Redefining consumer trust

ESG integrity threats in the product lifecycle

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01 Introduction

The Indian consumer market is experiencing remarkable growth and the market size is projected to soar to an impressive USD 6 trillion by 2030[1], positioning India as a pivotal player in the global consumer landscape. This surge is fueled by a burgeoning middle class, digital transformation, and evolving consumer preferences. Environmental, Social, and Governance ("ESG") considerations have also become essential for organisations to gain consumer trust. Health and safety have become priority and consumers want to deal with ethical organisations.

The "ESG" regulatory landscape is becoming more stringent, with the regulators increasing the disclosures and reporting of "ESG" metrics, such as:

Securities and Exchange Board of India ("SEBI") mandated the top 1,000 listed companies to disclose "ESG" performance under Business Responsibility and Sustainability Reporting ("BRSR") and 'BRSR core', which is aligned with global sustainability reporting standards

The Companies Act, 2013 requires organisations to report details pertaining to conservation of energy as part of the Board of Directors report

The Reserve Bank of India ("RBI") has included green projects in priority sector lending and notified the "framework for acceptance of green deposits"

SEBI has also introduced the "ESG" Rating Provider ("ERP") and the ESG Investing framework

The below laws and regulations are also related to the "ESG" domain:

- Prevention of Corruption Act, 1988
- Environment (Protection) Act, 1986
- Minimum Wages Act, 1948
- Food Safety and Standards Act, 2006
- Drugs and Magic Remedies (Objectionable Advertisement) Act, 1954
- Bureau of Indian Standards
- Companies Act, 2013
- Securities and Exchange Board of India Regulations, 2015
- Consumer Protection Act, 2019
- Advertising Council of India Code
- Cable Television Networks (Regulation) Act, 1995
- E-commerce Rules, 2020.

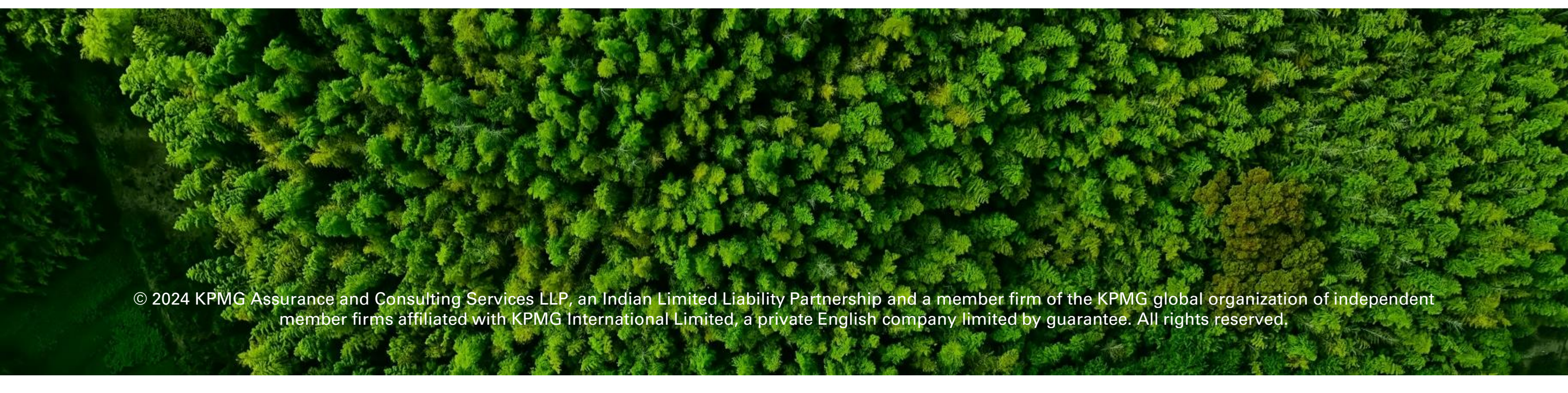
Non-compliance of "ESG" regulations may result in significant penalties and reputational loss due to the heightened expectations for corporate responsibility on environment and social equity. For instance, the SEC imposed USD 68 million in civil penalties for "ESG" issues in FY2023[2]. Similarly, enforcement by Indian regulators is also expected to become stricter as the "ESG" environment matures in India. Recent high-profile cases regarding misleading advertisements being discussed in the Supreme Court of India have underscored the importance of upholding integrity by organisations in the consumer markets sector. The landscape is further complicated by the rise of social media influencers, who pose significant questions on product safety, manufacturing practices, waste disposal, among others. "ESG" integrity risks could severely impact organisations in the consumer markets sector throughout the product lifecycle - covering product development, procurement, manufacturing, marketing, sales and distribution, among others. Organisations need to be proactive in effectively mitigating the "ESG" risks to ensure long term sustainability and enhance financial performance.

