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## **ESG: Real impact over vague intentions**

The corporate world is filled with acronyms and initialisms, some confusingly similar and others oddly familiar. Let's unravel ESG and CSR.

For some time, Corporate Social Responsibility (CSR) was the code for the integration of social and environmental concerns into business activities. The core focus of CSR could be viewed as voluntary philanthropic activities to enhance a company's reputation, "*feel good*" initiatives that told "*nice narratives*".

CSR is not a measurable tool directly linked to performance, and companies could elect to participate. Because of this, consistency and factual reporting were neglected.

### **ESG: A Financial Risk Tool**

Coined in 2004, The term ESG was a product of a UN initiative where Kofi Annan invited leaders from major financial institutions to integrate sustainability into capital markets. This established the business study that non-financial E, S, and G factors materially impact long-term investment value and risk.

The aim was to create a quantifiable framework for investors to spot hidden risks (e.g. poor governance, environmental liabilities) for better informed decisions, beyond mere ethics or reputation.

ESG stands for Environmental, Social and Governance. It is a framework used to assess how a company manages risks, opportunities, and impacts relating to sustainability, ethics, and responsible business conduct. Unlike older corporate social responsibility (CSR) models, ESG is measurable, reportable, and increasingly linked to financial performance and regulatory compliance.



For South African companies King III (2009) made integrated reporting mandatory for Johannesburg Stock Exchange (JSE) listed companies, embedding the concept of business as an integral part of society. Companies were required to report on their sustainability and financial performance in a single document detailing how they impacted the environment, society, and economy.

The new King V™ Report, which replaces King IV™ and took effect on 1 January 2026, refines but also deepens ESG integration. It is supported by a continuously updated legislative landscape, including the Climate Change Act 22 of 2024 (which makes carbon budgets legally binding) and the Companies Amendment Act 16 of 2024 (which formalises director accountability, remuneration and social & ethics committee mandates).

### The Core Problem ESG Aims to Solve

Broadly, ESG is an attempt to fix a critical market failure where corporate actions generate significant "side effects" at great cost to society, such as:

- **Climate Change & Environmental Degradation:** Pushing companies to measure, report, and reduce their emissions, pollution, and natural resource depletion.
- **Social Inequality & Injustice:** Addressing human capital issues from diversity and fair labour to modern slavery, particularly in South Africa's effort to tackle vast inequality.
- **Corporate Scandals & Governance Failures:** Providing oversight on issues like board diversity, executive pay, transparency, and ethics to prevent misconduct.

### ESG Elements

#### Environmental (E)

Focuses on how a company impacts the natural environment. This includes:

- **Climate change and carbon emissions:** Scope 1 (direct emissions), Scope 2 (indirect emissions), and Scope 3 (indirect emissions in the value chain) emissions reporting, required under International Financial Reporting Standards (IFRS) S2: Climate related disclosures, and the Climate Change Act.
- **Energy efficiency:** Including transition to renewable energy, energy intensity per unit of production, and compliance with the Carbon Tax Act 15 of 2019.
- **Water use:** Water scarcity risk, water recycling, and compliance with the National Water Act 36 of 1998.
- **Waste management:** Circular economy principles, hazardous waste disposal, and extended producer responsibility (EPR) schemes.
- **Pollution control:** Air emissions (e.g. particle pollution, Sulphur oxides) under the Air Quality Act 39 of 2004.



- **Biodiversity and environmental compliance:** Impact on ecosystems, deforestation, and adherence to the National Environmental Management Act 107 of 1998 (NEMA), including potential liability for environmental damage.
- **Climate adaptation:** Mitigation of Physical risks to assets (floods, droughts, fires) and transition risks (policy, technology, market shifts).

Examples:

A mining company must now report on tailings dam safety, water usage per ton of ore, and rehabilitation liabilities. A retailer must report on packaging waste and cold chain emissions.

