Woke-washing — An Emerging ESG Risk?

Compliance and Ethics

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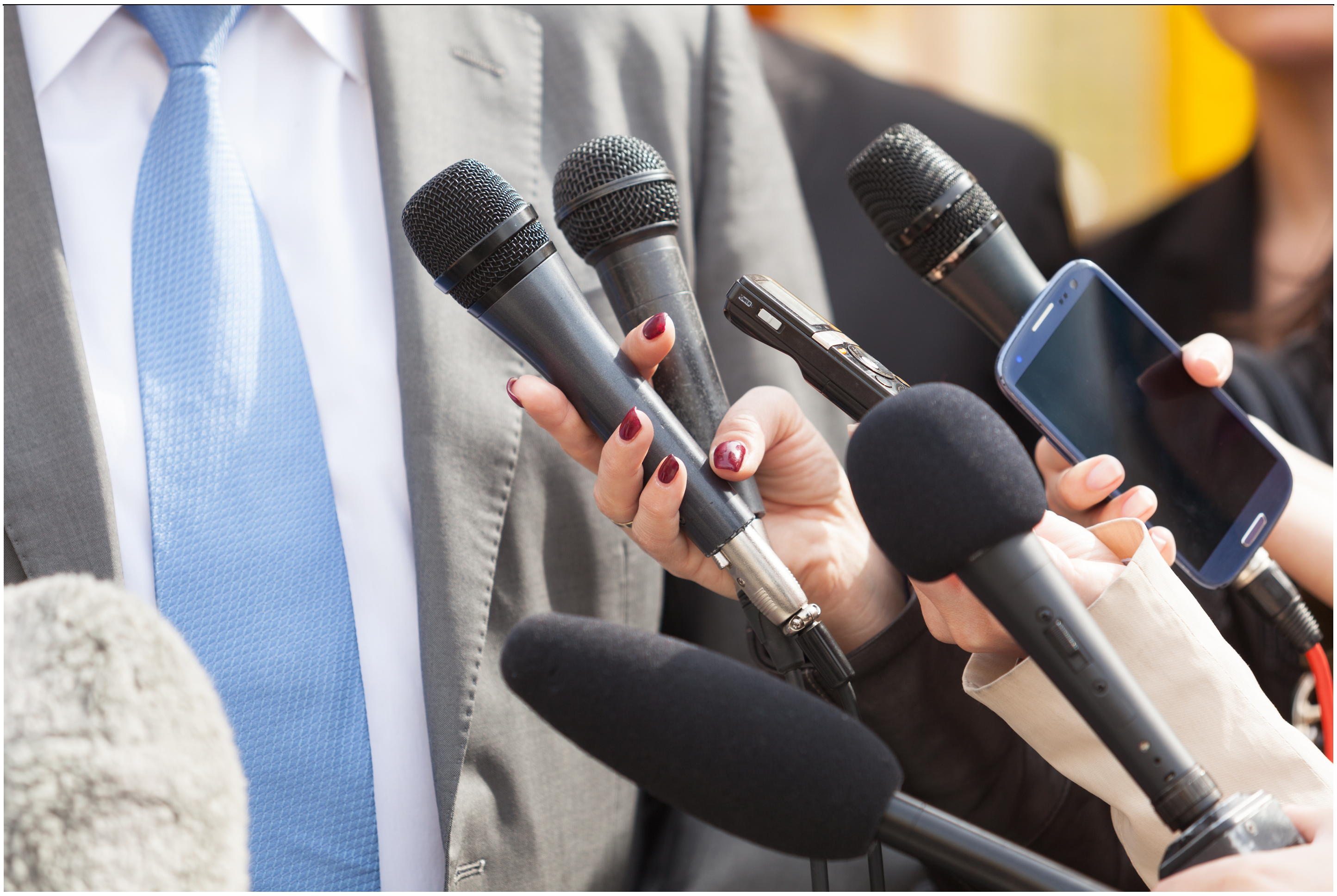
Woke-washing occurs when businesses make public statements about commitments to social issues but take no action, thereby causing substantial environmental, social, and governance (ESG) risk.

Without tangible action and concrete data backing up the public commitments, a genuine desire to do the right thing can evolve into a public relations nightmare. High-profile news stories involving racial diversity, equality, democratic protest, female empowerment, and the rights of low- and no-income individuals show good intentions gone awry.



