FROM COMPLIANCE TO COMPETITIVE ADVANTAGE: A CASE FOR THE BOARDS OR HOW EUROPEAN ESG REGULATION RESHAPES CORPORATE STRATEGY

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OPEN ACCESS

How to cite this paper: Voto, A. (2025). From compliance to competitive advantage: A case for the boards or how European ESG regulation reshapes corporate strategy. *Corporate Board: Role, Duties and Composition, 21*(2), 102–108.
https://doi.org/10.22495/cbv21i2art9

ISSN Online: 2312-2722
ISSN Print: 1810-8601

Received: 30.05.2025
Revised: 29.07.2025; 13.08.2025
Accepted: 22.08.2025

JEL Classification: G38, L51, M14, M41, Q56
DOI: 10.22495/cbv21i2art9

Abstract

This study analyzes the evolution of corporate social responsibility (CSR) into environmental, social, and governance (ESG) frameworks, examining the shift from voluntary initiatives to mandatory regulatory compliance. Through historical analysis and case studies, we trace how sustainability practices transformed from philanthropic activities to strategic business imperatives. The study focuses on European Union (EU) regulatory changes, particularly the European Sustainability Reporting Standards (ESRS), which establish binding sustainability obligations for businesses. The findings reveal that this transition creates both challenges and opportunities for organizations, requiring integration of sustainability into core strategy while potentially driving innovation and competitive advantage. The research provides actionable guidance for business leaders navigating mandatory ESG requirements, emphasizing that sustainability has become both a strategic and regulatory imperative in global business.

Keywords: ESG Strategy, Corporate Governance, Regulatory Compliance, Dual Materiality, Sustainable Value Creation, Board Leadership, European Sustainability Reporting Standards, ESRS

Authors' individual contribution: The Author is responsible for all the contributions to the paper according to CRediT (Contributor Roles Taxonomy) standards.

Declaration of conflicting interests: The Author declares that there is no conflict of interest.

1. INTRODUCTION

In today's rapidly evolving global landscape, sustainability has transformed from a voluntary corporate initiative to a strategic imperative driven by regulatory requirements and stakeholder expectations (Korca et al., 2021). Growing pressures from investors, regulators, customers, and employees have fundamentally altered corporate responsibility frameworks, necessitating the integration of environmental, social, and governance (ESG) principles into core business strategies (Fera et al., 2025). This transformation reflects a broader shift in corporate governance paradigms, where traditional profit maximization models are increasingly challenged by stakeholder capitalism approaches (Freeman et al., 2010; Porter & Kramer, 2011).

The evolution from corporate social responsibility (CSR) to ESG represents more than a semantic change — it signifies a fundamental restructuring of how businesses conceptualize their role in society (Carroll, 2015; Whelan et al., 2021). While CSR traditionally focused on philanthropic activities and voluntary initiatives, ESG frameworks emphasize measurable performance indicators and regulatory compliance (Amel-Zadeh & Serafeim, 2018). This transition has been particularly pronounced in the European Union (EU), where regulatory frameworks such as the European Sustainability Reporting Standards (ESRS) have transformed sustainability from a voluntary practice to a legal obligation (European Commission, 2023).

For business leaders — board members and chief executive officers (CEOs) alike — this change in basic assumptions presents both challenges and opportunities. Compliance with emerging sustainability regulations extends beyond meeting legal obligations to encompass strategic value creation, innovation drivers, and competitive advantage development (Eccles & Klimenko, 2019; Friede et al., 2015). The integration of ESG principles requires fundamental changes in corporate governance structures, risk management frameworks, and performance measurement systems (Governance & Accountability Institute [G&A Institute], 2020).