1. India poised to become third-largest consumer market: WEF, Retail News, ET Retail, January 2019
2. SEC.gov | SEC Announces Enforcement Results for Fiscal Year 2023, U.S Securities and exchange commission,November 2023

02 Typical "ESG" integrity risks in a product lifecycle

Product lifecycle stages	"ESG" integrity risks	Illustrative examples
Product development	• Overstate or falsely claim product durability, energy efficiency or environmental benefits • Inadequate safety testing or quality assurance processes • Compromise product safety features for higher profitability	A cartel of manufacturers purposefully reduce the lifespan of lighting products
Product certification	• Counterfeit or unauthorised use of certification labels/trademarks • Payment of bribes to inspectors from certification bodies/agencies • Lack of transparency by withholding data or information during compliance reviews • Potential product misrepresentation by using substitute samples for testing • Concealing negative or failed certification results	Use of fake energy efficiency certification labels on electronic appliances to mislead consumers, resulting in hefty fines
Procurement of materials/ services and incurring capital expenditure	• Unethical sourcing of minerals and materials from exploitative sources • Anti-competitive practices like bid-rigging, price-fixing or collusion with suppliers • Misrepresentation of country-of-origin labels or quality parameters of raw materials • Unethical labour practices by exploiting migrant, temporary or underage workers	Artisanal mining of cobalt used in electric vehicles, leading to safety hazards for workers
Manufacturing	• Data integrity issues by tampering with or misreporting emissions, waste or effluent levels • Improper handling and management of hazardous materials and waste • Compromising worker safety due to lack of proper equipment and training • Unethical labour practices of excessive working hours or underpayment of wages • Use of banned or sub-standard raw materials or manufacturing equipment • Falsification of inspections, maintenance records or regulatory compliance data	Lack of adequate safety equipment and training at factories, leading to accidents and injuries, attracting negative media attention and regulatory scrutiny
Packaging and distribution	• Misrepresenting recyclable content or biodegradability of packaging materials • Data integrity issues around transportation, logistics and carbon footprint data • Unethical practices like smuggling or trafficking counterfeit goods • Customs violations through mislabelling, undervaluation to evade duties/fees	False claims of using 100% recyclable packaging, whereas the actual recycling rate was substantially lower, leading to legal action

Product lifecycle stages	"ESG" integrity risks	Illustrative examples
Marketing and advertising	• Deceptive, unsubstantiated or misleading marketing claims about products • Lack of transparency around sponsored content or paid endorsements • Failure to disclose material product risks, limitations or information • Data integrity issues like falsifying testimonials, reviews and performance data • Unethical practices like illegal telemarketing, spamming and privacy violations	A consumer products brand fined by court for misleading advertisements
Product utility	• Providing misleading usage instructions or omitting critical information • Inadequate hazard labeling for chemical, electrical or health risks • Potential product misrepresentation by selling uncertified/counterfeit products • Making unsubstantiated energy, emissions or environmental impact claims • Unethical practices aimed at premature product failure or planned obsolescence	Software updates reduced the processing speed of mobile phones, leading to accusations of planned obsolescence
Destruction of damaged/ expired products	• Illegal dumping or improper disposal of hazardous waste and e-waste • Misrepresenting materials as recycled, whereas actually dumping such materials as waste • Circumventing extended producer responsibility disposal fees and costs • Tampering of packaging to recycle damaged/expired products as good quality products by manipulation of product labels	An electronics manufacturer illegally dumped e-waste in developing countries, facing reputational damage
Reporting and disclosure requirements	• Misrepresenting or window-dressing "ESG" metrics or achievement of parameters • Lack of transparency by failing to disclose "ESG" related violations or incidents • Inadequate internal controls over "ESG" data collection and reporting • Obstructing/withholding information or falsifying evidence • Unethical influence like bribing assurance providers and verifiers	Falsification of carbon data reporting by multiple organisations, leading to regulatory action



03 How can organisations mitigate "ESG" integrity risks?

Organisations should plan to mitigate the "ESG" integrity risks in their existing risk management framework. It is essential to have a dedicated "ESG" risk oversight structure to ensure adequate "ESG" compliance and remediation measures for "ESG" related incidents. Following measures could be considered by organisations for adopting a holistic approach to "ESG" integrity risk management:

Risk management framework - design a comprehensive risk management framework and strengthen processes relevant to maintaining "ESG" data integrity, "ESG" reporting metrics and "ESG" related compliances.

Third-party due diligence - include "ESG" parameters as part of due diligence and background checks conducted for employees and third-parties associated with the organisations.

