Regulatory Oversight Podcast: Navigating ESG: The Growing Importance and Compliance Challenges (Part One)
Host: Stephen Piepgrass
Guest Host: Michael Yaghi
Guests: Brooke Hopkins and Rob Sayegh

Stephen Piepgrass:

Welcome to another episode of *Regulatory Oversight*, a podcast that focuses on providing expert perspective on trends that drive regulatory enforcement activity. I'm Stephen Piepgrass, one of the hosts of the podcast and the leader of the firm's Regulatory Investigations Strategy and Enforcement Practice Group. This podcast features insights from members of our practice group, including its nationally ranked State Attorneys General Practice, as well as guest commentary from business leaders, regulatory experts, and current and former government officials. We cover a wide range of topics affecting businesses operating in highly regulated areas.

Before we get started today, I want to remind all of our listeners to visit and subscribe to our blog at RegulatoryOversight.com, so you can stay up to date on developments and changes in the regulatory landscape. Today, my colleague Mike Yaghi sits down with Brooke Hopkins and Rob Sayegh from the global management consulting firm Alvarez and Marsal for a special two-part series to discuss environmental, social and governance - or ESG - standards, strategy and compliance for companies. They will also compare the global expectations of ESG to those for companies in the United States.

Mike, a partner in our practice group, represents high profile clients in regulatory enforcement investigations and litigation, focusing particularly on consumer protection enforcement and regulatory issues. Brooke is a managing director at Alvarez & Marsal with over 25 years of experience in financial advisory and strategic consulting. She specializes in ESG compliance and risk programming, developing innovative solutions for corporate compliance and monitoring across various industries globally.

Rob, who joined us on an earlier episode to discuss State False Claims Acts, is a Senior Director at Alvarez & Marsal. He specializes in financial compliance and investigations, including anti-money laundering and fraud mitigation. I know we're all looking forward to your discussion.

Michael Yaghi:

Well, thank you, Stephen. I appreciate the introduction and I'm excited to be here with Rob and Brooke to talk about ESG; a very hot topic. Environmental, social, and governance. I'm sure our listeners are very familiar with the phrase and understand that it's a hot topic, not just domestically here in the US, but across the globe, including Europe. We're here today to talk a little bit about it and to help companies and businesses understand what some of the requirements are.

We're going to focus on Europe mainly, because there's a lot of good information and requirements coming to industry and we think it's an important topic. Real quick, I just want to talk a little bit at a high level ESG. It's really was coined about 20 years ago in a United Nations report and it was focused on helping financial industry focus on environmental, social, and governance issues when going through asset management, financial analysis, securities, etc. It's really grown over the last two decades and now it's becoming more and more prevalent and basically, companies are going to have to start addressing ESG issues.

The whole concept is a pretty broad banner. You could really go back in time and see that ESG has been around forever. For decades, quite frankly, a lot of employee rights and employee-employer relations and it's sort of, you could argue, is born out of a lot of that. Now it's bringing all of the business issues, not just focused on employees, but it's a broader banner now and it's including environmental issues and sustainability issues. Those are terms we hear about a lot.

How it's being implemented is through a lot of industry and companies trying to bring ESG into their corporate governance, essentially, but that's also complicated in terms of tracking and reporting and what are the standards, so to speak. Governments are also starting to focus on passing laws and requiring and implementing and requiring specific ESG principles. That's where we're going to focus on. Europe has already done that, while the debate rages on in America and there's a lot of opinions. It's an issue that's still going to be here. It's not going away. I mean, it's still up in the air and how it will shake out here domestically, but certainly in Europe, the EU has passed a multitude of regulations to try to bring some uniformity in requirements, in measurements of ESG compliance reporting, so that there's an actual measure, right?

Like I said earlier, we hear things like sustainable practices and what does that even mean, or how do you measure it? How do you know if a company's really implementing and making a difference through their ESG policies? I think I've been rambling on. Brooke, I don't know if you have –

Stephen Piepgrass:

Mike, if I can ask you a quick question?

Michael Yaghi:

Sure.

Stephen Piepgrass:

In going over ESG and with your background and your knowledge of what I think is a well-intended program ESG, why do you think that there's pushback, particularly in the United States on ESG?