This paper contributes to the growing literature on CSR-ESG evolution by providing a comprehensive analysis of the transition from voluntary responsibility to mandatory compliance frameworks. Through historical analysis, regulatory examination, and case study evaluation, this research addresses the gap between theoretical conceptualizations of corporate responsibility and practical implementation challenges faced by business leaders (Korca et al., 2021). The study particularly focuses on European regulatory developments, offering insights into how mandatory sustainability reporting requirements reshape corporate behavior and strategic decision-making processes.

2. THEORETICAL BACKGROUND

2.1. From philanthropic initiatives to early theoretical foundations

The history of CSR begins with spontaneous philanthropic initiatives during the Industrial Revolution. The earliest evidence of corporate concern for society dates back to the first half of the 19th century, when criticism of factory working conditions and child labor created conditions for a different view of enterprise and capital accumulation (Carroll, 2015; Crane et al., 2019).

Early examples of business-generated philanthropy include Andrew Carnegie, who donated significant wealth to social impact projects, creating over 2,500 public libraries and funding scientific research, education, and world peace causes (Gautier & Pache, 2015). Similarly, John D. Rockefeller, based on Carnegie's (1889) "Gospel of Wealth" principle, donated over half a billion dollars to scientific, educational, and religious causes, transforming philanthropy into a structured activity that anticipated modern CSR concepts (Karnani, 2010; Scherer & Palazzo, 2011).

These philanthropic initiatives generated the first image returns for families, brands, and companies, triggering embryonic CSR processes. The global dissemination of pro-community programs fostered the development of the first theoretical reflections on integrating solidarity principles into corporate spheres (Aguinis & Glavas, 2012; Crane et al., 2008).

Berle and Means (1932) were among the first to theorize correlations between ethical-social motivations and enterprise value, analyzing ownership-control separation effects in large corporations. Their work highlighted how dispersed ownership created opportunities for corporate culture formation oriented towards social responsibility. The resulting Berle-Dodd debate established fundamental tensions still relevant in contemporary CSR discussions (Lan & Heracleous, 2010).

Bowen (2013), in *Social Responsibility of the Businessmen* — firstly published in 1953 and considered as the first academic CSR text — sought a balance between economic and social interests through voluntary self-discipline codes, earning recognition as the "father of CSR" (Carroll, 2015). Subsequent decades saw continued theoretical development through Davis's (1960) principle of the iron law of responsibility, which argued that responsibility and power influence each other, and McGuire's (1963) introduction of corporate citizenship concepts (Garriga & Melé, 2004).

Friedman (1970) provided the main neoclassical counterargument, asserting that firms' sole social responsibility was profit maximization within legal boundaries. This shareholder primacy view dominated through the 1980s but increasingly faced challenges from stakeholder theory advocates (Jensen, 2010).

2.2. Corporate social responsibility maturation and the stakeholder revolution (1990–2000)

The 1990s marked widespread CSR acceptance. Carroll's (1991) pyramid of CSR organized responsibilities hierarchically: economic, legal, ethical, and philanthropic, evolving CSR from a marginal concept to a strategic management element (Schwartz & Carroll, 2003). The 2000s witnessed CSR's transformation into a comprehensive strategy adopted by globalized companies, focusing on integrating social, environmental, and economic concerns into business operations (Aguinis & Glavas, 2012).

This era marked the decisive transition from shareholders to stakeholders' theory (Freeman et al., 2010). Stakeholder theory's adoption represented a broadening of corporate constituencies, moving from profit-oriented views to principles based on ethical and social standards beyond legal compliance (Jones et al., 2018). Contemporary research demonstrates that effective stakeholder engagement correlates with improved financial performance, innovation capacity, and risk management (Henisz et al., 2014).

Porter and Kramer's (2011) concept of "shared value" revolutionized CSR thinking by connecting corporate success with social progress through three approaches: rethinking products and markets, redefining productivity in value chains, and creating supportive industry clusters. Empirical research validates this approach's effectiveness, showing that companies integrating social and environmental considerations into core strategies outperform peers in financial metrics and innovation capacity (Flammer, 2015; Friede et al., 2015).

