Unsplash © Calvin Kan

Profiting off panic: new green regulation creates a wild west

Carbon emissions disclosure and ESG reporting is becoming mandatory for all businesses as part of the push for net-zero. Our investigation reveals overcharging and greenwashing at the heart of this new market.

The pressure is on for businesses to be more transparent about their emissions, pay gaps and their ethics. As is to be expected, a new cohort of ESG consultants have arrived on the scene – promising to help them get there. But what if these businesses, which facilitate the measurement and management of ESG (environmental, social and governance) data, were actually standing in the way of long-term sustainability?

Over the past few weeks, *Maddyness* has taken a deep dive into the *ESG reporting* sector, surveying participating businesses and subject-matter experts. We've found that, with competing regulatory standards, frameworks, and advice, the space is a minefield for businesses hoping to do the right thing.

The core issue relates to data. Businesses are collecting the data underlying their final report or score themselves – but they're paying the kind of prices you'd expect them to be paying to have someone do this *for* them. And because they're collecting it themselves, it's often unverified, despite the shiny stamp of approval their chosen provider lends.

An estimate from 2019 suggests that the exclusion of SMEs from ESG led to a data gap in the UK's CO_2 emissions of around 272.88M tonnes CO_2e. And while legislation is starting to address this, it will fail – with data gaps remaining – if unscrupulous or deliberately misleading businesses can greenwash their figures. It will also fail if going green is too expensive for small businesses to manage.

As Duncan Grierson – founder of impact investing app Clim8 Invest, with 20 years experience as an entrepreneur and investor in cleantech – tells me:

"There is sadly a tonne of greenwashing happening, as companies pay expensive consultants to measure their carbon emissions with dodgy methods and then pay for expensive offsets from unreliable sources. There is no single source of truth and charlatans will continue to sell snake oil."

In essence, the sustainability reporting market is operating in a way that is far from sustainable.

Read also

Why do small businesses need to monitor their ESG? We spoke to the experts

The lay of the land

For several years it's been compulsory for large and publicly-listed UK companies to engage in some kind of emissions reporting. As time goes on, these laws are only becoming more stringent and more far-reaching. They are *starting to incorporate* the need to disclose climate change-related risk and how it's being managed, *as well as to address* the social and governance aspects of sustainability. Crucially, no longer relevant only to the big hitters, these laws are now impacting smaller, private businesses.

As we've previously reported, anyone participating in financial markets in the EU is now required, through something called the SFDR, to measure and disclose their ESG scores. Venture capital funds are therefore asking each of the businesses they invest in, even those in the UK, to report back on their ESG – so that they can provide a holistic account of their own footprints. This framework is set to be followed by the SDR, a similar, UK-specific legal framework.

The enshrining of all this in law is a big step. But businesses already know that they can't ignore the question of social and environmental impact. Consumer demand for transparency and progress is mounting. *2021 research* suggests that 97% of mid-market businesses are feeling pressure from stakeholders on environmental and social issues.

As Chris Forbes, founder of bamboo toilet roll business *The Cheeky Panda*, tells me: "It's something that our customers care about. And it's something that we can view as continuous improvement as well." Plus, he says, "We're starting to see a bit of delta between the pricing, in the public markets anyway, between pure-play green businesses and traditional businesses."

In response to all this, The Cheeky Panda recently made a personalised sustainability calculator internally. "People will sell stuff that might sound great, but might have absolutely zero impact," Forbes maintains. "You only really understand what you should be doing as an owner… if you've actually done your own homework, your own analysis of what your business is actually doing."

An emerging and unregulated market

The problem is: measuring *ESG is an arduous and arbitrary task*, especially for small businesses short on time and cash. You need to somehow find and track information relating to everything from waste production and data security, to labour standards and raw material sourcing at all points of the supply chain. Then you need to cross-reference it with a set of standards, and formulate it into a report / score.

You can see the appeal of a third-party service promising to do all this for you – to take this boring but necessary service off your hands. And indeed, the corporate ESG reporting market is *now worth* around $1.6B, and forecasted to increase by 21% a year over the next six years.

Major institutional players, such as the Big Four, have expanded their offering to include SFDR alignment and ESG ratings services. Nascent issues with this were *highlighted* by Jean Eaglesham in the *Wall Street Journal* earlier this year, plus they are unaffordable for SMEs. To plug this gap, numerous software-as-a-service startups have also emerged from the hype.

