ENERGY POLICY STUDIES No. 1(14)2024:62-81, e-ISSN: 2545-0859

Role of ESG reporting in small and medium-sized enterprises: benefits, challenges and the EU's regulatory push

Emir Gürlevük

DOI: https://doi.org/10.62316/KMEI2006

Abstract: This article examines the growing importance of Environmental, Social, and Governance (ESG) reporting, focusing on small and medium-sized enterprises (SMEs) and the European Union's (EU) regulatory framework. The research is structured around three key questions: the motivations behind the EU's implementation of ESG regulations, the benefits SMEs can derive from adopting ESG reports, and the challenges businesses face during this process. Moreover, the article explores how the EU's regulatory push is driven by goals related to environmental sustainability, social responsibility, and corporate governance, aiming to align with global climate initiatives. It also investigates how SMEs can benefit from ESG reporting by improving operational efficiency, securing access to capital, and building stronger stakeholder relationships. However, it acknowledges the significant challenges faced by businesses, including compliance costs, difficulties in data collection, and the complex nature of regulatory requirements. Through a comprehensive analysis, this paper provides insights into the evolving role of ESG in shaping business practices and policy, with particular emphasis on its impact on SMEs and the broader EU economy. The findings aim to contribute to a better understanding of ESG as a strategic tool and its implications for businesses within the EU regulatory context. At the end of the article, the case study thoroughly details how DHL, a company that has proven itself in the logistics sector and ESG reporting, managed the process and the key aspects they focused on.

Key words: SMe, Corporate Social Responsibility (CSR), Sustainability, European Union, Enviromental, Social and Governance (ESG) Report

Introduction

The term 'ESG' was introduced in 2004 in 'Who Cares Wins' and was introduced to find ways to incorporate the aspects of ESG into the capital market (Helfaya, Morris, Aboud, 2023, as cited in Swiss Federal Department United Nations of Foreign Affairs and United Nations, 2004). From this point on, ESG is seen as an extension of traditional CSR (Corporate Sustainability Report) and socially responsible investment. The era in which organizations solely prioritized an increase in company profits has long since ended. This is because the global population is facing issues such as the climate crisis, global warming, and the depletion of natural resources. Therefore, the ESG (Environmental, Social, and Governance) report, established to protect these concerns, is one of the essential reports for companies to survive and use global resources efficiently. Investors and consumers expect organizations not only to succeed in production or service delivery but also to be responsible for topics such as environmental management, waste management, and energy use, which will be written about later in this article. This expectation places a responsibility on companies, which must also heed the importance of these issues as societal and environmental conditions change globally, as well as the emergence of regulations enacted by governments on these matters. The Corporate Sustainability Reporting Directive (CSRD) aims to make it mandatory for companies to report on sustainability,

environmental, social, and governance (ESG) issues. According to the following timetable, companies will fall under the scope of the CSRD: In 2024, large public companies with more than 500 employees and large non-EU listed companies will be required to report. In 2025, all large companies meeting two of the following three criteria will be included: (1) an annual average of 250 employees or more, (2) total assets of €25 million (an increase from €20 million under the Commission's recent amendment), or (3) €50 million in sales (up from €40 million under the amendment). The SMEs (Small and Medium-sized Enterprises), which are the subject of this article, will be required to start reporting from 2027. However, uncertainties remain as standards have not yet been established. Listed SMEs may report using less intensive standards and can request an exemption from reporting requirements for two additional years, allowing them to delay reporting until 2029. Non-listed SMEs are not subject to the CSRD but may choose to report voluntarily under simplified standards if sustainability information is requested. Finally, in 2028, companies located outside the EU with sales exceeding €150 million in the EU must be either a large or listed subsidiary or a significant EU branch. These companies are required to submit reports the year after they fall under the scope of the CSRD.

What motivates the European Union to implement ESG regulations

The European Union and its member states are facing a significant challenge. They aim to promote sustainable development to comply with international agreements such as the 2030 Sustainable Development Goals and the 2050 climate neutrality targets. Achieving this requires numerous fundamental changes that will contribute to global sustainability. The EU is implementing regulations that impose new obligations on businesses, initially targeting large and listed companies; however, these regulations will also extend to small and medium-sized enterprises (SMEs) operating within supply chains. When examined in terms of environmental, social, and governance (ESG) factors, these regulations encompass various aspects, including: the usage of energy resources by an organization, its waste management policies, efforts towards net-zero emissions, impacts on biodiversity and the climate crisis, water pollution, and deforestation. Additionally, they address the organization’s connections and effects on local communities where it operates and provides services, stakeholder relationships, accurate consumer information, data protection and privacy policies, health and safety practices, as well as efforts toward human rights and ethical principles. They also cover decision-making factors necessary for good governance, corporate transparency, accountability, inclusiveness, and compliance culture.

