

ESG principles and social responsibility

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Abstract. In the face of escalating global challenges such as climate change, social inequality, and governance failures, corporations are increasingly adopting Environmental, Social, and Governance (ESG) principles and emphasizing Corporate Social Responsibility (CSR). This paper critically examines the integration of ESG principles into CSR strategies within the contemporary corporate landscape. We address challenges such as inconsistent reporting standards, data quality and availability, integration of ESG into investment decisions, conflicts between short-term financial results and long-term ESG goals, and regulatory variations across countries. Our findings underscore the need for harmonized ESG reporting standards and regulatory frameworks, the importance of comprehensive stakeholder engagement, and the necessity of viewing sustainability as a long-term strategic objective. The paper provides an in-depth understanding of how corporations can navigate these challenges, thereby aligning their operations with global sustainability goals and enhancing their societal impact. This analysis will benefit corporate leaders, policy-makers, investors, and scholars interested in the evolving intersections of ESG principles and CSR.

1 Introduction

In an increasingly globalized world, the role of corporations in society is changing. As key contributors to economic growth, their influence extends far beyond profit generation. Companies now have to consider a broader range of stakeholders, including employees, customers, communities, and the environment, in their decision-making processes. This shift has led to the rise of Environmental, Social, and Corporate Governance (ESG) principles and a renewed focus on social responsibility [1, 2].

ESG principles refer to a set of standards that guide the sustainability and ethical impact of an organization. The 'E' stands for environmental considerations, the 'S' for social aspects, and the 'G' represents governance standards. Collectively, these principles aim to ensure businesses operate in a manner that is sustainable, socially beneficial, and well-governed[3].

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2 History of ESG-principles regulation

International law does not specifically mandate the application of Environmental, Social, and Governance (ESG) principles. However, various international agreements, guidelines, and standards promote the principles that form the basis of ESG [4].

Here are some of the international frameworks that support ESG principles:

1. The United Nations Global Compact

The United Nations Global Compact is a voluntary initiative that encourages organizations to adopt sustainable and socially responsible policies, and to report on their implementation. It encompasses ten principles in the areas of human rights, labor, environment, and anti-corruption, which align closely with ESG principles[5].

2. The Principles for Responsible Investment (PRI)

Supported by the United Nations, the Principles for Responsible Investment (PRI) provides a framework for incorporating ESG factors into investment decision-making processes. It has six principles that focus on ESG issues in the context of investment practices[6].

3. OECD Guidelines for Multinational Enterprises (1976, revised in 2011)

These guidelines by the Organisation for Economic Co-operation and Development (OECD) provide non-binding principles and standards for responsible business conduct in a global context consistent with applicable laws and internationally recognized standards. The guidelines cover areas such as employment and industrial relations, human rights, environment, information disclosure, combating bribery, consumer interests, science and technology, competition, and taxation [7].

4. The United Nations Sustainable Development Goals (SDGs) (2015)

The United Nations Sustainable Development Goals (SDGs) consist of 17 goals designed to address the world's most pressing social and environmental challenges by 2030. Businesses around the world are encouraged to align their strategies and operations with these goals, which cover a broad range of ESG issues [8].

5. The Paris Agreement (2016)

The Paris Agreement aims to limit global warming to well below 2, preferably to 1.5 degrees Celsius compared to pre-industrial levels. This agreement involves financial commitments from countries and puts a strong emphasis on the need for businesses to transition towards a low-carbon economy, which is a key aspect of ESG's environmental pillar [9].

3 Social responsibility in the corporate context

Corporate Social Responsibility (CSR) refers to the commitment by businesses to act ethically and to contribute to economic development while improving the quality of life of the workforce and their families, the local community, and society at large [10]. It is an approach that integrates social and environmental concerns into business operations and interactions with stakeholders.

Ethics play a significant role in CSR. Corporate ethics policies guide businesses towards promoting honesty, fairness, and integrity. It involves adhering to laws and regulations, avoiding harm to the environment or communities, and abstaining from deceptive financial practices or false advertising [11].

CSR is not just about philanthropy; it is also about how businesses generate their profits. A company's economic responsibilities include being profitable for shareholders, creating jobs in the community, and stimulating economic growth. This requires corporations to engage in fair trade practices, ensure the safety and quality of their products or services, and

consider the full life cycle costs of their activities, including the environmental and social costs [10].

Businesses are expected to comply with the laws and regulations that govern their operations. This is seen as a fundamental duty in the corporate world. Legal responsibility encompasses a wide range of areas, from labor and employment laws to environmental regulations and fair trade practices [12].