These platforms' sole objective is to help businesses measure and manage their stats. They're touted as more accessible for small businesses, in terms of usability and price point, with no compromise on the quality of the end result.

However, beneath the promises and energetic green branding, all is not as it seems. Our research reveals two particularly glaring issues with the way this section of the industry is currently operating. They relate to the fact that, in many cases, the bulk of the work is actually being done by startups themselves.

No data collection

Many ‘ESG data providers’ aren’t actually providing data. They are simply pitting it against a framework, which can generally be accessed for free online, and coming out with sleek visual displays. It is up to startup employees to populate a spreadsheet-style platform with raw intel, a process that tends to involve two to four weeks of questionnaires and back-and-forth with suppliers.

Undoubtedly, this service has some value. ESG best practice remains opaque, so there’s a lot to be said for having someone hold your hand through the process. But average costs sit at around £5-10K a year. That’s higher than you’d expect to fairly pay. It’s more akin to what you’d expect if the platform was retrieving data for you.

Maddyness was shown new research by Marc Lepere, an ESG researcher at King’s College London, and the cofounder of *ESGgen*. In the so-called ‘ESG data provider mystery shopping project’, a researcher played the role of a prospective SME customer, booking demos, attending webinars and making enquiries to providers – between December 2021 and February 2022.

This revealed some key offenders. For ‘a suite of software modules that allow you to easily meet your ESG reporting commitments’, IBM-owned Envizi charges a minimum of $30K a year. It doesn’t work with small businesses; the implication being ‘come back when you can afford us’. Atlas Metrics, the self-described ‘single source of truth for your ESG data’, does work with SMEs. Prices start at €8K a year for a spreadsheet-input platform.

Carbon emissions only platforms Normative and BeZero Carbon were also surveyed. Normative’s offering starts at €12K per year – but it has also partnered with Google to launch a free carbon footprint calculator for small businesses, accessible *here*. When we reached out to BeZero Carbon, cofounder Tommy Ricketts said:

‘Our focus is on actual climate transition & corporate change management. Nor really just taxing SMEs. That said, the industry is definitely a free-for-all and there’s plenty of people offering poor services at inflated costs.’

Envizi and Atlas Metrics didn’t respond to our request for comment.

Our own research on data collection and pricing

Building on Lepere's research, *Maddyness* has also surveyed additional providers over the past few weeks, asking whether they measured data themselves or whether clients found and input it, plus inquiring on pricing.

We received notable responses from Novisto, PlanA, SmartHead, Diginex, Kodiak Hub, and Celsia. We didn't hear back from NossaData, Ethixbase, and Sphera.

On the first point, Novisto said '… Our objective is to give full control of the whole process to our customers… Novisto allows companies to collect and track their own non-financial data in a rigorous format with all the necessary controls to ensure high data quality.' On pricing, it was circumspect, stating 'Pricing is discussed on a case by case basis with interested parties.' It's hard to find much on its website.

PlanA's responses were more encouraging. Among other things, its representative said: 'When needed, we support companies in the data mapping process to locate the required data within the existing systems and facilitate their uploading onto our secure platform.' Pricing for its basic platform starts at €1,999 per year.

When, later on, we spoke to PlanA on the value for money question, they maintained that 'carbon accounting affects multiple elements of cost: carbon cost itself (from compensation to official EU carbon pricing: 5-60 EUR /t), time saving on reporting, and of course the team efforts you save on figuring out the technicalities of carbon measurement.'

Although all relying on companies to input their own data, SmartHead and Diginex were also more affordable, sitting closer to the £1,000-a-year starting mark. In SmartHead's case, pricing peaks at €22,680 a year – for enterprises, including an ESG data management tool. Diginex didn't disclose how quickly costs build up. Its CEO Mark Blick told me: 'Our overall goal has been to design a product suited for any company, no matter the budget or experience level.' KodiakHub was again reluctant to disclose pricing.

As for Celsia, founder Petter Reistad told me that clients input data themselves, and prices start at €5K a year, with most clients at €20K a year.

Later on I was told: 'Our solution is 60-70% cheaper and takes 200% less time than a consulting service or if a company decides to implement their own solution. Besides calculating the EU Taxonomy, our platform offers the opportunity to continuously monitor it and adapt accordingly, considering your company’s target score. The data is represented in an easy to understand way.’

ESGgen has released a self-assessment tool – much like what others are charging thousands of pounds for – *for free*. This follows in the footsteps of similar tools and resources made available, also at no cost, by *ESG_VC.*

Data quality – is it assured?

