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# **TYING THE THREADS BETWEEN INVESTMENT AND LEGALITY OF ENVIRONMENT, SOCIAL AND GOVERNANCE MATTERS (ESG)**

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## **ABSTRACT**

ESG investments have often been questioned on the areas of legality, returns, potential growth and sacrifice of financial returns. To broach the concerns of people regarding their well-being, environmental safety, inclusivity in business, recognition to gender diversity have become crucial for business leaders. Whether sacrificing financial returns on ESG helps in rectifying the cracks in environment and governance is debatable where the conclusion is still indeterminate. While there exists mandatory disclosure requirements and reporting framework on ESG imposed by the authorities, there still remains grey areas on the efficacy of the strategies to enhance and improve the return on investment on ESG. To answer a few concerns surrounding the potential aspect and legality of ESG investments is the purpose of this paper where there are examples of Companies earning money through ESG investments and companies spending their capital and revenue expenditure on the upliftment of the economy.

## **Evolution of Concept of Environment, Social and Governance**

Relevance can be placed on United Nations Millennium Summit held in the year 2000 which helped the world leaders unplug the importance of ESG investments and threw a coin of thought into the well of their minds. Emphasis was placed on crucial train of thoughts such as human rights, working conditions, the environment, social governance and how the theory behind these topics meddled with investments and risk management of a Company and resonates with folk at the same time. Early 2000s have put the business units and the leaders under the microscope to bring about a revolution by introducing indicators such as Principles for Responsible Investment (PRI), the Climate Disclosure Standards Board (CDSB) and the Sustainability Accounting Standards Board (SASB)<sup>1</sup> and such likewise community-oriented theories. Sustainable Development Goals were formulated in the year 2015, which laid down several targets for the businesses to achieve by displaying the hope that it would result in the world becoming a sustainable economy with better standard of living, vacating the space for contemplating the growth and development of human beings.

### **ESG investment or sacrifice of financial returns?**

The incent to invest in ESG portfolio funds is traced back to European countries where Corporate Governance covered experiments and research in the field of whether investors are willing to sacrifice their financial returns for better ESG score, if or not, linked to improving performance of the Company<sup>2</sup>. The internal corporate politics influences the external world where the underperforming companies censured ESG their reason for poor performance. United Nation's sustainable development goals bridge the gaps between embracing investment in ESG and shortfall in the returns behind it by setting an agenda of 17 goals to be achieved by the year 2030 for a sustainable economy. What most people are worried about is whether or not sacrificing short term performance is worth the long-term potential benefits of investing in ESG. Transparency and proliferation have been one of the key drivers of investment in ESG bonds. Statistics and studies of researchers in past years have proven that a lot of patience is required in earning the returns from ESG investment which is often not considered and treated as an agenda or a target by corporates and organizations where gaining short-term profit seems easier. It has also been collectively concluded basis testimonials of big corporate leaders that

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<sup>1</sup> IBM, <https://www.ibm.com/think/topics/environmental-social-and-governance-history>

<sup>2</sup> Harvard Business Law, <https://hbr.org/2022/03/an-inconvenient-truth-about-esg-investing>

changes instilled by spending money in the betterment of environment such as climatic changes, better living standards, clean water have not been given enough priority due to the underrated phenomenon of people well-being and good standard of living. Certain initiatives taken for the upliftment of the environment is also masked and benefited under the concept of Corporate Social Responsibility mandated by Section 135 of Companies Act, 2013 where a lot of tax benefits are availed. While the debate still continues to bridge the gap between short term and long-term benefits, returns on ESG are certain if placed reliance on and speculated on for long-term returns.

### **Highlights on the ambiguity on the belief on data with no universal standards**

To enable softer and easier compliances on reporting lines of ESG, Securities Exchange Board of India (SEBI) has made several amendments and insertions in the law simplifying the disclosure requirements by enhancing transparency and commitment towards sustainability. Investors and Companies were often posed with the risk of belief on data and statistics due to the absence of universal standards on ESG ratings, reporting or investment which inspired SEBI to lay down guidelines thereby removing ambiguity. SEBI has made it mandatory for top 1000 listed entities (calculated basis market capitalization) to disclose ESG related data in the form of Business Responsibility and Sustainability Reporting (BRSR) annexed to their Annual Report annually. Preventive measures against greenwashing by the Company have motivated the regulators to develop regulations for Mutual Funds as well to minimize the non-financial risks. BRSR have been formulated to include critical ESG attributes and Key Performance Indicators (KPIs)<sup>3</sup>. Centered on filling the openings in the betterment of Indian Environment and maintaining good Governance, the KPIs have been detailed to include data on Green-House Gas emissions, Waste management, Water footprint, employee well-being, inclusive development, gender diversity and such other related disclosures. Such indicators have been proved successful in removing the ambiguity of presence of universal data to measures performance in the arena of ESG investments by the Companies. Question may arise as to why only top listed entities have been mandated to make such disclosures and the others are curtailed from the same. The smaller companies, private entities and other body corporates earn lesser profits which usually does not leave them room to speculate investment on environmental needs and are focused mainly on the growth and expansion of the Company. However, to ensure such body corporate's commitment towards the growth of environment

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<sup>3</sup> SEBI, [https://www.sebi.gov.in/sebi\\_data/meetingfiles/apr-2023/1681703013916\\_1.pdf](https://www.sebi.gov.in/sebi_data/meetingfiles/apr-2023/1681703013916_1.pdf)

and to instill habits of good corporate governance in them, Corporate Social Responsibility is imposed on them by the regulators where they have to spend a certain amount mandated by law for the upliftment of the environment and people where they also enjoy certain benefits of taxation and brand promotion as well. Various concepts have been designed on these lines for ensuring accurate disclosures on ESG such as Global Reporting Initiative Standards, United Nations Sustainable Development Goals (UNSDG's), Sustainability Accounting Standards Board (SASB) Standards<sup>4</sup>. The evolution of the mandatory disclosure requirements has eliminated the uncertainty and indefiniteness of the availability of reporting lines on ESG investment and initiatives taken by the corporates. While there is still lack of universal data to certify the returns on ESG investment, the authorities and regulators of law assume it necessary for Corporates to work for the advancement of the economy aiming to achieve the 2030 agenda of Sustainable Development Goals stipulated by the United Nations and work for the overall development and growth of the Country as well.