Philanthropic responsibilities refer to the corporate actions that contribute to society beyond their economic, legal, and ethical responsibilities. These actions include making charitable donations, investing in community programs, supporting education, and providing voluntary services to the community [10].

While many businesses recognize the importance of CSR, implementing it effectively can be a challenge. Some of the issues include balancing the interests of different stakeholders, measuring the impact of CSR activities, integrating CSR into business strategies and operations, and communicating CSR efforts effectively to stakeholders[13].

4 The role of ESG in financial performance

The role of Environmental, Social, and Governance (ESG) factors in financial performance is a topic of significant interest among investors, companies, and regulators. While the specific relationship can depend on a variety of factors including industry, geography, and time horizon, there is a growing body of research indicating that strong ESG performance can positively influence financial performance.

1. Risk Management:

Companies with robust ESG practices are often better positioned to manage emerging risks, particularly those related to environmental and social issues. For instance, companies that proactively address environmental concerns may be less exposed to regulatory fines or reputational damage. This can help reduce volatility and potential losses, contributing to better financial performance [14].

2. Operational Efficiency:

ESG principles can drive operational efficiency. For instance, companies focusing on environmental principles often invest in resource efficiency measures (such as energy efficiency or waste reduction), which can result in cost savings. Similarly, good governance practices can improve decision-making processes and reduce the risk of costly scandals or litigation [15].

3. Access to Capital:

Investors are increasingly considering ESG factors in their investment decisions. This trend can influence a company's cost of capital, with research indicating that companies with strong ESG performance often enjoy a lower cost of capital [16].

4. Long-term Value Creation:

ESG factors can be crucial drivers of long-term value. For instance, a company's social practices (such as human capital management and stakeholder engagement) and governance structure (including board diversity and executive compensation) can significantly impact its long-term strategic success and profitability) [14].

5. Investor Returns:

Several studies have found a positive relationship between ESG performance and investment returns. While these results can vary depending on the specific methodologies and time horizons used, the general consensus is that ESG factors can have a material impact on investment returns [17].

5 Socially responsible investing and ESG

Socially Responsible Investing (SRI) and Environmental, Social, and Governance (ESG) principles are interconnected concepts that reflect the incorporation of ethical, social, and environmental considerations into investment decisions.

SRI, also known as sustainable, green, or ethical investing, is an investment strategy that considers both financial returns and social/environmental good to bring about positive change. It traditionally involved negative screening, i.e., excluding certain sectors (like tobacco, alcohol, or weapons) or companies based on ethical considerations. Over time, it has evolved to include positive screening (selecting companies that demonstrate social or environmental benefits) and impact investing (directing capital to solve social or environmental issues) [18].

ESG principles provide a set of criteria for assessing a company's operations in terms of its environmental impact (such as energy use, waste, and pollution), social responsibility (including labor practices, data protection, and community development), and governance (covering issues like corporate structure, executive compensation, and shareholder rights). These principles help to evaluate the potential risks and opportunities associated with sustainable business practices [3].

The integration of ESG factors into investment decisions is a key part of SRI. Investors use ESG data to assess how companies manage risks and opportunities related to environmental, social, and governance issues. This approach is based on the belief that such factors can have a material impact on a company's financial performance and, therefore, on investment returns.

In fact, the Principles for Responsible Investment (PRI), launched by the United Nations in 2006, encourage investors to use ESG factors in their decision-making process. The six PRI principles offer a global standard for responsible investing as it relates to ESG factors.

Many studies have examined the financial performance of SRI and ESG investments. While results can vary, a substantial number of studies suggest that incorporating ESG factors into investment decisions does not necessarily result in lower returns and may, in fact, enhance financial performance [17].

6 Case studies: successful ESG and social responsibility integration for civilians civil rights protection

I've observed numerous companies that have successfully integrated Environmental, Social, and Governance (ESG) principles and Social Responsibility (SR) into their business models, strategy, and operations. This integration often yields significant benefits, including enhanced reputation, reduced risk, operational efficiency, and long-term value creation. Here, I will explore a couple of these cases to elucidate the benefits and strategies of successful ESG and SR integration.

1. Unilever's Sustainable Living Plan

Unilever, a multinational consumer goods company, has been a pioneer in integrating sustainability into its business model. Unveiled in 2010, Unilever's Sustainable Living Plan aimed to decouple growth from their environmental footprint while increasing their positive social impact [19].

