

### Steve Lydenberg

This paper argues that the social factors that have driven increased voluntary environmental, social, and governance (ESG) disclosure over the past three decades are sufficiently compelling to lead to mandated disclosure worldwide. Whether ESG data will then be fully integrated into corporate management and investment practices ultimately depends on the willingness of governments, stock exchanges, and the accounting profession—along with corporations, investors, consumers, and other members of society—to acknowledge the essential role these data can play in bringing about the alignment of market forces with society’s interests.

### Foreword

An old management adage says *you get what you measure*. That’s why any decent MBA program will ensure that its students graduate with a keen knowledge of both management and financial accounting. The rationale is that every manager should not only know how profit is generated, but also be able to report on it to investors, regulators, and other stakeholders.

Few of us today doubt the significance of the environmental and social pressures the world is under. Nor can we doubt the significance of private sector activity both in generating these difficulties and in helping resolve them. Yet there is still no mandate enforcing either the measurement or the disclosure of sustainability.



Global Corporate Governance Forum



IFC Global Corporate Governance Forum supports corporate governance reforms in emerging markets and developing countries. The Forum develops advanced knowledge and training products promoting good practices in corporate governance and facilitates capacity building of director training organizations engaged in implementing corporate governance reforms.

The Forum partners widely with international, regional and local institutions, and draws on the guidance of its global network of private sector advisors and academic research network.

The Forum is part of the **IFC Corporate Governance Group**, located in the Environment, Social and Governance Department. It is a donor-supported facility, co-founded in 1999 by the World Bank and the Organisation for Economic Co-operation and Development (OECD).

In this Private Sector Opinion, Steve Lydenberg describes some of the numerous initiatives that have attempted to resolve this problem. Many dedicated people and groups—nongovernmental organizations and stock exchanges, investors and regulators, and private information providers such as Bloomberg and Trucost—have been trying for a generation to promote disclosure. Even His Royal Highness The Prince of Wales has added his voice to those calling for corporate disclosure. All of these advocates understand that you get what you measure, and that if we are to have a sustainable planet then we had better measure the degree to which the private and public sectors manage their current activity so that we, collectively, live within planetary boundaries.

Lydenberg recommends that we establish a single global standard—and mandate reporting against it—as the best way forward. He is right, but this approach faces some challenges. Most of the obstacles should be easy to address, but so far they remain frustratingly intractable.

For instance, there is the question of whose standards: who determines the standards to be reported against? It is a good question. But we need to be careful not to let the best become the enemy of the good. True, there are significant difficulties in deciding what sustainability standards might look like. But exactly the same problem existed when financial accounting reports were first mandated in the 19th century. The solution then—which may inform us now—was not to wait until agreed standards were set, but rather to ask the board of the company to make best efforts to report, and to ask an auditor to verify that what had been reported was a “true and fair” depiction of the company’s state of affairs.

A second challenge concerns capability. Some companies find reporting to be too difficult and complex. Again, we may borrow a solution from other approaches to corporate governance. Where it is difficult to mandate best practice, for example, regulators have put in place a “comply or explain” regime: the company either reports or explains why not. Rather than fail to report, companies usually do their best to comply.

*David Pitt—Watson*

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# Emerging Trends in Environmental, Social, and Governance Data and Disclosure: Opportunities and Challenges

Steve Lydenberg<sup>1</sup>

Now well into the second decade of the 21st century, we've seen substantial progress in promoting the disclosure of corporations' environmental, social, and governance (ESG) policies and practices. Governments, investors, and corporations themselves encourage making this information available, because it can play a valuable role in managing corporations, assessing their long-term risks and rewards, and aligning their policies and practices with those of society.

However, how the disclosure of corporate ESG data in the future will ultimately play out remains uncertain. Three scenarios are possible:

- Corporate disclosure of ESG data will remain essentially voluntary, with all the problems of inconsistency and irregularity that voluntary disclosure inevitably entails. Without institutionalization, it becomes little more than a passing fad and eventually fades.
- ESG disclosure will be mandated worldwide, with regular reporting in reasonably comparable formats. Corporate ESG reports continue to be published and evaluated separately from the strategic management of corporations and from the primary considerations of investment decision making.
- ESG disclosure will be integrated with corporations' financial disclosures, merging these two realms and placing them on equal footing. Integrated disclosure leads to fundamental changes in corporate management and in investment practices.