As things stand, businesses are unknowingly doing the work they’ve hired others to do. They’re shelling out, but shouldering much of the productivity hit themselves. But there’s another problem with self-assessment – one that’s a real threat when you think about what all this is actually for: accountability, decarbonisation and better working culture.

If a business, rather than a third-party, is collecting and inputting data itself, it might be inclined to smooth things out a bit. With pressure from customers, investors and governments so high, there’s a temptation to overreport in some areas, and underreport in others. They also might just get stuff wrong.

Many of these ESG platforms don’t have proper protocol when it comes to data assurance. So, however trustworthy their seal of approval might seem to a customer or investor, it’s sometimes built on pretty thin ground.

Daniel Jeczmien, Lepere’s cofounder at ESGgen, is familiar with completing ESG investor questionnaires in previous VC-backed companies. He knows first-hand that data quality is questionable. He says: ‘I assume investors unknowingly aggregate all the questionable ESG data from their portfolio companies, package it nicely into nice infographics, and share it across their LPs and institutional investors – and that’s how the false information propagates. If the data is not assured by professional accountants it’s not worth the paper it’s written on.’

There is a developing conversation around who is best-placed to offer assurance in the world of ESG. Some argue that *because* ‘ESG is not typically based on accounting information but rather on climate science, human capital, and other areas of expertise’, an accountant is not always the best person for the job. Others maintain that chartered accountants are the only people who can audit ESG data with the same level of scrutiny and fairness as we see in financial reporting.

Globally, only half of all companies publishing sustainability information have had it externally assured. And, as a 2021 IFAC report *asserts*, ‘For those that do obtain assurance, it is often being provided by consultants or others, and not by independent professional accountants who possess the unique combination of skills, qualifications, experience, and the professional ethical obligation to act in the public interest.'

When *Maddyness* asked software platforms about how they ensure authenticity, we received a mixed bag of responses. Some offer some form of independent verification, others don't. None were CPA-assured.

Novisto said, 'Companies want to have ownership of their own data collecting, which includes the data verification processes… ESG professionals do not want to wait for a software provider to manually verify their own data as it can cause delays in their process. All data users collect through Novisto is auditable and verifiable to the source.' Saying the data is auditable isn't the same as saying it has actually been assured by a professional.

PlanA said it 'has verification systems embedded in the data collection process'. It also said, 'Our scientific approach, emissions factors and calculations for Corporate Carbon Footprints (CCF) are… third-party certified by TÜV Rheinland, one of the world's leading verification service providers.'

Diginex said verification intensity depends on the needs of specific users. Some authentication tools are built into the platform, such as a blockchain-enabled audit trail, and 'companies that require something more formal' benefit from a global relationship with SGS, 'the world's largest testing, inspection, and certification company to provide cost-effective assurance services that cater for all budgets.'

Celsia and SmartHead said they implement third-party verification where necessary.

Maddyness has heard about one business, which had previously used a well-known carbon-accounting platform, finding out that they had been underreporting their carbon footprint by as much as 40% – after undergoing a more extensive audit. We have also heard about a carbon accounting platform that relied heavily on averages, so as to reduce the input burden on businesses, with businesses ultimately left confused because any changes they made didn't make much of an impact.

As Adam Kramer, CEO of nZero, told Eaglesham in a separate *Wall Street Journal* story, 'There's an underlying belief in boardrooms that there's going to be a scandal about underreporting'.

Read also

Join The Dots: Taking a methodical approach to ESG for your startup

Looking forward

The challenge is to find a solution that's affordable, ideally leading to long-term cost savings for small businesses, but also watertight. And while implementing sustainability reporting laws is an achievement in itself, clarity is urgently needed from the top. So too is assistance.

According to Martin McTague, national chair of the *Federation of Small Businesses* (FSB):

'With the need for urgent action to facilitate the transition to net zero, it is understandable that increasing numbers of investors and corporations are looking at the ESG profiles of those they work with. This push should not, however, be translating into greater costs for small businesses, who are keen to play their part, but often don't have the resources, deep pockets or dedicated specialists enjoyed by large firms.'

'Collaboration is paramount: coordinated efforts from government, big corporations, regulators and small businesses on the ground to facilitate adoption of ESG initiatives is what will take us forward.'

What's for sure is that the ESG reporting landscape is a wild west – with bad actors obscuring genuinely important work, and leaving stakeholders out of pocket but not much more sustainable.

Article by FLORENCE WILDBLOOD