Unilever set ambitious goals such as halving the environmental impact of its products across the lifecycle by 2030, improving the health and wellbeing of more than a billion people by 2020, and sourcing 100% of their agricultural raw materials sustainably by 2020. Their approach involved extensive stakeholder engagement and transparency, comprehensive reporting, and an unwavering commitment to their goals, even when facing short-term costs or complexities. As of 2020, Unilever had made substantial progress towards these targets,

demonstrating that a commitment to ESG and SR can drive both sustainability and business success [20].

2. Patagonia's Responsible Business Model

Patagonia, an American outdoor apparel company, is renowned for its commitment to environmental and social responsibility. They've implemented initiatives such as using recycled materials in their products, investing in renewable energy, and supporting environmental nonprofits through their "1% for the Planet" pledge [21].

Moreover, Patagonia has proactively addressed social responsibility by providing onsite childcare, promoting fair labor practices, and advocating for policies like parental leave. Despite pursuing practices that may seem at odds with maximizing short-term profit, Patagonia has experienced strong financial growth, indicating that a commitment to ESG and SR can also yield financial benefits [22].

These cases demonstrate that successful integration of ESG and SR principles requires a long-term strategic commitment, stakeholder engagement, transparent reporting, and an ability to balance short-term costs with long-term benefits. These companies' successes offer inspiration and guidance for other businesses seeking to integrate ESG and SR principles effectively.

7 Challenges and opportunities in implementing ESG principles

The integration of Environmental, Social, and Governance (ESG) principles into business strategy and operations presents both challenges and opportunities for organizations.

Challenges in ESG Integration:

1. **Lack of Standardization:** The absence of standardized frameworks for ESG reporting poses a significant challenge for organizations. Different stakeholders may have varying expectations regarding the extent and nature of ESG disclosures [23].

2. **Data Quality and Accessibility:** Assessing ESG performance requires reliable, accessible, and timely data. However, many organizations struggle with data collection and analysis, complicating their ESG efforts.

3. **Short-term Financial Pressures:** Balancing short-term financial objectives with long-term ESG goals can be challenging. Companies often face pressure from shareholders to deliver immediate returns, which can conflict with the longer-term investments required for substantial ESG initiatives

4. **High Initial Costs:** Adopting ESG practices can require significant upfront investment, which might deter some organizations. These costs can arise from changing business processes, acquiring new technologies, or providing additional training for employees.

Opportunities in ESG Integration:

1. **Risk Management:** Organizations that adopt robust ESG practices can better manage and mitigate various risks, ranging from reputational to regulatory, thereby enhancing their business resilience [14].

2. **Operational Efficiency:** ESG initiatives can improve operational efficiency by promoting resource conservation, waste reduction, and process optimization, potentially leading to cost savings [15].

3. **Access to Capital:** Firms demonstrating strong ESG performance often enjoy better access to capital, as a growing number of investors and financial institutions prioritize ESG criteria in their investment decisions[25].

4. **Enhanced Brand Reputation:** Companies that successfully integrate ESG principles can enhance their brand reputation, potentially leading to increased customer loyalty and market share [26].

The implementation of ESG principles, although challenging, offers substantial opportunities for organizations. By addressing these challenges and capitalizing on the opportunities, businesses can achieve greater sustainability, resilience, and long-term success.

8 The incorporation of environmental, social, and governance (ESG) principles into national legislation

The incorporation of Environmental, Social, and Governance (ESG) principles into national legislation is a global trend, with several countries leading the way.

In France, for instance, the 2015 Energy Transition for Green Growth Act (Article 173) provides a robust example. This law requires asset managers and institutional investors to disclose how they incorporate ESG criteria into their investment decisions. They are also required to report on the carbon footprints of their portfolios, demonstrating how environmental considerations, specifically related to climate change, are embedded in the legal framework [27].

Similarly, in the United Kingdom, the Companies Act 2006 and The Pension Funds Act 2021 have made strides in integrating ESG principles into legislation. The Companies Act demands that directors report on a range of ESG risks that might affect their business. The Pension Funds Act goes a step further by mandating pension fund trustees to include in their statement of investment principles an explanation of how they consider ESG and climate change factors in their investment decisions [28].

Across the European Union, the Non-Financial Reporting Directive (NFRD) adopted in 2014, requires large companies to disclose information on their operational methods and how they manage social and environmental challenges. The goal of this legislation is to aid investors, consumers, policymakers, and other stakeholders in assessing the non-financial performance of large companies, encouraging responsible business practices [29].

