ESG: A POSITIVE CURVE MUCH BEYOND CSR

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"Legacy is not what we did for ourselves, but what we are doing for the next generation!"

ABSTRACT

There is much hype about the Country moving forward firmly for the '*panchamrit*' and net-zero carbon emission by 2070 to usher in green industrial and economic transition and yes, to an extent there are considerable reasons to believe this to be real and not a propaganda for any political or commercial motive. The Union Budget of 2023 does not only put the "Green Energy and Measures" as one of the priority items, but also through various direct and indirect linkages with the other budget inclusions and the complementary schemes launched by the Government in the recent times have paved a decent way to achieve the objectives.

Having said that there are some obvious question marks on the manner of implementation of these green credit schemes and its incorporation into the statutes. Its not the first time when "Go Green" is buzzing around the corporates and individuals, would be interesting to see whether this ends up being another blunt sword or finally puts some legal clothing to the otherwise social and ethical principals of CSR and ESG.

INTRODUCTION

Talking about CSR and ESG, for a layman there are a lot of existing fancy notions and terminologies which are enough to confuse any mind. “Sustainability”, “Socially Sustainable”, “Corporate Social Responsibility”, “Corporate Governance”, “Green Consumerism”, “LiFE”, and a lot other similar or overlapping terminologies are not uncommon to anyone now a days. For law school students, in fact the distinction between any of these two terminologies has been a very common examination question as well since years, and unfortunately with years the terminologies are getting added but the differences are simply getting thinner. The reason for putting across these obvious (and apparently harmless point) is to highlight the failure of any of these measures to practically make a difference or achieve the target for which these concepts were introduced. As blunt as it could be, Half of these simply turned out to be a tool for white (or rather, green) washing the image of the corporate houses. A very simple question for all those who advocate the green measures and initiatives, what exactly is the target we are trying to achieve? does it even make a commercial sense to impose such obligations or expectations on corporates who are not even engaged in manufacturing or any such activities which relate to or harm the environment in any manner? Why are we stretching the scope with each of such notions and still not making these mandatory or attaching any legal sanctions to the violations? Questions are many, and quite possible to invite varied views and justifications for each such point. To me, the first instance (or the very genesis) of this entire sustainability notion is perhaps the Bhopal Gas Tragedy and the havoc caused by it. The natives and generations of the area are still under the terror of the tragedy which took pace decades ago. Very much from then, the regulators, NGOs and administrative bodies are working towards making these linkages between the corporates, business, development, and the society. However, the concept has somewhat got shaken and at times over stretched thereby limiting or compromising on the development, commercial aspects and the growth of market with absolute clean (I would rather say, complete green) products. One such example is the recent news on the fall off of an acquisition of packaged mineral drinking water by Tata group and (unwarranted) speculation on the linkages with the “green” objectives of the group. Based entirely on my personal view, while the usage of plastic should not be encouraged, we need to weigh the benefit of social and health benefits of hygienic mineral water at affordable price for masses as well under the wider coverage of such sustainable and social goals.

The purpose of this write up is however not to question to raise the shortcomings of all these well intended green notions, but to stress on the scope and some really genuine attempts from the corporates as well as regulators under the head of "ESG" (which to my mind, is by far the most effective mechanism and tool for all the stakeholders involved in the process) which goes much beyond the last such hyped notion of CSR, and certainly in the correct direction.

WHAT IS THE DEMARCATING LINE FOR ESG?

We know, ESG stands for Environmental, Social and Governance- and these are very much the three pillars of the notion. But how does it differ from the other similar sustainability notions bending on environment, climate and social motives? Firstly, I think the acronym "ESG" is a misnomer to an extent, given the coverage and parameters which spread across almost all non-financial factors. The ultimate target of ESG is to capture all the non-financial risks and opportunities inherent to a company's regular business and governance activities. It would not be wrong to say that ESG in essence captures in the very underlying motive of not only taking responsibility of corporate's own actions but also mythologically working towards improvement at all levels thereby ultimately leading to a conscious organisation, society and the World!

REGULATORY REGIME: A PARADIGM SHIFT!

There are two ways to look at the differentiating line- One from the regulatory perspective and the other (and more relevant) from the investors' perspective. While at the international and domestic level both the Government and regulators have been consistently trying to make the ESG norms and reporting more embedded into the regulatory system, there is still some time for this to be completely entrenched into the existing framework, specifically for the private companies and unlisted companies. There has been a gradual widening of scope of ESG policies and that the ESG policy environment is moving away from a voluntary regime to a mandatory one. The current regime focuses on the reporting requirements for the top 1000 listed companies (by market cap). It took years for the regulators to gradually reach it to the mark of 1000, but still the progress has been steady and received positively by the corporates and communities alike. It started in 2011, with the National Voluntary Guidelines (NVG, in line with the established UN Millennium Development Goals) on Social, Environmental, and Economic Responsibilities of Business as released by the Ministry of Corporate Affairs (MCA). Followed by the Business Responsibility Report (BRR) in 2012 by the Securities Exchanges Board of India (SEBI). While BRR was a semi effective measure with a decent coverage, with time and global developments the relevance for all obvious and anticipated reasons started fading away. The change became inevitable with the national level reports questioning the quality of data and accuracy of the reporting being made. This paved way for the current Business Responsibility and Sustainability Reporting (BRSR) framework. BRSR is not only has a coverage similar to BRR in terms of listed companies, but also is quite aligned with the internationally recognised and tested reporting standards like United Nations Sustainable Development Goals (UN-SDGs) and Global Reporting Initiative (GRI). The entire BRSR mechanism has a solid foundation and requires quite a depth research and methodical working by the corporates to fulfil the compliance and reporting under it. To that extent, it would not be overstretching to say that BRSR is a leap beyond from any of the erstwhile mechanisms. This has very well been acknowledged by the corporates globally as well.

