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**Evolving ESG Reporting Governance, Regime Theory, and Proactive Law: Predictions and Strategies**

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Evolving ESG Reporting Governance, Regime Theory, and Proactive Law: Predictions and Strategies

Adam Sulkowski* and Ruth Jebe**

Transparency on ESG (environmental, social, and governance) is an important, if imperfect, step in striving for sustainability. Because a constellation of non-profit organizations created voluntary reporting frameworks with little government involvement, ESG reporting governance is institutionally dense and fragmented. Reporting companies and information users have both expressed dissatisfaction. In 2020, standard setting organizations indicated their intent to cooperate to simplify ESG reporting rules. In a different yet similar context, scholars utilize regime theory to understand institutional density and the potential for international cooperation, primarily among states. This article is the first to apply regime theory to ESG reporting governance architecture to better understand this unusual arena of rulemaking. It identifies key obstacles to global consolidation of ESG reporting governance and predicts that differences between the reporting philosophies in the European Union and the United States are among the factors that will prevent global consolidation of ESG reporting governance. This article concludes with advice for practitioners. It draws upon law and strategy and proactive law literature to propose approaches for reporting companies navigating the complex landscape of ESG reporting governance.
INTRODUCTION

ESG reporting has long been used as a tool to promote sustainability.¹ Scholars recognized its potential to improve business’ human rights performance,² to further environmental policy goals,³ and to foster better stakeholder relations.⁴ Civil society organizations also recognized the potential power of ESG disclosure and created a plethora of reporting standards.⁵ With organizations identified by acronyms, the ESG reporting landscape became an “alphabet soup” of standard-setters.⁶

ESG reporting has increasingly commanded the attention of business. The Global Reporting Initiative claims to have 10,000 reporting firms worldwide using its framework and to have reached the milestone of 50,000 reports uploaded to its Sustainability Disclosure Database as of October 2018.⁷ The Corporate Register, a non-profit organization that focuses on collecting

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¹ The terms “environmental, social, and governance (ESG),” “sustainability,” “non-financial,” and “corporate social responsibility” reporting have been used interchangeably in the past to describe reports with different degrees of emphasis on environmental, social, and/or governance issues, and to distinguish these reports from mandated financial disclosure. This article uses the term “ESG reporting” to refer to this type of reporting.


⁵ Reporting frameworks generally provide principles-based guidance on what broad topics are covered in a report, as well as how the report should be structured. Reporting standards provide specific, detailed requirements for what should be reported according to each topic, including metrics. Frameworks and standards are complementary tools. Response of the Sustainability Accounting Standards Board to the Public Consultation on the Revision of the Non-Financial Reporting Directive, SUSTAINABILITY ACCT. STANDARDS BOARD (June 2020), https://www.sasb.org/wp-content/uploads/2020/06/SASB.NFRDWhitepaper.FINAL-005.pdf. This article uses the term “standards” to refer to reporting frameworks and reporting standards and the terms “standard setting” and “standard setter” to refer to, respectively, the process of creating standards and reporting frameworks and the organizations that do so.


ESG reports, has a directory of over 150,000 reports prepared by 22,000 different organizations. KPMG has released an annual examination of corporate ESG reports every year since 1993.

However, with growth has come confusion and disappointment. ESG reporting developed a complex ecosystem, a constellation of standard-setters, each creating its own reporting standards. There is now a consensus that existing ESG reporting mechanisms are not achieving their anticipated impacts. Companies that issue reports face pressure from different stakeholder groups to report under multiple frameworks, depending on the group’s preference, given the plethora of voluntary reporting frameworks coupled with their voluntary nature. The transaction costs associated with reporting across multiple frameworks are a frequent topic in board discussions of ESG reporting. Reporting companies complain of the “reporting treadmill” where they spend more time gathering and reporting data than improving their operations. ESG information users face a corresponding set of issues related to the generally poor quality of available ESG information. Critics argue that ESG reporting suffers from a lack of standardized metrics and a corresponding lack of information comparability, a focus on quantity of disclosure rather than quality of disclosure, and they have occasionally raised doubts about the reliability of external assurance of reporting.

Both sets of issues are traceable to the complexity of ESG reporting governance. ESG reporting is fundamentally a creature of private ordering. Governments generally have showed little interest in regulating ESG disclosure. In the absence of government action, non-state actors created ESG disclosure standards and have dominated the field since its inception, creating and defining ESG reporting as we know it. This development has resulted in a complex and confused...

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14 Sarfaty, supra note 12, at 580–81.


The system may have reached a breaking point recently with increased calls for consolidation of standard setters and simplification of reporting standards. Responding to those calls, in September 2020, the five most prominent ESG reporting standard-setters, the Global Reporting Initiative (GRI), the Climate Disclosure Standards Board (CDSB), the CDP (formerly known as the Carbon Disclosure Project), the International Integrated Reporting Council (IIRC), and the Sustainability Accounting Standards Board (SASB), released their statement of intent to cooperate to achieve reforms in the ESG reporting landscape. Commentators, however, expressed cautious optimism around the announcement.

Consolidation of the ESG reporting ecosystem may be easier to announce than to achieve. The clearest path to consolidation of the ESG reporting ecosystem is for governments to mandate ESG disclosure around globally accepted reporting standards. Mandated reporting would level the reporting playing field by establishing a required standard for all reporting companies, thus addressing a key drawback of voluntary systems. Further, adopting a unitary ESG reporting standard that harmonizes the existing multiplicity of standards into one, would simplify the system for reporting companies and for information users. Unfortunately, the widespread government mandates needed for consolidation of the system are unlikely to happen. Absent government action, consolidation of ESG reporting will require the cooperation of key ESG reporting governance actors. To the extent they benefit from the current fragmented state of ESG reporting, these actors may have little incentive to act cooperatively. Instead, they may act to preserve their own position within the ESG reporting ecosystem. This dynamic leaves open the question of whether the ESG reporting context will change significantly.

This article undertakes to examine ESG reporting governance architecture to assess the likelihood of future cooperation needed to consolidate ESG reporting governance, an unexamined question in the ESG reporting literature. To gain analytical leverage on this complex question, we look to the field of international relations and its concept for investigating international cooperation, regime theory. Regime theory is employed to understand institutional density and international cooperation within regimes, where regimes are defined as the collected norms, rules, and institutions that comprise a governance architecture. Regime theory literature provides a starting point to analyze the potential for global cooperation needed to simplify ESG reporting

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ESG governance. Though regime theory was originally conceived as a tool to explain cooperation between nations, this article applies regime theory to the novel context of a governance system dominated by non-state actors to deepen our understanding of private governance systems.

The article begins by describing the ESG governance ecosystem in Part I and identifies the key actors that drive ESG reporting and are critical to any movement to consolidate. Part II examines the governance ecosystem through the lens of regime theory, where we challenge the popular viewpoint that the ESG reporting standard setters and governance will consolidate and conclude that the governance architecture as presently constituted is not positioned to support consolidation. Rather, fragmentation of the system is likely to continue, with a key fracture line solidifying between United States and European Union (EU) approaches. In Part III, we combine our regime theory analysis with the literatures on legal strategy and proactive law to suggest business practices to navigate the continued complexity of ESG reporting.

I. ESG REPORTING AND ITS GOVERNANCE ECOSYSTEM

Corporate ESG disclosure is comprised of two components, centered on reporting companies as the information producers of the system. Reporting companies use the standards created by standard setters to collect information into ESG reports. Companies then release their reports to those who use information directly to assess company performance and to intermediaries who process the information to issue ESG ratings. A first step for reporting companies is to identify the standards to use for their reports. In financial reporting, this step is simplified because there is one standard, created and mandated by the government for that jurisdiction. By contrast, ESG reporting is a polycentric system, dominated by private standard setters creating multiple voluntary disclosure standards, with limited government involvement. The system is further complicated by different entities with differing ideas on what should be disclosed in the reports, as reflected by the different definitions of materiality used by various actors in the system.

Corporate reporting, whether financial or non-financial, is grounded in the idea that companies must disclose material information. Different definitions of materiality represent different ideas of what information must be disclosed. The pluralistic nature of ESG reporting, with its multitude of actors, standards, and materiality definitions, makes for a complex ecosystem. Figure 1 provides a high-level snapshot of the ecosystem, described in this section.

Fig. 1 The ESG Reporting Governance Ecosystem
A. Private Standard Setters

ESG reporting originated with civil society demands for company disclosure on environmental and social performance. In the absence of government action to foster such reporting, non-profit organizations acted as private standard setters and took the lead to craft standards for ESG reporting. This section overviews key private standard setters.

1. The Group of Five

A group of the earliest innovators in the field defined the contours of ESG reporting and created the most widely used ESG reporting standards. Referred to as the Group of Five, they have dominated the field and remain important actors in the governance of ESG reporting.

   a. Global Reporting Initiative (GRI)

GRI was founded in 1997 with the objective of developing a broad, comprehensive, and systematic business reporting framework that encompassed economic, environmental, social, and governance information. GRI’s mission was to make sustainability reporting standard practice for all

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companies to promote transparency, and it has successfully implemented the dominant framework for sustainability disclosure with over 15,500 companies preparing reports using the GRI framework through 2020. GRI’s overarching disclosure principle is that companies report on “material” topics. For purposes of GRI reports, the guidelines define material information as information that reflects the organization’s “significant economic, environmental and social impacts” on stakeholders or that might “substantively influence the assessment and decisions” of stakeholders. This expansive conceptualization of materiality was the foundation for comprehensive reporting for a broad audience comprised of multiple stakeholder groups.

**b. Climate Disclosure Standards Board (CDSB)**

Subsequent developments in the sustainability reporting field highlight the evolution of society’s conception of ESG disclosure. The late 1990s saw increasing focus on the topics of global warming and climate change and a growing realization of the role business-generated carbon emissions played in climate change. New organizations created reporting frameworks in response to this focus on climate. In 2007, an international consortium of business and environmental non-profit organizations formed the Climate Disclosure Standards Board to increase and standardize corporate reporting of environmental information; CDSB released its framework in 2010. The CDSB framework defines material information as information about environmental impacts that is expected to have “significant positive or negative impact on the organization’s financial condition and operational results,” and identifies investors as the target audience for reporting under the framework.

**c. The CDP (formerly the Carbon Disclosure Project)**

A second reporting organization also arose to focus its attention on the intersection between investors and climate-related information. The CDP was established to develop a mechanism for

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25 *Id.* at 10.


27 *CDSB Framework, supra* note 26, at 1. The CDSB framework does not specify its own metrics or performance indicators for reporting but relies on principles developed by other organizations like CDP, GRI, and SASB. *Id.* at 10–11.

