

# ESG fraud and ethical risk

The Environmental, Social and Governance, or 'ESG', landscape is rapidly evolving. Organisations everywhere are under regulatory, customer and investor pressure to adopt ESG-related principles. Such change presents opportunity and new risks of fraud. PwC has combined decades of sustainability and anti-fraud expertise to develop this taxonomy, which can help guide you on your ESG journey.

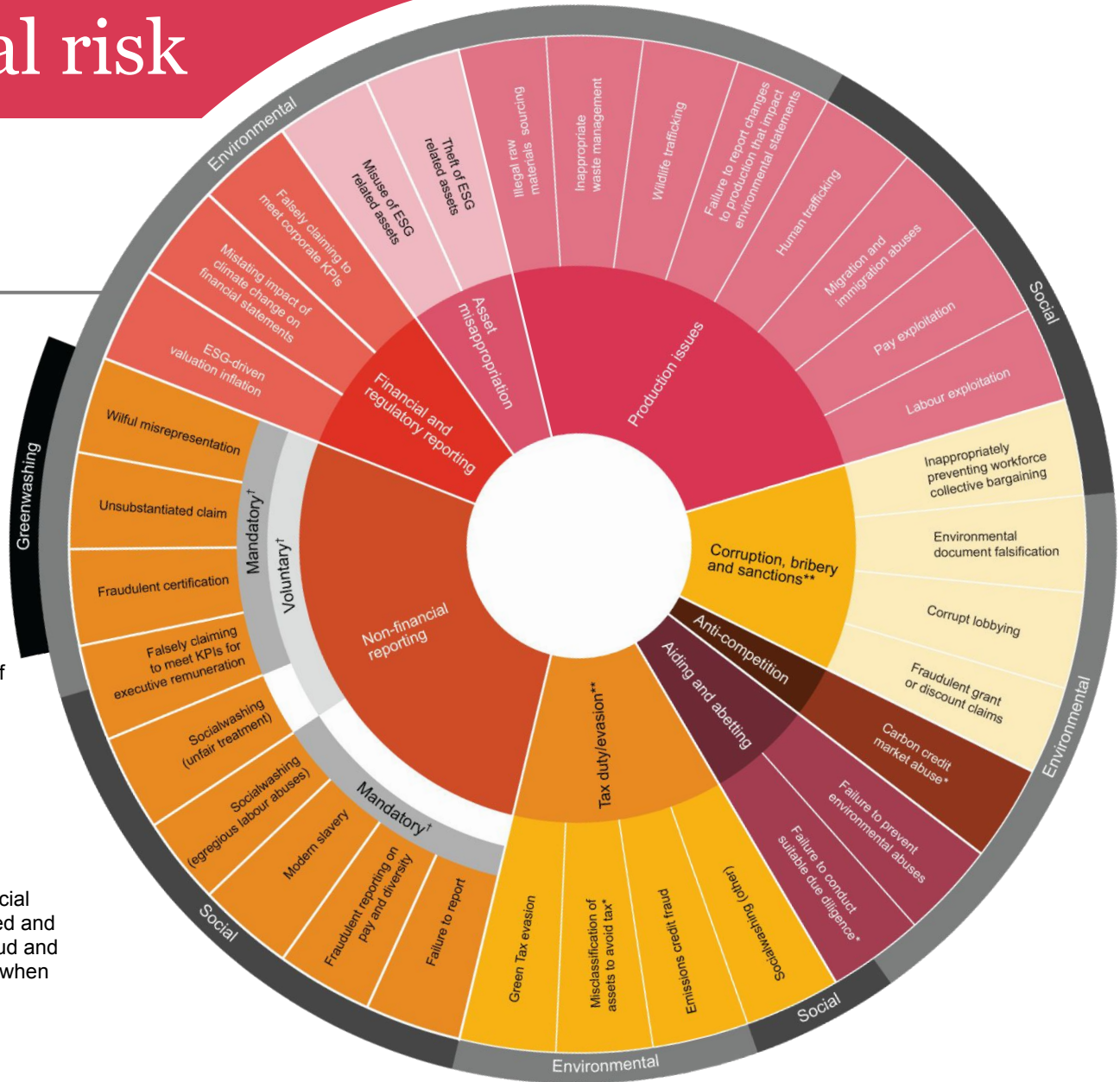
## Exploring greenwashing further

ESG fraud and ethical risk is a broad topic with many diverse components. We believe greenwashing to be one of the most prominent and important, because it is comparatively easy to commit, it is potentially high impact, and it can come in many different forms. The wheel draws out those we feel to be fraudulent; but there are other types of greenwashing which, whilst not necessarily fraudulent, still present reputational risks:

- **Ambiguous:** Generalised, unspecific claims, often 'buzzword' rich, that make validation or refutation difficult
- **Misleading:** Claims that are technically correct and appear positive but are not 'in the spirit' of 'E' or 'S'
- **Narrow focus:** Promoting positive actions whilst ignoring negative impacts elsewhere
- **Best of a bad bunch:** Promoting negative actions as positive by virtue of the fact that the alternatives are worse
- **Softening standards:** Working to reduce or undermine ESG-related standards and certifications, thus 'lowering the bar'
- **The halo effect:** No explicit statements, but using context, imagery and associated marketing to give the impression of 'E' or 'S' benefit

## Governance

The 'G' of ESG, governance, underpins all aspects of environmental and social matters, including when considering ESG fraud and ethical risk. Well founded and robust governance processes are an essential component of preventing fraud and misconduct. Failures of governance are almost always a contributing factor when ESG fraud does occur.