When public statements don't match actions, companies should expect negative press. wellphoto / *Shutterstock.com*

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Companies also use woke-washing to try to change public opinion and improve their bottom lines. Companies are under pressure by investors and shareholders to show how they are socially conscious and this leads to certain in-house teams trying to come up with slick new ways to differentiate themselves from competitors, without perhaps thinking through all potential ramifications. Take the case of energy companies deploying “climate delay discourse” to make the argument that the move away from carbon-based fuels should be slowed because of a disproportionate impact on the poorest in society — a possibly wise consideration that only tells part of the story.

There are countless examples of companies proudly declaring their ‘passion’ and ‘commitment’ to the highest levels of health and safety and employee wellbeing standards leaving their employees frustrated by the huge discrepancies between those lofty ideals and their own lived experiences working at the company.

Reputational risk also presents legal risks by drawing unwanted attention in the form of regulatory enforcement and consumer class actions for false or misleading advertising, lawsuits from activist shareholders, denial of capital from institutional investors and banks seeking socially responsible investment opportunities, decreased ability to attract and retain talent, and loss of customer loyalty.

The ethical problem of woke-washing

Woke-washing creates two basic ethical problems:

1. **Misrepresentation,** when a business champions solutions to social or environmental problems that the business creates or to which it contributes.

2. **Self-service,** when a business leverages a social or political cause that aligns with the interests of the business.

These ethical problems are not abstract or academic: they are concrete problems with material consequences that every business must consider.

Following an ESG framework

Using ESG as a framework for evaluating business practices has taken hold. Fueled by dire predictions of global warming and increased attention to diversity, equity and inclusion, businesses have turned to ESG to help distinguish themselves for their employees, customers, and other stakeholders. Businesses are increasingly held accountable for not meeting the standards that they themselves set, such as representing adherence to a recognized ESG reporting framework or industry standard.

Adhering to a standard ESG framework helps businesses stay true to their policies. Blue Planet Studio / *Shutterstock.com*

An ideal ESG framework sets out very clear values which strongly and authentically aligns with the very raison d'etre of the company. For example at Nokia, a technology company investing heavily in the future potential of the next steps in the industrial digitisation, at the heart of their ESG policy is the genuinely held belief that 'going green' is a driver of value creation and new revenue streams. They believe there are opportunities in the twin strategies of green and digital and success in reaching climate goals in the world is heavily dependent on digital.

Legal risks

Greenwashing, providing false information, whether or not knowingly, about the soundness of a company's services or products, has become a flagrant practice along with woke-washing.

We have seen high profile examples in the form of enforcement action against DWS and Goldman Sachs and a publicly-traded Brazilian mining company for its misleading environmental claims about the Brumadinho dam.

The growing list of Advertising Standards Agency cases in the United Kingdom shows that the rise of ESG litigation could firmly include woke-washing as a basis for shareholder litigation or other forms of legal action. Similarly, in the United States, the Securities and Exchange Commission, which requires public companies to disclose "material" financial risks, released proposed rules earlier this year governing how public companies disclose material climate-change risks. SEC rules that require public companies to disclose sufficient information, to allow investors to assess the extent to which firms invest in their workforce, are expected. In the EU, the imminent German Supply Chain legislation (in force, January 2023) has been foreshadowed by the EU Council's recent decision (November 2022) to approve the much-anticipated Corporate Sustainability Reporting Directive. This demonstrates a strong direction towards more regulation, accountability and inevitably, to disputes based on shortcomings in relation to these rules and the expectations that emanate from them comings in relation to these rules and the expectations that emanate from them.

For in-house lawyers, PR campaigns around ESG themes are known to be potential high-risk areas purely because of the constantly evolving complex world we live in. It is therefore always a good idea to prepare a 'crisis plan' on how to deal with any potential fallout and line up a crisis committee with the relevant stakeholders in order to respond quickly and effectively to any eventuality.

Tips for avoiding woke-washing

Before taking a stance on a particular social or political issue, make sure not to over promise with ambitious public commitments that are aspirational but impractical.

- **Look within**. Before taking a stance on a particular social or political issue, make sure not to over promise with ambitious public commitments that are aspirational but impractical. Assure the board is fully aligned and willing to commit the financial and human capital resources needed to honor commitments. Otherwise, understate and over perform on cause-linked commitments to minimize woke-washing challenges.