Michael Yaghi:

Yeah. That's an excellent question. It's really a political issue. I think both sides, generally, have the best of intentions. But when things become political, they become a little bit more emotionally charged. I think people who challenge it, I don't think are necessarily against the concept of ESG. They just want to make sure that it's something that is being implemented in an effective and sound way, right? For example, we see it a lot in America in investments and whether or not companies are investing shareholder money, or people's money into the right investments. Some government, or some people want to focus on making sure that those investment decisions are focused mostly on profit and not necessarily, for example, ESG issues if they're not going to be the most lucrative investment possible.

I do think on both sides, and the ESG movement is very much focused on environmental issues, climate issues, which all make sense, good corporate governance and sound corporate governance and all those things. If you could just bring this both sides together to focus on, all those things really do drive toward, I think, effective business and profit. In many ways, because it's such an exploding movement, you're not going to get away from it, right? You could almost argue that if you're not investing in companies, for example, that have sound ESG policies, then it's probably not going to be a profitable investment, right? Because there's such a growing movement toward people focused on this.

The downside is, and I think this is where Europe was trying to bring some clarity and some actual – some benefit to the movement, which is, well, how do you measure it? What is it? How do you know a company's at? I mean, companies could throw ESG and environmental and social and governance all over the place in media and in their materials, but how do you know whether they're making a difference? How do you know what they're doing specifically to make a difference, so that investors, shareholders, consumers, for example, if they want to patronize businesses that are focused on ESG, that's their prerogative, but how do you measure it?

I think that's where Europe is trying to say, "Let's bring some clarity to what this is, how can we monitor it? How can we have reporting on it?" We're not there yet in the States, because I think there's still – just the debate rages on. I do think at some point, there's going to be either a uniform law, or states are going to start passing regulations. It's here to stay. We just don't know yet what it's going to look like necessarily. Maybe the European model is just that, a pretty good model. We'll see how it unravels.

Brooke Hopkins:

It forces that to a certain extent. I think you make great points highlighting other stakeholders, too. If we look back, if you recall, 1970 was when the Friedman Doctrine came out. If you recall what that is, the purpose of a company is to drive profits for shareholders. In 1984, there was a business professor, his name was Friedman. The Friedman Doctrine. Then Professor Friedman, who said, "No, no. You create value through stakeholders. Not to shareholders, which might I think."

That's exactly what you were saying. It's investors, consumers, suppliers, others who are part of the business. Well, I think some of you as businesses have recognized that. Again, going back to your point, they're not politicizing it, because their consumers are saying, "This is what we want. We're not going to buy your product if you don't show sustainability." But in a lot of cases, you have to have regulation and that's what Europe has done. They have come out with various regulations, focusing first on the finance community.

They had SFDR, which focused on investments and pretty much everything you're saying. How can you make it measurable? Well, the finance community is all numbers pretty much. You can take those and measure what's the return? Is sustainable funds offering just as good, or better returns? Well, what we've seen is they do and they don't. They waffle back and forth. But what we're not seeing is consistent down with those.

Europe took another step and came up with CSRD. This one arose from a previous regulation, which was the non-financial reporting directive, NFRD. One thing about ESG, it's like the government, you get so many acronyms, it's nauseating. NFRD went to CSRD, corporate sustainability reporting directive. This has been rolled out. Companies large, companies in Europe are required to report, and this covers over 90 different topics across EESNT. Now, most of those companies are going to figure out what's material to them. It's probably less than 90.

Ultimately, that's a lot of reporting. If you think about companies who are present in Europe, but maybe not European-based companies, okay, hello, US, those who have significant subsidiaries in Europe might have to start reporting at certainly as 2027, or by 2029. US companies with a presence in Europe are likely going to be consistently reporting. While the political scene in the US plays pickleball back and forth with ESG, regulations are coming out to say, “If you want to do business in Europe, you need to comply with these requirements.”