As can be seen, the European Union does not mandate ESG reports solely for sustainability and environmental development. Rather, it also aims to enhance investor awareness, promote social responsibility and transparency, gain a competitive advantage, ensure regulatory compliance and legal obligations, manage risks, and address the impact on society and stakeholders. By making ESG reporting compulsory, the EU seeks to promote sustainability and integrate economic growth with environmental, social, and governance responsibilities.

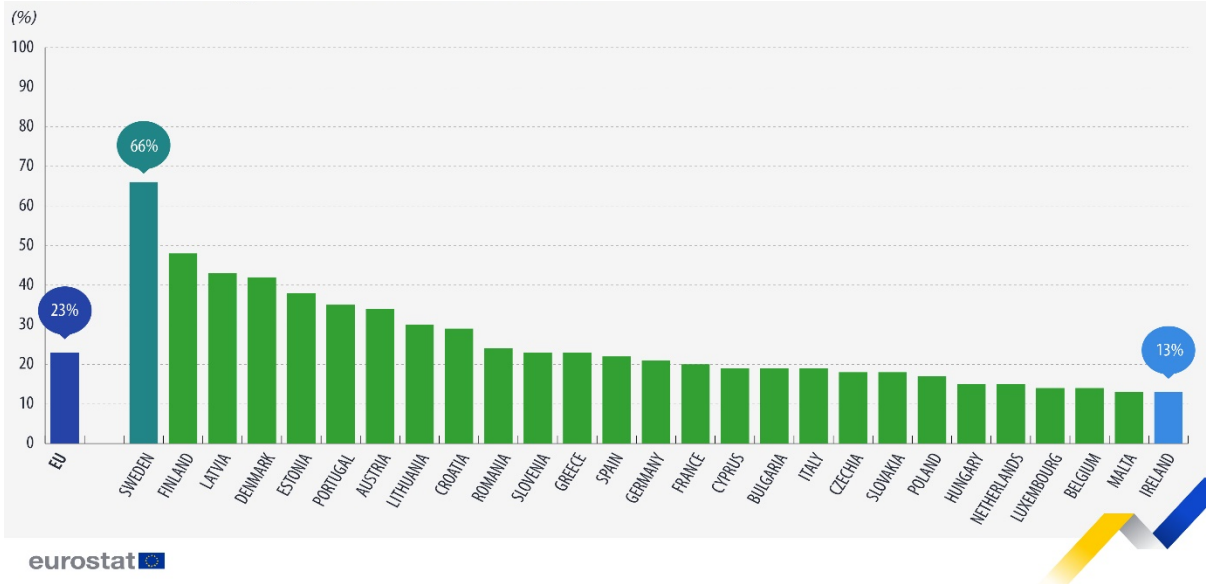
The European Union's environmental interest in ESG (Environmental, Social, and Governance) reporting is driven by key objectives such as achieving sustainable development goals, combating climate change, and ensuring environmental sustainability. ESG reporting provides companies with a framework to assess their environmental, social, and governance performance, and the EU is working on regulations to make this reporting mandatory. In alignment with the 2030 sustainable development goals, the EU focuses on environmental objectives like reducing carbon footprints, preserving biodiversity, encouraging a circular economy, and ensuring the sustainable use of natural resources. Comprehensive policies and regulations, including the European Green Deal and the EU Environmental Action Programs, are in place to meet these targets.

For instance, the EU Green Deal sets new CO_2 (carbon dioxide) standards requiring all new cars and vans registered in Europe to be zero-emission by 2035. As a step toward this goal, average emissions of new cars must be reduced by 55% by 2030, and emissions from new vans by 50%. This will place road transport on a path toward zero-emission mobility by 2050 (European Commission 2021). Furthermore, these regulations extend beyond road transport to include measures in aviation and maritime transport. For example, there are targets to gradually reduce the average annual greenhouse gas intensity of energy used on ships, with a focus on promoting renewable and low-carbon fuels. In aviation, to encourage sustainable aviation fuels (SAF), the required share of SAF to be blended with kerosene by aviation fuel suppliers has been increased, and this blend must be provided at EU airports (European Commission 2021). SAF fuels, made from renewable materials such as mustard seeds, sugarcane, and used cooking oil, serve as low-carbon alternatives to traditional jet fuels, contributing to both recycling and reducing carbon emissions.

At the EU level, the share of renewable sources in gross final energy consumption reached 23.0% in 2022. Compared to 2021, this represents an increase of 1.1 percentage points (pp).

This figure was 19.1% in 2018 and is estimated to reach 24.1% in 2023. According to the available data, in 2022, Sweden led among EU countries, deriving 66.0% of its gross final energy consumption from renewable sources. Finland (47.9%) and Latvia (43.3%) also utilized significant amounts of renewable energy. Denmark (41.6%) and Estonia (38.5%) increased their energy consumption through wind and solid biofuels. Portugal (34.7%) and Austria (33.8%) turned to renewable energy sources supported by hydropower and biofuels. However, countries like Ireland, Malta, Belgium, and Luxembourg had renewable energy shares ranging from 14.4% to 13.1%. In total, 17 of the 27 EU members reported shares below the EU average of 23.0% (Tab. 1). This data can be considered a result of the EU's positive insistence on the use of renewable sources in energy.