To prevent woke-washing, make sure all board members understand their commitments. Ground Picture / *Shutterstock.com*

- **Seek input.** To help mitigate woke-washing challenges, choose causes that matter not only to the business but also to employees, customers, and other stakeholders by consulting experts, campaign/advocacy groups and people who are directly affected.

- **Examine motives**. A business leveraging a socially relevant cause to distract attention from other business transgressions will be found out — likely first on social media.

Wrongdoings, often broadcast first on social media, can be detrimental to a company's reputation. Rawpixel.com / *Shutterstock.com*

> Many challenges of woke-washing are levelled against businesses that do not understand their human, material, and technical supply chains.

- **Understand the supply chain**. Many challenges of woke-washing are levelled against businesses that do not understand their human, material, and technical supply chains. Mitigate this risk by implementing stronger supply chain auditing and incorporating woke-washing risks into risk management process.

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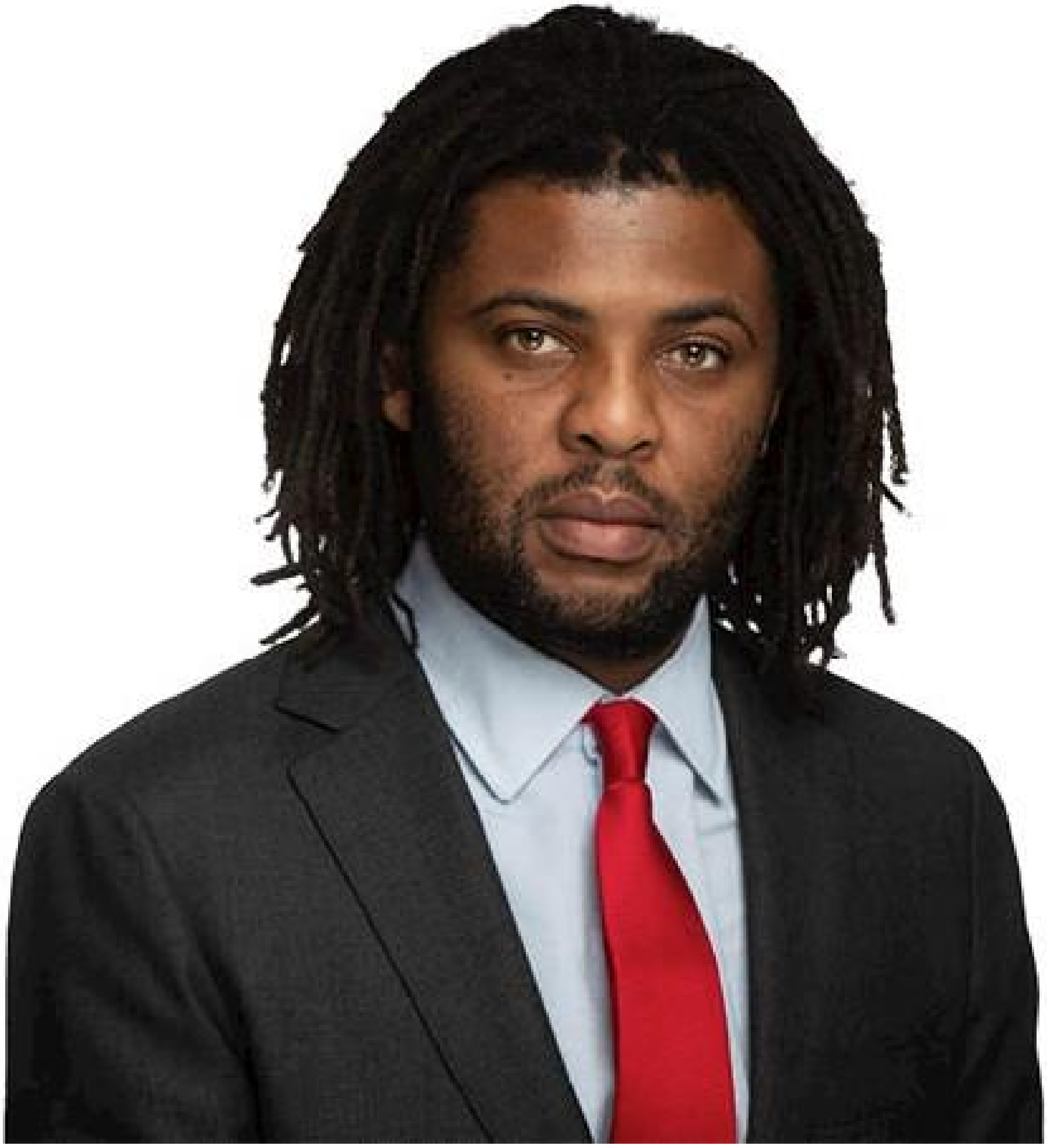

