them coming to us and asking what to do…"

Sustainability is wide-ranging, shifting and ambiguous. Given this, Boards need to determine the focus of their organization as best they can. They need to be clear on the ESG targets to prioritize. The mandate and reporting lines for the CSO need to align with these.

An Unsustainable Matrix? The Eclectic Ecosystem of the CSO



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Today's CSOs have a pivotal role. They face the opposite battle to that of their their predecessors: fuzzy mandates, crossed reporting lines and demands from multiple stakeholder groups.

Where Do We Go From Here?

In our next article we'll look more deeply at how the role of the CSO has evolved. We'll argue that beyond technical skills and a single, multi-faceted CSO function, 'sustainable sustainability' needs a rethink.

Not only a review of the CSO role, but transformation throughout boards, the C-suite, senior leadership teams, and organizational culture as a whole.

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About Amrop

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We help our clients find and develop Leaders For What's Next.

Shaping sustainable success is our mission, craft and passion.

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