28 *Id.* at 12.

29 *Id.* at 6.
companies to report their greenhouse gas emissions and carbon usage. Its process invites company disclosure through sector-specific questionnaires that request information on carbon usage and other carbon issues. Its approach to materiality mimics that of financial reporting, with all items on the questionnaire presumably considered material by CDP. Currently, more than 2,400 European companies report through the CDP.

The CDSB and CDP frameworks provided much-needed attention on climate change. However, these single-dimension frameworks over-simplify sustainability by focusing solely on environmental issues.

d. The International Integrated Reporting Council (IIRC)

While the CDSB and CDP focused on disclosure of climate-related information, the International integrated Reporting Council pursued disclosure of a broader range of ESG factors. In 2010, a global coalition of regulators, investors, companies, and standard-setters created the IIRC to develop a framework for integrated reporting. The IIRC aimed to create a new framework that would articulate the links between financial performance and nonfinancial issues within a single report, known as an integrated report. The IIRC released its first framework in 2013 and set out a principles-based approach to reporting that focused on the concept of materiality to determine report content. The IIRC framework identifies its intended audience as providers of financial capital.

It grounded its definition of materiality for integrated reporting purposes to identify environmental and social issues that affect a firm’s ability to create value for investors over the

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37 INTERNATIONAL <IR> FRAMEWORK, supra note 34, at ¶ 1.9–1.11. The framework does not dictate specific report content or reporting indicators. Id. at ¶ 1.9–1.10.
38 Id. at ¶ 1.7. The <IR> Framework defines providers of financial capital as “[e]quity and debt holders and others who provide financial capital, both existing and potential, including lenders and other creditors.” Id. at 54.
short, medium, and long-term. This focus on investors as the report audience also informed the approach of the newest member of the Group of Five, the Sustainability Accounting Standards Board.

e. Sustainability Accounting Standards Board (SASB)

For the Sustainability Accounting Standards Board, the purpose of corporate disclosure is to draw the connection between ESG factors and the financial value of the firm. Established in 2011, SASB is an independent standard-setting organization for sustainability accounting standards. Its mission is to extend accounting infrastructure to incorporate material sustainability factors into financial filings and draw a direct connection between sustainability and financial materiality. SASB builds its reporting standards using the concept of materiality for financial reporting, as defined by the U.S. Supreme Court, which focuses on information that a reasonable investor would consider important. Consistent with this definition, SASB targets investors as the key audience for reporting under its standards. The SASB system’s core is its industry-specific reporting standards, which identify a range of specific sustainability topics that meet the definition of financial materiality for the identified industry.

2. Task Force on Climate-Related Financial Disclosures (TCFD)

The mid-2010s saw other entities entering the ESG reporting governance arena. Prompted by adoption of the Paris Agreement on Climate in 2015, the Financial Stability Board established the industry-led Task Force on Climate-related Financial Disclosures to develop a voluntary climate-related financial disclosure system. The TCFD positioned its final recommendations to be used as part of financial filings, using the definition of financial materiality of the jurisdictions where companies filed. The TCFD framework has had considerable global uptake in its short life. For example, the TCFD status report for 2021 claimed 2,600 organizational supporters for the

39 Id. at ¶ 3.17.
40 ABOUT US, SUSTAINABILITY ACCT. STANDARDS BOARD, https://www.sasb.org/about/.
41 SASB CONCEPTUAL FRAMEWORK, SUSTAINABILITY ACCT. STANDARDS BOARD 1 (2017).
45 TASK FORCE ON CLIMATE-RELATED FINANCIAL DISCLOSURES, RECOMMENDATIONS OF THE TASK FORCE ON CLIMATE-RELATED FINANCIAL DISCLOSURES 1–3 (June 2017). Creation of the board was requested by G20 leaders as a result of concerns about the economic impacts of climate change and climate information for the financial community.
46 Id. at 17.
framework, 1,000 of them since the 2020 report. In addition, the report identifies eight countries with TCFD-aligned climate reporting requirements.

3. World Economic Forum (WEF)

The World Economic Forum commenced work on recommendations for ESG reporting in 2017. In response to industry feedback on the complexity of ESG reporting, the WEF sought to present a simpler model for ESG disclosure. It released a set of fifty items, called the Stakeholder Capitalism Metrics (SCM), drawn from existing voluntary reporting standards and characterized as “universal” metrics. The WEF advocated incorporating ESG items in mainstream corporate disclosure, utilizing the concept of financial materiality. It acknowledged the long-term timeframe of ESG issues and recognized a category of “pre-financial” topics, issues that were likely to become material to firms’ financial performance.


Most recently, the International Financial Reporting Standards Foundation (IFRS) entered the ESG reporting governance arena. The IFRS is a London-based not-for-profit organization whose mission is to develop global standards that bring transparency and accountability to financial markets. Many countries require the use of IFRS standards as part of corporate financial reporting systems. After public consultation, it determined that it could contribute to consolidation of ESG reporting and it established its own sustainability standards board to develop a global baseline of ESG reporting standards for investors.

The IFRS’s standard setting work has drawn on existing investor-focused reporting standards, including those of the SASB and the TCFD, for its prototype standards, which were released in

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48 Id. at 3.

49 WORLD ECON. F., MEASURING STAKEHOLDER CAPITALISM TOWARDS COMMON METRICS AND CONSISTENT REPORTING OF SUSTAINABLE VALUE CREATION 6, 14 (2020).

50 Id. at 7, 13–14.

51 Id. at 14.


2021. The general reporting standard shows the IFRS approach to materiality as consistent with its financial reporting standards. Disclosure under the IFRS ESG standards is intended for use by investors and other users of financial reporting and tracks the definition of financial materiality followed by the U.S. In late 2021, the IFRS entered into an agreement to consolidate the CDSB, IIRC, and SASB into the IFRS sustainability standards board.

B. Governments

Private standard setters have taken the lead to create ESG reporting frameworks and presently dominate its governance ecosystem. Recently, though, governments have entered the field of ESG reporting. This section overviews two key governmental actors, the EU and the United States.

1. The European Union

While private actors established early ESG reporting, governments were largely silent, with the notable exception of the EU. The EU became one of the first government entities to mandate sustainability reporting through its 2014 Non-Financial Reporting Directive (NFRD). Consistent with EU policy objectives around environmental and social issues, the NFRD introduced a materiality concept that attempts to encompass a wide variety of stakeholder interests. Called double materiality, the concept required companies to report both on how sustainability issues affect firm performance and on firm impact on the environment and society.

In 2019 the EU adopted the European Green Deal (EGD) and identified corporate sustainability disclosure as an important leverage point for financing the sustainable growth contemplated by the EGD. In the face of general dissatisfaction with implementation of the NFRD and feedback from the public that showed support for mandating a single ESG reporting

56 Id. at ¶ 11.
57 Id. at ¶ 10.
60 Communication from the Commission to the European Parliament, the European Council, the Council, the European Economic and Social Committee and the Committee of the Regions – The European Green Deal, at 2, COM (2019) 640 final (Nov. 12, 2019). The EGD’s objective is to transform the EU into a resource-efficient and competitive economy with no net emissions of greenhouse gases by 2050. Id.
61 Eur. Commission, supra note 59, at 1–2; EUR. PARLIAMENT, supra note 58, at 1–2.
62 Feedback included complaints that sustainability information lacked comparability, reliability, and relevance, and that the existing system imposed potentially undue burdens on reporting companies. EUR. PARLIAMENT, supra note
standard, the European Commission tasked the European Financial Reporting Advisory Group (EFRAG) with developing recommendations for future ESG reporting in the EU. The European Commission’s Proposal for a new Corporate Sustainability Reporting Directive (CSRD), issued in April 2021, retains the double materiality concept and calls for a more prescriptive approach to ESG reporting governance that includes mandating specific disclosure items. The first set of standards under the CSRD is scheduled to be adopted by October 2022.

2. The United States

The year 2020 saw a change in U.S. presidential administration and what some hoped would be greater attention to ESG issues. The U.S. approach to ESG reporting stands in stark contrast to that of the EU. While the EU is pursuing a course of increasingly prescriptive reporting to support sustainability policy goals, the U.S. government has a more hands-off attitude to sustainability issues in general and to ESG reporting specifically. Without a broad policy commitment to ESG as a foundation, the only federal regulatory connection to ESG disclosure is through the financial reporting system, administered by the Securities & Exchange Commission (SEC), and its concept of financial materiality. Early attempts to force SEC rulemaking to require enhanced ESG disclosure failed. Progress was made in 2010 when the SEC issued interpretive guidance, referred to as the Climate Guidance, that identified climate change risk as potentially material, at 4; Eur. Commission, Request for Technical Advice from European Corporate Reporting Lab@EFRAG 1 (June 25, 2020) [hereinafter Request for Technical Advice]. In addition to flagging comparability, reliability, and relevance issues, report users complained that companies simply failed to report some information that was important to them and that information was often insufficiently digitalized which complicated locating and using information. Id.

EUR. PARLIAMENT, supra note 58, at 7.


EUR. Commission, supra note 59, at 42, ¶1.

Id. at 45. For example, the Proposal states that the reporting standards shall specify the information companies are to disclose about the environment, including information about climate change adaptation and mitigation, water and marine, resources, resource use, pollution, and biodiversity. Id. 45–46.


For example, a notable line of cases involved the Natural Resources Defense Council’s attempts to force the SEC to promulgate rules for corporate disclosure of environmental policies, which it claimed were required under the U.S. National Environmental Policy Act (NEPA). For discussion of the litigation, see Robin S. Miller, NRDC v. SEC: A Question of Judicial Review, 6 COLUM. J. ENVTL. L. 217 (1980); Fern L. Frolin, Toward Corporate Environmental Disclosure: NRDC v. SEC, 6 B.C. ENVTL. AFF. L. REV. 155 (1977); Williams, supra note 13, at 1246–59.
information. Unfortunately, enforcement of the Climate Guidance has been lax. Legislative attempts to increase sustainability disclosure have included the conflict minerals disclosure provisions of the Dodd-Frank Act. More recently, the SEC issued a Concept Release in 2016, seeking public comment on a host of disclosure issues, including mandating environmental and social disclosure. To date, the Concept Release has yielded no action by the SEC to expand environmental or social reporting requirements.

The SEC under the Biden Administration has been more open to pursuing improved ESG disclosure to protect investor interests. Early 2021 saw a flurry of activity by the SEC, including


71 See generally Stephen Kim Park, Targeted Social Transparency as Global Corporate Strategy, 35 NW. J. INT’L L. & BUS. 87 (2014). See also, Fisch, supra note 33, at 938–39. The Dodd-Frank reporting provisions required the SEC to promulgate rules requiring companies to disclose the country of origin for conflict minerals used in their products. Portions of the Dodd-Frank provisions were subsequently ruled a violation of the First Amendment. Nat’l Ass’n of Mfrs. v. SEC, 800 F.3d 518 (D.C. Cir. 2015).