Tab 1. Overall Share of Energy from renewable sources in 2022 in Europe



Source: Eurostat 2023.

The environmental section of ESG reporting allows companies to present their environmental impacts to the public more transparently. This transparency enhances credibility among stakeholders, investors, and society, thereby strengthening the reputation of businesses. The EU is considering making ESG reporting mandatory not only for large companies but also for SMEs. In this context, reporting on the environmental performance and sustainable business practices of SMEs is emerging both as a legal requirement and as a tool for enhancing their competitive advantage (European Union 2022).

Additionally, ESG reporting is closely related to the EU's efforts to transition to a circular economy. The circular economy is an economic approach where the value of products, materials, and resources is maintained in the economy for as long as possible, and waste generation is

minimized (Önder, 2018, as cited in European Commission, 2015). Through ESG reporting, companies are expected to assess and optimize environmental aspects such as resource use and waste management. This approach is important in alignment with the EU's goals for transitioning to a low-carbon economy, emphasizing the preservation of natural resources and the minimization of environmental risks.

In summary, the carbon emission reduction targets established under the European Green Deal are part of the environmental perspective of ESG reports. Companies disclose the measures they take to reduce their carbon footprint, the sustainable energy sources they utilize, and their circular economy practices in their ESG reports, thereby fulfilling legal requirements and contributing to the EU's overall goals for a sustainable future. This makes companies' environmental performance more transparent to investors and the public, thereby supporting the necessary transformation for a more sustainable economy. The EU's approach to ESG reporting from an environmental perspective not only helps businesses assess their environmental impacts but also supports them in achieving social, economic, and environmental sustainability goals. This process enables companies to fulfill their environmental responsibilities, manage environmental risks, and contribute to the EU's green transition objectives.

The European Union views ESG (Environmental, Social, and Governance) reporting as a tool for social responsibility. Within the framework of social sustainability, it emphasizes how companies should contribute to their employees, communities, and other stakeholders. Key aspects include protecting workers' rights, ensuring safe working conditions, and supporting community-benefiting projects. On the other hand, Davis (1973) argues that a company is not socially responsible simply by meeting the minimum legal requirements. He believes that companies should go beyond legal obligations and accept additional social responsibilities. This means that just protecting workers' rights does not automatically establish a corporate social responsibility (CSR) culture. As previously mentioned, alongside the "E" (Environmental) in ESG reports, consumers and stakeholders now expect companies to provide information regarding ethical practices, how employees are treated, and their safety. This social responsibility is not necessarily tied directly to a company’s business operations. Companies that demonstrate their CSR awareness by sponsoring civil society organizations, charity campaigns, or volunteer projects show a broader commitment to social responsibility. For instance, a 2019 Edelman survey revealed that 53% of consumers believe that brands should contribute to at least one social issue unrelated to their direct business operations. This indicates that consumers are increasingly preferring companies that focus not only on business goals but also on contributing

to social causes. In essence, consumers expect brands to be sensitive to societal issues and to play an active role in solving them.

Corporations with an awareness of social responsibility can become more respected and recognized in society. This is because people are empathetic beings, and negative aspects such as mistreatment of employees, exploitation, or harm to the environment and animals can discourage consumers and investors from supporting such companies. For instance, if an SME is part of a larger company's supply chain and engages in worker rights violations, these actions could lead to significant loss of reputation and financial setbacks when noticed by other companies or the public. A good example of how investor and public perception can shift regarding companies that violate worker rights is the case between Foxconn and Apple. Foxconn, a major Chinese supplier that manufactures Apple products, came under public scrutiny in the 2010s due to reports of poor working conditions. Allegations surfaced that workers were forced to work excessive hours, were underpaid, and faced inadequate safety standards. These issues became even more visible after tragic incidents, including worker suicides. In response, Apple introduced new standards, demanding that Foxconn and other suppliers improve workers' rights, and increased inspections. Additionally, Apple collaborated with third-party auditors to ensure better working conditions.

The European Union's regulatory push in ESG (Environmental, Social, and Governance) reporting aims to ensure that companies meet their responsibilities regarding labor rights, societal contributions, and consumer obligations. Companies are required to provide transparency on issues such as accurate consumer information, data protection and privacy policies, support for impoverished communities, workforce diversity, equality, inclusion, employee engagement and satisfaction, health and safety, human rights, ethical principles, fair wages, labor standards, and sustainable supply chains (European Union 2022).