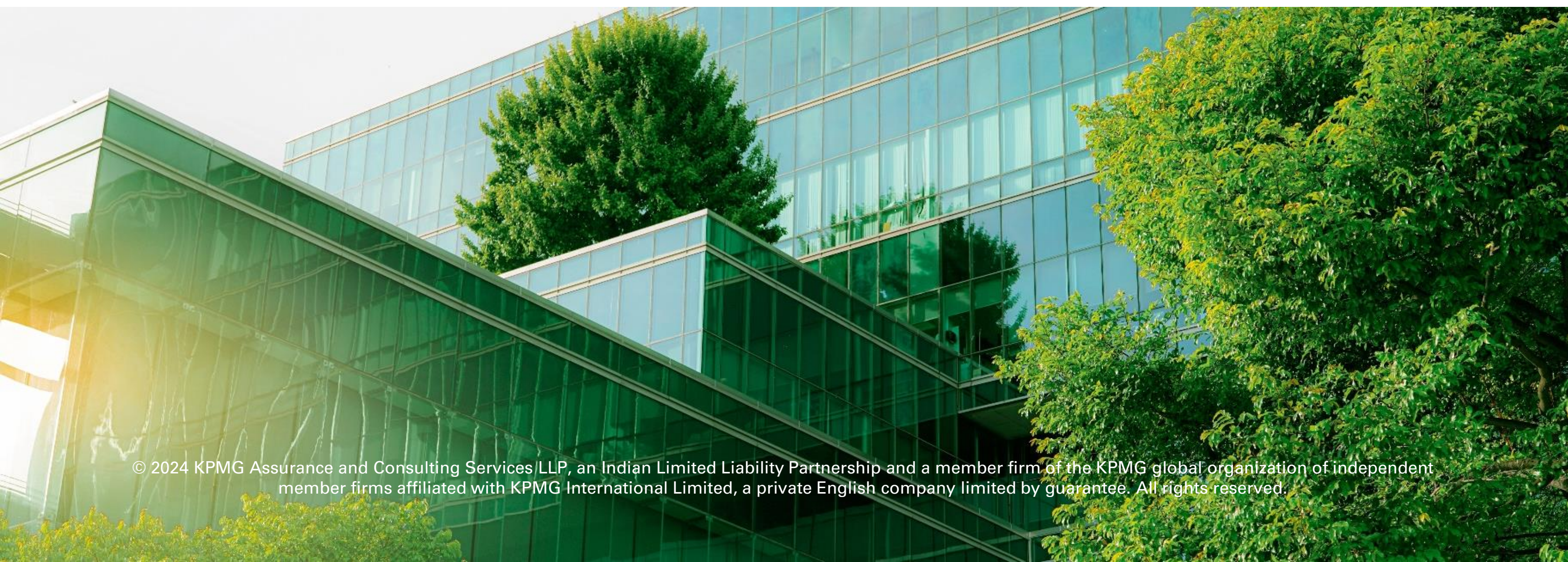
Early warning signal mechanism - develop a tech-based early warning signal mechanism and conduct periodic proactive reviews to detect any red flags indicating "ESG" related non-compliances or breaches.

Training and awareness - provide trainings and conduct awareness workshops for employees and third parties associated with the organisation to make them aware of the applicable "ESG" regulations and repercussions of non-compliance.

Root-cause investigations - conduct investigations of "ESG" related allegations, such as greenwashing, reporting manipulation, regulatory breaches, misuse of grant funding, general ethics/compliance violations and whistleblower complaints.

While the "ESG" landscape is still evolving in India and across the globe, multiple organisations have implemented best practices for responsible sourcing, which set clear requirements for third parties associated with them on various parameters such as traceability, labour practices, and environmental impacts. Innovative approaches such as blockchain technology are being explored to enhance supply chain traceability and integrity and to track food products from farm to store, improving food safety and transparency.

With the "ESG" regulations becoming progressively stringent, organisations must implement robust "ESG" governance framework, strengthen supply chain traceability and foster a culture of transparency and accountability throughout the product lifecycle. The advent of social media has led to consumers exercising greater scrutiny while taking purchasing decisions, with a preference towards "ESG" oriented organisations. Hence, a stronger focus towards "ESG" compliance would ensure long-term profitability, enhance consumer trust and sustainability for organisations.



KPMG in India contacts:

Akhilesh Tuteja
Partner and Head - Clients and Markets
E: atuteja@kpmg.com

Manoj Kumar Vijai
Partner and Head - Risk Advisory
Office Managing Partner – Mumbai
E: mkumar@kpmg.com

Namrata Rana
Partner and National Head of ESG
E: namratarana@kpmg.com

Nikhil Sethi
Partner and National Head - Consumer Goods
E: nikhilsethi1@kpmg.com

Suveer Khanna
Partner and Head - Forensic Services
E: skhanna@kpmg.com

Mustafa Surka
Partner - Forensic Services
Risk Advisory - Consumer Markets and Retail Leader
E: mustafasurka@kpmg.com

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