
Stefano Cascino Maria Correia June 19th, 2025

# ESG needs global regulation

*Multinational corporations' complex cross-border ownership structures allow them to reallocate activities that hurt their ESG performance in one location to another with laxer rules. **Stefano Cascino** and **Maria Correia** write that global ESG performance can only achieve meaningful improvements through coordinated efforts that close the regulatory gaps.*

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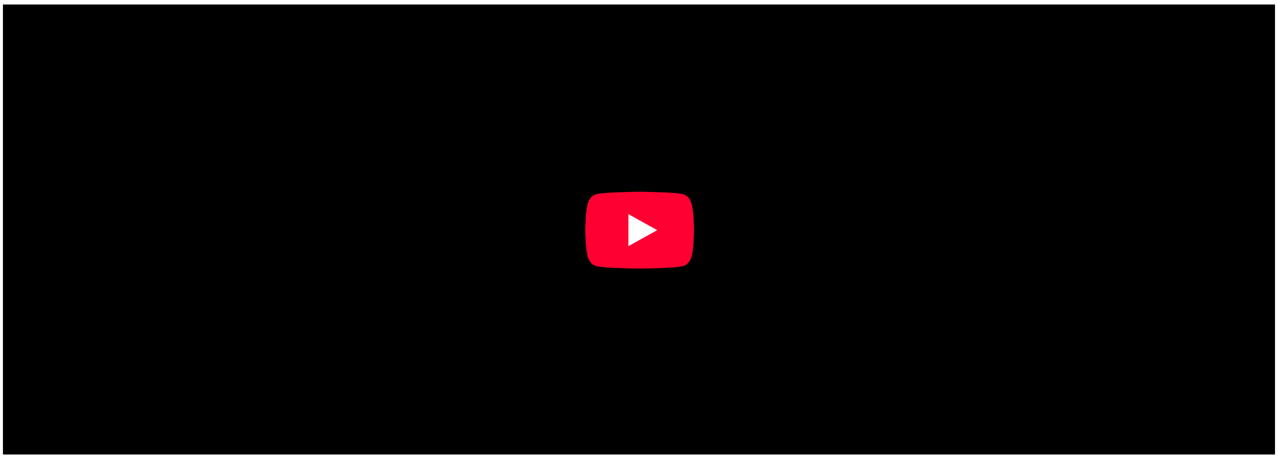
Environmental, social, and governance (ESG) disclosure mandates have become an increasingly popular tool for regulators worldwide. These mandates require companies to publicly report their policies, practices and performance on issues ranging from greenhouse gas emissions and human rights to corporate governance and transparency. The idea is straightforward: greater disclosure should lead to better accountability, more informed stakeholder scrutiny and, ultimately, improved ESG performance.

Our recent research, however, reveals a more complicated picture, particularly for large, multinational business groups—when a parent company controls multiple legally independent subsidiaries. They account for nearly a third of global GDP, with complex ownership structures and cross-border operations that give them large flexibility to respond to new regulations.

Business groups span multiple countries and regulatory environments. While ESG mandates improve parent companies' own ESG performance, they also create incentives for these groups to strategically shift related risks to their subsidiaries, especially those located in countries with weaker governance and less effective enforcement. This pattern of "regulatory arbitrage" within business groups raises critical questions about the effectiveness of current ESG disclosure mandates and highlights the need for greater coordination across borders.



## Strategic flexibility

To exploit differences in regulatory regimes, business groups can reallocate ESG-intensive activities within their own corporate boundaries, rather than simply improving ESG performance uniformly across the entire group.

For example, a parent company based in a country with strong disclosure rules may face intense scrutiny for any lapses, but its subsidiaries in countries with weaker institutions or social norms often face far less. This flexibility to “arbitrage” ESG risks across borders can undermine the spirit of disclosure mandates that aim to improve the group’s overall footprint in this area.

## Evidence of ESG risk shifting

To examine how business groups respond to ESG disclosure mandates, we studied a large sample of listed business groups and their subsidiaries. We focused on how subsidiaries’ ESG performance changes when the parent country adopts new disclosure mandates. Our findings reveal a striking pattern. After the introduction of these disclosure mandates in the parent company’s home country, subsidiaries experience a significant increase in the occurrence and frequency of ESG breaches.

