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ESG Strategies for Boards

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Compliance with ESG will help maintain the interdependence of the earth's varied elements, ensuring a viable and sustainable future for humanity. Furthermore, it will open up a plethora of commercial prospects.

Business Sustainability (BS) has become one of the prime issues for any company seeking long-term growth. ESG (Environment, Social, and Governance) holds the key to business sustainability. In fact, ESG bodes well for the planet, society, and human beings as a whole. Companies will have to brace themselves and start embedding ESG as an integral agenda item in their boardroom discussions, strategies, and follow-up action plans. A recently released study by Deloitte in India indicates that only 27% of businesses feel that they are adequately equipped to be compliant with ESG. There is a dire necessity for corporate India to take note and start getting ready with the preparedness for ESG compliance, as India has pledged certain goals at the world forum, COP-26.

Background

The Paris Agreement of 2015, also known as COP-21, was the first legally binding international treaty signed by 196 countries on climate change. The United Nations summit on Sustainable Development was held on September 25–27, 2015, in New York, and its charter was adopted in the form of the 17 Sustainable Development Goals (SDG-2030) for attainment by 2030. The pledge for Net Zero was also taken with the objective of cutting greenhouse gas emissions to an ideal zero level. Various nations clearly stated their NDCs (Nationally Determined Contributions) at the COP-26 in Glasgow. Prime Minister Narendra Modi's 5-point programme called 'Panchamrit' (five nectars) outlined India's goals, which are: increase in non-fossil energy capacity to 500 GW; meet 50% of energy requirements through renewable energy (RE); reduce carbon emissions by 1 billion tonnes; reduce carbon intensity in the Indian economy by 45% by 2023; and achieve net zero by 2070. The government has declared green growth as one of the seven priority areas in the budget for the years 2023–24. The board of directors needs to steer the efforts of corporations in this direction.

Global Bodies and Standards

Various global standards, such as GRI, SASB, UNGC, TCFD, and others, have been established to facilitate doing business with higher ESG compliance. The Indian government and the corporate sector have commitments to fulfil as members of the Committee of Nations. SEBI has already laid down guidelines by laying down a framework for reporting via BRSR for the top 1000 companies from 2022–23 onward. Various companies have set their net zero goals in that direction and have aligned their ESG efforts with Net Zero and the SDGs. That is where the BoD has the onerous responsibility of achieving these targets in a time-bound manner. This calls for a deliberate strategy and meticulous and disciplined execution thereof.

ESG Risks

Implementation of the SDGs and Net Zero pose many physical, operational, financial, regulatory, reputational, political, and transitional risks. Physical risks are already visible in the form of air, water, soil, and oceanic pollution, as well as the loss of biodiversity, lives, and infrastructure. Greenhouse gas (GHG) emissions have led to air pollution and global warming, leading to an increase in sea levels and the recurrence of typhoons, cyclones, hurricanes, wildfires, floods, and draughts. These have resulted in the destruction of property and the loss of biodiversity and human life. All this and cyber fraud lead to huge financial losses. Reputational risk has an irreparable impact on brand value, market value, and the reputation of the organisation. The regulatory risk always looms large, as almost all the regulatory framework is rule-based in nature, and all compliance issues need to be met meticulously. If not met, it may lead to reputational and financial losses. The transition risk arises from the switch from the present state to the aspired state. The EU has already passed the bill for the Carbon Adjustment Border Mechanism (CBAM), whereby carbon emissions will be charged on steel, aluminium, fertilisers, cement, hydrogen, and electricity. This will have a $10 billion impact on Indian trade. This may also cause a domino effect, with other countries passing similar legislation. Political hazards require careful consideration and policy formulation. Although geopolitical risks such as the Ukraine War, US-China tensions, and so on are beyond any company's control, they must be considered.

Gaps between the Goal and Reality

There are gaps between the NDCs and the current scenario. Currently, India's solar energy capacity is 63.89 GW, as against 280 GW projected by 2030 (out of an overall 500 GW of RE). A capacity of 140 GW has been projected for wind energy, which is much beyond the current capacity of 42.8 GW. India's emissions in 2021 were 2.7 GT (gigatons) and could increase to 3.9 GT by 2030. This calls for a comprehensive decarbonization strategy that would encompass all sources of carbon emissions. As per the study carried out by the RBI, this would require an investment to the tune of 2.5% of GDP. The cost of green hydrogen, which is currently at Rs 300 per kg and is slated to drop to Rs 160–170 by 2030, remains a challenge as it will not be competitive.

