EDITORIAL: Can gender equality and auditing be ESG issues?

Dear readers!

We are pleased to share with you the recent issue of the journal Corporate Governance and Organizational Behavior Review.

Recently, there has been a significant shift in research focus on finance in general and corporate governance in particular. As corporations are moving forward from traditional ways to run companies, the business community interests are now increasingly oriented towards emerging issues like environmental, social, and governance (ESG), gender and racial equality, and artificial intelligence (AI).

The ESG framework is used to assess a company’s sustainability and ethical practices. It has been initially used by socially conscious investors to evaluate potential investments. Historically, the first ESG-type index — Domini 400 Social Index — was created by Amy Domini from KLD Research & Analytics in 1990. Yet, the term ESG came into existence in 2004 in a report from leading banks and investment firms for the United Nations (UN Global Compact, 2004). In finance, we can relate to the experience of two renowned finance professors Alex Edmans (London Business School) and George Serafeim (Harvard Business School).

As mentioned by Edmans (2023), “Now is the peak of ESG. It’s front and center in the minds of executives, investors, regulators, business students, and even the public... A total of 4375 investors managing $121 trillion had signed the Principles for Responsible Investment (PRI) by the end of 2021” (p. 3).

Serafeim (2021) wrote the following in the introduction of his papers: “ESG has risen from an obscure and niche concept to a widely used term around the world. When I started working in this area, most (if not all) of my students at Harvard Business School had no idea what ESG meant. Nowadays, they use the term ESG in the classroom taking it as a given that everyone understands what they are referring to. The same experience I have had as a board member, advisor, and investor. ESG has become a common term heard in investment committees, corporate management, and board director meetings. This is a remarkable development for a concept that barely existed a decade ago” (p. 2).

Now that the business community and researchers have adopted the ESG philosophy, the next biggest challenge could be to make sure that ESG scores and metrics capture what they are meant for. Indeed, many studies have pointed out strong disagreement among the leading providers of ESG ratings unlike bond rating (Dimson et al., 2020) or that these ratings diverge (Berg et al., 2022).

There is evidence that the composition of the board influences corporate’s financial performance. Particularly, female directors have a considerable impact on board actions and firm productivity. Female directors have better attendance records than male directors and are more likely to join monitoring committees (Adams & Ferreira, 2009).

One of the most comprehensive studies on this topic called When Women Lead, Firms Win, Sandberg (2019) found that firms with female chief executive officers (CEOs) and chief financial officers (CFOs) have produced superior stock price performance, compared to the market average. In the first 24 months after appointment, female CEOs saw a 20% increase in stock price momentum and female CFOs saw a 6% increase in profitability. Using data on corporate environmental violations, Liu (2018) found that firms with greater board gender diversity are less often sued for environmental infringements.

Audit quality is also gaining more track in this ESG era. Auditing requires accuracy, transparency, and reliability of the information which are needed by agencies for the assessment of a company’s ESG policies. A remarkable study by Del Giudice and Rigamonti (2020) investigates the change in ESG scores after corporate misconduct is
made public. Del Giudice and Rigamonti (2020) have discovered that no significant ESG score adjustment occurs after the scandal becomes public, thus, implying that rating agencies provide an accurate interpretation of the firm’s sustainability. However, their results differed when clustered between audited and unaudited reports. Firms whose reports are audited by third parties did not exhibit significant changes in their scores after a scandal, whereas companies whose reports are not audited, detected a worsening of the ESG scores that are statistically significant. This proves that the reliability of ESG scores can benefit from the auditing of sustainability reporting by third parties. It also acts as an assurance of the quality of the company’s ESG information.

All of these ask the question of whether gender or/and racial metrics, as well as auditing quality, should be included in ESG scores. This has hit research yet but S&P Global (2020) questioned the opportunity to have gender as a clear criterion of ESG score.

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REFERENCES