73 Id. at 69.

74 For example, the acting director of the SEC Division of Corporation Finance issued comments advocating that the SEC play a role in development of a global sustainability reporting framework. John Coates, ESG Disclosure – Keeping Pace with Developments Affecting Investors, Public Companies and the Capital Markets, U.S. SEC.
actions to heighten the agency’s enforcement focus on disclosure under the 2010 Climate Guidance,\textsuperscript{75} creation of an ESG disclosure enforcement Task Force,\textsuperscript{76} and opening of a public comment period on SEC disclosure rules with an eye to improved disclosure on climate change issues.\textsuperscript{77} The agency’s proposed rule on climate-related disclosure was released for public comment in March 2022.\textsuperscript{78} The proposal is generally in line with past SEC action on ESG reporting, especially with the 2010 Climate Guidance. Rather than mandate disclosure across a range of ESG issues, the rule is narrowly focused on climate-related risks.\textsuperscript{79} Moreover, the rule hews to the traditional definition of financial materiality as to what information must be reported, stating that companies must disclose information on risks that are “reasonably likely to have a material impact on its business, results of operations, or financial condition.”\textsuperscript{80}

C. Information Users

There are a variety of entities that make use of ESG information for a variety of purposes. Civil society originated the ESG reporting movement and are still key direct users of corporate ESG disclosure. The ESG reporting ecosystem is also populated by information intermediaries, third parties that rate or rank companies’ ESG performance. These entities rely on corporate ESG reports as the basis for their ratings. Finally, recent years have seen the rise of investors as users of ESG information. Increasingly, large asset owners are integrating ESG factors into their investment decisions, using company ESG reports or ratings from ESG data services. Information users may interact with reporting companies in an effort to improve corporate ESG disclosure and may engage with standard setters to influence the trajectory of standards.

D. The Governance Architecture of ESG Reporting and the Call to Consolidate

The ESG reporting ecosystem is characterized by institutional density, with an increasing number of institutions and entities operating within this arena. The previous section overviewed the primary actors, and there are additional entities with some level of connection to ESG reporting.\textsuperscript{81} This proliferation of institutions and actors, without coordination across entities, yield a confused


\textsuperscript{78} The Enhancement and Standardization of Climate-Related Disclosures for Investors, 17 C.F.R. 210, 229, 239, 249 (proposed Mar. 21, 2022).

\textsuperscript{79} \textit{Id.} at 7. The proposed rule draws on the TCFD framework. \textit{Id.} at 27, 35.

\textsuperscript{80} \textit{Id.} at 1, 42–44.

\textsuperscript{81} Estimates as to the number of ESG reporting frameworks initiatives vary from 230 to nearly 400. See Cheri Hasz, \textit{The U.S. Oil and Gas Industry Should Be a Leader and Follow the EU’s Lead on ESG Disclosure}, 29 TUL. J. INT’L & COMP. L. 135, 138 n.22 (2021).
governance space. Further, ESG reporting is characterized by an inverted governance configuration: while there is fledgling government interest in ESG reporting, the space is dominated by private actors. Government has played a decidedly subordinate role in ESG reporting governance.

This configuration raises issues for the development and functioning of ESG reporting governance architecture. The decentralized and polycentric approach to ESG reporting catalyzed development of the disclosure movement but created complexity that has become counterproductive. 2020 saw some movement toward apparent consolidation. In response to complaints about the complexity of the ESG reporting landscape, the Group of Five issued their statement of intent to move toward a “comprehensive” corporate reporting scheme. The SASB and the IIRC subsequently merged into a unified organization, the Value Reporting Foundation (VRF), and in 2021 the ISSB announced that the CDSB and VRF would consolidate with the ISSB. The consolidation movement signals the need to evaluate whether current ESG reporting governance architecture and activities will foster the global cooperation needed to effectively consolidate ESG reporting. The field of international relations supplies a conceptual tool for investigating this question and ESG reporting’s governance ecosystem in the form of regime theory.

II. ASSESSING THE LIKELIHOOD OF GLOBAL COOPERATION TO CONSOLIDATE ESG REPORTING

The clearest path to consolidation of ESG reporting governance is through government regulation. The EU has chosen this path, opting to create, mandate, and administer its own ESG reporting standards. The CSRD may work to overcome ESG reporting issues related to companies that are required to report under the new standard. However, it will not address issues for those companies outside the mandate. For example, U.S. companies with operations in the EU may come under the CSRD, but their operations outside the EU will not. The EU acting on its own, however, cannot harmonize all aspects of ESG reporting. Global harmonization requires cooperation among the various elements of the ESG reporting ecosystem, especially among standard setters. Key questions for the future of ESG reporting, then, are how likely is it that the parties will actually cooperate, and how do we assess that likelihood. One lens to view the potential for actors to cooperate in this manner is regime theory.

A. Regime Theory as a Lens to Predict Cooperation

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82 GLOBAL REPORTING INITIATIVE, supra note 18.


International relations scholars developed regime theory as a tool to understand and explain situations where nations forgo some of their self-interest to cooperate with other nations. Regime theory notes that actors will cede some of their own interest, under certain conditions, on issues that cannot be addressed adequately by individual countries. A regime can be viewed as the agreements and principles that are the basis for this cooperation. The classic form of a regime is an international treaty, signed by multiple nations as evidence of their intention to cooperate on a particular issue. Global regulation of climate change, for example, demonstrates both the success and limits of a regime. Climate change regulation is centered around the United Nations Framework Convention on Climate Change (UNFCCC), a multilateral treaty that recognized the need for countries to cooperate to combat climate change. The treaty garnered broad global support and has been ratified by 197 countries. The UNFCCC is an expression of the ratifying members’ willingness to sacrifice some degree of sovereignty and self-interest to regulate activities that contribute to climate change.

Regime theory originally focused only on the actions of countries, working in hierarchical relationships anchored in an international treaty. More recently, scholars have argued for the value of regime theory as an explanatory lens for less structured constellations of actors that include both states and private actors such as non-governmental organizations and multinational corporations. The climate change regime reflects this polycentric approach to climate governance. The UNFCCC process provides for non-governmental organizations (NGOs) to be

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86 A regime is commonly defined as the “principles, norms, rules, and decision-making procedures around which actor expectations converge in a given issue-area.” Stephen D. Krasner, Structural Causes and Regime Consequences: Regimes as Intervening Variables, 36 INT’L ORG. 185, 185 (1982).


88 Id.

89 See, e.g., Keohane & Victor, supra note 85, at 8 (identifying traditional view of regimes as state-constructed international institutions); VINOD K. AGGARWAL, INSTITUTIONAL DESIGN FOR A COMPLEX WORLD 4 (1998) (claiming regimes are developed to regulate the actions of states); Zaring, supra note 85, at 305 (noting in 1998 that leading regime theory scholars grounded the theory in actions of states).


admitted as observers; to date, nearly 3,000 NGOs have achieved that status. In addition, the United Nations actively solicits participation by business in climate change activities as part of continuing negotiations under the UNFCCC. A major issue in the study of regimes is the challenge of building regime cohesion in the face of a multitude of actors. Regimes are often fragmented, with multiple actors proposing different systems of norms and scholars debating the benefits and harms of fragmentation. Some see fragmentation in a regime as a source of innovation or as providing opportunities for broader participation by groups often excluded from governance processes. However, many scholars argue that fragmentation creates regulatory chaos with overlapping regimes making obligations unclear. Fragmentation also provides opportunities for regulatory arbitrage, in particular forum shopping, where regime actors pick and choose which parts of a regime to join based on their own self-interest. Multiple points of authority in a regime can dilute the authority of all parts of the regime. Global climate regulation reflects the dynamics of regime fragmentation and highlights some of the limits to global cooperation. Despite the UNFCCC’s auspicious start, attempts to negotiate agreements to implement it proved problematic. The Kyoto Protocol (Kyoto) was a key

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94 See, e.g., Business is Key Driver of Global Climate Action, UNITED NATIONS FRAMEWORK CONVENTION ON CLIMATE CHANGE (June 28, 2016), https://unfccc.int/news/business-is-key-driver-of-global-climate-action (recounting business action to reduce climate impacts); RACE TO ZERO CAMPAIGN, UNITED NATIONS FRAMEWORK CONVENTION ON CLIMATE CHANGE, https://unfccc.int/climate-action/race-to-zero-campaign (recruiting support from business for move to zero carbon economy) (last visited June 22, 2022).

95 Amandine Orsini, Jean-Frederic Morin & Oran Young, Regime Complexes: A Buzz, a Boom, or a Boost for Global Governance?, 19 GLOBAL GOV. 27, 29 (2013) (noting that all regime complexes exhibit some degree of divergence).


97 See, e.g., Helfer, supra note 96, at 8 (contending that fragmentation can increase opportunities for participation by weaker states); Kenneth W. Abbott, Philipp Genschel, Duncan Snidal & Bernhard Zangl, Orchestration: Global Governance Through Intermediaries, in INT’L ORG. AS ORCHESTRATORS 7 (Kenneth W. Abbott 2015) (claiming that fragmentation can provide non-state actors openings to participate in governance).


99 Forum shopping in the regime context has been defined as the strategic use of different institutional settings to make progress on an individual agenda. Amandine Orsini, Multi-Forum Non-State Actors: Navigating the Regime Complexes for Forestry and Genetic Resources, 13 GLOBAL ENVTL. POL. 34, 41 (2013). Regime theory scholars describe forum shopping as a negative consequence of fragmentation. Raustiala & Victor, supra note 90, at 299; Alter & Meunier, supra note 98, at 16.

tool to advance the aims of the UNFCCC. The EU ratified and became a major proponent of the Kyoto Protocol’s approach,101 however, agreement ran into a significant roadblock when the Protocol failed to achieve U.S. Senate ratification102 due to concerns over the Protocol’s potential to harm U.S. interests.103 To guard its interests, the United States initiated an alternative regime, the Asia-Pacific Partnership on Clean Development and Climate (APP), an agreement among seven Asian rim countries104 to pursue objectives that were not part of the UNFCCC.105 U.S.-led resistance to Kyoto thus fractured the UNFCCC regime. While creation of the APP may be seen as innovation within the regime, the U.S. refusal to ratify Kyoto weakened the potential for the UNFCCC regime to work effectively against climate change.106 The ebb and flow of global cooperation also played out in the most recent agreement related to the UNFCCC, the Paris Agreement,107 with the U.S. position on the Agreement varying with presidential administrations.108

An important stream of international law scholarship employs concepts similar to those of regime theory to investigate the fragmentation of international law. The concept of legal pluralism describes situations where multiple and overlapping legal norms and legal systems regulate a given


103 David Malakoff & Erin Marie Williams, Q&A: An Examination of the Kyoto Protocol, NPR (June 6, 2007, 12:00 AM), https://www.npr.org/templates/story/story.php?storyId=5042766 (noting then-President Bush’s contention that the emission cuts required by Kyoto would hurt the U.S. economy without providing significant environmental benefits).


