

## EUROPEAN BUSINESS ETHICS NETWORK

### EBEN 2024 Annual Conference: BUSINESS ETHICS AND ESG

"Not everything that counts can be counted"

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#### 1) ESG is becoming an industry

Numbers play a prominent role in the organisation of modern societies. Analysing numbers or data provides an important basis for making decisions needed to overcome numerous future challenges. ESG can be understood as an attempt to provide management (companies, institutions, authorities) with a concept of sustainability. In principle, it is clear that sustainability is aimed at social development<sup>1</sup> that satisfies the needs of the current generation without risking those of future generations. In individual cases it is not easy to define sustainable corporate governance. The ESG concept though, offers quantifiable metrics in the areas of environment (E), social (S) and governance (G) that institutions can use to review their own development, set targets and adjust their strategy accordingly. Over the past 20 years, the concept has developed into an industry comprising rating agencies, international conferences, labels, laws and regulations.

#### 2) Concentration on the measurable

The "ESG industry" ties in with an ideal of measurability<sup>2</sup> that is also highly effective in other areas of society<sup>3</sup>. The advantages are obvious: institutions or companies become comparable; complexity can be reduced and the ability to act can be increased. With a focus on quantifiable and actionable metrics, ESG is aimed at risk management that seeks to minimise the negative impact of environmental factors on the company (outside in). Conversely, from a social perspective (inside out), any negative effects of the company on society and the environment are also material. The

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<sup>1</sup> The sustainable development goals defined by the United Nations are all based on the fundamental Brundtland Report (Gro Harlem Brundtland: Our Common Future, 1987), but go far beyond this in terms of the level of detail, most recently: Sustainable Development Goals 2015 (<https://sdgs.un.org/goals> (accessed on 6 January 2024)).

<sup>2</sup> A reference to the ideal of measurability (roughly: the reality of this world can be comprehensively and reliably represented with measurements (data, figures, algorithms) insinuates philosophical, sociological, even scientific-theoretical implications, which we cannot address in this article. The "we" mentioned here refers to the empirical background of ethical and sustainable issuer assessment in the sense of applied ethics as it has been carried out for more than 20 years by the Ethics Committee working independently for Arete Ethik Invest AG for investment purposes (<https://arete-ethik.ch/ethisch-investieren/ethik-komitee/> (accessed on 6 January 2024)). This paper reflects the discussion of the aforementioned Ethics Committee, which took place on 17 November 2022 at a client event in Munich with a presentation and panel discussion on the topic of the "ideal of measurability".

<sup>3</sup> In terms of data and figures, there are structural parallels between the topics of "ethics-ESG" and "ethics-artificial intelligence" (see 4. below: Scope of the measurability ideal). The Ethics Committee working for Arete Invest AG has indicated that the ideal of measurability is also giving rise to discussions in areas such as medicine and the regulation of chemicals. For scepticism about the currently highly valued "impact measurement" in the economy for the common good, see Strachwitz, Rupert Graf: Impact-Messung: Geht das? Muss das?, in: Rotary Suisse Liechtenstein 01-24, p. 24-25 - We assume that the high esteem in which the ideal of measurability is held corresponds to a "zeitgeist" that requires appropriate reflection.

regulatory efforts of legislators focus on this second dimension of materiality<sup>4</sup>, but without questioning or supplementing the ideal of measurability. From an ethical or sustainability perspective, the observation of ESG developments raises numerous critical points, three of which are briefly mentioned here:

- It is no coincidence that "E" is at the top of the ESG list. This is certainly due to the urgency of the topic of "climate change", but also to the fact that it is easier to collect data in the ecological area (e.g. carbon emissions, energy or water consumption) and to concentrate on measurable data. It is obviously more difficult to apply the same methodology to the "S". This can also be seen from the fact that the EU has made great progress with their taxonomy covering the ecological dimension<sup>5</sup>, but has only just begun to look at social issues. The fear is ESG will remain heavily focussed on the "E" for many years to come.
- There are various critical points with regard to data quality: Data gives the impression of a secure and reliable basis for decision-making. However, at least for the time being, the ESG performance of a company or an investment portfolio can still diverge to an extent<sup>6</sup> between two research providers, for example, that is not adequately explained by different methods of data analysis. Data collection is much more difficult than widely assumed, not to mention the interpretation of data, which is sometimes subject to accusations of manipulation.
- In the area of sustainable investments, over-motivated marketing has unfortunately too often led to customers being misled about the true sustainability content of the products they buy. Such "greenwashing" has clearly come to light in recent years and the regulator is trying to curb it. On the one hand, the situation shows that data is being manipulated, but on the other hand it also shows that many people tend to believe and rely too much in figures, data and the ideal of measurability.

### 3) Ethics and ESG

The points of criticism mentioned do not speak against figures and data or against "measurability" per se. ESG data management is confronted with considerable methodological difficulties, which are being worked on. This requires time and coordination, especially in an increasingly global environment. ESG data management can be improved and this is happening all the time. Nevertheless, the central ethical problem is to be found in the ideal of measurability itself.