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<sup>1</sup> Steve Lydenberg, a partner in Strategic Vision for Domini Social Investments, has over three decades of experience in the responsible investment field, with KLD Research & Analytics and Trillium Asset Management, among other organizations. A founding director of the Initiative for Responsible Investment at the Hauser Institute for Civil Society at Harvard University, he is author of "Reason, Rationality and Fiduciary Duty" and "On Materiality and Sustainability: The Value of Disclosure in the Capital Markets" as well as several books on responsible investment, including *Corporations and the Public Interest* (Berrett-Koehler) and *Dilemmas in Responsible Investment* (Greenleaf) with Céline Louche.

This paper argues that the social factors that have driven increased voluntary ESG disclosure over the past three decades are sufficiently compelling to lead to mandated disclosure worldwide. Whether ESG data will then be fully integrated into corporate management and investment practices is more problematic and ultimately depends on the willingness of governments, stock exchanges, and the accounting profession—along with corporations, investors, consumers, and other members of society—to acknowledge the essential role these data can play in bringing about the alignment of market forces with society’s interests.

### Evolution of ESG disclosure

More than 10,000 corporations and other organizations had issued ESG reports as of 2013.<sup>2</sup> These reports are variously classified as sustainability, corporate social responsibility, citizenship, or environmental, health, and safety reports and vary substantially in the specifics and thoroughness of the data they disclose. Their present incarnation represents one aspect of the relatively long and varied evolution of ESG reporting. Three broad phases in this evolution can be distinguished, corresponding generally to an increasingly sophisticated understanding of the meaning of corporate social responsibility (CSR) and the related concept of sustainability.

ESG reporting had its origin in corporations’ philanthropy and community-affairs programs. In the 1970s in the United States, for example, companies with a major role in the national economy, such as General Motors and Ford, or in local economies, such as Cummins Engine in Columbus, Indiana, were leaders in issuing reports on their philanthropic and community involvement. At that same time, companies in the life insurance industry joined to form the Clearinghouse on Corporate Social Responsibility through which they invested in and reported on their economic development programs in inner cities.<sup>3</sup>

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<sup>2</sup> See the website of The Corporate Register at <http://www.corporateregister.com/>, last accessed October 1, 2013.

<sup>3</sup> See Kirstin Moy, Debra Jensen, and Karen Murrell, *Community Investment in the Insurance Industry*, prepared for Altrushare Securities, November 2009, at [http://altrushare.com/pdf/Insurance\\_Industry\\_Nov2009.pdf](http://altrushare.com/pdf/Insurance_Industry_Nov2009.pdf), last accessed October 1, 2013.

Similarly today in developed and emerging markets, corporations establishing CSR programs for the first time frequently create and report on programs that are confined to charitable giving and local community development. Although these CSR initiatives suggest that corporations recognize their obligations to their communities, they often are limited, paternalistic, and unrelated to core business strategies—and do not confront the firms' major controversies or affect their core business strategies.

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Starting in the 1970s, a second approach to disclosure of ESG data was adopted by legislatures and regulators, initially in the United States and soon thereafter elsewhere. In response to widely publicized crises and scandals, governments mandated the disclosure of issue-specific data. The 1984 Bhopal disaster, for example, led directly to the passage of the Emergency Planning and Community Right-to-Know Act (1986) that required most U.S. companies to report on the storage, recycling, and release of toxic chemicals at their plant sites. Other countries throughout the world have followed suit with similar toxics-release legislation, including Mexico where such data became available starting in 2006.<sup>4</sup>

Since the 1970s, governments have used legislation and regulation to mandate the disclosure of other specific ESG data sets. In 1975, for example, in response to concerns about unfair bank lending practices, the United States enacted the Home Mortgage Disclosure Act, which forced banks to disclose the amounts and locations of their lending. In 1977, in response to a series of widely publicized scandals, the U.S. Congress passed the Foreign Corrupt Practices Act, which prohibits U.S. corporations from making bribes overseas, while the Securities and Exchange Commission required disclosure of such bribes. In emerging markets in recent years, corporate governance policies have been the subject of extensive regulatory and disclosure requirements, with countries such as South Africa, the Philippines, Hungary, and Malaysia leading the way.<sup>5</sup>

<sup>4</sup> For a summary of the Mexican legislation, see <http://www.rtknet.org/files/MexicoPRTR.pdf>, last accessed October 1, 2013.