According to Khan (2011), corporate governance is a system that regulates the processes, policies, and relationships between stakeholders to control, manage, and achieve the goals of companies. This broad term encompasses processes, traditions, policies, laws, and institutions. Corporate governance aims to ensure that an organization achieves its objectives and regulates relationships among stakeholders, including the board of directors and shareholders. While the definition of corporate governance generally follows certain lines, a more formal and widely accepted definition is provided by the Organization for Economic Cooperation and Development (OECD) in the "Principles of Corporate Governance" report published in 2004. According to the OECD, corporate governance involves a series of relationships between a company's

management, board, shareholders, and other stakeholders. This structure defines the company's objectives and outlines ways to achieve these goals and monitor performance. Furthermore, the existence of an effective corporate governance system helps build the trust necessary for the smooth functioning of a market economy. Corporate governance lowers capital costs and supports companies in using resources more efficiently to foster their growth (OECD 2004: 11).

The governance standards set by the European Union (EU) in ESG reporting include various regulations aimed at ensuring transparency, accountability, and ethical behavior in company operations. These regulations can be defined as follows: The Board Composition and Independence: The EU emphasizes the importance of diverse, independent, and competent boards for effective corporate governance. Board members must have the necessary qualifications and experience to ensure the long-term success of the company. Transparency and Accountability: The EU promotes open and honest communication between companies, shareholders, and other stakeholders. This involves providing accurate information about business operations, performance, and strategies in ESG reports, enabling stakeholders to hold companies accountable for their actions. Shareholder Rights: EU regulations stress the protection of shareholder rights, particularly in decision-making processes. For shareholders to have a significant influence on corporate governance, companies must serve the interests of all stakeholders, not just the board or managers. Ethical Behavior and Compliance: EU laws require companies to adhere to ethical principles, legal requirements, and social responsibility in their operations. This includes compliance with anti-corruption laws, respect for human rights standards, and fair treatment of employees. Long-Term Strategy and Risk Management: The EU mandates that companies implement long-term sustainability-focused strategies and establish adequate risk management practices to address environmental and social risks (European Commission 2021).

The European Union places significant importance on "Governance" or more specifically, "Corporate Governance" in ESG reporting, emphasizing companies' adherence to ethical standards and sustainability requirements. This governance allows stakeholders and investors to access more detailed and transparent information, ensuring that company operations are visible and in line with legal and ethical norms. As a result, it addresses potential concerns and attracts new investors, leading to safer, ethical stock markets, improved company sustainability, and enhanced financial performance. The positive impacts of corporate governance are discussed in the article's section on ESG reporting benefits for SMEs.

The Benefits of ESG Reporting for Small-Medium Enterprises

Small and Medium-sized Enterprises (SMEs) often form the backbone of a country's economy. In fact, these businesses represent 99% of all businesses in the EU. The definition of SMEs is particularly important in terms of access to financing and EU support programs targeting these businesses (European Commission). Therefore, the European Union aims to enhance market vitality and help SMEs adapt to the modern world by subjecting them to necessary regulations and reports.

However, SME classifications differ between countries. Typically, the key factor in classification is the number of employees, which divides companies into micro, small, or medium-sized enterprises. Due to fluctuations in currency or exchange rates, revenue amounts cannot be perfectly aligned, so countries have set their own criteria. For example, while the required number of employees for a company to be classified as an SME is the same in Turkey as in Europe, the annual net sales revenue or any part of its financial balance sheet has been adjusted in Turkey. In Turkey, the revenue must not exceed 500 million Turkish liras for medium-sized enterprises, 100 million for small enterprises, and 10 million for micro enterprises (KOSGEB 2023).

The key point to understand here is the definitions or criteria set by countries before classifying companies as SMEs. This is clearly demonstrated by UNIDO’s establishment of 50 different definitions for small-scale industries across 75 countries (Onyiriuba, 2016, as cited in Evborokhai 1989). Therefore, as mentioned earlier, even if employee count is considered, other classifications may vary between countries. Each country defines SMEs according to its own economic needs, and these definitions are generally based on fundamental criteria such as sales turnover, balance sheet size, capital, and number of employees. However, the quantitative values of these criteria differ from country to country. For this reason, there is no universally accepted single definition of an SME (Onyiriuba, 2016).

However, since much of our focus is on the European Union, the companies referred to as SMEs from now on will be those that align with the EU's own definition and scales. According to the EU definition, the key factors determining whether a business qualifies as an SME are outlined in Table 2.

Tab. 2. Categorization of companies according to SME classifications in EU

Company category	Staff headcount	Turnover	or	Balance sheet total
Medium-sized	< 250	≤ € 50 m		≤ € 43 m
Small	< 50	≤ € 10 m		≤ € 10 m
Micro	< 10	≤ € 2 m		≤ € 2 m

Source: SME definition, https://single-market-economy.ec.europa.eu/smes/sme-fundamentals/sme-definition_en (access 27.10.2024).

However, when presenting this table, the European Union has also noted: 'These ceilings apply to the figures for individual firms only. A firm that is part of a larger group may need to include staff headcount/turnover/balance sheet data from that group too.'

ESG (Environmental, Social, and Governance) reporting, when prepared in accordance with European Union standards, provides significant benefits to SMEs. The importance of profitability for a company's sustainability is undeniable; profitability is achieved through factors such as increasing sales, exploring new business areas, or expanding with additional branches. However, while ESG reporting may not directly generate profits, it indirectly supports a company's sustainability, enhances investor confidence, and increases market value.