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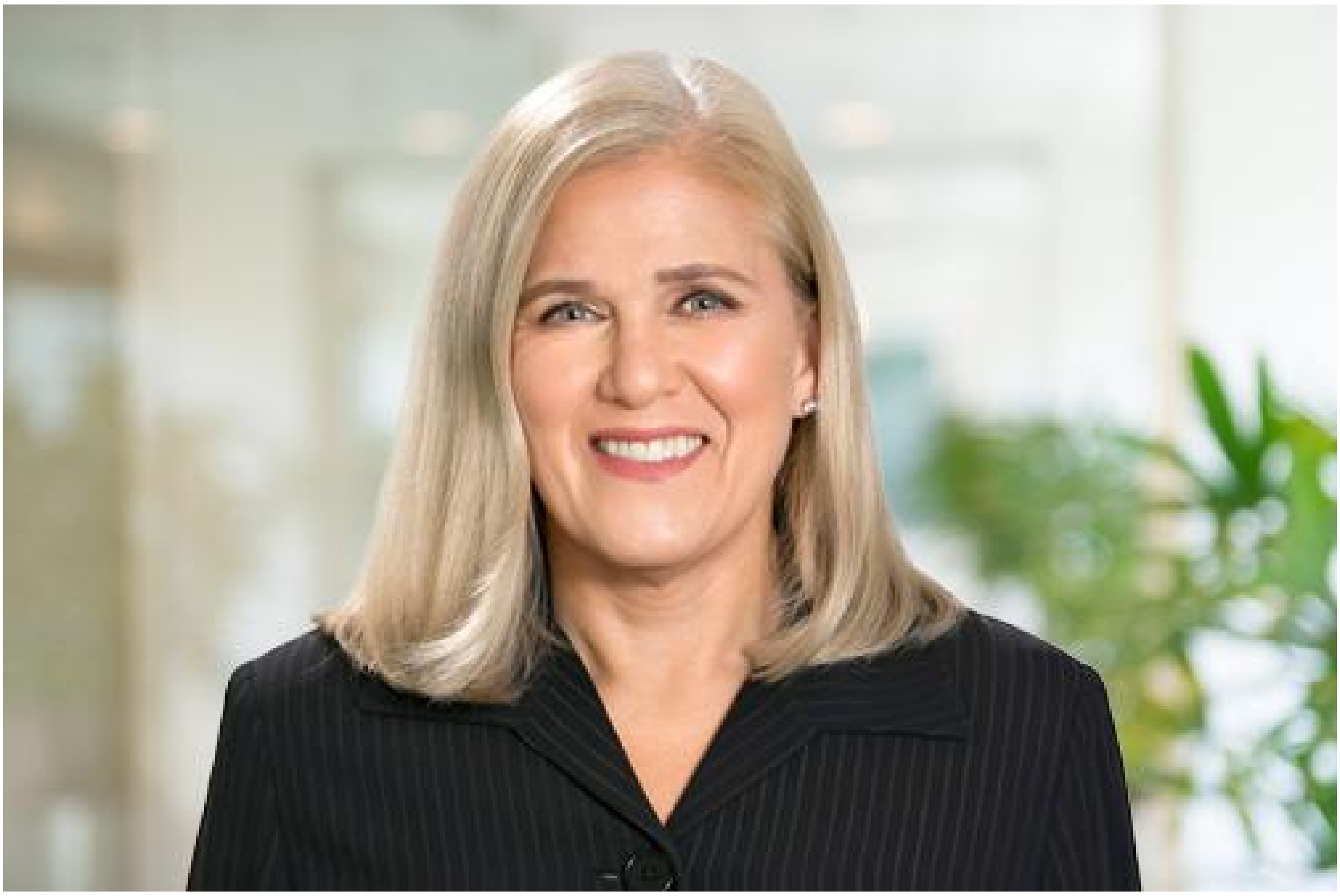

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