<sup>5</sup> See United Nations Conference on Trade and Development, *Corporate Governance Disclosure in Emerging Markets: Statistical Analysis of Legal Requirements and Company Practices* (New York and Geneva: United Nations, 2011): 9.

These regulatory actions often occur in response to environmental or social crises or controversies and can be detailed in their reporting requirements. However, these issue-specific reports capture only a relatively random set of ESG data without providing a comprehensive overview of companies' records.

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In the late 1990s, the increasingly apparent need for more systematic ESG disclosure prompted the creation of several global initiatives—including the Global Reporting Initiative (GRI) and the United Nations Global Compact—that have made comprehensive disclosure of ESG data worldwide one of their primary goals. These initiatives—stressing broad stakeholder engagement, the incorporation of international norms and standards, and voluntary disclosure—have been remarkably successful in

increasing availability of ESG data. According to CorporateRegister.com, the number of corporations and other organizations issuing CSR or sustainability reports has risen from relatively few in the early 1990s to over 10,000 by 2013. As of that year, the GRI maintained a database of some 14,000 sustainability reports from over 5,000 organizations, based to a greater or lesser extent on its reporting framework.<sup>6</sup>

The best of this new breed of CSR reports represent a quantum leap in comprehensiveness over more limited philanthropic-oriented reports and issue-specific, government-mandated disclosure requirements. Nevertheless, many of these new reports remain idiosyncratic in their form and content and sporadic in their publication.

### **Forces driving mandated disclosure**

The need for regular, consistent, and comparable data is not the only compelling factor in the push toward mandated CSR reporting. A number of long-term, fundamental trends are also driving this need. Among them are the following:

<sup>6</sup> See the GRI database, at <http://database.globalreporting.org/>, last accessed October 1, 2013.

***Lack of trust in finance.*** As a result of more than a decade of scandals and crises, the financial services and banking industries are now among the least trusted in our society.<sup>7</sup> Moreover, traditional financial accounting is no longer seen as adequate or trustworthy. Two pieces of major legislation aimed at reforming accounting standards and banking practices have been passed in the United States since 2000 (Sarbanes-Oxley in 2002 and Dodd-Frank in 2010) without producing an apparent increase in trust in either.

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***Materiality and the long-term investor.*** For institutional investors the potential long-term financial impact of environmental and social issues such as climate change and water scarcity is increasingly apparent.<sup>8</sup> As sovereign wealth funds and national and local pension funds grow in size, their long-term perspective in the marketplace is increasingly driving the demand for data on such issues, which have long-term financial, as well as sustainability, implications for society and the environment.

***Demographics.*** As the world rapidly approaches a population of nine billion, the complexity of problems increases, as does the interrelatedness of the parties that must participate in their solutions. To cite just one example, it takes extensive, coordinated efforts by governments, nongovernmental organizations, and corporations to assure safe and fair working conditions at vendors to the apparel and footwear industries. Without substantial monitoring and accompanying data, these complex problems cannot be adequately addressed.

***Social justice.*** As hundreds of millions of people around the world are lifted out of extreme poverty, they are voicing legitimate demands for access to medicines and health care, to telecommunications and information technology, and to financial services on a par with those of their better-off peers.<sup>9</sup> Knowing which companies have committed resources, and in what ways, to serving the bottom of the pyramid is essential to making progress toward satisfying these demands.

<sup>7</sup> See "2013 Trust Barometer Reports Financial Services is Least Trusted Industry Globally," at <http://www.edelman.com/news/2013-edelman-trust-barometer-reports-financial-services-is-least-trusted-industry-globally/>, last accessed October 8, 2013.