This concept can be compared to the use of concrete and steel in constructing a building. Reinforced concrete serves as the foundation of the structure, akin to a company's profitability. However, properly curing the concrete or employing vibration techniques to strengthen it enhances the building's durability, much like ESG reporting contributes to long-term corporate health. Similarly, in the field of electrical and electronic engineering, the pathways and batteries on a circuit board represent a company's profitability. The soldering of these pathways, symbolizing ESG reporting, ensures long-term operational reliability. Without soldering, the circuit may function temporarily but will eventually fail due to oxidation.

In conclusion, ESG reporting may not be a mandatory requirement for a company's operations—at least until the European Union mandates it universally—but it serves as a strategic tool to enhance and maintain profitability. It strengthens investor relations, ensures corporate viability, and offers a competitive advantage, highlighting its importance as more than just a compliance measure.

When evaluated in the fields of business and finance, ESG (Environmental, Social, and Governance) reporting offers significant benefits to SMEs. These reports hold considerable value for all stakeholders. The potential users of ESG reports include investors, customers, employees, competitors, lenders, media, non-governmental organizations, academics, analysts, and researchers (Şeker & Şengür 2022). Therefore, the preparation of ESG reports in a clear and comprehensible manner positively influences these stakeholders and provides substantial advantages to businesses.

The benefits of ESG reporting for SMEs can be summarized as follows:

Investment attraction potential: ESG reporting highlights a company's commitment to environmental and social responsibility, which can attract environmentally-conscious investors and facilitate financing opportunities. Additionally, by fulfilling these responsibilities, a company can increase its brand awareness and prestige through its social and environmental contributions.

For example, participating in global aid efforts or social projects can enhance a company's reputation. If a company operating in Country A provides support to Country X, which has experienced a natural disaster, or contributes to a public awareness project in Country X, this could create a positive perception in that region. However, it is essential that such actions are not carried out solely for marketing purposes. Social and environmental responsibilities should stem from the genuine goodwill or social sensitivity of the company's leaders, reflecting a sincere approach. In this way, both ethical values are upheld, and sustainable success is achieved.

Competitive advantage: ESG practices provide businesses with a significant edge over competitors. Sustainability-focused strategies enhance a brand's reputation, attracting more customers. These initiatives not only demonstrate that a company is profit-driven but also show its commitment to environmental and social responsibility. ESG reporting transparently reflects a company's adherence to these values, distinguishing it from competitors. This, in turn, allows the company to appeal to a broader customer base and secure long-term success.

Risk management: ESG reporting allows companies to more effectively assess environmental and social risks. This helps businesses anticipate future operational disruptions, thereby reducing potential costs and ensuring a more efficient operation. By adopting a proactive approach to environmental changes, social issues, or governance challenges, companies can achieve sustainable performance in the long run.

Legal compliance: In regions such as the European Union, regulations regarding ESG reporting are increasingly becoming stricter. Early adopters among SMEs can more easily comply with these regulations, avoiding potential penalties and gaining a competitive advantage. This enables companies to meet their legal obligations more efficiently, reduces future operational risks, and supports sustainable growth.

Partnership and supply chain relationships: Large companies may require compliance with ESG standards within their supply chains. SMEs that engage in ESG reporting have a higher chance of partnering with these large companies. As mentioned earlier, ESG reporting will be mandatory for large companies in the European Union starting in 2024. As a result, companies that operate in accordance with ESG standards are more likely to be included in the supply chains of these organizations. By doing so, SMEs can not only establish themselves within these supply chains but also continue their sustainable growth with the support of these larger companies.

Cost Savings: Environmental sustainability practices, such as energy efficiency, can significantly reduce operational costs. These practices optimize the company's energy consumption, leading to long-term reductions in energy bills. This, in turn, positively impacts the company's balance sheet and can increase profit margins. Additionally, reducing resource consumption lowers the company's environmental footprint, enhancing its reputation within society and among environmental stakeholders. Thus, sustainability strategies not only generate cost savings but also support the company's long-term economic and environmental sustainability.

Employee Engagement: Compliance with social and governance criteria can increase employees' loyalty to the company and also strengthen the desire of talented and qualified individuals to work at your company. For example, in 2021, when Honda Turkey decided to close its factory in Çayırova, it offered meaningful closure compensation and special rewards to all its employees. This included a performance bonus equivalent to one month's salary for employees with no absenteeism or reports, 48 months of salary for employees with more than 10 years of service, and 40 months of salary for those with less than 10 years. Honda’s commitment to its employees not only occupied a significant place in the Social section of its ESG report but also became a gesture that was widely talked about across Turkey for a long time.