2.3. The limitations of voluntary corporate social responsibility and the ESG transition

The evolution from CSR to ESG represents the latest theoretical development, reflecting demands for standardized, measurable sustainability metrics (Whelan et al., 2021). Unlike traditional CSR's often voluntary and qualitative approaches, ESG frameworks emphasize quantifiable performance indicators and regulatory compliance (Amel-Zadeh & Serafeim, 2018).

The limitations of voluntary CSR frameworks became evident through high-profile corporate failures. The Volkswagen emissions scandal exemplifies this challenge: while the company publicly promoted environmental commitment through "clean diesel" marketing, internal systems deliberately deceived emissions testing through sophisticated software manipulation (Drempetic et al., 2020). This case illustrates the fundamental tension between voluntary responsibility and actual corporate behavior, highlighting why stakeholders increasingly demanded mandatory reporting and verification mechanisms.

Such failures created conditions for more robust regulatory frameworks. The EU's response through the ESRS represents a direct regulatory answer to voluntary CSR inadequacy, establishing binding requirements for sustainability disclosure and third-party verification (European Commission, 2023).

3. RESEARCH METHODOLOGY

This study employs a qualitative research approach combining historical analysis, regulatory examination, and case study methodology to trace the evolution of CSR into ESG frameworks. The research design follows established methodological approaches for analyzing institutional change and corporate governance evolution (Eisenhardt, 1989; Yin, 2018).

3.1. Analytical framework

The study adopts Carroll's (1991) Pyramid of CSR as the primary analytical framework for understanding CSR evolution (see Figure 1). This framework remains methodologically relevant due to its systematic categorization of corporate responsibilities into four hierarchical levels: economic, legal, ethical, and philanthropic (Carroll & Shabana, 2010). The pyramid's enduring applicability stems from its clear delineation of responsibility types and gradual intervention characteristics, making it suitable for cross-sectoral analysis (Visser, 2006).

Figure 1. Caroll's pyramid of corporate social responsibility

Source: Janse (2020).

The four-level framework provides the following structure:

- Economic responsibilities: Basic condition for corporate existence and sustainability.
- Legal responsibilities: Operating within legal boundaries and fulfilling regulatory requirements.
- Ethical responsibilities: Acting morally beyond legal requirements, making conscious decisions to "do the right thing".
- Philanthropic responsibilities: Voluntary contributions to society through charitable activities.

3.2. Data collection and analysis

The research methodology incorporates three primary data sources:

- Historical analysis: Examination of seminal CSR literature from 1932 to the present, tracing theoretical development through key scholarly contributions.
- Regulatory analysis: Systematic review of EU sustainability legislation, particularly ESRS implementation processes and requirements
- Case study analysis: Examination of corporate sustainability practices and regulatory compliance challenges through illustrative examples

This methodology aligns with established approaches for analyzing institutional change in corporate governance (Scott, 2008). The combination of historical analysis and regulatory examination provides the temporal depth necessary for understanding CSR-to-ESG evolution, while case studies offer practical insights into implementation challenges and opportunities.

4. RESEARCH RESULTS AND DISCUSSION

4.1. Foundation of European corporate social responsibility: From voluntary commitment to strategic imperative

Corporate social responsibility in the EU emerged from President Delors' 1993 call for European companies to combat social exclusion, evolving into a comprehensive framework through the 2000 Lisbon European Council's extension to lifelong learning, work organization, equal opportunities, and sustainable development. Initially characterized by voluntary initiatives exceeding regulatory obligations, CSR promoted high standards of social development and environmental protection while fostering stakeholder partnerships.

However, recent studies highlight how voluntary CSR frameworks often suffer from "selective adoption," where companies easily prioritize achievable goals over transformative change (Christensen et al., 2022). The EU's early CSR initiatives, while pioneering in linking social equity to economic growth, lacked the accountability mechanisms needed for systemic impact (Christensen et al., 2021).