<sup>8</sup> For climate change and water and their relevance to long-term institutional investors, see the studies published by the Boston-based organization Ceres, "Assessing Water System Revenue Risk: Considerations for Market Analysts" and "Global Investors Survey on Climate Risk 2013," at <http://www.ceres.org/resources/reports>, last accessed October 8, 2013.

<sup>9</sup> See the website for the Access to Medicines Index for an example how ESG data is currently used to assess the performance of the pharmaceutical industry on access to medicines, at <http://www.accessmedicineindex.org/>, last accessed October 8, 2013.

**Natural resources.** Our omnivorous consumer society is posing a dual environmental challenge. The capacity of our ecological systems to absorb the wastes generated by this consumption is in doubt, as witnessed by the increasing concentration of carbon dioxide in our atmosphere and the pollution of our lakes, rivers, and even oceans. In addition, the capability of the stocks of certain essential natural resources to feed ongoing consumption is questionable. Various rare earths and precious metals, for example, are already in short supply, and phosphate fertilizers may soon be also.<sup>10</sup>

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These five secular trends are important to the mainstream financial community, as can be seen in the growing number of signatories to the Principles for Responsible Investment, including asset owners and asset managers of some \$35 trillion. In addition, large pension and sovereign wealth funds—such as the Norwegian Pension Fund, the Netherlands-based PGGM (also known as PFZW), and the California Public Employees Retirement System—

incorporate the language of sustainability and responsible investment into their policies and practices.<sup>11</sup>

### Who will mandate?

Assuming that mandated disclosure of ESG data is desirable, who can impose such requirements? Legislators and regulators, stock exchanges, and the accounting profession are best positioned and most likely to fill this role.

*Government*, through legislation or regulation, is unquestionably capable of mandating ESG disclosure. In a number of developed and emerging markets, governments have already imposed various reporting requirements. Those legislated by France are among the most extensive and specific, with a 2001 law requiring its largest publicly traded companies to report annually on some 40 key ESG indicators along with their financial data.

<sup>10</sup> On supplies of phosphate fertilizers, see Tom Philpott, “Are We Headed toward Peak Fertilizer?” Mother Jones, November 28, 2012, at <http://www.motherjones.com/tom-philpott/2012/11/are-we-heading-toward-peak-fertilizer>, last accessed October 1, 2013.

<sup>11</sup> In 2013, *Responsible Investor* initiated an awards program for the large and small pension funds reporting best on their sustainability and responsible investment practices. For a listing of some of the pension funds with the best reporting on sustainability and responsible investment practices, see [http://www.responsible-investor.com/events/events\\_page/ri\\_reporting\\_awards\\_2013\\_results/](http://www.responsible-investor.com/events/events_page/ri_reporting_awards_2013_results/). CalPERS and PGGM (aka PFZW) were among those receiving an award.



A number of emerging-market nations already impose CSR disclosure requirements. In 2010, for instance, the Indonesian government required companies listed on its stock exchanges to start reporting on the effects of their activities on society and the environment. Indian law requires major listed companies to implement and report on CSR programs to which two percent of earnings must be devoted. Taiwan's financial market regulator mandated CSR disclosure by all listed companies in 2008. And since 2007, Malaysian law compels listed companies to publish CSR information in their annual reports.<sup>12</sup> While national governments have the capability to assure that major firms report CSR data, the approaches adopted for these reporting requirements vary considerably from nation to nation in their scope, level of detail, and stringency.

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*Stock exchanges*, through their listing requirements, offer a second promising avenue for mandating disclosure of ESG data. Emerging-market countries have taken a lead in this approach, frequently viewing ESG disclosure as a means of enhancing the attractiveness of their companies to investors. The JSE (Johannesburg Securities Exchange), for example, in 2004 launched its Socially Responsible Investment index, which encouraged CSR disclosure, and then in 2009 required listed companies to integrate their sustainability and financial reporting.