### **The efficacy of engagement strategies: Indeterminate or Certain**

There exists a lot of active engagement strategies which enables the corporate leaders to increase the visibility and promote their brand by investing in ESG needs of people. It is very crucial to investigate and understand the areas where the investment would meet the return of engagement strategies as well. Strategies developed, which engage the community helps in earning more return on investments made than to not have people's attention. Active engagement strategies involves determining the plan and developing the engagement strategy which helps in drawing attention of the public and raises awareness for the need of growth of the economy and well-being of the people. For instance, ARCIL (Asset Reconstruction Company India Ltd) has collaborated with Indian Railways to install dustbins in western and central railways units in Mumbai<sup>5</sup>. The strategy developed by the Company proves to be a crucial and public involvement strategy where crores of people have their eyes on such an initiative every day and also helps in the promotion of the brand of the Company. To flourish and expand such a method where target reaches a large number of people, helps in maximization of the effect and outcome of such money spend is the need of the hour. It is considered vital to link the outcome and success to employee's well-being to increase visibility and effect of ESG investments<sup>6</sup>. Corporates are run by people and for people where the health

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<sup>4</sup> TUV Rheinland, <https://www.tuv.com/world/en/activities-on-entreprise-level.html?verbid=130>

<sup>5</sup> ARCIL, <https://www.arcil.co.in/csr-project/culmination-railway-dustbins-installation>

<sup>6</sup> TRELIS, <https://trellis.net/article/4-strategies-elevating-internal-esg-engagement/>

and attention to the needs of “people” is necessary. If investments are made for the betterment of environment, climatic changes and in making an attempt to improve the lifestyle of their employees by the Companies, the need to worry pertaining problems such as poor health standards, bad Air quality Index and such other concerned problems will decrease thereby increasing in productivity of the employees. Therefore, the act of creating a nexus between success rate of ESG and employee’s comfort and wellness can prove the efficacy of the quote – “to kill two birds with one arrow”, where one is to increase the productivity of employee and the other is to promote the brand, resulting in achieving the long-term agenda of the Country. To perform well in the market is subjected to the debate between Good Corporate Governance and mandatory requirements stipulated in law, where a lot of Companies restrict themselves from observing good Corporate Governance due to constraints of funds and is forced to do the bare minimum requirements by law. Companies like as Reliance Industries Limited, Hindustan Unilever Limited, Bharti Airtel, Infosys and others have also incorporated ESG Committees as a part of the Board of Director’s Committees where the committee comprises of experts in the respective field to guide, advise, help and suggest the Directors of the Company about the ESG initiatives to be taken, linking of ESG returns to the growth of employees, strategies towards the melioration of a sustainable environment thereby ensuring good corporate governance by the Company. Companies use ESG models, discussions on improving the well-being of the employees, socially including people from different communities, ratings of their ESG disclosures, conducting sessions on the importance of ESG investment and inculcating Social Impact Assessment as useful methods for successful ESG disclosures and compliance. Diversifying the investment in various arenas and involving different stakeholders proves as an efficient way in comparing the return from different sources and choosing the most performing method amongst them.

### **Does ESG helps in addressing global concerns with increasing issues?**

Corporations since ages were driven by only one motive which was to earn profit and maximize the initial investment of the promoters. To make money was the only inspiration behind great ideas of people becoming corporate leaders in the industry. To address global concerns like gender diversity, hunger, poverty, life below water, renewable energy was never on their mind until the discovery of Environment, Social and Governance (ESG) concept. The environmental issues of the economy keep on increasing where ESG acts as a life-saving jacket and helps in protecting the economy from drowning in these concerns. Countries across the globe has

inculcated the agenda to improve the ecosystem and work on the niche areas of environmental protection. ESG helps the companies in formulating a motive to address and solve global concerns relating to inclusivity, diversity, gender biasness, living standards, water and air quality on earth. ESG investment helps as a ladder in developing good connection between the producers and consumers where consumers place their trust and money on the companies which is helping in their well-being. ESG ratings and disclosures serves as a transparent benchmark to analyze the performance and growth of a Company. According to the analysis based on Corporate Knights Global 100 Ranking<sup>7</sup>, there exists various Companies which has helped in the advancement and upliftment of the economy. Centered on energy efficiency, grid digitalization, power solutions, developing climate friendly alternatives, projects on solar energy, there are numerous Companies which have spent their revenue and capital expenditure on environmental projects and has worked towards making the economy more sustainable. While Indian companies contribute less towards ESG, companies in Italy, France, United States, Canada, United Kingdom are indeed performing better. Multiple discoveries have been made to ensure economic-friendly and maximization usage of resources to prevent scarcity of the same and leading the world towards a green transition. To earn profits and to invest in ESG are mutually reinforcing where the exclusivity of both helps the companies achieve their goals and vision. Therefore, to integrate sustainability and environmental development as a business strategy can help the world in climbing the ladder fast towards a green ecosystem and leading the nation towards a better era. It is not only the responsibility of the Companies but also of individuals to help in the advancement of the economy and help in the revolution of the ecosystem.

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<sup>7</sup> ESG Next Conference, <https://esgnextconference.com/top-50-esg-compliant-companies-globally/>