



ESG reporting: A theoretical framework

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Abstract

Environmental, Social, and Governance (ESG) reporting has emerged as a pivotal framework for assessing corporate sustainability and ethical practices. This research paper delves into the intricacies of ESG reporting, emphasizing its significance in fostering transparency, accountability, and long-term value creation. The study explores the environmental, social, and governance components of ESG reporting, providing a comprehensive analysis of each dimension. Furthermore, it examines standardized frameworks for ESG reporting, highlighting their role in enhancing comparability and reliability across organizations. Through a qualitative and exploratory approach, the paper analyzes existing literature, industry practices, and case studies to offer insights into the current landscape of ESG reporting. The findings underscore the critical role of standardized frameworks in promoting consistent and meaningful ESG disclosures, thereby contributing to informed decision-making by stakeholders and supporting the broader agenda of sustainable development.

Keywords: ESG reporting, standardized frameworks, sustainability, corporate transparency

Introduction

Environmental, Social, and Governance (ESG) is a comprehensive framework that evaluates an organization's impact and performance across three key dimensions: environmental stewardship, social responsibility, and corporate governance. ESG serves as a mechanism to assess non-financial factors that influence an entity's long-term sustainability, ethical practices, and overall societal contributions. By addressing these dimensions, ESG fosters a holistic approach to value creation and risk management. ESG reporting refers to the systematic disclosure of data and information related to an organization's environmental, social, and governance practices. It provides stakeholders—including investors, customers, employees, and regulators—with a transparent view of how the organization is managing risks and opportunities associated with ESG factors. These reports may be integrated with financial disclosures or presented as standalone documents, aiming to communicate an organization's commitment to sustainability and ethical operations.

ESG reporting has gained significant importance in recent years. Firstly, it serves as a critical tool for investor decision-making, offering insights into a company's long-term viability and sustainability. Secondly, regulatory compliance has become a driving force, with governments and regulatory bodies worldwide increasingly mandating the disclosure of ESG practices. Thirdly, it builds stakeholder trust by demonstrating accountability and integrity, thereby enhancing credibility among customers, employees, and the wider community. Additionally, ESG reporting aids in risk mitigation by identifying and addressing potential financial, operational, and reputational risks. Companies that excel in ESG practices also gain a competitive advantage, differentiating themselves in the market and attracting customers and investors with shared values. Lastly, robust ESG frameworks are instrumental in fostering resilience, adaptability, and sustainable growth, contributing to long-term value creation for all stakeholders.

Review of literature

Eccles et al. (2012) [3]: This seminal study emphasized the integration of ESG factors into corporate strategy, highlighting that companies with robust ESG reporting exhibit superior financial performance, enhanced stakeholder engagement, and reduced risk exposure over time. The study underscored the necessity of embedding sustainability into the core business strategy.

Khan, Serafeim, & Yoon (2016) [6]: These researchers explored the materiality of ESG issues and demonstrated a positive correlation between material ESG disclosures and firm value creation. Their findings suggested that focusing on industry-specific ESG metrics leads to better financial outcomes and operational efficiency.

KPMG (2020) [7]: KPMG's global survey revealed that 80% of the top 250 global companies now engage in ESG reporting. The study attributed this growth to increasing regulatory mandates, evolving stakeholder expectations, and the rising influence of sustainable investment practices.

Friede, Busch, & Bassen (2015) [4]: This meta-analysis of over 2,000 studies revealed a significant positive relationship between ESG performance and financial performance, challenging the traditional assumption that sustainability comes at the cost of profitability. The analysis demonstrated that integrating ESG considerations can drive long-term success.

Ioannou & Serafeim (2019) [5]: This research examined the impact of ESG disclosure on transparency and information asymmetry. The authors found that enhanced ESG transparency fosters trust and enables more efficient capital allocation by reducing information gaps between firms and investors.

Bebbington & Unerman (2018) [1]: These authors critiqued existing ESG reporting frameworks, highlighting the need

for global standardization to improve comparability and reliability. The study emphasized the importance of aligning ESG metrics with the United Nations Sustainable Development Goals (SDGs).

Chatterji *et al.* (2016) ^[2]: This study investigated the accuracy of ESG ratings and pointed out inconsistencies in scoring methodologies across rating agencies. These inconsistencies, the authors argued, undermine stakeholder confidence and necessitate a more unified approach to ESG evaluations.

SASB (2021) ^[8]: The Sustainability Accounting Standards Board emphasized the importance of aligning ESG reporting with materiality principles to ensure that disclosures focus on issues most relevant to stakeholders and business objectives. The study highlighted the role of industry-specific standards in achieving greater relevance and impact.

GRI (2021) ^[8]: The Global Reporting Initiative explored the evolution of sustainability reporting and advocated for a multi-stakeholder approach to developing ESG standards. The study stressed the importance of transparency and inclusivity in shaping ESG frameworks.