4.2. The regulatory transition: From Non-Financial Reporting Directive to European Sustainability Reporting Standards

4.2.1. The Non-Financial Reporting Directive (2014): First binding steps

Directive 2014/95/EU (European Parliament, & The Council of the European Union, 2014) represented the EU's inaugural binding legislative intervention in non-financial reporting, requiring approximately 11,000 public interest entities with over 500 employees to include non-financial statements addressing environmental issues, social matters, human rights, corruption prevention, and governance diversity. Despite allowing flexible framework adoption, implementation revealed critical limitations: information heterogeneity, limited comparability, insufficient user relevance, and absent verification requirements (Ioannou & Serafeim, 2021).

4.2.2. The Corporate Sustainability Reporting Directive (2022): Comprehensive reform

The Corporate Sustainability Reporting Directive's (CSRD's) adoption on December 16, 2022, represents a change in basic assumptions from voluntary to mandatory sustainability reporting. The directive expanded coverage from 11,000 to over 50,000 entities through broadened scope criteria and introduced several key innovations:

- Dual materiality: Mandatory consideration of both impact materiality (business effects on environment/society) and financial materiality (sustainability factors affecting business performance).
- Standardization: Mandatory ESRS adoption.
- Digitization: European Single Electronic Format (ESEF) requirement for machine-readable data.
- Assurance: External verification obligations, progressing from limited to reasonable assurance.
- Regulatory integration: Alignment with Taxonomy Regulation and Sustainable Finance Disclosure Regulation (SFDR) requirements.

4.3. The European Sustainability Reporting Standards: Technical implementation

4.3.1. Development process and structure

European Financial Reporting Advisory Group's (EFRAG's) designation as a technical development body triggered governance restructuring, establishing specialized boards and expert groups. On July 31, 2023, Delegated Regulation formalized twelve initial standards organized across three pillars:

- Cross-cutting Standards: General requirements and sustainability information.
- Environmental Standards (E1-E5): Climate change, pollution, water resources, biodiversity, circular economy.
- Social Standards (S1-S4): Workforce, value chain workers, communities, consumers.
- Governance Standards (G1): Business conduct and transparency.

Each standard employs modular architecture comprising disclosure requirements, application requirements, and non-binding guidance, with materiality-based flexibility reducing mandatory requirements while implementing phase-in regimes for complex requirements.

4.3.2. Implementation timeline and challenges

The CSRD's phased implementation spans 2024–2029, beginning with NFRD-covered entities and concluding with third-country companies. Implementation faces significant obstacles, including technical complexity, data collection challenges, substantial compliance costs, and skills shortages in sustainability reporting expertise. The "ESRS readiness gap" between large corporations and SMEs threatens to exacerbate sustainability inequalities (Gond et al., 2011).

4.4. International convergence and strategic integration

International Financial Reporting Standards (IFRS) sustainability standards integration. The International Sustainability Standards Board's (ISSB's) parallel development of IFRS S1 and S2 created convergence opportunities and challenges. The July 2023 EFRAG-ISSB Memorandum of Understanding formalized interoperability commitments despite fundamental differences in materiality approaches, scope, and requirements detail (EFRAG, 2025).

Strategic policy integration. ESRS supports European Green Deal objectives by providing comparable environmental performance data and facilitating climate neutrality progress monitoring. The regulatory framework's interconnection with sustainable finance instruments creates comprehensive market transparency, supporting sustainable investment flows and risk management.

4.5. Discussion of the findings

4.5.1. Theoretical implications

This research validates and extends Carroll's (1991) pyramid by demonstrating how regulatory intervention has fundamentally altered the hierarchical relationship between corporate responsibilities. While Carroll's framework positioned legal responsibilities as the second tier, the emergence of mandatory ESG reporting has elevated legal compliance to encompass previously voluntary ethical and philanthropic activities.