106 Keohane & Victor, supra note 89, at 10 (referring to the effect of the UNFCCC as mostly symbolic).


108 The United States was an original signatory of the Paris Agreement when it was negotiated in 2015. However, the Trump administration in 2017 declared the U.S.’s intention to withdraw from the agreement because of the “unfair economic burden imposed on American workers, businesses, and taxpayers by U.S. pledges made under the Agreement.” Press Statement, Michael R. Pompeo, Secretary of State, On the U.S. Withdrawal from the Paris Agreement (Nov. 4, 2019), https://2017-2021.state.gov/on-the-u-s-withdrawal-from-the-paris-agreement/index.html. In February 2021, the U.S. rejoined the Paris Agreement. Press Statement, Antony J. Blinken, Secretary of State, The United States Officially Rejoins the Paris Agreement (Feb. 19, 2021), https://www.state.gov/the-united-states-officially-rejoins-the-paris-agreement/.
activity.\textsuperscript{109} For example, international trade is governed simultaneously by national, regional, and international legal systems that overlap and can sometimes impose conflicting legal obligations on parties.\textsuperscript{110} These multifaceted legal systems are the corollary of the regimes of regime theory. Legal pluralism specifically recognizes that both states and private actors play a role in generating the norms in a given legal system.\textsuperscript{111}

For legal scholars, pluralism represents the fragmentation of international law.\textsuperscript{112} International law scholars have identified several forms of fragmentation\textsuperscript{113} and positive and negative outcomes of fragmentation similar to those identified in fragmented regimes.\textsuperscript{114} Fragmentation of the law creates the same regulatory chaos as regime theory scholars note\textsuperscript{115} and the same potential for stronger states to undercut the positions of weaker states.\textsuperscript{116} Fragmentation is seen as reducing the effectiveness of the international legal system.\textsuperscript{117} The international law literature recognizes the contribution regime theory makes to assessing global cooperation,\textsuperscript{118} making regime theory a useful lens to examine the ESG reporting governance ecosystem and the potential for the cooperation needed to harmonize standards and simplify the system.

B. ESG Reporting Governance as a Regime


\textsuperscript{111} Engle, \textit{supra} note 109, at 870, 877 (discussing private normative ordering); Paul Schiff Berman, \textit{Global Legal Pluralism}, 80 S. CAL. L. REV. 1155, 1157–58 (2007) (contending that government is not the sole creator of norms).


\textsuperscript{113} \textit{see, e.g.}, Mads Andenas, \textit{Reassertion and Transformation: From Fragmentation to Convergence in International Law}, 46 GEO. J. INT’L L. 685, 694–98 (2015) (identifying three forms of fragmentation in international law). Adenas’s substantive fragmentation and institutional proliferation are analogous to cooperative and conflictive fragmentation in a typology created by international relations scholars. \textit{See} Biermann, \textit{supra} note 96, at 19–21.

\textsuperscript{114} Benefits include accommodation of a plurality of viewpoints and enhanced innovation. Megiddo, \textit{supra} note 110, at 122; Berman, \textit{supra} note 109, at 321.

\textsuperscript{115} Int’l Law Comm’n, \textit{supra} note 112, at 11, 14; Megiddot, \textit{supra} note 110, at 122; Berman, \textit{supra} note 109, at 320.

\textsuperscript{116} Eyal Benvenisti & George W. Downs, \textit{The Empire’s New Clothes: Political Economy and the Fragmentation of International Law}, 60 STAN. L. REV. 595, 596–604 (2010) (arguing that fragmentation can inhibit the evolution of a more democratic international regulatory system by undercutting the power of weaker actors).


The ESG reporting ecosystem functions as a pluralistic regime dominated by private actors. In the absence of government action establishing ESG reporting, private actors took the lead to create the necessary governance elements. The Group of Five established basic principles of disclosure that are generally adopted by the other actors in the ecosystem. Further, standard setting organizations used multi-stakeholder processes that included potential reporting companies to create their standards.\textsuperscript{119} Investors, as information users, have had increasing impact on the development of standards.\textsuperscript{120} The standards created by the Group of Five and the TCFD are used by the majority of reporting companies and now also serve as the basis for global standard setting. For example, the EU’s current activity to create a new ESG reporting Directive and its double materiality concept build on work done by GRI,\textsuperscript{121} and EFRAG and GRI are now “co-constructing” the reporting standards for the new EU CSRD.\textsuperscript{122} However, the system also reflects the negative outcomes often encountered in fragmented regimes. The chief frustration with the current system is the regulatory chaos that has resulted from multiple organizations creating multiple reporting standards, none of which has legal preeminence over the others. This reality catalyzed the Group of Five to issue its Statement of Intent to Work Together toward comprehensive reporting. In light of the Statement and the hopes it engendered, we investigate whether the Statement and subsequent activity in the field will result in the level of global cooperation needed to consolidate ESG reporting.

C. Cooperation Strategy Options for Standard Setters

The consolidation of ESG reporting governance requires the cooperation of key actors in the ecosystem to revise the existing governance structure. Even national mandates on ESG reporting, unless grounded in a common approach, will not result in a unitary ESG reporting system. Global cooperation by organizations is not binary; it exists on a continuum from no cooperation to partial cooperation to complete cooperation.\textsuperscript{123} The question for regime actors, then, is to what extent are they willing to compromise their self-interest. This section reviews possible cooperation strategies and predicts that the cooperation needed for the sought-after consolidation of the ESG reporting ecosystem and simplification of ESG reporting is unlikely to happen.

1. No co-operation with the consolidation movement

\textsuperscript{119} Multi-stakeholder processes include stakeholder input on the content of standards and public comment periods on draft standards. \textit{GLOBAL REPORTING INITIATIVE, GLOBAL SUSTAINABILITY STANDARDS BOARD DUE PROCESS PROTOCOL 5–6 (2018); SUSTAINABILITY ACCT. STANDARDS BOARD, SASB RULES OF PROCEDURE 5 (2017).}


\textsuperscript{123} Keohane & Victor, \textit{supra} note 89, at 7 (describing the continuum between highly fragmented and highly integrated regimes).
Under this strategy, standard setters decline to participate in the consolidation movement, electing to go it alone. This strategy makes sense only for standard setters that are strong enough to eschew cooperation. None of the private standard setters is pursuing this strategy, as all are electing to engage in some level of cooperation. However, the SEC’s reluctance to engage with key ESG standard setters as it crafts the U.S. approach to ESG reporting could be seen as rejecting a cooperation approach. Given the dominance of U.S. stock exchanges in the global capital market, the United States may be in a position to chart its own path, regardless of the movement to consolidate ESG reporting governance.

2. Full cooperation with the consolidation movement

Under this strategy, organizations abandon protection of their own self-interest in the interest of consolidating ESG reporting governance. This is the clearest cooperation path to reduce the number of standard setters and standards. However, it is the least desirable alternative for standard setters because it would require some of them to terminate their own organizations.

The Statement of Intent issued by the Group of Five in 2020 raised hopes that the major standard setters were ready to fully cooperate to consolidate ESG reporting. The Statement purported to outline an approach to identify a globally agreed upon set of sustainability disclosure requirements, which sounds similar to a drive toward a single unified ESG reporting standard. Closer reading of the Statement, however, undercut this hope. The institutions agreed to work toward a “comprehensive” reporting system that showed how their various standards could be used in a “additive” way. The goal of cooperation was to demonstrate how the standards were interoperable and could be used concurrently, but not to reduce the number of standards. Demonstrating the relationships between the Group of Five standards may help reporting companies better understand the uses of the different standards, but, given that the number of reporting options remains the same, it does not constitute consolidation or simplification of the system. In late 2020, key standard setters were intent to preserve their institutions’ existence, rather than fully cooperate to improve ESG reporting. To date, only the CDSB has pursued a strategy of full cooperation, merging with the IFRS and sunsetting itself in January 2022.

3. Partial cooperation with the consolidation movement

A strategy of partial cooperation is akin to regulatory arbitrage, where actors use opportunities within the regulatory system itself to pursue their self-interest rather than acting for the good of the regime. Parties pursue this strategy where it is to their benefit to at least appear to cooperate

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125 STATEMENT OF INTENT, supra note 18, at 3.

126 Id. at 1–2.

127 Id. at 14.

by remaining part of the consolidation discussion, but where they may still calculate how to best serve their own interests. Preservation of an organization’s own norms and standards may undermine consolidation of ESG reporting by continuing the fragmented condition of the regime, explored in the next section.

D. Fragmentation as a Barrier to Consolidation of ESG Reporting

ESG reporting regime actors have a variety of reasons for acting to preserve their own interests, rather than fully embrace the consolidation movement. However, reluctance to cooperate will maintain the fragmented nature and complex structure of ESG reporting. ESG reporting governance exhibits two types of fragmentation, institutional and normative, that make consolidation of ESG reporting governance unlikely.

1. Institutional Fragmentation of ESG Reporting Governance

ESG reporting governance reflects the fragmentation that arises when regime actors use strategies that protect their own interests.\textsuperscript{129} Strong actors may have minimal incentive to coordinate their actions in a fragmented regime,\textsuperscript{130} and may contend for governance turf.\textsuperscript{131} Much of this dynamic is evident in the recent activity among the Group of Five and beyond. The Group of Five’s Statement of Intent was a rationalization for co-existence, rather than a call for consolidation, with most members continuing their existence. The TCFD and WEF continue their individual activities and the CDP published its timeline for continued use of its reporting architecture in 2022.\textsuperscript{132}

The IFRS and its newly formed sustainability standards board are touted as a possible leverage point for the cooperation needed to consolidate ESG reporting governance. Through the IFRS Technical Readiness Working Group (TRWG), key ESG standard setters have contributed technical expertise toward the IFRS standards.\textsuperscript{133} The greatest hope for cooperation to unify ESG reporting is the consolidation of the VRF into the IFRS. The IFRS will take ownership of both the SASB reporting standards and the IIRC reporting framework in June 2022.\textsuperscript{134} Although the future

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\textsuperscript{129} Biermann, \textit{supra} note 96, at 30.

