ESG REPORTING: REGULATORY PROGRESS AND FUTURE IMPERATIVES

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Abstract

*The concept of sustainable business practices has evolved globally through the emergence of the Environmental, Social, and Governance (“**ESG**”) criteria aimed to benefit the institutions, those investing in such institutions, and society. The essay focuses on the evolution of the ESG from Corporate Social Responsibility (“**CSR**”) in India by way of disclosure regulation that enables companies’ transparency reporting. This essay examines the central role that SEBI has played in recent times, especially on the latest Business Responsibility and Sustainability Report (“**BRSR**”) norms. It emphasizes the need for standardized ESG rating providers and illustrates how India can shape its own unique ESG narrative drawing upon lessons from global experiences. It further highlights the multifaceted benefits of ESG reporting for both the investors and the companies, paving the way for a more sustainable and responsible business landscape.*

Keywords: *ESG; CSR; BRSR norms; Ethical Business Conduct; Greenwashing*

I. INTRODUCTION

In today’s dynamic business landscape, a strong Environmental, Social, and Governance (**“ESG”**) rating is crucial for successful enterprises and investors. “*ESG is a framework that helps stakeholders understand how an organization is managing risks and opportunities related to environmental, social, and governance criteria (sometimes called ESG factors).”*[1] For instance, a company that encourages diversity, and environmental conservation and has robust anti-corruption measures would be considered to have a higher commitment towards ESG Goals.

Investors use ESG criteria as benchmarks which help evaluate whether the given company is responsible enough and compliant with its stakeholders’ expectations. ESG reporting happens when the company provides details about how it performs on environmental, social, and governance issues.[2] Therefore, this reporting may be considered as presenting investors with a

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[1] United Nations Department of Public Information, ‘The Global Compact, Who Cares Wins: Connecting Financial Markets to a Changing World’ (December 2004) 57899-December 2004-2,000.

[2] UN Global Compact, ‘Private Sustainability Finance’(unglobalcompact.org) <https://unglobalcompact.org/take-action/action/private-sustainability-finance> accessed 26 November 2023.

broad-stroked snapshot of how the organization impacts key issues for decision-making for consumers in line with their personal values.

The practice of embracing the ESG framework has proven beneficial for both investors and companies. Such an approach increases inflows of funds of varied character from different countries, therefore, building up brand value for the company. Consequently, investors get an avenue to match their values with investments, often yielding returns comparable to or better than the traditional approaches, particularly when investing in brands that prioritize ESG values.

Additionally, ESG engagement contributes to a competitive strength in the relevant market. Surveys among consumers and professionals in different fields suggest that a growing number of people are prepared to opt for green products and IT solutions from companies that uphold strong ESG practices.[3]

Moreover, investors and lenders have expressed interest in integrating ESG reporting. Businesses seek for investments as an emerging trend whereby earnings reports are coupled with separate “ESG” figures’ disclosures. More than one-fourth of investment companies are showing keen interest in sustainable investing funds which project an increase in number within a few years.[4] In response to growing concerns after the COVID pandemic, climate change, and resource misuse, investors are increasingly drawn to businesses aligning with sustainable practices while scrutinizing those lagging behind with outdated approaches.

In addition, ESG covers investor’s interests as well as boosting the company’s financial results. Simple measures of sustainability such as cutting down on paper usage as well as the adoption of energy-efficient upgrades may increase a company’s profitability and provide better returns.[5] Adherence to ESG regulations is also about risk management; it implies less exposure to penalties from regulators for non-compliance of ESG regulations which in turn results in stronger earnings. The example of Nestle making the commitment to moving from traditional plastic to food-grade recycled plastics shows that such ESG commitments may be used to reduce costs associated with compliance as well as reduce the carbon footprint of a business.[6]

II. EVOLUTION OF CSR AND ESG NORMS

[3] Anne Field, ‘Americans Want To buy Green, But They Don’t Trust Companies’ (Forbes, 26 June, 2022) <https://www.forbes.com/sites/annefield/2022/06/26/americans-want-to-buy-green-but-they-dont-trust-companies/?sh=2c7c2c2a73f0> accessed 26 November 2023.