Research methodology:

Research Design: This study adopts a qualitative and exploratory approach to analyze ESG reporting practices, frameworks, and their impact on stakeholders. A systematic review of literature, coupled with comparative analysis across industries, provides the foundation for understanding the theoretical and practical implications of ESG reporting.

Data Collection: Secondary data sources, including articles, corporate ESG reports, industry publications, and guidelines from standard-setting bodies such as GRI, SASB, and TCFD, form the basis of the analysis. Additionally, case studies from diverse sectors enrich the discussion.

Scope: The study focuses on:

- Identifying and evaluating key ESG reporting frameworks.
- Analysing the impact of ESG reporting on investors, regulators, and other stakeholders.
- Comparing ESG reporting practices across industries and geographic regions to identify trends and gaps.

Limitations-

- Dependence on secondary data introduces potential biases due to selective reporting and varying data quality.
- Variability in ESG metrics complicates comparability across industries and jurisdictions, limiting the generalizability of findings.
- The rapid evolution of ESG standards and practices may render some observations time-sensitive.

Analysis and discussion:

Environmental, Social, and Governance (ESG) reporting has become an essential aspect of corporate transparency and accountability. This document delves into the intricacies of ESG categories, detailing the specific components that organizations should report under each pillar. Additionally,

it provides an in-depth analysis of standardized reporting frameworks, emphasizing the Task Force on Climate-Related Financial Disclosures (TCFD).

1. Details of ESG Categories:

1.1. Environmental (E):

The environmental component of Environmental, Social, and Governance (ESG) reporting is a critical aspect that evaluates a company's impact on the natural environment. This component encompasses various factors that reflect a company's commitment to sustainability and responsible environmental stewardship. This dimension examines a company's environmental impact and sustainability strategies.

1. **Climate Change Mitigation:** Companies are expected to disclose their strategies for reducing greenhouse gas emissions, including targets for carbon neutrality and the adoption of renewable energy sources. Transparent reporting on these initiatives demonstrates a commitment to addressing climate change.
2. **Resource Management:** Efficient use of natural resources—such as water, energy, and raw materials—is vital. Reporting should cover resource consumption patterns, recycling efforts, and initiatives to minimize waste, highlighting the company's dedication to sustainability.
3. **Pollution and Waste Management:** Companies must detail their practices for managing emissions, effluents, and waste. This includes strategies for reducing air and water pollution, managing hazardous materials, and implementing waste reduction and recycling programs.
4. **Biodiversity and Conservation:** Reporting should address the company's impact on biodiversity, including efforts to preserve natural habitats, protect endangered species, and engage in conservation projects. This reflects a commitment to maintaining ecological balance.
5. **Environmental Compliance and Risk Management:** Companies are expected to disclose their adherence to environmental regulations and standards. This includes compliance with local and international environmental laws, as well as the identification and management of environmental risks that could affect operations.

By thoroughly addressing these areas in ESG reporting, companies provide stakeholders with a clear understanding of their environmental stewardship and sustainability practices. This transparency is essential for building trust and demonstrating a commitment to responsible environmental management.

1.2. Social (S):

The Social component of Environmental, Social, and Governance (ESG) reporting evaluates a company's impact on society, focusing on its relationships with employees, customers, suppliers, and the communities in which it operates. This category evaluates a company's social responsibility. Key areas include:

1. **Labor Practices and Employee Relations:** Companies are expected to disclose their labor practices, including fair wages, safe working conditions, and respect for workers' rights. This also encompasses policies on child labor, forced labor, and freedom of association. Transparent reporting in this area demonstrates a commitment to ethical labor standards.
2. **Diversity, Equity, and Inclusion (DEI):** Reporting should cover initiatives aimed at promoting diversity and inclusion within the workforce. This includes gender diversity, racial and ethnic diversity, and support for underrepresented groups. Companies should disclose their DEI policies, training programs, and measurable outcomes to showcase their commitment to an inclusive workplace.
3. **Human Rights:** Companies are expected to disclose their adherence to human rights principles, including policies to prevent discrimination, harassment, and violations of privacy. This also involves ensuring that business operations do not contribute to human rights abuses in the supply chain.
4. **Community Engagement and Impact:** Reporting should detail the company's engagement with local communities, including philanthropic activities, volunteer programs, and efforts to address community needs. This reflects the company's role in contributing to societal well-being.
5. **Product Responsibility and Safety:** Companies are expected to disclose their commitment to product safety and quality, including measures to ensure that products and services meet safety standards and do not harm consumers. This also involves transparency regarding product sourcing and labelling.

By thoroughly addressing these areas in ESG reporting, companies provide stakeholders with a clear understanding of their social responsibility practices. This transparency is essential for building trust and demonstrating a commitment to positive social impact.