\textsuperscript{130} Alter & Meunier, \textit{supra} note 98, at 19; Benvenisti & Downs, \textit{supra} note 116, at 597–98.


\textsuperscript{133} Members of the Technical Readiness Working Group include the CDSB, TCFD, VRF, and IIRC. IFRS Foundation, \textit{SUMMARY OF THE TECHNICAL READINESS WORKING GROUP’S PROGRAMME OF WORK 3} (2021).

of the integrated reporting framework is not clear, incorporating the SASB standards and IIRC framework into the forthcoming IFRS standards will modestly reduce the overall number of standards. However, cooperation around the IFRS is only partial. Although they contributed to development of the forthcoming IFRS standards, it is not clear that the status of TCFD or WEF work on ESG reporting will change. It does not appear that the TCFD will merge with the IFRS; it could continue its standard setting activities unchanged. There is also no word from the WEF as to whether it will continue its work on its Stakeholder Capital Metrics. The WEF Metrics are somewhat broader in scope than the IFRS approach, which could mean the WEF promotes its framework in the EU as their materiality definitions align broadly.

While the IFRS’s work on ESG reporting could provide a modest degree of consolidation and simplification of ESG reporting governance, two key issues remain. First, the IFRS standards, like most other ESG reporting standards, are voluntary. Countries may or may not adopt the standards as mandatory or suggested for national ESG reporting. The United States, for example, has historically been reluctant to accept global standards, as evidenced by the U.S. failure to adopt the IFRS standards for financial reporting. Even countries that choose to follow the IFRS standards can adopt them in whole or only in part. Thus, the IFRS standards will still likely result in different ESG reporting obligations in different jurisdictions, leaving reporting companies with a patchwork of obligations across jurisdictions. The many countries without mandatory ESG reporting requirements also leave companies with the ultimate decision on which standards to use for reporting, and the decision leaves them open to the pressure to report under multiple standards. As long as the IFRS standard is voluntary, it will not overcome the fragmentation issues that result from multiple standard setters and standards.

More significantly, the IFRS focus on financial materiality as the standard to determine what must be reported is at odds with some countries’ policies. The EU, for example, is constructing its ESG reporting around the concept of double materiality, which includes both ESG impacts on the financial health of a company and ESG impacts the company creates for society. The fracture along normative lines presents a heightened challenge for cooperation and for the consolidation of ESG reporting.

2. Normative Fragmentation of ESG Reporting Governance

The consolidation of ESG reporting must overcome the normative divide embedded in the different definitions of materiality used by different standard setters. As discussed above, one side of the

\[135\] INTEGRATED REPORTING FRAMEWORK, supra note 134 (noting that the IASB and ISSB will determine how to utilize the integrated reporting framework).

\[136\] ISSB: FREQUENTLY ASKED QUESTIONS, IFRS FOUNDATION, https://www.ifrs.org/groups/international-sustainability-standards-board/issb-frequently-asked-questions/ (last visited June 24, 2022) (noting that it is for individual countries’ authorities to decide whether to mandate use of IFRS standards).


\[138\] Biermann, supra note 96, at 28–29.
divide is comprised of entities that target investors as primary information users using the definition of financial materiality; these entities include the IFRS, the VRF, and the SEC. The other side of the divide, represented by the EU and the GRI, uses a more expansive definition of materiality to suit the information needs of a broader array of stakeholders. Recent movement by ESG reporting standard setters highlights this split. For example, the relationship established between the VRF, the CDSB, and the IFRS makes sense because the organizations share a focus on the provision of information for investors through the definition of financial materiality. This constellation of institutions may also connect to the U.S. focus on ESG as part of financial reporting. This coalition stands in contrast to the ESG reporting philosophy of the EU where the double materiality construct is designed to serve society broadly, not only investors. The agreement between EFRAG and the GRI to co-construct standards for the CSRD underscores their normative symbiosis. The EU is pursuing “ambitious” goals through its double materiality standard, a standard designed to serve society as a whole. The United States, however, is on a quite different trajectory. U.S. efforts to improve ESG reporting lag behind much of the rest of the world and continue to face resistance. Scholars cite the dominance of the shareholder primacy norm as a key reason for U.S. regulators’ reluctance to expand disclosure requirements. Indeed, the proposed climate disclosure rule, with its focus on information that is financially material to investors, can be seen as an outgrowth of the U.S. shareholder primacy norm. Rather than the broad commitment to ESG represented by the EU’s CSRD, the U.S. proposal is a modest extension of existing rules. Additionally, a recent agreement between the GRI and the IFRS, while claiming to align their standards, enshrines the distinction between financial materiality and double materiality in its two-pillar approach. The combined strength of these forces undercut the potential for global


cooperation to consolidate ESG reporting and its governance and indicate that fragmentation of the ESG reporting regime will continue.

The normative conflict is important to recognize because the divergence is not just about ESG disclosure; rather, it is a divergence in the definition of sustainability and the norms associated with it.\textsuperscript{144} For example, the financial materiality focus for ESG reporting can be seen as part of a movement to financialize\textsuperscript{145} sustainability, a movement that has been criticized as resulting in a selective and weak form of sustainability that excludes elements that cannot be expressed in financial terms.\textsuperscript{146}

Some propose a concept called dynamic materiality as a bridge for this normative divide. Dynamic materiality posits that the concept of materiality has become more fluid\textsuperscript{147} and that what is considered material information changes over time.\textsuperscript{148} The increasing ability of stakeholders to influence investors’ perceptions of what is material fuels this fluidity and change.\textsuperscript{149} Thus, issues that are not presently considered financially material may become so over time as investors become aware of stakeholders’ interest in new issues and begin incorporating that consideration into their investment decisions.

The importance to investors of company actions on climate change may exemplify aspects of this dynamic. For example, in the United States, non-profit environmental groups catalyzed the SEC’s release of interpretive guidance on the materiality of climate change.\textsuperscript{150} Their argument is that this dynamism will effectively expand the scope of what is considered financially material, to the extent that it will eliminate the division between financial and non-financial materiality.\textsuperscript{151} The potential impact of dynamic materiality, however, may be more limited and problematic than some argue. Even the originators of the concept recognize that it will not fill all materiality gaps and that not every issue will meet the definition of financial materiality.\textsuperscript{152}

A second issue is the uncertainty and potential time frame involved in this evolutionary process. Stakeholders may convince investors of the materiality of individual ESG factors, but what if they fail or cannot inspire action quickly enough? It took environmental groups several


\textsuperscript{145} Financialization in the corporate context is represented by structures that prioritize shareholder interests. Stephanie Hiss, \textit{The Politics of the Financialization of Sustainability}, 17 COMPETITION & CHANGE 234, 239 (2013).

\textsuperscript{146} Id. at 243; Davide Cerrato & Tomaso Ferrando, \textit{The Financialization of Civil Society Activism: Sustainable Finance, Non-Financial Disclosure and the Shrinking Space for Engagement}, 10 ACCT., ECON., & L.: A CONVIVIUM 1, 18 (2020).

\textsuperscript{147} TRUVALUE LABS, \textit{DYNAMIC MATERIALITY: MEASURING WHAT MATTERS} 4 (2020).


\textsuperscript{149} Id. at 9; TRUVALUE LABS, supra note 147, at 6–8.

\textsuperscript{150} See supra note 69 and accompanying text.

\textsuperscript{151} Robert G. Eccles & Bhakti Mirchandani, \textit{We Need Universal ESG Accounting Standards}, HARV. BUS. REV. (Feb. 15, 2022).

\textsuperscript{152} TRUVALUE LABS, supra note 147, at 8.
decades to convince the SEC to expand financial reporting to include any ESG factors.¹⁵³ For some ESG issues, we may not have the time needed for dynamic materiality to catalyze change in investor attitudes. Finally, the dynamic materiality concept still allows for, and in fact may promote, the financialization of sustainability. Impacts that cannot be measured in financial terms or that are too small to affect investors’ decisions may still negatively affect other stakeholders. Relying on the financial materiality construct of dynamic materiality reduces sustainability to what matters to investors, leaving the interests of other groups diminished or ignored all together.¹⁵⁴

It is overly optimistic to predict that cooperation between ESG reporting standard setters will consolidate ESG reporting, and it is unlikely that governments will mandate the same standards. Government action from the EU CSRD and SEC may somewhat simplify ESG reporting governance by replacing multiple private actor-created frameworks with a single mandated framework in their respective jurisdictions. However, this government action looks to institutionalize the divide between ESG norms, leaving true global consolidation an illusion. This reality leaves reporting companies with key strategic decisions to make as they continue to navigate the fragmented ESG reporting ecosystem.

III. IMPLICATIONS, IMPACTS, AND IDEAS FOR PRACTITIONERS

This section investigates the implications of the preceding analysis for the world of business practice. We present a brief review of closely related streams of literature at the nexus of management and law that provides general principles for how to plan and strategize. We then translate the principles garnered from the literature into suggestions for how to think about, plan, and act in the fragmented governance environment of ESG reporting.

A threshold question, as we transition from application of theory to suggestions for management and the practice of law, is whether practitioners agree with our application of regime theory to render a prediction. Namely, do practitioners also believe it is more probable that approaches to reporting will remain balkanized? The following quotes are indicative of a quiet consensus among practitioners. An executive at a firm that advises all of the Global Fortune 30 firms with manufacturing activities on ESG issues but does not have a vested interest in reporting per se, summarized a common perspective: “My gut sense is that companies will continue to take different approaches to reporting until external forces make it too inconvenient.”¹⁵⁵ Others agreed: “We can’t even agree on the meaning of ‘sustainability’ let alone standards for reporting. . . . We want, and we won’t give up, the power to selectively disclose what we want,”¹⁵⁶ citing concerns about increased liability risk related to disclosure.

Full consolidation also seems unlikely due to the number of ESG reporting service providers with a vested interest in maintaining some aspect of the status quo.¹⁵⁷ There is a

¹⁵³ See supra notes 68–73 and accompanying text.

¹⁵⁴ Christopher M. Bruner, Corporate Governance Reform and the Sustainability Imperative, 131 YALE L.J. 1217, 1242 (2022).

¹⁵⁵ Quote provided under condition of anonymity.

¹⁵⁶ Quote provided under condition of anonymity.