Now, one thing I think is important for clarification, there's regulations, there's also frameworks. Lots of companies who have gotten into ESG have complied with frameworks. GRI, a CDP, SASB, TCFD, again, multitude of acronyms for you. What these frameworks do is tell you how to measure different areas of your business for sustainability topics. It could be diversity, it could be labor, it could be supply chain, it could be climate, waste, energy, corporate governance. As we head down, regulations ramping up, impacting European companies, for sure. They are now. But also, US companies, they shouldn't toss away those frameworks, because what you'll see is you can map those frameworks to CSRD, which is fantastic, because that puts you a step ahead, too.

Rob Sayegh:

When you're talking about this and we're talking about US companies and put aside where it's headed in the direction of the US, which I think, Mike is right that in some iteration, it's coming to the US. Current, today, if I'm a US company doing business in Europe, there are 500 employees or more and requires and demands that you comply with CSRD, if you're doing business in Europe. Now, my question is, is it just – well, first off, are employees, does it matter where the employees are? If I have 200 employees in Europe and 9,000 in the US, am I still required? Are there other requirements that the US companies could be drawn into CSRD with?

Brooke Hopkins:

Yeah, potentially.

Rob Sayegh:

Right. When doing business, is it tangently? What is the definition of doing business in Europe if I'm a US company?

Brooke Hopkins:

Yeah, it depends. If you're a listed company in Europe, meaning you have to do reporting within Europe, you're likely going to have to comply with CSRD, if you need the thresholds you mentioned earlier. If you're not, and you're a wholly owned subsidiary in the US or Japan, you might not qualify until later years. It's something you definitely want to make sure to talk to securities counsel, in-house counsel, external counsel, about to make sure you don't make assumptions.

We don't have much business over there. We don't have many employees. Well, guess what? Yes, you do. 500 employees is not that many when you think about some significance of city, or at least for US-based companies. It's a great question, because what you should be doing is flagging this for counsel to take a look at.

Rob Sayegh:

Well, and if US companies ignore this, or they're not reviewing what they need to, and they actually are subjected to CSRD, and they fail to take the proper actions, what potentially can happen in 2027?

Brooke Hopkins:

Fines. I mean, I foresee significant fines coming out of this, for sure.

Rob Sayegh:

And brand issues, I would think, as well, right?

Brooke Hopkins:

Yes, absolutely. It's not just Europe. There's many countries who are working on ESG-focused regulations, some of which that have been rolled out. We know California has rolled out reporting that goes through Scope 3. If you're doing business in California, you're going to have to start reporting if you meet certain thresholds. This isn't, again, a company should be looking at ESG to understand how it increases the overall value of the company. It truly does. This is something that it's not political, nor should it be. Because businesses to operate in modern world have to address things like climate, because the topography where their businesses sit is going to be different in 10, 20, 30 years.

It's different, because we are bringing in different cultures, different ethnicities. We are doing business with third-world countries that you have to be able to bring certain requirements to for labor, appropriate labor, no child labor, not any labor sanctions and general corporate governance, which means the board should be very tuned in to how a company is doing ESG across the business. Because it's going to be up to them to make sure from a governance standpoint that it's being executed not only well, but for the benefit of the company, for the benefit of stakeholders to create that corporate value.

Michael Yaghi:

It's interesting, because there's still a patchwork of state laws, like you mentioned, California, right? Some states have passed pro-ESG regulation, some states have passed anti-ESG regulation. It's still, like I was saying earlier, it's really this evolving landscape in America, but it's very specific and we know what's required in Europe. To Rob's earlier point, if companies aren't focused on that, don't get distracted with the evolving landscape in America. You really need to focus on what is coming down the pike in Europe, what you need to be doing in 2026, and focus on those requirements, to your earlier point, Brooke, to avoid all the penalties and violations and branding issues, etc., that will come from that.

When you were talking about boards should be focused on it, and I think what Rob was alluding to earlier, they should be really not ignoring it elsewhere, but focus on Europe right now, because there are specific requirements that you should be following.

Brooke Hopkins:

It's coming down the pike. CSRD is one. The CS3D, so the due diligence is following closely behind. I'll also mention, UK Modern Slavery Act. In the Queen's last speech, her focus was to strengthen that mandate, which they're doing. It hasn't rolled out yet, but it's forthcoming. This means supply chains will be impacted in the US, absolutely.