1.3. Governance (G):

The Governance component of ESG reporting assesses how a company is directed and controlled, focusing on the structures, policies, and practices that ensure accountability, fairness, and transparency in its operations. The governance component evaluates an organization's internal systems, processes, and practices that ensure accountability, transparency, and ethical behaviour. Key aspects to be reported include:

1. **Board Composition and Structure:** Companies are expected to disclose the composition of their boards, including the balance between executive and non-executive directors, diversity, and independence. A well-structured board is crucial for effective oversight and strategic decision-making.
2. **Executive Compensation:** Transparency in executive compensation is vital. Companies should detail how executive pay aligns with performance metrics and

long-term shareholder value, ensuring that compensation structures do not incentivize excessive risk-taking.

3. **Shareholder Rights and Engagement:** Governance reporting should include information on shareholder rights, including voting mechanisms and engagement practices. This ensures that shareholders can effectively influence corporate decisions and hold management accountable.
4. **Ethical Conduct and Compliance:** Companies are expected to disclose their policies and practices related to ethical conduct, including anti-corruption measures, compliance with laws and regulations, and mechanisms for reporting unethical behavior. This demonstrates a commitment to integrity and legal compliance.
5. **Risk Management:** Effective governance includes robust risk management frameworks that identify, assess, and mitigate various risks, including financial, operational, and reputational risks. Reporting should detail these frameworks and how they are integrated into the company's strategic planning.

By thoroughly addressing these areas in ESG reporting, companies provide stakeholders with a clear understanding of their governance practices, fostering trust and demonstrating a commitment to responsible corporate behaviour.

2. Standardized reporting frameworks

Standardized frameworks for Environmental, Social, and Governance (ESG) reporting provide structured guidelines for organizations to disclose their sustainability performance. These frameworks aim to enhance transparency, comparability, and accountability in ESG reporting. Below are some of the most widely recognized frameworks:

1. **Global Reporting Initiative (GRI):** The GRI Standards are among the most widely adopted frameworks for sustainability reporting. They offer a comprehensive set of guidelines covering a broad spectrum of economic, environmental, and social impacts. The GRI Standards are structured into Universal Standards, Sector Standards, and Topic Standards, allowing organizations to tailor their reports to their specific context and stakeholder needs.
2. **International Financial Reporting Standards (IFRS) Sustainability Disclosure Standards:** Developed by the International Sustainability Standards Board (ISSB), the IFRS Sustainability Disclosure Standards aim to provide a global baseline for sustainability-related disclosures. These standards are designed to be used by companies to report on sustainability-related risks and opportunities that are material to investors, thereby enhancing the comparability and reliability of ESG information.
3. **Sustainability Accounting Standards Board (SASB) Standards:** The SASB Standards provide industry-specific guidelines for disclosing financially material

sustainability information. They focus on the subset of ESG issues most likely to affect the financial performance of companies within a specific industry. In 2022, SASB was integrated into the IFRS Foundation, aligning its standards with the global sustainability reporting landscape.

4. **Task Force on Climate-related Financial Disclosures (TCFD):** The TCFD recommendations offer a framework for companies to disclose climate-related financial risks and opportunities. They focus on governance, strategy, risk management, and metrics and targets related to climate change, aiming to provide investors and other stakeholders with consistent and comparable information.
5. **CDP (formerly Carbon Disclosure Project):** CDP provides a global platform for companies to disclose their environmental impacts, focusing on climate change, water security, and deforestation. It offers a comprehensive system for measuring, managing, and sharing environmental information, enabling companies to demonstrate environmental stewardship and transparency.
6. **Integrated Reporting Framework (IR):** Developed by the International Integrated Reporting Council (IIRC), the Integrated Reporting Framework encourages companies to provide a holistic view of their strategy, governance, performance, and prospects in the context of their external environment. It aims to demonstrate how an organization creates value over time.
7. **United Nations Global Compact (UNGC):** The UNGC is a voluntary initiative encouraging businesses worldwide to adopt sustainable and socially responsible policies. It is based on ten principles covering human rights, labor, environment, and anti-corruption, and encourages companies to report on their progress annually.

These frameworks and standards serve as essential tools for organizations to communicate their ESG performance effectively, meet stakeholder expectations, and contribute to global sustainability goals. The choice of framework often depends on the organization's industry, stakeholder requirements, and specific sustainability objectives.

Conclusion

ESG reporting is a strategic imperative for organizations striving to achieve long-term sustainability and stakeholder trust. Transparent and standardized ESG disclosures enable companies to address risks, attract investments, and foster resilience. However, challenges such as inconsistent standards, high costs, and greenwashing must be addressed to enhance the credibility and impact of ESG reporting. Future research should explore harmonizing global standards, leveraging technology, and developing innovative metrics for intangible ESG dimensions.

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