¹⁵⁷ These include enterprises and individual consultants selling customized solutions, their own systems, and dashboards and scoring systems to aggregate and make sense of data.
multiplicity of services in this arena, including the major accounting and consultancy firms, a variety of information platforms, and more than one hundred ratings companies, each with different questionnaires, methodologies, scopes, and audiences. Entrepreneurs are still founding new companies that aspire to provide novel internal ESG dashboards or new gold standard ratings generators, with investors pouring $570 million into environmental data startups in the first six months of 2021 alone. More established companies are also entering this crowded-yet-growing arena. In both the short and longer term, the variety of services and approaches to data seems to not militate in favor of convergence toward a harmonized and simplified approach to what gets disclosed and how.

To summarize, the variety of services dealing with ESG data that have invested resources in distinct approaches indicates there will be inertia not to radically change. In other words, there is path dependence that hinders rather than propels simplification and harmonization at the level of implementation. As much as theory and practice suggest that ESG reporting standards...
and norms will not be fully consolidated nor simplified, it is important to qualify this prediction, and acknowledge that the future of the ESG reporting governance regime writ large, including norms, is not completely certain. At least one alternative scenario could emerge. There is the possibility, for example, that the EU’s approach will, \textit{de facto}, create something of a worldwide norm, because international firms will opt to adopt one uniform standard across their global operations rather than tolerate the inefficiencies of redundant-and-inconsistent reporting methods. The phenomenon of EU standards impacting norms internationally has been observed in other contexts, and is known as the Brussels effect.\textsuperscript{167} However, this scenario would be limited to cases where it improved operational efficiencies or did not reveal potential liabilities, and as Professor Virginia Harper Ho points out, in the United States, the SEC seems to be set firmly on a fundamentally different course in the arena of ESG reporting governance.\textsuperscript{168} To disambiguate and clarify: it is almost certain, as Professor Harper Ho points out, that public ordering in the U.S. context will remain quite distinct from that of the EU.\textsuperscript{169} Nonetheless, many global firms may voluntarily adapt their practices to fit the EU’s new rules across all reporting jurisdictions. In other words, the EU approach may alter the private ordering of norms and action. It therefore cannot be fully ruled-out that the new EU standard may have an outsized global impact on what firms \textit{voluntarily} do, tilting global markets of ESG data service providers to gravitate toward the EU’s principles and approach.

Practitioners agree with the predictions of Part II based on theory: that the ESG reporting governance landscape is fragmented (complex), and seems unlikely to change, but there is some degree of uncertainty and ambiguity as to what may drive changing norms. This result presents strategic issues for business, which we explore below.

A. \textit{Guidance From Works on Law and Strategy and Proactive Law}

There are two different streams of literature that examine the relationship between business strategy and legal context: that of legal strategy and proactive law. Both advocate for lawyers and other professionals to work closely together.\textsuperscript{170} Both urge taking a holistic view and being proactive in terms of engaging with stakeholders and the legal environment.\textsuperscript{171} They both advocate

\begin{itemize}
  \item \textsuperscript{167} See Anu Bradford, \textit{The Brussels Effect}, 107 NW. U. L. REV. 1, 3 (2012). It is a well-documented fact that, in some contexts, companies adopt one standard based on one significant jurisdiction’s rules, rather than maintaining multiple approaches tailored to a variety of standards. \textit{Id.} at 6. See also Dominique Sinopoli & Kai P. Purnhagen, \textit{Reversed Harmonization or Horizontalization of EU Standards?: Does WTO Law Facilitate or Constrain the Brussels Effect?}, 34 WIS. INT’L L.J. 92, 98–99 (2016) (summarizing circumstances in which this may or may not occur). In the U.S., California laws can have a similar effect on national norms. See Deborah Keeth, \textit{The California Climate Law: A State’s Cutting-Edge Efforts to Achieve Clean Air}, 30 ECOLOGY L.Q. 715, 717 (2003).
  \item \textsuperscript{168} See generally Harper Ho, supra note 15.
  \item \textsuperscript{169} Id.
  \item \textsuperscript{171} See Siedel & Haapio, supra note 170, at 655, for their description of “a walk to the balcony” in the context of proactive law. Bagley’s original working paper, still publicly available, is Constance E. Bagley, \textit{What’s Law Got to Do with It: A Systems Approach to Business and Society} (Harv. Bus. Sch., Working Paper No. 06-038, 2006).
\end{itemize}
for detecting and eliminating problems before they escalate by approaching stakeholder engagement authentically as a two-way street. But the fields tend to differ in a few ways.

Legal strategy literature tends to focus more on the use of law to create economic value for the firm. The recent trend, as illustrated by the works of Robert Bird, has been to focus on competitive advantage more than risk mitigation, with a greater emphasis on private ordering more than influencing regulation, and the value of legal strategy has been explored in contexts of legal uncertainty. Proactive law scholars are more likely to urge the pursuit of certainty and clarity in the legal environment and tend to discuss the broader aim of generating shared benefits with stakeholders, although Professors George Siedel and Helena Haapio have discussed proactive law as a means to competitive advantage, and proactive law scholars are more likely to consider efforts to influence public regulation.

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175 But see Bagley, supra note 170, at 598–602.


178 Helena Haapio, supra note 177, at 21–34.


180 See Siedel & Haapio, supra note 170, at 641.

181 Id. at 641–56. But see Bagley, supra note 170, at 601–02.
The two theories taken together provide guidance on building strategy for a variety of contexts (both legally clear and legally uncertain), across a variety of regulatory frameworks (public and private) and to achieve risk mitigation and competitive advantage. Together, they present a portfolio of corporate strategies to address a complex and fragmented landscape.

Professor Stephen Park’s recent article building on legal strategy in the context of sustainability suggests that leaders take a wide view, be adaptive, and be better communicators of normative values with stakeholders.\(^{182}\) Park’s article points to the limitations of law and strategy literature in the context of complexity caused by disruptions and urges further research.\(^{183}\) We answer this call by looking to literature in the field of strategy, and what it suggests for contexts of complexity caused by fragmented governance. The strategy literature, and, more recently, legal strategy literature on how to respond to VUCA (volatile, uncertain, complex, and ambiguous) situations\(^{184}\) provides some steps for translating the broad themes of legal strategy and proactive law into specific steps for action.\(^{185}\) As explained in Part II, the challenge of ESG reporting governance is that it is fragmented and characterized by legal pluralism. ESG reporting is therefore complex and somewhat ambiguous, in that the exact cause-and-effect relationships between norms and stakeholders and institutions and standards can be opaque. While theory and practice both suggest the recent consolidation trend in ESG standards and governance is short-term and will not substantially advance, that trajectory is uncertain. ESG reporting governance thus reflects the contextual criteria noted in the VUCA literature, making the action steps proffered by that literature relevant to our analysis.\(^{186}\) These ideas, including their recent integration into legal strategy literature, suggest more specific direction than what has been provided in previous works on legal strategy and proactive law.

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\(^{183}\) See id. at 750.


\(^{185}\) As pointed out by Park, law and strategy is “not doctrinally rigid or normatively dogmatic” and tends to shy away from prescriptive advice. Park, supra note 182, at 719. VUCA has been applied to law recently, finding similar actionable advice to what the authors independently derived below. See Robert C. Bird, VUCA, 12 VA. L. & BUS. REV. 367, 402–23 (2018).

\(^{186}\) Although the VUCA paradigm was popularized by the U.S. Army War College (Bird, supra note 185, at 373–75) a close antecedent and steps for action in such contexts were articulated by two scholars of leadership in the 1980s, Warren Bennis and Burt Nanus, in their book, LEADERS: THE STRATEGIES FOR TAKING CHARGE (1986). See Herbert F. Barber, Developing Strategic Leadership: The US Army War College Experience, 11 J. MGMT. DEV. 4 (1992). As suggested by Nathan Bennett and G. James Lemoine, volatility can be countered by agility, which entails building-up extra resources to allow quick investments in new courses of action. Nathan Bennett & G. James Lemoine, What a Difference a Word Makes: Understanding Threats to Performance in a VUCA World, 57 BUS. HORIZONS 311, 312–14 (2014). Uncertainty can be countered by collecting more information. Id. at 314–15. Complexity can be countered by restructuring internal operations to mirror external complexities. Id. at 315–16. Finally, ambiguity can be countered by experimentation, which entails testing multiple approaches to any issue where old rules of the game may no longer apply. Id. at 316–17. Others, such as Robert Bird, have applied this lens and related prescriptive ideas to the role of business lawyers and independently came to suggestions that are consistent to what we will specifically offer for the context of ESG reporting. See Bird, supra note 185, at 402–23.
Consistent with the guidance and the practice of these related streams of literature and the positions of the authors who have produced them, this section addresses practitioners, including but not limited to managers and attorneys. 187

B. Suggestions for Practice on How to Think, Plan, and Act

This subsection takes the distilled principles from the bodies of literature reviewed above and applies them to the context of ESG reporting governance and standards to yield specific advice. We divide this examination into two aspects. The first is external, meaning the interaction of the firm with stakeholders that are not directly associated with the firm through employment. This aspect includes but is not limited to the bodies that set standards for ESG reporting. In this outward-facing context, we consider the opportunities and risks presented by the external environment of a firm. The second is internal, meaning the people and processes inside an organization. In this inward-facing context, we consider the aspects of a firm that give it strengths and weaknesses that can lead to competitive advantage in the context of fractured and complex ESG reporting governance.

1. External: Strategies vis-à-vis Reporting Standard Setters

As will be further explained and explored below, the key opportunities in a fractured and complex ESG reporting governance context are the potential to influence regulation, the option to engage in regulatory arbitrage, the chance to be seen as a leader in transparency, and the opportunity for authentic dialogue that improves the functioning of the firm and outcomes for all stakeholders. The key risk is transaction costs from reporting through multiple frameworks.

   a. The extremes of engagement: non-engagement with standard setters or engagement with all standards

First, management of a firm always has the option of not engaging with any standard-setting body or stakeholder groups. This option may seem attractive in the short term, as it costs less not to invest any effort or attention in stakeholder engagement or standard-setting, and there is the opportunity to freeride on whatever industry-friendly standards one’s competitors may succeed in influencing. This option is advised by neither the legal strategy literature nor literature on proactive law. Being a passive recipient of standards means having no voice or agency in setting the rules of the game, which means risking operating under unfavorable rules. A related yet distinct risk is

potentially being blindsided by a change in expectations of stakeholders and investors, which may or may not be related to the evolution of ESG reporting governance.

On the other end of the spectrum is the option to adopt all standards, which effectively takes the most arduous conceivable approach to ESG reporting. Literature on legal strategy and proactive law does not support such an approach, in that it does not manifest either intentional shaping of rules, nor an approach geared to creating and maintaining competitive advantage.