The procedural and methodology used under the BRSR framework require a detailed insight and study to understand how the reports are prepared and the scope it has. While SEBI has prescribed guidelines and inclusions for the reports, there is no fixed format or manner of making such reporting. Currently most of the companies are following the format in line with their global counterparts and standards of GRI and Sustainable Accounting Standards Board's standards (SASB). In additional to a formal reporting, many companies are disclosing data through webpages as well. Also, the reporting and disclosure has a very direct nexus with the nature of business of the company. A company engaged in manufacturing or energy activities may have a different materiality threshold for disclosures then the one in service sector or an e commerce business. Companies report on issues that are material to them and their business (which determines their interface with the stakeholders and society). All of this is This is beyond the scope of this write up and requires a study of its own. However, to give a quick overview, the reporting mechanism and standard is embraced on the pillars of "RRR" – *Revive, Rejuvenate and Restore*, thereby not only protecting but improving and promising a better world to the next generation. It includes the general non-financial disclosures, environmental impact, carbon dating reporting, green power and credits, anti-corruption and money laundering measures, socially conscious measures, improvement and quality of employment satisfaction, robust reporting mechanism internally in the system and with the stakeholders, to name a few of such parameters.

INVESTORS' SENTIMENTS- A POSITIVE TREND!

The effect of such a robust mechanism and reporting, which starts at an internal level and ultimately ends up being a factor of much of an external interest for the stakeholders as well. That's where the second perspective gains importance. ESG and it's reporting today has become a very significant tool for the investors to judge their target investee companies. It's a popular belief that your ESG score is directly proportional to the returns which the investors can expect on their investment in such entities. Needless to say, its just not a proposition but a well-researched and logically (plus, arithmetically proven) theory. However, by linking it straight with the returns, I dint want to undermine the change in outlook and the real importance accorded by a lot of socially conscious corporates and investors now a days, who are actually working on creating a green world and better organisations for the reasons much beyond the mere green credits and scores. In fact, for such factors there are several other fancy notions which can be very well applied by the corporates and the investors. ESG, however, carries a baggage of trust and well-intended motive with it. More and more investors are incorporating ESG elements into their investment decision making process. With this, an ESG compliant entity is expected to attract more funding than the one with a lesser conscience towards it- and yes, that's the global investor sentiment also proves as on date. Following the European and US market trends, where a growing number of institutions would only invest in funds that are deemed to be compliant with ESG-investing principles, India is also witnessing the same trend now. In terms of both objectives and practices, a considerable emphasis on environmental aspects of sustainability and social dimensions has been placed by the investors.

ROLE OF LEGAL COUNSELS

To a point all of this sound very operational and compliance based. Perhaps more for the operations and business teams of the corporate to ensure the embedding of the principals in their ground level working and the Compliance team to methodologically review, collate and report the final data and disclosures to the authorities. This in fact is true, but only a half truth.

Any organisation, irrespective of the nature of its activities and more relevant for certain sectors and industries, rely a lot on their counsels not only for documenting the policies and understanding, but also ensuring its due adherence and implementation which dealing with stakeholders and other contracting parties. Any organisation would function only in collaboration with a long list of external and internal stakeholders. If the well-intended principals are not embedded in the dealings and contracts with the stakeholders, the actual implementation of the same in the underlying dealings and business is next to impossible. Again, the role is much beyond simply documenting or drafting the contracts with such principles included, but to actually (and reasonably) put the intention and motive of such principles across the negotiation desk to the other parties and stakeholders so that these are not simply the fancy clauses on paper, but the actual guiding principles for the parties. This may involve a complex discussion, given the direct conflict with commercial objectives, lack of mandatory legal clothing at times and the involvement of additional resources from both sides. A watertight ESG compliant contract binder of an organisation is like (and not to exaggerate) little more than 1/3rd of the job done. Post this, the counsels play a significant role in day-to-day interface between the organisation and stakeholders on the issues of ESG related principles which directly or indirectly find their roots in such contracts and internal policies. This is multiple steps ahead of CSR initiatives which are mostly internal with less or no involvements of stakeholders or contracting parties. Depending upon the nature of organisation and its business, the role may vary and extend even beyond the one illustrated here.

WHAT'S MORE AND NEXT?

Investors' sentiments are in right place and expected to positively grow only in this regard. What's expected more to my understanding is from the regulators. There are many steps which are in pipeline and expected to be implemented soon. One such step is the regulatory framework for ESG Rating Providers (ERPs). ERP scheme proposed by SEBI. It would be interesting to see if SEBI would follow the voluntary model like other jurisdictions or attempts to make it stronger as suggested by various reports. Stakeholders' comments and feedback on the proposal are still open!

Another, possible measure could be to the actual implementation of the proposal of SEBI that ESG scheme should invest at least 65 per cent of its asset under management (AUM) in companies which are reporting on comprehensive BRSR and are also providing assurance on BRSR Core disclosures. This could turn out to be a huge plus and incentive for the companies diligently following the reporting and working on ESG measures. On the other side of this, negative measures on downgrading the ESG ratings which were witness in European market is something which is still to be tested for Indian market. Probably too nascent for the domestic market as of now and could backfire the positive steps taken as of now.

The current BRSR regime is limited to the top 1000 listed companies only. While the scope in terms of number is steadily increasing, its high time to loop in the private and unlisted entities (may be in phase wise) to ensure a wider coverage.

Lastly, the budget announcements on green credits are anticipated to be a big thing. Implementation of the same is the key here. The amendments to the environmental statutes and other policy decisions in this regard would be worth noticing. A huge anticipating for this space!