Globalization: From 2028 (possibly extending to 2031), companies wishing to operate in the European Union will face difficulties in conducting trade within EU countries unless they comply with ESG reporting. This is not limited to the EU; other major countries, such as the

United States, China, and Russia, may also make it harder for companies without ESG reporting to operate in their territories. In this context, SMEs can gain a competitive advantage in global markets by learning and adopting ESG reporting early. SMEs that start preparing these reports before the requirements are enforced will have the opportunity to globalize more cost-effectively and swiftly.

Other benefits I would like to briefly mention, aside from the topics above, include: ESG reporting reduces information asymmetry, ensures the accessibility of management decisions, protects shareholders' rights, helps create anti-corruption and anti-takeover policies, promotes consumer health, safety, and data privacy in products and services, encourages gender equality and women's employment by promoting the presence of women in management positions and boards, and fosters collaboration with stakeholders within an accountability framework. Due to these potential benefits, the demand for the information included in ESG reports and the use of ESG performance data is steadily increasing, and this usage is expected to become more widespread globally in the coming years (Şeker & Şengür 2022).

In Summary, ESG reporting offers significant benefits to SMEs. Although it may not directly increase profitability, it supports long-term sustainability by enhancing investor confidence, boosting market value, and improving a company's reputation through environmental and social responsibility. ESG reporting helps companies better manage environmental and social risks, comply with regulations, and proactively address potential operational disruptions.

SMEs benefit from ESG reporting by becoming eligible to be part of large companies' supply chains, which is particularly crucial as ESG reporting becomes mandatory for large companies in the European Union in 2024. These practices also promote environmental sustainability, leading to cost savings and reduced operational costs, while increasing brand recognition. Moreover, ESG-focused companies can foster a loyal workforce and attract skilled employees.

The growing global trend of mandating ESG reporting means that SMEs that adopt these practices early will be able to better compete in international markets. Additionally, ESG practices promote consumer health, safety, and privacy, protect shareholders' rights, encourage gender equality, and foster collaboration with stakeholders, all of which contribute to the company’s competitive edge and long-term success.

Challenges for SMEs in the implementation of ESG reporting

Approximately 400 million SMEs worldwide continue to form the backbone of economies. These businesses account for over 95% of all companies and contribute 60-70% to global employment, playing a critical role in job creation. However, despite being classified in the same category, SMEs differ significantly due to factors such as geographic location, culture, knowledge base, managerial competencies, and employee skills.

These differences make it unrealistic to expect the same quality and efficiency in ESG (Environmental, Social, and Governance) reporting transitions from all SMEs. For instance, some businesses may not have even heard of ESG reports, while others, despite being aware, have yet to take action. Meanwhile, some actively provide ESG reports. This global diversity can pose significant challenges, especially when attempting to establish a standardized global framework or practice.

For example, one country's workforce might be industrious, productive, and respectful of rights but lack effective enforcement of rules. Conversely, another country's workforce might show low motivation and efficiency, yet strictly adhere to regulations. Such variations make implementing global policies or standards challenging, presenting either burdensome rules or aspirational targets for many companies.

This section focuses on the challenges SMEs may encounter while implementing ESG reporting. It is crucial to note that these challenges are not uniform across all businesses. Even within the same country or region, companies may face different obstacles. Therefore, a broad perspective is essential to understanding the fundamental challenges SMEs face in ESG reporting processes.

As Ang (2024) states, limited budgets, human resource challenges, and lack of understanding are some of the key factors preventing small and medium-sized enterprises (SMEs) from starting ESG (Environmental, Social, and Governance) reporting." However, let's explore these challenges in more detail:

1) Resource Shortage: Lack of data quality and standardization cause the problem of appropriate assessing of companies' ESG performance SMEs often lack the financial and technical resources necessary for ESG reporting (Clark et al., 2015). SMEs often lack the financial and technical resources necessary for ESG reporting. The process of ESG reporting involves collecting data, analyzing it, creating reports, hiring or contracting experts, and setting up

cooperation agreements, among other activities. All these steps are costly and time-consuming, which is a significant barrier for businesses with small budgets.

2) Lack of Awareness: Many SMEs do not have sufficient information about the benefits ESG can bring to their businesses or the potential consequences of failing to implement ESG reporting. In fact, particularly in countries outside the EU, many SMEs may not even be aware of the existence of ESG. Although this lack of awareness might not seem like a significant issue today, it could pose serious challenges in the future when it becomes difficult to adapt to ESG standards. Delaying implementation could lead to more costly and complex processes.

3) Compliance Costs and Complexity: ESG standards are typically designed for large businesses, making it more difficult for SMEs to comply. For example, SMEs that have not previously implemented worker rights or occupational health and safety standards may struggle to meet the "Social" component of ESG. Another example is that integrating ESG factors into investment decision-making processes also creates practical challenges for investors, such as determining materiality, establishing appropriate benchmarks, and measuring the financial impact of ESG considerations (Grewal & Serafeim, 2020).