## Social (S)

Focuses on relationships with people and society, including:

- **Labour practices and employee wellbeing:** Fair wages, working hours, collective bargaining, and compliance with the Labour Relations Act 66 of 1995 (LRA) and Basic Conditions of Employment Act 75 of 1997 (BCEA).
- **Health and safety:** Occupational Health and Safety Act 85 of 1993 (OHSA) compliance, injury frequency rates, and psychosocial safety (burnout, harassment).
- **Diversity, equity and inclusion (DEI):** Employment Equity Act 55 of 1998 (EEA) compliance, gender and race representation at board and management levels, pay gaps, and accessibility for persons with disabilities.
- **Human rights:** UN Guiding Principles on Business and Human Rights, modern slavery due diligence in supply chains.
- **Community impact:** Social and Labour Plans (important in construction and mining), local procurement, resettlement practices, and management of community grievances.
- **Customer protection and data privacy:** Protection of Personal Information Act 4 of 2023 (POPIA) compliance, responsible marketing, and product safety.

Examples:

A logistics company must track driver fatigue management, road accident fatality rates, and the working conditions of third-party contract drivers. A financial institution must monitor data breach notifications and complaints handling from vulnerable customers.

## Governance (G)

Focuses on leadership, ethics, and oversight, including:

- **Board structure and independence:** Proportion of independent non-executive directors, separation of CEO and chair, director tenure limits, and evaluation processes.
- **Ethics and anti-corruption:** Prevention and Combating of Corrupt Activities Act 12 of 2004 (PRECCA) compliance, gifts registers, whistleblower policies, and anti-bribery management systems (ISO 37001).



- **Risk management:** Enterprise risk management (ERM) integration, emerging risks (e.g. AI, climate litigation), and risk appetite statements.
- **Regulatory compliance:** Compliance function independence, regulatory breach reporting, and operational licence monitoring.
- **Executive remuneration:** Claw back provisions, ESG-linked performance conditions, and disclosure of pay ratios (CEO-worker pay gap).
- **Shareholder rights:** Proxy voting, related-party transaction approvals, and minority shareholder protection.
- **Internal controls and accountability:** Financial and non-financial internal controls, internal audit coverage of ESG data, and audit committee oversight.

Examples:

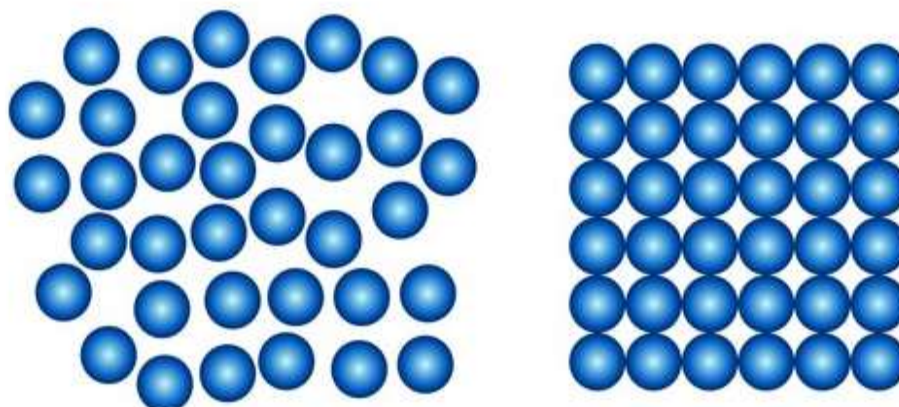
A state-owned entity must disclose political donations, tender irregularities, and board member conflicts of interest. A tech company must disclose AI governance frameworks and algorithmic bias testing.

## ESG Shift

ESG has evolved from a voluntary, broad concept under CSR, to a structured, core business and governance requirement enforced by law, capital markets, and supply chains. It is also a rapidly transforming framework due to its socio-economic context.

Investors, banks, development finance institutions, and insurers increasingly assess ESG performance before: investing, financing, underwriting or entering partnerships (joint ventures, offtake agreements). ESG is not just a global trend, but a strategic imperative tied to long-term legitimacy and value creation.

Partner with Cyclopedic Consulting to align and build a robust ESG policy and culture.



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