In 2007, Bursa Malaysia (formerly Kuala Lumpur Stock Exchange) created a framework for CSR reporting and encouraged listed companies to include CSR disclosure in their annual reports. In 2010, the Hong Kong stock exchange launched its Corporate Sustainability Index, and the Shanghai stock exchange announced the creation of its Environmental Protection Index. As of 2012, Brazil's Bovespa stock exchange requires listed companies to publish CSR reports or explain why they do not.<sup>13</sup>

<sup>12</sup> See the website of the Initiative for Responsible Investment for a listing of such requirements by governments and stock exchanges around the world, at <http://hausercenter.org/iri/about/global-csr-disclosure-requirements>, last accessed October 8, 2013.

<sup>13</sup> A number of these stock exchanges are working through the UN-affiliated Sustainable Stock Exchanges Initiative to promote these policies and practices. See the website of this organization for further details, at <http://www.sseinitiative.org/>, last accessed October 8, 2013. See also "Carrots and Sticks Promoting Transparency and Sustainability: An update on Trends in Voluntary and Mandatory Approaches to Sustainability Reporting," 2009, at <https://www.globalreporting.org/resource/library/Carrots-And-Sticks-Promoting-Transparency-And-Sustainability.pdf>, last visited October 14, 2013.

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Because global stock exchanges are relatively few and have an interest in standardization of policies, they represent a potential avenue for the coordinated implementation of standardized disclosure standards. In 2013, to encourage standardized disclosure among stock exchanges globally, CERES, the Investor Network on Climate Risk and a coalition of responsible investors submitted to NASDAQ a proposed model for the consistent integration of ESG data disclosure into the listing requirements for all stock exchanges worldwide.<sup>14</sup>

*Accounting standards* provide a third avenue for the effective mandating of ESG disclosure. Such standards could potentially be developed and maintained through methods similar to those the Financial Accounting Standards Board uses for financial data in the United States. This is the approach currently advocated by the newly created Sustainability Accounting Standards Board (SASB). Starting in 2013, SASB embarked on the development of a set of sustainability key performance indicators that are the most material for specific industries. In addition, the International Integrated Reporting Council (IIRC), based in the United Kingdom, advocates the integration of ESG data into financial reporting to help investors assess companies' full value-creation potential. The IIRC draws much of its expertise and proposed disclosure principles from the accounting profession. Its goal is publication—in a single annual report—of both the ESG data and the financial data most material to the long-term success of the firm.<sup>15</sup>

It is difficult to predict which of these three approaches will be the first to find a means to mandate the systematic disclosure of ESG data on a global scale. Stock exchanges, through listing requirements, offer a relatively straightforward mechanism to attain that end, but all three approaches in their different ways are likely to play important roles.

<sup>14</sup> See "Investors Announce Proposal for Sustainability Listing Standard for Global Stock Exchanges," press release, April 8, 2013, at <http://www.ceres.org/press/press-releases/investors-announce-proposal-for-sustainability-listing-standard-for-global-stock-exchanges>, last accessed October 8, 2013.

<sup>15</sup> See <http://www.sasb.org/wp-content/uploads/2013/07/SASB-Outcome-Review-Report-Healthcare.pdf> for an example of SASB's sustainability key performance indicators for the health-care industry. Also see <http://www.theiirc.org/consultationdraft2013/> for its consultation draft of proposed guidelines for the integration of ESG and financial reporting, last accessed October 8, 2013.

## Integration as a pathway to fundamental change

If disclosure of ESG data is to serve as an effective tool in addressing challenges that are among the most pressing of the 21st century, the data need to be integrated into both corporate management and investment decision making.

Currently, even among corporations with the most advanced CSR programs, CSR functions tend to be compartmentalized, with corporate philanthropy, diversity, human resources, ethics, vendor standards, and environment, health, and safety operating separately in their different realms. Equally serious is the failure of top management and boards of directors to incorporate CSR considerations into strategic decision making. CSR measurement and goal setting may be communicated to and approved by both, but they are only rarely integrated into the long-range strategic planning and the basic business models of corporations. The internal availability of CSR data is a necessary prerequisite for this integration to take place.