4) Lack of Management Support: The lack of commitment from top-level management can negatively impact the ESG reporting process. If some managers are indifferent to ESG issues, other board members may need to spend time and effort persuading them, which can delay the process. The absence of management support is one of the main reasons ESG initiatives fail to gain acceptance and be effectively implemented within organizations. Moreover, according to Gernego et al. (2024), the lack of standardization and transparency in ESG rating methodologies can be seen as one of the barriers to ESG integration. This indicates that the board of directors needs to take this matter more seriously.

5) Cultural and Regional Differences: Geographical and cultural factors create significant diversity in ESG practices. While some regions have a high level of ESG awareness, others may have very low awareness. This diversity can make it difficult to prepare a standardized report on a global scale. Each region’s unique interpretations and applications of ESG could prevent SMEs from achieving the desired efficiency, making the process more complex and costly over time.

In Summary, The challenges SMEs face in implementing ESG reporting include information gaps, lack of expertise, financial constraints, limited awareness of ESG reports, difficulty complying with standards, insufficient workforce, cultural differences, technological

limitations, and a lack of understanding of the importance of ESG. To overcome these challenges, SMEs can seek local consultancy services, organize training and awareness programs on ESG topics, and share knowledge and experiences with other similar companies.

Case Study: ESG Practices in Limser

Port operations and the logistics sector are under increasing pressure to align with Environmental, Social, and Governance (ESG) criteria. As part of Kınay Holding, Limser has taken various steps to integrate ESG criteria into its activities. This study aims to analyze Limser's ESG strategies, the challenges it has faced, and its performance in this area, drawing lessons from its experience

Limser was established in 2009 under Kınay Holding to carry out port operations and related logistics activities. Its name is derived from the first three letters of the Turkish words "Liman" (Port) and "Servis" (Service). Currently, the company operates actively in the Aliağa and Samurlu districts of İzmir, Turkey, providing services such as empty and full container storage, handling, container repairs, and container delivery to vehicles. In port services, they offer machine-assisted or manual container stuffing/unloading, full inspection/examination services, lashing/unlashing, and collaborate with TCEGE Port Operations to conduct ship operations.

If we are to examine Limser's compliance with and approach to ESG reports in detail:

- Enviromental

Limser prioritizes two fundamental criteria in its environmental approach: reducing carbon emissions and managing waste. The company has identified energy efficiency as a primary goal in port operations, minimizing unnecessary use of machinery and vehicles, and preventing electricity from being wasted by workers. These practices have been implemented to reduce both costs and the use of fossil fuels. Additionally, the use of electric and low-emission equipment has been increased, and projects aimed at reducing dependency on fossil fuels have been launched.

In terms of waste management, Limser has invested in infrastructure to separate industrial and organic waste generated at the port and to improve recycling rates. Recycling bins are available within the port and storage facilities, and the company adopts a disciplined and

systematic work approach to reduce waste and environmental pollution, rather than acting arbitrarily. These environmentally conscious practices have led the local community to view Limser positively, recognizing its efforts to minimize harm to nature.

Moreover, to protect the marine ecosystem, waste generated within the port area is regularly cleaned and disposed of through collaboration with TCEGE.

- Social

It can be said that Limser has made significant progress in the social aspect of ESG reporting. The rights provided to employees are at a level far above the standards of other companies. For instance, employees are offered balanced and nutritious lunches prepared by a professional dietitian, free of charge. These meals are carefully prepared to include desserts, beverages, and essential nutrients required daily. Additionally, transportation services are provided to facilitate employees' commute to and from work. For those who miss the service, managers offer free rides to public transportation hubs. Limser has minimized the hierarchy between workers and management, creating a more equitable work environment where managers actively work alongside employees. Workers can comfortably request leave, negotiate changes in their schedules, or ask for permission to leave early if their work is completed ahead of time. These practices demonstrate Limser's commitment to valuing its employees' rights, personalities, and efforts.

Moreover, the company maintains a dedicated occupational health and safety specialist at its facility, ensuring regular checks of employees' equipment. Mandatory occupational health and safety training and exams are provided for new hires. Limser prioritizes the health and safety of its employees, requiring medical check-ups for new hires, including tetanus vaccinations and comprehensive health screenings, all covered at private hospitals by the company.

In terms of diversity and inclusion, Limser employs a high number of women. For example, female forklift operators, who are rarely seen in the logistics sector, are part of the workforce. The company supports the professional development of such employees by covering expenses such as license renewals and exam fees. Women are employed in various roles, including forklift operations, warehouse duties, office work, and other service areas. Additionally, Limser places significant emphasis on employing individuals with disabilities, providing job opportunities for those with physical impairments or serious health conditions.

Lastly, Limser places great importance on employee and intern training. Each year, the company invites new interns from all over Turkey, organizes conferences at universities, and

ensures that interns collaborate with managers to gain practical experience. The company provides detailed training for new employees and interns, offering not only theoretical knowledge but also hands-on and active work experience.