\* Emergent issue. Likely already occurring, but we predict a much greater regulatory and public focus in the next 5-10 years

\*\* In some jurisdictions the ethical risk arises both from internal non-compliance, and from the failure to prevent third parties from behaving inappropriately

† Non-financial reporting is split between mandatory and voluntary, to reflect the current various forms of disclosure

# ESG fraud and ethical risk illustrative examples

Non financial reporting		Financial and regulatory reporting	Asset misappropriation	Production issues	Tax/duty evasion**	Corruption, bribery and sanctions**	Aiding and abetting	Anti-competition
Mandatory†	Voluntary†							
<p><b>Greenwashing (wilful misrepresentation):</b> Intentional under-reporting carbon emissions</p> <p><b>Greenwashing (unsubstantiated claim):</b> Claiming comparably low carbon emissions without appropriate evidence or supporting methodology</p> <p><b>Greenwashing (fraudulent certification):</b> Falsely obtaining a certificate of compliance with pollution management standards by concealing relevant facts</p>	<p><b>Greenwashing (wilful misrepresentation):</b> Promoting knowingly false green credentials for a product or service in order to market it to customers and consumers</p> <p><b>Greenwashing (unsubstantiated claim):</b> Claiming a product is recyclable without the evidence to support the statement</p> <p><b>Greenwashing (fraudulent certification):</b> Continuing to claim to abide by sustainable forestry certification requirements despite knowingly changing to unsustainable sourcing</p>	<p><b>Corporate KPIs:</b> Failure to disclose a climate risk issue that could have a material effect on a key performance indicator</p> <p><b>Mistating impact of climate change on financial statements:</b> Knowingly under-providing for damage caused by extreme wildfires</p> <p><b>Asset valuations:</b> Fraudulently misrepresenting the sustainability benefits of a business in order to inflate its value in a transaction</p>	<p><b>Theft of ESG related assets:</b> Theft of environmental monitoring infrastructure or mobile drone technology</p> <p><b>Misuse of ESG related assets:</b> Using funds ring-fenced for decarbonisation projects for non-ESG related expenditure</p>	<p><b>Failure to report changes to production that impact environmental statements:</b> Failure to relabel free-range eggs as barn eggs after implementing measures to prevent the spread of avian influenza</p> <p><b>Wildlife trafficking:</b> Including in your supply chain the import, export or use of protected wildlife and plantlife</p> <p><b>Waste management:</b> Improper collection, transport, recovery or disposal of chemical byproducts and gaseous emissions</p> <p><b>Illegal raw materials sourcing:</b> IUU (Illegal, Unreported and Unregulated) fishing in the supply chain</p>	<p><b>Green Tax evasion:</b> False declaration of fleet emissions resulting in evaded tax charge on emissions</p> <p><b>Misclassification of assets to avoid tax*:</b> Reporting plant and machinery as a newer (more efficient) model than it is, thereby evading taxes due on older (less efficient) models</p> <p><b>Emissions credit fraud:</b> Knowingly reclaiming VAT paid out on the purchase of inflated carbon credits</p>	<p><b>Fraudulent grant or discount claims:</b> Falsely claiming to have invested in local carbon offsets in order to benefit from local development grants</p> <p><b>Corrupt lobbying:</b> Lobbying the local government to inappropriately grant fishing rights in a marine protected area</p> <p><b>Environmental document falsification:</b> Falsifying forestry and logging permits</p>	<p><b>Failure to prevent environmental abuses:</b> Failure to take the necessary actions to prevent dumping of sewage in rivers and oceans</p> <p><b>Failure to conduct suitable due diligence*:</b> Failure to conduct supply chain environmental due diligence required under incoming EU regulations</p>	<p><b>Carbon credit market abuse*:</b> Colluding to artificially inflate the price of a class of carbon credits</p>
	<p><b>Falsely claiming to meet KPIs for executive remuneration:</b> Where an executive bonus is dependent on achieving an emissions reduction KPI and reporting has been manipulated to achieve the target</p>							
<p><b>Socialwashing (egregious labour abuses):</b> Declaring compliance with the Uyghur Forced Labor Prevention Act, whilst knowingly failing to comply</p> <p><b>Modern slavery:</b> Claiming in a modern slavery statement to conduct suitable due diligence and training without ever carrying it out</p> <p><b>Fraudulent reporting on pay and diversity:</b> Fraudulent reporting in the gender pay gap report</p> <p><b>Failure to report:</b> Failure to disclose reportable health and safety incidents</p>	<p><b>Socialwashing (unfair treatment):</b> Making unsubstantiated claims regarding social mobility achievements</p> <p><b>Falsely claiming to meet KPIs for executive remuneration:</b> Where an executive bonus is dependent on achieving a diversity KPI and reporting has been manipulated to achieve the target</p>	<p><b>Corporate KPIs:</b> Understatement in reporting of community impact risks for a new project material to the company</p>		<p><b>Labour exploitation:</b> Use of forced labour in operations and/or across the supply chain</p> <p><b>Pay exploitation:</b> Withholding of wages of an employee as a form of coercion</p> <p><b>Human trafficking:</b> Using labour that has been illegally trafficked within or across borders</p> <p><b>Migration and immigration abuses:</b> Exploiting migrant labour through inappropriate control of their immigration status</p>	<p><b>Socialwashing (other)*:</b> Falsely claiming to meet employee diversity targets to evade possible future taxes or export finance requirements</p>	<p><b>Inappropriately preventing workforce collective bargaining:</b> Failure to allow workers to unionise in an illegal way or in a way that may indicate forced labour</p>	<p><b>Failure to conduct suitable due diligence:</b> Failure to conduct supply chain human rights due diligence required under legislation such as incoming EU regulations</p>	

Environmental

Environmental (Greenwashing)

Social

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RITM10710056