China offers an example from the Asia-Pacific region. In 2007, the China Securities Regulatory Commission (CSRC) and the Environmental Protection Administration (EPA) introduced the Green Securities Policy. This policy requires listed companies to disclose environmental information and enforces penalties for non-compliance, marking a significant step in integrating environmental principles into China's legal and financial systems [30].

These examples underline the growing acknowledgment of ESG principles in lawmaking and regulatory practices worldwide.

9 The application of environmental, social, and governance (ESG) principles

The application of Environmental, Social, and Governance (ESG) principles is not without its challenges. Here are some of the most common issues faced by organizations and investors today:

1. **Inconsistent Reporting and Standards:** One of the main challenges is the lack of consistent reporting standards. Companies often have different interpretations and ways of reporting ESG data, which can make it difficult for investors and stakeholders to compare and assess performance[3].

2. **Data Quality and Availability:** ESG data is often incomplete, inconsistent, or non-comparable. This is due to a lack of uniform reporting requirements, as well as the fact that many companies are still in the early stages of incorporating ESG principles into their operations[17].

3. Integration into Investment Decisions: While awareness and interest in ESG factors have grown, many investors still struggle with how to integrate these factors into their investment decisions. This is partly due to the aforementioned issues with data quality and comparability [31].

4. Short-term vs. Long-term Goals: Companies often face pressure to deliver short-term financial results, which can conflict with the longer-term nature of ESG goals. Achieving sustainability often requires significant upfront investment and the benefits may not be realized for many years [32].

5. Regulatory Differences: Different countries have different regulations and standards when it comes to ESG. This can create complexities for multinational corporations trying to apply ESG principles across their operations [33].

10 Future directions: ESG Principles, social responsibility, and corporate sustainability

In considering the future of Environmental, Social, and Governance (ESG) principles, social responsibility, and corporate sustainability, we see a roadmap with several key milestones. An increase in regulatory oversight is anticipated. As societies worldwide become more conscious of environmental and social issues, regulations to ensure businesses meet ESG standards are likely to become more rigorous[34].

Another milestone is the growing attention investors are paying to ESG factors. Recognizing that these factors can significantly impact a company's financial performance and risk profile, investors are expected to increasingly incorporate ESG factors into their investment decisions [17].

In terms of reporting and disclosure, advancements towards standardizing ESG reporting will likely lead to enhanced transparency and comparability among businesses across industries [35]. Additionally, future developments in technology and big data analytics are set to offer more detailed and robust ESG data, thereby improving ESG performance measurement and management.

We also anticipate a stronger integration of ESG considerations into supply chain management, thereby extending sustainability initiatives beyond a company's operations to include its suppliers.

In terms of governance, businesses are expected to focus more on social and governance aspects, such as diversity and inclusion, fair labor practices, privacy and data security, and corporate ethics [36].

Lastly, the push for sustainability is likely to inspire innovative business models based on principles such as circular economy, renewable energy, and sustainable consumption [37].

Overall, while the path to fully integrating ESG principles, social responsibility, and corporate sustainability into business practices may be challenging, those companies that successfully navigate this transformation can reap substantial benefits including competitive advantage, operational efficiency, risk mitigation, and enhanced stakeholder relationships.

11 Conclusion

The integration of Environmental, Social, and Governance (ESG) principles into businesses, financial markets, and legal frameworks represents a significant global shift towards sustainable development. These principles are not only pivotal in driving responsible investment and operational behaviors but also in shaping regulations and national legislation.

Historically, ESG principles have been a core component of international law, treaties, and conventions. Today, their importance is magnified by the increased global urgency to

address environmental and social challenges. The application of ESG principles, while presenting certain problems such as lack of standardization and data quality issues, also provides considerable opportunities, including enhanced brand reputation, improved operational efficiency, and better access to capital.

Corporate social responsibility plays a crucial role in this context, providing a foundation for businesses to engage in ethical practices, value creation, and stakeholder management. Empirical evidence suggests a strong relationship between ESG integration and financial performance, emphasizing the financial viability of socially responsible investing.

Notwithstanding the challenges in implementing ESG principles, case studies provide numerous examples of successful ESG and social responsibility integration. Looking forward, it is expected that these principles will drive innovations in business models, shape national legislations, and become more prominent in investment decision-making.

In essence, ESG principles, social responsibility, and corporate sustainability are not just emerging trends, but essential factors for future business resilience and success. This transformation is inevitable and those organizations that effectively navigate this change stand to gain significant competitive advantages, proving that sustainability and profitability are not mutually exclusive but rather mutually reinforcing goals.

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