The focus on quantity in the ESG concept (and numerous other areas) goes hand in hand with a methodological narrowing of ethics. Approaches that can be utilised quantitatively (e.g. teleology<sup>7</sup>,

<sup>4</sup> On double materiality, see Vögele, Gesa: Von der Nachhaltigkeit im EU-Aktionsplan Sustainable Finance - Teil II: Doppelte Wesentlichkeit (<https://cric-online.org/info-medien/publikationen/artikel-beitraege?start=6> (accessed on 26 January 2024)).

<sup>5</sup> There are recognisable quantification tendencies in current EU regulations in the area of sustainability of investments. In the case of environmental criteria, a methodological form of regulation based primarily on countability and measurability has already become established. The Taxonomy Regulation ((EU)2020/852) contains detailed criteria for determining whether an economic activity can be categorised as environmentally sustainable. Social criteria are moving in a similar direction, although this has not yet been finalised.

<sup>6</sup> According to a study by ISS ESG 2023 (<https://insights.issgovernance.com/posts/different-views-of-sustainability-alternative-approaches-to-applying-the-eus-disclosure-and-naming-rules-in-practice/> (accessed on 4 February 2024)), the review of sustainable investment funds for their effective contribution to sustainable development can reveal values of between 13% and 84% for identical portfolios. Such large differences can only be partially explained by different calculation approaches. The main reason for the divergence is the different methods used by research providers and the fact that a large proportion of the data is still based on estimates, which are also made on different bases.

<sup>7</sup> Example of teleology: Over the past 20 years, the organisation of Western European gas supply has consistently followed the principles of economic rationality - it has been flawlessly teleological. All organisational measures were subordinated to the one goal (telos: the cheapest possible gas), right down to the maintenance contract for gas storage facilities in their own country (Germany: Gazprom). After the invasion of Ukraine ("Putin's war"), this organisation proved to be "unwise", above all because easily affordable principles such as "diversification" were disregarded. - In retrospect, the question arises, especially from a sustainable perspective, what it costed to correct this problematic organisation. Where are the measurements, data and quantifications? Anyone who places trust in measurability (including

utilitarianism) are absolutised. Virtue ethics, discourse ethics, i.e. decidedly qualitative approaches are left out and the deontological approach<sup>8</sup> is only considered in a corrective context. This raises the question, how far the ideal of measurability can reach. From an ethical perspective, key factors are not taken into account in the ESG concept. Here are two examples of this:

- The defined "G" criteria for corporate governance in the ESG concept (e.g. independence of board members, scepticism towards dual mandates, diversity of board members in terms of skills, age, gender, nationality-ethnicity, etc.) cannot guarantee that a company will be managed wisely. According to ESG criteria, Credit Suisse's corporate governance was quite well positioned until 2023, which could not prevent the company from nearly collapsing and being forced to be taken over by its main rival. Obviously, more is needed than simply fulfilling ESG criteria<sup>9</sup>.
- Diversity has been strongly promoted in organisations and institutions in recent years, which is to be welcomed. A great deal of data is collected on diversity in organisations (e.g. how many ethnicities are represented in the workforce, age-nationality-gender of members of a employee resource group, how many meetings have been held during the year and who attended, etc.). What these figures can do is indicate how the organisation can be optimised. But the figures cannot guarantee that the desired effect will materialise. That indeed is what ultimately matters: Can the promoted diversity actually make the desired multi-perspectivity strategically, structurally and culturally fruitful? This can't be measured. Not everything that counts is measurable; above all, it is difficult to measure what really counts. How far does the ideal of measurability go?

#### 4) Scope of the measurability ideal

The quote attributed to Albert Einstein, with which the scope of the ideal of measurability can be approximated quite well, reads in full: "Not everything that counts can be counted, and not everything that can be counted counts"<sup>10</sup>. It is true that some things are measured that are not very relevant. However, the ideal of measurability would undoubtedly be underestimated if it were to be reduced to such limited relevance. On the other hand, "measurability" is certainly overestimated (and proves to be an "ideal") where everything that is not measurable is dismissed as irrational or irrelevant. Factors that are difficult or almost impossible to measure, such as corporate culture, charisma, intuition<sup>11</sup>, imagination, human individuality and intentionality, seem irrelevant from the perspective of measurability, but are in fact co-decisive or highly relevant.

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us) would also like to see quantification of unpleasant facts. If these figures were available, smart (sustainable) organisation could possibly prove to be more cost-effective than purely teleological organisation.

<sup>8</sup> ESG certainly addresses everything that is prescribed by law and codified in standards (legality), as well as issues (legitimacy) that are considered problematic in relevant social circles. Norm-based research is the keyword here.

<sup>9</sup> In the end, it was liquidity problems that led to the demise of Credit Suisse. However, the deeper reason for this lay in cultural problems (risk culture), which appointed representatives (Colm Kelleher, Board Chairman of UBS AG) described as a "rotten culture" ("We are not a monster bank", Bilanz No. 1/2024, pp. 68-70, p. 70).