Practitioners agree these first options do not make sense, as evidenced by their engagement with both standard setting multi-stakeholder frameworks like GRI, plus the number of comments to the 2016 SEC concept release, which totaled more than 25,000. Clearly, non-engagement and staying silent are not preferred approaches. The other extreme of trying to adopt multiple standards is equally unsatisfactory in the real world. Reporting companies often complain that they are confused by the many different ESG reporting frameworks and struggle to distinguish them, making it difficult for companies to decide which reporting frameworks are most relevant and how to allocate their information disclosure resources. Exacerbating this confusion is the reality that different information users often favor different reporting frameworks and push companies to report through their framework of choice. The result is that companies feel compelled to issue reports under many of the Group of Five frameworks, increasing transaction costs to the company, and resulting in dissatisfaction with this approach as well.

b. Regulatory arbitrage, and possible engagement to preserve arbitrage opportunities

The second option, consistent with the pattern of partial cooperation alluded to above, is to take advantage of the fragmented reporting governance environment and engage in arbitrage. Regime theory scholarship also recognizes that fragmented regime complexes provide opportunities for regulatory arbitrage. Multiple scholars discuss the likelihood of fragmentation to allow for forum shopping among regimes, where regime actors pick-and-choose which regimes to join based on pursuit of their own self-interest. ESG reporting has its own versions of forum-

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188 More than 500 corporations and organizations comprised of businesses are GRI members. GRI MEMBER DIRECTORY, GLOBAL REPORTING INITIATIVE, https://www.globalreporting.org/reporting-support/gri-community/community-members/ (last visited June 24, 2022).

189 See Harper Ho, supra note 72, at 73 (citing to COMMENTS ON CONCEPT RELEASE: BUSINESS AND FINANCIAL DISCLOSURE REQUIRED BY REGULATION S-K, U.S. SEC. & EXCH. COMMISSION, https://www.sec.gov/comments/s7-06-16/s70616.htm (last visited June 24, 2022)).


191 Drezner, supra note 100, at 66.

192 See supra Part II.

193 Forum shopping in the regime context has been defined as the strategic use of different institutional settings to make progress on an individual agenda. Orsini, supra note 99, at 41. Other regime theory scholars describe forum shopping as a negative consequence of fragmentation. Raustiala & Victor, supra note 90, at 299; Alter & Meunier, supra note 98, at 16; Helfer, supra note 96, at 8.
shopping. Because frameworks are voluntary adopted, companies have wide discretion to decide exactly what and how to disclose under any given framework.

The representative quotes from practitioners included above illustrate their embrace of this selective approach to what is disclosed. Companies, or their hired professionals, use several strategies to engage in ESG reporting while effectively making their reports less useful. The first is including expansive materiality assessments that add volume, details and narrative about how management engages in stakeholder dialogue, yet effectively provides a justification for not including certain data. These companies then embrace their prerogative to decide what specific disclosure items to act upon or ignore, as well as choosing to disclose only information that portrays the company in a positive light or to disclose information in broad, general terms. As one executive at a consumer brand (defined by their embrace of sustainability in its core activities) once rhetorically asked, when explaining why the company would “never again” produce an ESG report: “How many pictures of smiling brown babies do you need to see before you realize these reports are b.s.” In other words, as detailed by another ESG reporting implementer-turned-critic-and-scholar: it is de rigueur for ESG reports to be misleading in terms of what and how data is presented and to catalog positive vignettes of charitable side projects rather than profound-and-needed changes to core activities. The sheer length of typical reports and failure to present concise, comparable, comprehensive, credible, and current data are other manifestations of companies engaging in the first variety of forum shopping. The ability to manipulate reporting processes has had a negative impact on the quality of information disclosed, undercutting the comparability and utility of the disclosures.

The other manifestation of forum shopping, as alluded to above, is active engagement with standard setting organizations in a manner that is entirely self-serving. The results of Virginia Harper Ho’s empirical analysis of comments submitted in the 2016 SEC Concept Statement are suggestive of both forum-shopping tendencies. First, the substance of company comments revealed reporters’ attitudes against mandated minimum disclosures, plus their engagement in registering these opinions in the rule-making system manifests the second kind of forum-shopping conduct. A minority of comments from reporting corporations (10%) supported any kind of increased and

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194 See supra, Part II.


196 Harper Ho, supra note 16, at 488.

197 Anonymous source.


200 See supra notes 10–14 and accompanying text.
specific disclosure requirements, compared to 88% of investors. In contrast, 75% of reporters clearly opposed the use of prescriptive disclosures, in contrast to less than 6% of investors. In other words, in this data, and the comments that comprised the dataset, we see the willingness of reporting organizations to find ways and pretexts to effectively under-disclose, plus engagement with standard setting organizations that preserves their prerogative to under-disclose.

We therefore see a clear tension between resistance of firms against harmonization and mandating of ESG reporting, and, on the other hand, rhetoric and the wishes of investors to harmonize, simplify, and require mandatory minimum ESG disclosures. This tension can be explained by firms’ pursuit of competitive advantage and their belief that regulatory arbitrage is more advantageous for that purpose. While such arbitrage may appear to be a better strategy in the short-term, in the longer term firms are likely better off with a simpler and less fragmented set of ESG reporting rules. This points to a potentially useful line of future empirical inquiry. It also provides the segue from moving from describing what most companies do, to our suggestions about what would be a more optimal approach to ESG reporting, starting with guidance on how to interface with the ESG reporting governance regime.

c. Active and constructive engagement with standards-setters and stakeholders

The third option is to lobby governmental and non-state standard-setting bodies to simplify, harmonize, and make minimum disclosures mandatory, or some variation of this approach, such as asking for a targeted set of transparency initiatives. It is a truism expressed in the proactive law movement that firms prefer regulatory certainty. Management literature also observes that corporate strategies function best when there is certainty in a company’s environment, as opposed to uncertainty. Legal strategy and proactive law both allow for lobbying rule-makers, with legal strategy literature tending to focus more on the benefits that result in terms of competitive advantage. Proactive law theory emphasizes that attorneys should assist management in working to shape the rules of the game, with attorneys functioning as active creators rather than passive recipients of rules. Having established these broad foundations and guidance in extant literature, we will now specify how they can be applied in greater detail.

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201 Harper Ho, supra note 72, at 95.
202 Id.
203 See Harper Ho, supra note 72.
204 It has been posited that mandating minimum ESG disclosures would serve the interests of firms by providing clarity and certainty and therefore improving efficiency. See Adam Sulkowski & Sandra Waddock, Beyond Sustainability Reporting: Integrated Reporting is Practiced, Required and More Would Be Better, 10 U. ST. THOMAS L.J. 1060, 1084 (2013).
205 See Hess, supra note 2, at 5–10.
206 See Siedel & Haapio, supra note 170, at 642–56.
208 See Bagley, supra note 170, at 598–602.
209 See Haapio, supra note 177, at 21–34.
i. Engagement with government standard-setters

First, with regard to government standard setters, proactive law principles provide the clearest direction: reduce risk through cooperation to create certain rules. The outcomes of applying legal strategy ideas depend on the time horizon of a decision-maker: a longer term view aligns with cooperating to create certain rules, while a short-term approach militates in favor of possibly boosting competitive advantage by preserving more autonomy over disclosure. We suggest taking a longer-term approach to strategy, which aligns with the guidance of proactive law and leads us to suggest cooperating with, for example, the SEC in the movement to bring greater clarity and certainty to ESG disclosure. The SEC’s recently proposed rule on climate-related disclosures is an example of an opportunity to shape the contours of climate reporting. A longer-term view recognizes that mandatory climate reporting will likely happen, and it should lead a firm to participate in any comment period, using experience with the TCFD standard to inform feedback. Rather than trying to obstruct the process, a firm could constructively engage in the rule-making process.

At any rate, the SEC’s recently proposed rule only relates to climate and preserves an approach based on materiality assessments, so even firms with a shorter-term approach should not have a particularly strong reason to object to this rule. Those firms with a longer-term perspective may actually start advocating for mandatory minimum disclosures that are broader in scope and less subject to discretion of other parties.

ii. Engagement with private standard setters

This option raises a separate-and-distinct front for external stakeholder interactions. Firms have the opportunity to engage with private standard setters to move consolidation forward. Firms should work collaboratively through organizations such as the Business Roundtable to voluntarily agree upon, and commit to, reporting under the same standard and working with investors and other stakeholders to determine which standard to embrace, most likely GRI or SASB. This may encourage standard setters on the periphery to align with or to consolidate with stronger players. Once again, proactive law principles militate in favor of a cooperative approach that builds certainty and consensus about rules. Embracing legal strategy from a longer-term perspective aligns well, inasmuch as creating certainty about the future boosts a firm’s future competitiveness by allowing it to plan investments and activities with confidence.

iii. Engagement with stakeholders

The key steps to leverage opportunities and minimize risks, based on the literature of legal strategy and proactive law, involve keeping an expansive and holistic view and engaging constructively with stakeholders. Specifically and tangibly, this translates to building or maintaining strong ties with relevant stakeholder groups to be sure that mandated and chosen voluntary standards meet their information needs.

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211 See Bagley et al., supra note 172, at 12–13; see Siedel & Haapio, supra note 170, at 657–61.
This approach is consistent with the guidance of scholars who suggest that firm leadership authentically engage in a broad dialogue and focus on problem-solving with stakeholders. This approach may further involve firms raising awareness of an ESG issue, seeking information to identify potential ESG problems, and aligning stakeholders into coalitions to support shaping reporting practices, norms, rules, and standards, in ways that co-create value for both the firm and its stakeholders. It is consistent with the suggestion of several legal strategy scholars that firms embrace feedback loops, or, as David Hess refers to the concept, an action cycle. In this context, it means approaching ESG communication as an authentic two-way street that can improve firm functioning rather than a one-way reporting exercise.

All of the foregoing advice on stakeholder engagement dovetails with the advice of Eccles and Mirchandani, who built upon the work of TruValue Labs and underscored the growing capacity of stakeholders, who are connected, informed, and empowered by information technology, to affect the definition of materiality over time as it is applied in practice. Our guidance on stakeholder engagement is also consistent with opinions associated with the World Economic Forum, which, in collaboration with Boston Consulting Group, points out that the rate of immaterial issues that become material is accelerating and that the general availability of data and transparency is growing.

Our advice to pursue authentic two-way communication to ensure that new reporting standards meet evolving stakeholder expectations is likely to serve a firm and its stakeholders well in any contingency. The advice should be constructive, however the governance of ESG reporting may (or may not) evolve, including scenarios in which legal pluralism in the ESG regime endures. This approach should work, for example, if the governance framework evolves, as suggested by New Governance, in which government serves as an orchestrator of stakeholder dialogue.