This effect is particularly concentrated in countries with weaker institutions and lower risk of legal liability for parent companies. Meanwhile, incidents involving the parent company itself decline, and the group’s overall ESG performance improves modestly. In other words, while the aggregate group-level data show progress, much of this improvement comes from reshuffling, rather than real changes, in underlying practices.

## Financial constraints

We also find that these patterns are driven largely by financially constrained business groups, which have fewer resources to implement costly ESG upgrades across all operations. For them, regulatory arbitrage becomes a more attractive, or even necessary, way to comply with new disclosure mandates at the parent level.

Where exactly these risky activities are shifted matters. Manufacturing subsidiaries, often removed from direct consumer scrutiny, see a larger spike in ESG incidents than retail subsidiaries. The same happens to subsidiaries in countries with lower environmental performance standards, weaker rule of law and less civil society oversight. This evidence suggests that parent companies are actively weighing the relative costs of ESG incidents across jurisdictions and exploiting differences in institutional quality to manage overall group risks.

# How firms execute ESG strategies

Business groups can execute these strategies in two ways. One way is by ramping up production and asset use in subsidiaries that face weaker ESG scrutiny. Another way is by strategically restructuring by divesting from high-risk subsidiaries that could expose the group to reputational or legal harm. This “pruning” of the corporate tree helps groups manage overall ESG risk exposure without directly improving the practices of subsidiaries.

# Limits of piecemeal regulation

Our findings underscore a crucial limitation of ESG disclosure mandates as they exist today. While these rules do improve transparency and drive some improvements in parent-level ESG performance, they can also incentivise multinational groups to simply move risky activities to jurisdictions with weaker protections or oversight. The result is that, in some cases, these mandates may inadvertently exacerbate ESG risks in other parts of the world.

This points to the urgent need for coordinated, cross-border ESG regulation that recognises the complex corporate structures of multinational groups. Relying solely on country-by-country disclosure rules leaves gaps that sophisticated business groups can exploit. A global approach to ESG regulation could instead help ensure that sustainability mandates have real bite.

# Broader lessons for stakeholders

For investors, NGOs, and policymakers, our findings point to the importance of looking beyond parent-company disclosures and examining the broader corporate group and supply chain. Ultimately, if ESG regulation is to truly address global environmental and social challenges, it must grapple with the organisational realities of multinational groups. Disclosure mandates remain an important tool, but they must be complemented by stronger due diligence obligations, broader group-level accountability, and policies that limit the ability to hide risky practices behind the corporate veil.

# Conclusion

The rise of ESG disclosure mandates represents an important step toward better corporate accountability. Yet, as our research shows, multinational business groups have both the means and the incentives to arbitrage these regulations: improving parent-level ESG performance while shifting risks elsewhere.

This dual reality, with progress at the top but hidden risks within, demands a rethinking of ESG policies to ensure that the entire corporate ecosystem is held to account. Only through coordinated efforts that close the regulatory gaps can we hope to achieve meaningful improvements in global ESG performance.

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### About the author

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Stefano Cascino is an Associate Professor of Accounting at LSE. His primary research interests include disclosure regulation, corporate governance, and credit markets. His research has generated the interest of practitioners and standard setters, including the Australian Accounting Standards Board (AASB) and International Accounting Standards Board (IASB), and has been cited in outlets such as the Columbia Law School Blue Sky Blog, Harvard Law School Bankruptcy Roundtable, and LSE Business Review. For his dedication to teaching, Stefano received the LSE Teaching Excellence Award in 2012, and the LSE Education Excellence Award in 2016, 2017, and 2018. He holds a PhD in Business Economics

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Maria Correia is a Professor of Accounting at the London School of Economics. Her primary research interests include credit markets, disclosure regulation, and corporate governance. Her research has been published in leading academic journals and has been covered, among others, by Politico, the Wall Street Journal and the Washington Post. She holds a PhD in Business Administration (Accounting) from Stanford University.

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