[4] Gallup Inc, ‘Where U.S. Investors Stand on ESG Investing’ (Gallup.com, 23 February 2022) <https://news.gallup.com/poll/389780/investors-stand-esg-investing.aspx> accessed 26 November 2023.

[5] David Silk and Carmen Lu, ‘Environmental, Social & Governance Law USA 2023’ (ICLG.com, 26 January 2023) <https://iclg.com/practice-areas/environmental-social-and-governance-law/usa> accessed 26 November 2023.

[6] Nestlé Press Release, ‘Nestlé creates market for food-grade recycled plastics, launches fund to boost packaging innovation’ (nestle.com, January 16 2020) <https://www.nestle.com/media/pressreleases/allpressreleases/nestle-market-food-grade-recycled-plastics-launch-fund-packaging-innovation> accessed 26 November 2023.

The Evolution of Environmental and Social Governance in India can be traced back to the amendments to the Companies Act[7] in 2015, which made India the first legal regime to make Corporate Social Responsibility ("**CSR**") mandatory. It is the groundwork that was laid down by CSR which will now help us build a resilient, comprehensive, and transformative ESG framework.

The concept of CSR was aimed at changing how companies function and using a certain amount of profits of the companies for the benefit of society.[8] While this idea does sound wonderful, the lack of effective enforcement has always been a major challenge. According to the KPMG report,[9] more than 52 out of the country's 100 largest companies failed to spend the required amount on CSR activities. Amongst these issues, another issue that had arisen was the fact the Companies Act, 2013 had no clear guidelines as to what constituted CSR Activities. This led to a lack of transparency and companies not meeting their statutory obligations for CSR Reporting.

Therefore, a need arose for companies across industries to implement sustainability with their business strategy itself, combining sustainability and social obligation with their business ideas itself. This led to the creation of ESG which not only helps in meeting the CSR objectives but also helps get a greater return on investment.

Further, it is important to note that there has been a change in investment patterns wherein investors have now started to incorporate ESG factors into their decision-making.[10] It is important to understand that it is always the role of capital and investors that will drive sustainability efforts more than any obligation that has been imposed on corporate boards. However, even though ESG is essentially a market-driven concept, regulators around the world including the Securities and Exchange Board of India ("**SEBI**") have framed rules and guidelines for ESG reporting and disclosure.

The first such guideline was in the form of a guidance note issued by SEBI in 2012,[11] which mandated top 100 listed companies to file Business Responsibility Reports ("**BRR**") from an ESG perspective. This was then updated in 2015 wherein SEBI issued its Listing Obligations and Disclosure Requirements ("**LODR**") Regulations[12] wherein BRR mandated a more detailed report, such as reporting on Greenhouse Gas Emissions, energy consumption and water usage among others. This Circular led to BRR being extended to the top 500 listed

[7] The Companies (Amendment) Act 2015.
[8] The Economic Times, 'What Is Corp Social Responsibility? Definition of Corp Social Responsibility, Corp Social Responsibility Meaning' (economictimes.indiatimes.com, February 18 2024) <https://economictimes.indiatimes.com/definition/corp-social-responsibility> accessed 20 February 2024.
[9] KMPG India, India's CSR Reporting Survey 2015 (December 2015).
[10] So Ra Park and Jae Young Jang, 'The Impact of ESG Management on Investment Decision: Institutional Investors' Perceptions of Country-Specific ESG Criteria' (2021) 9 (3) IJFS <https://www.mdpi.com/2227-7072/9/3/48>.
[11] SEBI Circular CIR/CFD/DIL/8/2012.
[12] Securities and Exchange Board of India (Listing Obligations and Disclosure Requirements) Regulations, 2015 [Last amended on October 23, 2023].

companies. Subsequently, over the years, SEBI has been consistently issuing circulars and guidelines[13] to enhance reporting measures.