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It's not easy to include ESG factors in strategic management and the development of business models. Doing so requires thinking that runs counter to much currently accepted management dogma. To begin with, it favors the stakeholder model rather than the stockowner model of the corporation. This shift effectively implies commitments to strategic investments in employees, customers, suppliers, communities, and the environment in ways that produce rewards for stockowners as well as for these stakeholders. It also means favoring the long term over the short term in the myriad situations where sustainability concerns arise. Monitoring of matters relating to the future sustainability of the environment and society, while at the same time pursuing corporate profitability, frequently necessitates long-term thinking and planning. Today's dominant emphasis on short-term profit maximization makes it difficult to consider the implications of ESG data in strategic management—and the fundamental changes that such consideration suggests.

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The second fundamental change in thinking that the comprehensive integration of ESG and financial data implies manifests itself in investment decision making. Today's investors typically define their goal either as beating an asset-based benchmark (for example, the performance of their portfolio versus that of a stock index) or as matching that benchmark at the least possible price (such as making automated trades in entire stock indexes). The former strategy is known as active management, the latter as passive.

Active managers currently incorporate financial data—but only occasionally ESG data—in projecting the future prospects of a company. Passive investors tend to ignore the specifics of both financial and ESG data related to specific stocks. Neither involves the comprehensive integration of ESG data.

The comprehensive integration of ESG data into investment decisions implies an approach akin to that advocated by proponents of the universal owner theory.<sup>16</sup> Universal owners are those who have portfolios so large that they represent, and have the potential to affect, the economy—the world beyond their portfolios. Individually—as well as collectively with other investors—their decisions have substantial implications for how our economy operates as well as for the preservation or destruction of environmental systems and the creation, preservation, or deterioration of valuable social assets.

*Sovereign wealth funds around the world, which cumulatively had assets under management of approximately \$6 trillion as of 2013, have an ability to influence entire economies along with a long-term interest in assuring that global economies thrive.*

The ESG records of particular companies, or of whole industries, help these investors understand the ramifications of their decisions beyond the limited bounds of their portfolios. For these investors, measurement of short-term, or even long-term, stock price relative to a benchmark is no longer the sole relevant investment consideration. Their goals include not only strong returns for their portfolios but also the preservation or enhancement of social and environmental assets throughout the economy.

Only through the comprehensive integration of ESG data can they make investment decisions that achieve these twin goals. Sovereign wealth funds around the world,

<sup>16</sup> This theory was first propounded by Robert Monks and Nell Minnow and later elaborated by James Hawley and Andrew Williams in *The Rise of Fiduciary Capitalism: How Institutional Investors Can Make Corporate America More Democratic* (Philadelphia, Pennsylvania: University of Pennsylvania Press, 2000): xv. See also Monks and Minnow, *Watching the Watcher: Corporate Governance in the 21st Century* (Cambridge, Massachusetts: Blackwell Publishers, 1996).

which cumulatively had assets under management of approximately \$6 trillion as of 2013,<sup>17</sup> are a primary example of what can be termed universal investors, having an ability to influence entire economies along with a long-term interest in assuring that global economies thrive.

## Implications for the future

The existence of mandated disclosure of systematic ESG data will in all likelihood open new avenues for academic research, new strategies for investment professionals, and increasingly nuanced governmental regulation. To date, most academic research using ESG data has focused on the relationship between a firm's CSR management and its profitability and on the relationship between investors' use of ESG criteria and their portfolio-level returns.<sup>18</sup>

Additional ESG disclosure will enable—and indeed call for—research into valuation models that assess the positive and negative ESG externalities created by corporations. This new approach to valuation is particularly challenging, because externalities as economists define them are factors that markets have not priced or cannot price. If valuations of ESG externalities are to be expressed in financial terms, then, by definition, markets need to be created for them or regulators need to impose costs on them—that is, they need to be internalized. The challenge of creating such markets or imposing such costs can be substantial, as can be seen in the ongoing efforts to create markets for the price of carbon emissions or to impose some level of legal liability on those responsible for greenhouse gas emissions. The creation of alternative non-price-related valuation methods may sound like a daunting task, but it is not inconceivable given the non-price-related fundamentals implicit in many matters of ESG concern.

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<sup>17</sup> For estimates of the assets under management of sovereign wealth funds, see <http://www.swfinstitute.org/fund-rankings/>.