Furthermore, in comparison to the aim of 5 MMT by 2030, the present capacity is almost nonexistent. Water stress caused by increased pollution and scarcity necessitates remedies. There is still more work to be done to ensure social equality, inclusivity, and diversity. Furthermore, annual growth rates of more than 6-7% must be maintained.

Business Opportunities

ESG presents a wide range of business opportunities that can be explored through innovation and technology. These include renewable energy, energy efficiency, sustainable transportation, sustainable fuel, sustainable agriculture, green manufacturing, green buildings, potable water, sustainable food products, the blue oceanic economy, smart cities and houses, green construction materials, waste management and recycling, innovative alternatives to plastics, et al. Moreover, compliance with appropriate ESG standards will boost business by attracting green finance, in addition to bolstering sales, as there is a perceptible shift towards green, organic, and sustainable products by consumers globally. The circular economy is another space for opportunity. For example, Apple is building its iPhone batteries from 100% recycled cobalt. Building sustainable communities through CSR (as mandated under the Indian Companies Act 2013) is another opportunity.

Responsibilities of BoD

Let us examine the Board of Directors' role in an ESG-related matter. It is accountable for the following:

1. Carry out the appraisal of the state of ESG preparedness of the firm with a gap analysis and transition plan to the desired end state.
2. To understand and identify the ESG issues of material impact on the business operations, reputation, and long-term growth of the company. These can be spotted on the materiality map.

3. Prioritise ESG issues and identify trackable and measurable metrics for monitoring. Set up goals accordingly.
4. Embed these ESG metrics during the planning of business strategy and operations for the next year to start with and allocate a sufficient budget.
5. Set up a monitoring mechanism for ensuring compliance and performance for the achievement of the goals through proper reporting mechanisms, policies, and procedures.
6. Maintain oversight over the compliance and achievement of targets, along with fiscal discipline, including a mechanism for mid-course correction if necessary.

Strategies

It is in this context that the BoD will have to integrate ESG with its strategy, planning, and execution. How should the BoD achieve this? It would be done through a steering subcommittee answerable to the Board of Directors, comprised of members from cross-functional areas such as the Audit Committee, Risk Management Committee, Nomination and Renumeration Committee, and functional areas such as operations, as needed. This will empower this committee with knowledge, experience, competence, and, most importantly, due weight. The materiality map will have to be prepared diligently. The ESG subcommittee will have to do a lot of diligence and make data-based recommendations. It is apt that the post of Chief Sustainability Officer (CSO) be created and a necessary oversight mechanism be instituted. The ultimate responsibility and accountability will vest with the BoD. Moreover, finance will play a crucial role in executing the action plan for ensuring compliance and tapping additional business opportunities. A sound governance framework that has the inherent capability of identifying and measuring traceable metrics through data collection, a robust enterprise risk management strategy, collaboration with the various stakeholders, a mechanism for monitoring and compliance with these metrics, a suitable organisational culture, talent attraction, grooming, and retention, an appropriate incentive structure, the identification of enabling technologies, sustainable finance and budget allocation, and enabling policies have to be instituted. BoD will have to elaborate on ESG through its agenda regularly at its quarterly meeting. The BoD will have to have the right strategy in place to attract green finance and tap this funding opportunity.

Conclusion

The ESG agenda provides a transformational opportunity for both the corporate sector and the government. It ensures that the planet, people, and corporations live in perfect harmony. Mindless appropriation of resources beyond the regenerative capacity of Mother Earth spells doom for society at large. Compliance with ESG will help maintain the interdependence of the earth's varied elements, ensuring a viable and sustainable future for humanity. Furthermore, it will open up a plethora of commercial prospects. A sustainability framework suitable for the organisation will have to be prepared, along with the implementation and disclosure mechanisms thereof. BoD has got its task well cut out, indeed. ■

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