In a landmark move in May 2021, SEBI radically improved ESG reporting with the introduction of the Business Responsibility and Sustainability Report ("**BRSR**"),[14] it enhanced the scope of ESG and mandated the top 1000 listed companies to file BRSR reports and disclose non-financial performance. Through the BRSR Reporting, SEBI allowed for ESG disclosures in a standardized manner for the listed companies. This led to the creation of a comprehensive set of guidelines which has improved the consistency of ESG reporting in India. The BRSR norms made requirements for ESG Reporting along the lines of the 9 principles given in the National Guidelines for Responsible Business Conduct ("**NGRBC**")[15] which was introduced by the Ministry of Corporate Affairs ("**MCA**") in 2019. In comparison to the BRR norms, the metrics related to climate and social issues have been further expanded and refined for greater attention to detail providing for a more detailed assessment. Further, disclosures related to value chain partners have been made mandatory, ensuring greater coverage of the company's environmental and social impact through its supply chain.[16]

Furthermore, the BRSR framework replaced the five reporting sections of the earlier BRR with a more concise three-section structure. However additional disclosures have been made mandatory within each section therefore enhancing overall reporting.

The three sections in BRSR include, firstly, the **General Disclosures**, to obtain basic information such as the size, location, and number of employees in the company. Secondly, **Management Disclosures**, wherein the companies must disclose information on policies and processes related to the NGRBC Principles, encompassing leadership, governance, and stakeholder engagement. Thirdly, **Principle-Wise Disclosure**, which requires the companies to disclose the company's performance against the Principles and the Core Elements of the NGRBCs. Companies are required to demonstrate their commitment to responsible business conduct through concrete actions and outcomes.[17]

Further, BRSR requires both mandatory and optional indicators and encourages companies to focus on sustainability challenges, and elaborate on their ESG targets, goals and achievements. Therefore, BRSR serves as an effective mechanism for a company's non-financial disclosures and is a significant advancement in ESG reporting.

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[13] Ministry of Corporate Affairs, Government of India, 'National Guidelines on Responsible Business Conduct' (10 December 2018) <https://www.mca.gov.in/Ministry/pdf/NationalGuildeline_15032019.pdf>.; SEBI (Listing Obligations and Disclosure Requirements) (Fifth Amendment) Regulations, 2019.

[14] Securities and Exchange Board of India (Listing Obligations and Disclosure Requirements) (Second Amendment) Regulations, 2012 (No. SEBI/LAD-NRO/GN/2021/22, 5 May 2021).

[15] Ministry of Corporate Affairs, Government of India, 'National Guidelines on Responsible Business Conduct' (10 December 2018) <https://www.mca.gov.in/Ministry/pdf/NationalGuildeline_15032019.pdf>.

[16] Umakanth Varottil, 'The Legal and Regulatory Impetus towards ESG in India: Developments and Challenges' [2023] SSRN Electronic Journal <https://www.ssrn.com/=4323313> accessed 26 November 2023.

[17] Indian Chamber of Commerce & EY India, 'Business Responsibility and Sustainability Reporting (BRSS)' (ey.com, 21 April 2023) <https://www.ey.com/en_in/climate-change-sustainability-services/brsr-reporting-and-the-evolving-esg-landscape-in-india> accessed 26 November 2023.

