SEC Settles with DIMA for ESG Infractions

Insights for Compliance and Risk

Part 2: 5 Things Deutsche Bank Did Right

The SEC ("Commission") announced a settlement with DIMA (DWA Investment Management Americas, Inc., a Deutsche Bank subsidiary),, on September 25, 2023 regarding several aspects of ESG and investments, and their marketing[1]. The settlement included a penalty of $19 million and a requirement to implement suitable controls. The Order describes several aspects of programs that were poorly designed and/or implemented, and problems arising from misalignment of external communications and internal practices. More on that in Part 3.

Douglas Hileman Consulting LLC (DHC) suggests that a careful read of the Order reveals several things that DIMA did right. These serve as the "bones" of a compliance and risk program. Let's look closely and see how these efforts can provide a good start for any organization, regardless of sector.

1. **DIMA recognized that ESG issues can pose material risk to all investments**. This is separate and apart from the ESG dedicated, actively-managed funds – "impact funds". DIMA saw the need to develop and apply a standard, consistent methodology to evaluate these risks in a broad range of investment analysis and decisions.

   Takeaway: ESG has confused companies ("preparers" for those public companies preparing SEC filings), users (investors and other stakeholders) alike for decades. Impact investing, such as investors excluding stocks involving gaming or tobacco, led the way in early years. The market capitalization of major companies has trended from tangibles to intangibles over time, with intangible value now comprising the majority of market cap value. An array of ESG topics pose risk and opportunity. Some ESG issue(s) are material to every company – but which issues to which companies? Over a decade ago, SASB[2] set out to reduce the confusion by identifying the material ESG issues for each industry sector, and developing disclosure topics for each.

[1] SEC press release found at https://www.sec.gov/news/press-release/2023-194; the SEC order at https://www.sec.gov/files/litigation/admin/2023/ia-6432.pdf

[2] The Sustainability Accounting Standards Board (SASB) was founded in 2011. SASB has merged with other organizations and is now a part of the International Sustainability Standards Board. See https://www.ifrs.org/groups/international-sustainability-standards-board/.

2. **DIMA began with one centralized approach**. The approach – the ESG Integration Policy and the ESG Engine – were to be used across the entire company. The intent of this approach was to ensure consistency across all investments where ESG was considered as a risk.

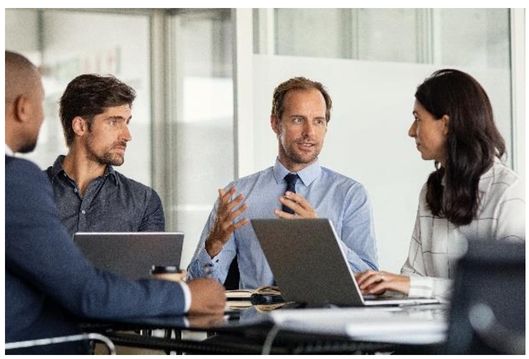
Takeaway: DIMA recognized that there should be one standard, organization-wide approach to identifying and evaluating ESG risk. DIMA created the ESG Integration Policy – not regional policies. DIMA created one ESG Engine, to be available worldwide. DIMA did not defer to regions, sector specialists, or investment managers to develop criteria or methodologies for themselves. At least, none were mentioned in the SEC settlement. While DIMA's initial intent was laudable, the flaws were in design and implementation consistent across the organizations, and consistent with messaging to the public and key stakeholders.

3. **DIMA had governance structures to enable internal discovery of this issue.** DIMA had a hotline. DIMA staff identified lack of execution on the Policy and raised the issue to superiors. What's more, they took actions.

Takeaway: Sarbanes-Oxley requires all publicly-traded companies to implement a confidential, anonymous way for whistleblowers to inform the company of questionable accounting practices. Internal hotlines can also be used to enable employees, business partners or stakeholders to report known or suspected instances of waste, misconduct or other abuse. Thoughtful, competent assessment of tips can be useful to direct appropriate resources to further evaluate and resolve potential problems.

4. **Internal Teams identified problems and took actions – twice**. The Order describes how responsible teams did an initial analysis. When subsequent actions were not enough, they launched an additional, more comprehensive review.

Takeaways: Responsible groups should be empowered to self-assess, including where they suspect efforts are not in alignment with company policies, procedures and requirements. The second effort sounds more comprehensive, and designed to present a more compelling case to management of the need to comply and for additional effort.



5. **DIMA cooperated with the SEC**. DIMA provided detailed factual summaries. SEC indicated this as a consideration when describing penalty and remedial measures.

Takeaway: The SEC announced two settlements with DIMA on the same day. The penalty for ESG settlement is $19 million. The penalty for a settlement for anti-money laundering (AML) infractions was $6 million. Consider the extent of effort financial institutions invest in AML, and the relative extent of investment in ESG risk management. The penalty for ESG was more than three times the amount that was imposed for AML. Even so, the penalty was likely reduced because of DIMA's cooperation with the SEC. With apologies to all readers involved in real estate investments, a key to [relative] success in dealing with the SEC is: cooperation, cooperation, cooperation.

About Douglas Hileman Consulting LLC

Douglas Hileman helps clients with Sustainability compliance, risk, programs, reporting and disclosures and audits. He is an author of COSO's supplemental guidance "Achieving Effective Internal Control over Sustainability reporting (ICSR)", which has taken the accounting and audit community by storm. He is the only non-CPA and only ESG specialist on the author team. He has over four decades of experience in operations, corporate, management consulting, Big 4 firm experience (including during early Sarbanes-Oxley years), and with his consultancy. He was on the Volkswagen Monitor Team for three years, as the senior environmental management/ auditing specialist, working on behalf of the DOJ. He is in demand for training, workshops, and presentations at conferences. One distinction is his ability to bridge the gap between traditional financial reporting professionals (Accounting, Internal Audit, Finance) and functions responsible for much of the Sustainability data and information (Environmental, HR, IT, Operations, Procurement, Real Estate, etc.). More at www.douglashileman.com.