<sup>18</sup> For an overview of research on the relationship between responsible investing and financial performance, see Lloyd Kurtz, "Looking Forward, Looking Back: A Hitchhiker's Guide to Research on Social and Sustainable Investment," which may be purchased at <http://fsinsight.org/insights/detail/looking-forward-looking-back-a-hitchhikers-guide-to-research-on-social-and-sustainable-investment>, last accessed October 8, 2013.

The availability of comprehensive ESG data will also facilitate—and call for—their incorporation into corporate strategic planning and the scenario building that is so often part of this planning, given the uncertain nature of the future in business. Corporate managers frequently use scenario building as a tool for envisioning their firm’s options in the face of future uncertainties. Theorists of ecological sustainability frequently stress the importance of scenario building in the assessment of environmental systems.<sup>19</sup> Although a handful of corporations concerned about sustainability issues—such as Ford and Shell—have experimented with sustainability-related scenario building, few have incorporated ESG data into the scenario-building aspects of their strategic planning. Research and experimentation are needed to explore the potential usefulness of this approach for corporate managers and long-term investors.

In addition, the availability of comprehensive ESG data may have implications for corporate and financial fiduciaries. Although the fiduciary duties of the two differ in certain respects, recent decades have seen both directed to pursue “maximization”

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principles—the corporate toward maximization of company profits, the financial toward maximization of portfolio returns. Some scholars now question the appropriateness of this direction, pointing out that company directors have a fiduciary duty to the corporation and its long-term viability, not to the stockowners and their profits-driven stock price; and that trustees of financial assets have a duty to their beneficiaries’ best interests, not to a portfolio and its returns relative to a benchmark.<sup>20</sup> The integration of ESG data into strategic management and investment decision

making may inform and modify the current emphasis on “maximization” as a fiduciary principle—perhaps in favor of such principles as preservation and sustainability, for example.

<sup>19</sup> See Simon Bell and Stephen Morse, *Sustainability Indicators: Measuring the Immeasurable?* (London: Earthscan, 2008).

<sup>20</sup> See, for example, Lynn Stout, *The Shareholder Value Myth: How Putting Shareholders First Harms Corporations and the Public* (San Francisco: Berrett-Koehler Publishers, Inc., 2012). Also see James Hawley, Keith Johnson, and Ed Waitzer, “Reclaiming Fiduciary Duty Balance,” *Rotman International Journal of Pension Management* 4, no. 2 (Fall 2011). Also, Steve Lydenberg, “Reason, Rationality and Fiduciary Duty,” *Journal of Business Ethics*, published electronically (January 2013), at <http://link.springer.com/article/10.1007%2Fs10551-013-1632-3#page-1>.

Finally, the existence of comprehensive ESG data should help regulators and legislators make better informed and more nuanced decisions on when and to what extent regulation and reform are—or are not—necessary. Currently, governments operate with only partial views of the extent and implications of corporate practices in social and environmental matters. Not surprisingly, they are often driven by current crises and daily headlines focusing on single issues when it comes to taking regulatory action. More complete ESG data will help these public agents take a longer-term, more comprehensive view when considering regulation in the public interest.

## Conclusion

I believe that the mandating of systematic ESG disclosure is at this point inevitable. Governments, stock exchanges, and the accounting profession have gone too far down the road to ESG disclosure to turn back now. Its prospective importance to investors, governments, and academics has been too clearly demonstrated to abandon its pursuit. Disclosure of ESG data has the potential to help address systemic challenges such as trust in corporations and the financial markets, the realization of social justice, the achievement of environmental sustainability, and the efficient allocation of assets.

How effectively comprehensive ESG data will ultimately be put to use will depend on the ability of corporate managers and institutional investors to comprehend the long-term benefits that the incorporation of these data into daily practice can have—benefits that accrue to not only their own operations but also to society more broadly, benefits that it will be necessary to realize if the challenges of a mid-21st century world with nine billion people are to be met. Once these ESG data have been disclosed, then the hard work of realizing their full potential begins—for all of us. The sooner the disclosure is mandated, the sooner this hard work can begin.

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