III. CHALLENGES OF ESG REPORTING AND THE WAY FORWARD

One of the biggest challenges faced by regulators during ESG disclosures is the issue of greenwashing. SEBI defines greenwashing as "*making false, misleading, unsubstantiated, or otherwise incomplete claims about the sustainability of a product, service, or business operation*".[18] Therefore the reliability of the data disclosed by corporations has always been an issue since there exists no way to ascertain the truthfulness or falsity of the allegations. An example of the same can be seen in the fashion industry, wherein clothing brands like H&M have claimed that their clothes are eco-friendly and sustainable, but there have been increasing allegations of increased waste generation and an increase in the carbon footprint.[19]

To combat these issues ESG Rating Providers ("**ERP**") will have a significant role to play. ERPs are independent agencies that assess entities and provide ratings that help the investor to decide a corporation's commitment towards sustainability. However, in India these ERPs are largely unregulated. To address this issue, SEBI in July 2023 amended the SEBI (Credit Rating Agencies) Regulation, 1999[20] to regulate the accreditation of ESG rating providers. According to these regulations a person or an entity that wants to act as an ESG rating provider must obtain a certificate of registration from SEBI.

This concept of ERPs is not a novel idea and is prevalent in jurisdictions like the United States of America and the European Union. The USA predominantly has four major ERPs (MSCI, ISS ESG, Sustainalytics, and FTSE Russell),[21] however, these companies don't have a standardized measure for assessing the performance of a corporation on environmental, social and governance factors. The factors considered for accreditation by these four majors are different which has resulted in chaos and failure in achieving the intended objective.

Therefore, India must take lessons and learn from the mistakes committed by other jurisdictions such as the EU and the USA which are currently a step ahead of India in ESG reporting and regulating ERPs. To ensure that a similar problem is not faced in India, a standardized comprehensive code is in the need of the hour.

IV. CONCLUSION

In today's volatile global economy, the importance of ESG has significantly increased. ESG can be called both a compass that directs a company towards ethical practices and an integral criterion for the investor wishing to follow ethical norms and values. It offers a pathway to

[18] Shiwangi Singh, 'Evolution of ESG Regime in India: Challenges and way forward' (iiprd.com, 21 September 2023) <https://www.iiprd.com/evolution-of-esg-regime-in-india-challenges-and-way-forward/> accessed 26 November 2023.
[19] Matthew Stern, 'H&M Case Shows How Greenwashing Breaks Brand Promise' (forbes.com, 13 July 2022) <https://www.forbes.com/sites/retailwire/2022/07/13/hm-case-shows-how-greenwashing-breaks-brand-promise/?sh=2f0d59381171> accessed 27 November 2023.
[20] Securities and Exchange Board of India (Credit Rating Agencies) Regulation 1999.
[21] Brian Tayan and others, 'ESG Ratings: A Compass without Direction' (corpgov.law.harvard.edu, 24 August 2022) <https://corpgov.law.harvard.edu/2022/08/24/esg-ratings-a-compass-without-direction/> accessed 20 February 2024.

infuse a sense of heart and humanity into the business world, presenting a revolutionary shift needed in today's landscape.

The transition from CSR to a comprehensive ESG reflects a significant shift in the Indian business landscape. The journey from CSR requirements laid out in the Companies Act to the current importance put on ESG reporting shows the country's commitment to transformative business practices.

The mandates by SEBI including the BRSR norms have solidified India's position. These regulations have bolstered transparency, pushing companies to integrate sustainability into their core strategies, ensuring a broader societal impact beyond mere profit accumulation.

However, the part towards a robust ESG framework will not be one without its own challenges. To tackle this, the need for a standardized code to ensure consistency will be crucial. Further learning from the experiences of the jurisdictions such as the USA and the EU, where ERPs do not have a standardized measure, India can regulate ERPs to achieve the intended objectives. Moreover, the role of Independent Directors should not be underestimated and SEBI's recognition of their importance and issue of directives highlighting expertise in ESG subjects will have an integral role to play to drive corporations towards sustainable ESG practices.

Going forward, India is at crossroads and must look back to global practices while forging its own independent approach. To follow this route in India, bridging regulatory gaps and ensuring ethical business conduct is essential for building a future where ESG doesn't remain confined as merely a regulatory framework but becomes an intrinsic part of the corporate ethos and the investor decision-making. Mandating ESG practices today may help avoid problems tomorrow, which will enable businesses to grow profitably in a changing economic landscape.