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214 See Bagley, supra note 172, at 11; Sulkowski, supra note 172, at 22–24; Orozco, supra note 172, at 97; Park, supra note 172, at 114.


216 Id.


218 See TRUVALUE LABS, supra note 147, at 6–11.

219 See WORLD ECON. F., supra note 148, at 7–9.

Likewise, two-way engagement fits well with Virginia Harper Ho and Stephen Park’s vision of a hybrid private-public ordering of disclosure rules, or if targeted transparency initiatives further develop as the governance architecture described by David Hess. It also is consistent with Park’s suggestions of a collectivist approach and with calls from both legal strategy and proactive law scholars to approach engagement with stakeholders and ESG data to detect and eliminate the causes of costly conflict. Authentically engaging with stakeholders to shape better transparency norms is also consistent with the original intent of ESG reporting, which was to disrupt and improve upon business-as-usual with regard to sustainability.

2. Internal: Boosting Strengths and Reducing Weaknesses

Strengths are defined as the internal aspects of a firm that give it advantage over competitors, or that make it uniquely adapted to carry out its tasks. Weaknesses are defined as internal attributes of a firm that diminish its ability to carry out tasks. Ultimately, although these are seen to be attributes over which management has more control (in contrast to external conditions), the actual advantage or disadvantage of an internal aspect of a firm is realized when the firm interacts with the world outside its boundaries. For example, its competitive advantage is manifested when it wins more market share, secures greater profit margins, and is valued by investors vis-à-vis competitors. These truisms are important to note, because we next explore implications of ESG reporting developments with regard to internal aspects of a firm. Yet, at times the significance of these attributes will be explained by reference to their value as determined by factors beyond the boundaries of the firm.

The advice of this section holds true, regardless of which of the three strategies (articulated in the previous section) a company chooses, and it builds from all of the previously described literature. In particular, the literature related to strategy in VUCA contexts helps to translate previously broad themes into actionable steps related to internal processes.

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221 See generally Harper Ho & Park, supra note 159. Stakeholder relations may continue to be vital even in situations where ESG reporting is standardized and mandated. See Lucien Dhooge, Beyond Voluntarism: Social Disclosure and France’s Nouvelles Régulations Économiques, 21 ARIZ. J. INT’L & COMP. L. 441, 452–68, 476–90 (2004).

222 See generally Hess, supra note 2, at 6–10.

223 See Park, supra note 182, at 747–49.

224 See Siedel & Haapio, supra note 170, at 665 (on engaging with stakeholders proactively to align goals and actions); Berger-Walliser et al., supra note 172, at 28–32 (on engaging in sustainability reporting).

225 Adam Sulkowski, 20 Years Ago He Gave Cannibals Forks. Now John Asks: Where’s the Disruption?, HUFFPOST (July 12, 2017, 10:32 AM), https://www.huffpost.com/entry/20-years-ago-he-gave-cannibals-forks-now-john-asks_b_59637fabe4b085e766b51450 (documenting an interview in which John Elkington, an early proponent of ESG reporting, lamented that the movement had failed to be the intended “whack to the head” of business leaders).


227 Id. at 51.

228 See Barney, supra note 165, at 100–01 (explaining the value of exploring the heterogeneity of firms with respect to internal resources); see also Michael E. Porter, How Competitive Forces Shape Strategy, HARV. BUS. REV. (Mar.–Apr. 1979), https://hbr.org/1979/03/how-competitive-forces-shape-strategy.
To hedge against any amount of risk of change in norms, firms are advised by Robert Bird to be agile,\textsuperscript{229} or, as Stephen Park calls it in the context of adapting to disruption, to be resilient.\textsuperscript{230} The literature on VUCA specifies what a firm can do internally to respond rapidly to changing conditions: build surplus capacity and slack.\textsuperscript{231} This notion is conceptually similar to the component of resiliency that Park calls adaptiveness,\textsuperscript{232} or the ability to adapt to new conditions, and he similarly discusses risk from an over-emphasis on efficiency interfering in a firm’s adaptiveness.\textsuperscript{233} In this context, this approach means hedging against the risk of changing industry norms or expectations of either regulators, non-state standard-setters, or those of stakeholders. The spare capacity that must be built (in the context of ESG reporting) is in information. In other words, the ability to rapidly and accurately disclose more information is an internal capacity that can be a comparative strength that may yield competitive advantage. An inability or delays in the ability to meet changing disclosure expectations can be a weakness.

Recent strategy literature on how to deal with uncertainty, complexity, and ambiguity (through more information gathering, mirroring external processes, and experimentation\textsuperscript{234}) in this context mirror similar recommendations by David Hess in the literature on New Governance: engaging in experiments reflecting stakeholder expectations such that data drives actions for improved performance.\textsuperscript{235} This recommendation is consistent with guidance from literature on legal strategy and proactive law, including recent works on feedback loops, or using the communication of information to improve firm functioning.\textsuperscript{236} It also is consistent with the vision of reflexive law,\textsuperscript{237} or the guiding of firms to continuously re-examine and improve their functioning,\textsuperscript{238} as applied in the context of ESG reporting.\textsuperscript{239} In more granular and specific terms, managers and attorneys can build strength in this domain by staying abreast of, and judiciously

\textsuperscript{229} See Bird, supra note 185, at 403–07.
\textsuperscript{230} See Park, supra note 182, at 740–44.
\textsuperscript{231} See Bennett & Lemoine, supra note 186, at 312–14.
\textsuperscript{232} See Park, supra note 182, at 744–47.
\textsuperscript{233} See id., at 740–44.
\textsuperscript{234} This approach of experimentation has been suggested in the similar context of the fragmented governance environment of marijuana. See Mike Schuster & Robert C. Bird, Legal Strategy During Legal Uncertainty: The Case of Cannabis Regulation, 26 STAN. J. L. BUS. & FIN. 362, 399–410 (2021); see also W. Michael Schuster & Jack Wroldsen, Entrepreneurship and Legal Uncertainty: Unexpected Federal Trademark Registrations for Marijuana Derivatives, 55 AM. BUS. L.J. 117, 120–23 (2018).
\textsuperscript{236} See generally Bagley, supra note 172; Sulkowski, supra note 172; Orozco, supra note 172; Park, supra note 182; Berger-Walliser, supra note 172; Siedel & Haapio, supra note 170.
\textsuperscript{237} Eric W. Orts, A Reflexive Model of Environmental Regulation, 5 BUS. ETHICS Q. 779, 779 (1995).
\textsuperscript{238} Id. at 779–80.
investing in, the latest developments for gathering, sharing, and using information.\(^{240}\) Equally important is appreciating the limitations of new data systems and technologies.\(^{241}\)

A key weakness or impediment to agility and the ability to gather, understand, and report more data, are organizational silos, even in the digital age.\(^{242}\) They are often best understood as the result of human weaknesses, such as the desire to protect status and turf, and are often the cause of institutional weaknesses.\(^{243}\) At worst, they lead to calcification, redundancy, waste, and prevent the flow of information.\(^{244}\) Therefore, to develop spare capacity to gather, understand, and use ESG data, and to experiment in its constructive usage, it may be necessary to build systems that allow for the frictionless and timely flow of data.\(^{245}\) In other words, in the context of ESG reporting in a continued fragmented and complex governance landscape, it is preferable to eliminate silos that limit information sharing, and to build firms’ capacity to gather, report, and act upon ESG data.\(^{246}\)

Besides building spare capacity so as to be agile, and eliminating silos that may restrict the free movement of information, recent works on dynamic materiality led us to some further specifics of how firms can adjust internal operations. These include continually assessing which issues are now material, or becoming material.\(^{247}\) It entails evaluating whether sufficient sources of data and opinions are being considered.\(^{248}\) Dynamic materiality literature also suggests asking if strategy and engagement with stakeholders are, at all levels, aligned and informed by what a firm determines to be future material issues.\(^{249}\) Finally, accepting dynamic materiality behooves a firm’s leadership to ask if the firm is changing its operations fast enough to optimize for what will soon become material performance measures.\(^{250}\) Once again, these steps are specific enough to be actionable, yet agnostic as to other strategic directions a firm may take, and sufficiently general to be constructive regardless of whether and how the ESG reporting regime may (or may not) evolve.

\(^{240}\) Joan MacLeod Heminway & Adam J. Sulkowski, *Blockchains, Corporate Governance, and the Lawyer’s Role*, 65 Wayne L. Rev. 17, 49 (2019).


\(^{244}\) Fabio Bento, Marco Tagliabue & Flora Lorenzo, *Organizational Silos: A Scoping Review Informed by a Behavioral Perspective on Systems and Networks*, 10 Societies 56, 56 (2020) (reviewing empirical studies finding that siloes interfere with information flows across organizations).

\(^{245}\) Sulkowski, supra note 241, at 318–19.

\(^{246}\) Heminway & Sulkowski, supra note 230, at 49–51; Bird, supra note 185, at 409 (stating the need to dismantle information barriers).

\(^{247}\) *World Econ. F.*, supra note 148, at 13.

\(^{248}\) *Id.*

\(^{249}\) *Id.*

\(^{250}\) *Id.*
CONCLUSION

ESG disclosure is an important mechanism to promote sustainability, especially in the absence of substantive regulation of ESG issues. From its origins as a tool of civil society to increase corporate disclosure, the field has grown to include many of the world’s largest companies as reporting entities. The ESG reporting regime, created by a multiplicity of private actors, is characterized by the complexity and fragmentation common in pluralistic systems. Information producers and information users are critical of the current state of affairs and both desire a simpler system of uniform standards.

The surest path to consolidation of ESG reporting standards is through government mandated disclosure grounded in a globally recognized standard, a path that seems unlikely. This governmental void has created an opportunity for private standard setters to consolidate and simplify ESG reporting and recent activity has suggested that is a real possibility. Yet, viewing the ESG reporting ecosystem through the lens of regime theory shows that significant fragmentation of ESG reporting will likely continue into the future.

Continued fragmentation of the system leaves reporting companies with a choice: continue to pick their way through complexity or advocate for the simplification they claim to want. This article argues that companies should recognize the investor demand for ESG information and work with investors and regulators toward a new understanding of the intersection between ESG factors and financial materiality. At the same time, firms must recognize the impact that the EU double materiality standard, and the divide between the U.S. and EU approaches to reporting, will have on firms with globally diversified operations. These companies should deepen authentic ties with stakeholders to meet current information needs but also to better prepare for future information needs. Proactive engagement with standard setters and information users is the best option to ease the burden and reduce the risks of navigating the complex environment. Doing so may help nudge the ESG reporting ecosystem toward the global standardization and harmonization that is necessary to make ESG disclosure an effective tool to achieve sustainability.