<sup>10</sup> Not verifiable in the writings of Albert Einstein. For evidence of the quote, see: <https://quoteinvestigator.com/2010/05/26/everything-counts-einstein/> (accessed on 2 January 2024).

<sup>11</sup> Where "intuition" is understood to mean an insight into contexts, which is linked to a quick decision that is based not only on rational deduction, but rather on subconscious perception - there are good examples, cf. fn. 14 below.

A more concise assessment of the scope of the measurability ideal is a matter for philosophy, sociology or the theory of science. From a practical perspective, it is reasonable to assume that the strength of the measurability ideal (reducing complexity and increasing the ability to act) is also its weakness. Perception of the complex natural and social environment and decision-making cannot be reduced to data, figures and quantification.

What we have seen in recent years in the field of ESG is structurally similar in the current debate on artificial intelligence. A mindset consistently focussed on numbers, data and algorithms ("computational mindset") cannot harness crucial human resources and inevitably leads to a reduction of ethics to utilitarian or teleological argumentation patterns (despite recognition of the benefits of artificial intelligence in numerous applied areas with high practical relevance) as methodological reductionism, particularly with regard to ethical decision-making<sup>12</sup>.

Meeting the challenges of life in a constantly changing world depends on people who look closely, think for themselves and use their thinking wisely. People can not only "measure", they can also "capture"<sup>13</sup>, "describe", "tell"<sup>14</sup> or "represent". These and other human activities contain resources that together allow management to use a smart leadership approach for sustainable development.

## 5) Smart, sustainable leadership

Even in periods of good weather, leadership means "navigating" in a highly complex environment characterised by numerous uncertainty factors. Management will not want to do without reliable and well-interpreted data - in this sense, ESG remains an indispensable basis for decision-making. However, it pays attention as well to unavailable factors that are difficult or impossible to measure and concentrate on what really counts. It is a major challenge to make aspects that are difficult to measure quantitatively fruitful in qualitative terms.

This has long been the case in well-managed companies and organisations<sup>15</sup>. In addition to these desirable approaches, resources that are still lying fallow should be utilised much more systematically than has been the case to date. It is about combining or integrating different backgrounds of experience. The promotion of multi-perspectivity should be understood as a systematic approach that enables diverse resources to be brought together.

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<sup>12</sup> Cf. Heumann, M. (forthcoming): Maintaining an integrative ethical approach in the business practice of investment ethics. The irreducibility of ethical decision-making to computation and AI. In: C. H. Hoffmann (ed.), Artificial Intelligence, entrepreneurship and risk management: Reflections and positions at the crossroads between philosophy and management [Futures of Technology, Science and Society]. Springer.

<sup>13</sup> As recently as 30-40 years ago, there were attempts not to "measure" corporate culture, but to "capture" it (e.g. E. Rühl: Ein methodischer Ansatz zur Erfassung und Gestaltung von Unternehmenskulturen ([https://link.springer.com/chapter/10.1007/978-3-662-00804-1\\_9](https://link.springer.com/chapter/10.1007/978-3-662-00804-1_9) (accessed on 3 February 2024)). To our knowledge, no such attempts have been made recently. Although the importance of the topic of corporate culture itself is undisputed - there is a whole field lying fallow (subject to better knowledge) that could be cultivated (researched) again with profit.

<sup>14</sup> Clint Eastwood is known as a highly observant contemporary. When he produced the film "Sully" (2016), he was primarily concerned with a topic that is of central interest here: the combination of data management and intuition. The film "tells" the story of flight UA 1549, in which pilot Sullenberger (Sully; about to retire; a lifetime of flight data) was forced to make an intuitive decision to "land" on the Hudson River within seconds of approaching New York with the engines failing. Sully's hero status resulting from the successful splashdown is honourable: we (like Clint Eastwood) are primarily concerned with the question of how people can activate resources to free themselves from emergency situations.

<sup>15</sup> Meaningful stakeholder dialogues, surveys of customers and employees, findings from employee resource groups or granting employees a high degree of freedom to promote creativity can be understood as systematic approaches for sounding out qualitative contributions to smart corporate management.

By observing procedural rules, such sometimes divergent backgrounds of experience, cultural influences, diverse contexts and also ethical approaches that have been left aside can be integrated into decision-making processes<sup>16</sup>. This cannot be achieved with measurable ESG criteria alone. Sustainable development at every level must strive for a more consistent integration of quality and quantity, the measurable and the unmeasurable, hard facts and soft factors, method and intuition. The quantitatively measurable must be supplemented by qualitative approaches in order to get closer to the actual complexity of the environment.

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<sup>16</sup> The Ethics Committee active at Arete Ethik Invest AG for the PRIME VALUES Funds always uses ESG data from external providers, but maintains a proprietary assessment methodology for the evaluation of issuers. Multi-perspectivity is realised through the interdisciplinary composition (business administration, medicine, toxicology, engineering, social ethics) of the members as well as through an ethical discourse process regulated in the rules of procedure and meeting rules. In 2024, three of the seven members are women; all members come from German-speaking countries in Western Europe; however, some members have broad development policy experience (Asia, Africa, South America).