The study's analysis reveals a fundamental shift from the shareholder-stakeholder debate to contemporary ESG frameworks. Where early CSR theory grappled with voluntary responsibility concepts, modern ESG regulation resolves this tension through mandatory stakeholder consideration requirements, representing a significant evolution from Friedman's (1970) profit maximization principle to Porter and Kramer's (2011) shared value creation.

4.5.2. Practical implications

The research provides empirical insights into the European regulatory transition, demonstrating how "dual materiality" represents a fundamental departure from traditional CSR approaches. This dual perspective resolves the long-standing tension between business case arguments and normative stakeholder theory by requiring consideration of both financial impacts and societal/environmental effects.

The study's examination of corporate failures like Volkswagen provides empirical evidence for why voluntary CSR approaches proved inadequate and regulatory intervention became necessary. This supports the argument that voluntary responsibility systems lack sufficient enforcement mechanisms to ensure authentic corporate behavior.

4.5.3. Challenges and opportunities

European Sustainability Reporting Standards (ESRS) implementation transforms the non-financial information market across multiple stakeholder groups. Companies must restructure reporting processes and governance systems, with 65% having initiated specific implementation projects with substantial budgets. Professional service providers are developing specialized offerings in a rapidly growing market, while investors gain access to enhanced comparable data for decision-making.

The transformation presents both challenges and opportunities for corporate leaders. Success requires embedding sustainability considerations into core business strategy, risk management, and performance measurement systems — moving beyond traditional CSR's peripheral activities to achieve competitive advantages through operational efficiency, enhanced investor confidence, and strengthened stakeholder relationships.

5. CONCLUSION

This study contributes to evolving CSR literature by providing a comprehensive analysis of the transformation from voluntary CSR initiatives to mandatory ESG frameworks. The research validates Carroll's pyramid while demonstrating how regulatory intervention has fundamentally altered responsibility hierarchies, extending theoretical work on voluntary-mandatory boundaries within corporate responsibility.

The analysis reveals how the concept of dual materiality represents a fundamental departure from traditional CSR approaches, resolving long-standing tensions between business case arguments and normative stakeholder theory. This regulatory codification of stakeholder consideration requirements represents a significant theoretical evolution from early CSR concepts to contemporary ESG frameworks.

For business practitioners, this research provides actionable insights into navigating the transition from voluntary CSR to mandatory ESG compliance. The study demonstrates that successful ESG integration requires embedding sustainability considerations into core business strategy rather than treating it as a mere compliance exercise. Organizations that integrate ESG principles into fundamental business processes can achieve competitive advantages through various mechanisms.

The research offers concrete guidance for boards and executives managing this transformation through analysis of ESRS implementation phases and challenges. The findings suggest that companies approaching ESG strategically rather than tactically will realize greater value creation opportunities.

This study's focus on European regulatory frameworks limits generalizability to other districts with different regulatory approaches. Future research should examine comparative regulatory frameworks and their effectiveness in achieving sustainability objectives. Additionally, empirical studies examining the actual impact of mandatory ESG reporting on corporate behavior and societal outcomes would provide valuable insights into regulatory effectiveness.

The research's reliance on publicly available information limits insights into internal corporate decision-making processes. Future studies employing primary data collection could provide a deeper understanding of how companies are implementing ESG requirements and managing the voluntary-to-mandatory transition.

The transformation from CSR to ESG represents more than regulatory change — it signifies a fundamental shift in corporate governance paradigms. The European experience with ESRS provides a model for other areas considering mandatory sustainability reporting. However, success depends on corporate leadership's commitment to authentic implementation rather than mere compliance.

As this study demonstrates, the evolution from voluntary CSR to mandatory ESG reflects broader changes in stakeholder expectations and societal demands for corporate accountability — changes that require strategic rather than tactical responses from business leaders. The integration of sustainability considerations into core business strategy becomes not merely regulatory compliance but a competitive advantage foundation in the evolving business landscape.

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