Yes, exactly to your point, despite the fact that the SEC climate rule is sitting and has a stay, because the court rule, nope, nope, it's not going anywhere. Europe is busy, and they're watching, and they're going to expect companies to comply, boards to govern that. I think to that point, Rob, you were going to talk to us a bit about what should companies do to prepare for this?

Rob Sayegh:

Yeah. No, absolutely. Thank you, Brooke. I do want to just – one thing to you, Mike, that you mentioned, and I think maybe you can even talk about it before I jump into some action plans, and maybe even some future remedies. It seems to me, where we are in America on this issue, and where Europe is different, is right now, American companies, whether it's culturally, or just more affirmative on it, think they have a choice on ESG, right? Whether you politically agree with it or not, or you don't embrace all of it, I do think the message that I would love to push out through our conversation now, but I would love to hear your thoughts on it is maybe it's a choice right now. But if you have a big global reach in your company, or you're going to be around for the next five to 10 years, it's like, you don't get to decide if you have to stop at a red light, you don't get to decide if you're going to pay your federal taxes or not. I think that we need to impress upon our listeners that this is not going to be ultimately a choice. This is the direction that we as a civilized world are headed to.

Michael Yaghi:

Yeah, I 100% agree. I think that's why I would encourage, in America, I would encourage all stakeholders to be less, I think, adversarial, right? This issue isn't going away. It makes more sense for all stakeholders to figure out what's – and it can be different than what Europe's doing, quite frankly, right? But can you sit at the table and figure out what is the best way forward to address all of the concerns on both sides regarding ESG? How do we implement it? What do we implement? Why is it being implemented? How do we monitor it? Why should it be monitored and how do you report on it? Why it should be reported?

Instead of having it come out of a one-sided political, whether it's anti, or pro, right, all sides should focus on what could we do to address everyone's concerns, let's work together and formulate the right policies and procedures. Because otherwise, I mean, I see this in a multitude of industries and areas. It's not just ESG. When you're a big company with a national and an international presence, but let's just say, national. Let's focus on that for the moment. You don't like to see a patchwork of state laws that conflict with each other. It just makes it harder to do business, right?

You want to have clarity in the law. You want to know what you're supposed to do, what your requirements are, so you are compliant and avoiding penalties, or other fines and fees and run your business. That's what companies are in the business of doing, right? Running their businesses, not fighting over these issues. Yeah, I would definitely encourage stakeholders in both the public and private sector, on all sides to simmer down and try to work together on this.

I do think everyone comes at it with the right, well-intended, but we're not listening to each other. That's the problem. I think if all sides can just sit down and talk through some of these things, I bet they'd find a lot of common ground. That's why I think it's important for our listeners to maybe know like, what could they be doing in Europe, right? We at least have that now, right? While the landscape is still shifting and evolving here, and there's some things you need to do in from one state to the next, what should they be doing to get ready for 2026 in Europe companies? That's what they need to be focused on.

Brooke Hopkins:

Just stay away from the political rhetoric, because I feel like, it's being used as a ploy to scare people, or to say, if you like ESG, you're soft. It's all about being soft, and it doesn't focus on making profit and da-da-da-da-da. Then there's the other side to that, too. That's rhetoric. Just focus on exactly what you're saying. This is how the world is moving. Figure out how it can benefit your business, and also figure out how you impact externally to make sure you're not having to report out that you're dumping waste in the wrong place, or inappropriately. That is what CSRD is focused on doing. There's double materiality, measuring impact, as well as financial. That will help you get there to do exactly what you're saying. The first step is just to understand what are we doing and how do we create value by doing this?

Rob Sayegh:

That's an excellent point, and I look forward to discussing that with you both next time, on the second episode of this two-part series.

Stephen Piepgrass:

Thank you Mike, Brooke, and Rob for your engaging discussion in part one of this special two-part series. I'm sure our listeners, like me, are looking forward to your continued discussion in part two. And thank you to our listeners for tuning in. Remember to subscribe to this podcast on your preferred platform, whether it's Apple Podcasts, Google Play, Stitcher, or any other. We look forward to having you with us for the second episode in the series soon.