- Governance

Limser adheres to principles of ethics and transparency by conducting all its operational processes openly with its investors. The company offers internal and external investors the opportunity to visit the facility to observe operational processes directly and address any concerns or inquiries they may have. Investors are even welcome to actively participate in these processes and contribute to management if they wish. Continuously enhancing its environmental sensitivity, Limser is committed to meeting its stakeholders' expectations regarding environmental goals and operates accordingly. The company places great importance on its investors and customers, regularly inviting them to its offices to strengthen relationships in a warm and hospitable environment. These efforts help renew mutual collaborations and restructure existing agreements.

Limser prioritizes environmental, social, and regulatory risks in its risk management approach. The company focuses on areas such as carbon emissions, energy use, workforce diversity, employee satisfaction, and legal compliance, clearly communicating its commitments in these areas to its stakeholders. To ensure an effective quality management system, Limser has embraced Process-Based Management and Risk-Based Thinking philosophies, integrating them as key components of its corporate culture. The company accepts legal requirements and other obligations as minimum standards, monitoring, measuring, and improving its compliance and responsibilities to ensure their sustainability.

Limser aims to maintain the highest level of information security in all areas of its operations and continuously improve its information security management system. The company identifies, evaluates, and implements necessary controls for risks related to the confidentiality, integrity, and accessibility of information. It also measures the performance of information security processes and uses this data to set objectives. By addressing its vulnerabilities and threats through investments in infrastructure, work environments, hardware, software, and training, Limser minimizes potential risks. Additionally, Limser is committed to meeting the security standards required by its customers, stakeholders, and legal obligations. This approach clearly demonstrates the company's governance advancements and its ability to provide a secure environment for its customers and investors.

As a result, Limser's commitment to sustainability and ethical practices not only strengthens its reputation among investors and stakeholders but also ensures long-term success in achieving its environmental and social goals. By focusing on reducing carbon emissions, efficient waste management, and employee well-being, the company sets an example in integrating sustainability into its core operations. With its ongoing investments in environmental initiatives and social responsibility, Limser demonstrates its commitment to creating a positive impact on the community, employees, and the environment. Moreover, through transparent governance and solid risk management, Limser is well-positioned to tackle the challenges it faces and continue contributing to a more sustainable future.

Conclusion

ESG reporting has become an increasingly important tool for businesses to align with sustainability, ethical governance, and social responsibility. Within the European Union's regulatory framework, ESG reporting offers both significant opportunities and notable challenges for SMEs. While it provides benefits such as attracting investments, gaining competitive advantage, and strengthening long-term operations, SMEs also face issues like limited resources, lack of knowledge, and the complexity of compliance processes. The European Union's regulatory push highlights the critical role SMEs play in achieving sustainability goals, encouraging these enterprises to integrate ESG principles into their operations. Although the transition may be challenging, SMEs that adopt ESG practices early can position themselves as leaders in sustainability, gain access to broader markets, innovate, and build strong relationships with stakeholders In the coming years, the success of SMEs in ESG reporting will depend on the implementation of simple and clear rules, better access to information and guidance, and the organization of educational programs to raise awareness on the subject. By overcoming these challenges and adopting ESG principles, SMEs can not only meet regulatory requirements but also transform the process into an opportunity to grow their businesses and achieve a stronger competitive edge.

.

Bibliography

1. Aboud, A. & Diab, A., *The Impact of Social, Environmental and Corporate Governance Disclosures on Firm Value: Evidence from Egypt.* Journal of Accounting & Emerging Economies, 8, 2018, p. 442-458.
2. Aboud, A. & Diab, A., *The Financial and Market Consequences of Environmental, Social and Governance Ratings: The Implications of Recent Political Volatility in Egypt.* Sustainability Accounting, Management and Policy Journal, 10, 2019. p. 498-520.
3. Brown, et al., *European Union advances mandatory ESG reporting standards, 2023,* HuntonAK. https://www.huntonak.com/the-nickel-report/european-union-advances-mandatory-esg-reporting-standards (access 27.10.2024).
4. *Sustainable Aviation Fuel (SAF) production: What's next.* (n.d.), https://www.honeywell.com/us/en/news/2022/11/sustainable-aviation-fuel-saf-production-whats-next (access 2.11.2024).
5. *Share of energy consumption from renewable sources in Europe,* 2024. European Environment Agency. Available at: https://www.eea.europa.eu/en/analysis/indicators/share-of-energy-consumption-from (access 3.11.2024).
6. *Edelman Trust Barometer Special Report: In brands we Trust?*, Edelman 2019, https://www.edelman.com/research/trust-barometer-special-report-in-brands-we-trust (access 13.11.2024).
7. *Merchant, B., Foxconn: Life and death in the forbidden city of Longhua.* The Guardian, 2017, https://www.theguardian.com/technology/2017/jun/18/foxconn-life-death-forbidden-city-longhua-suicide-apple-iphone-brian-merchant-one-device-extract (access 13.11.2024).
8. *23% of energy consumed in 2022 came from renewables, Eurostat 2023,* https://ec.europa.eu/eurostat/web/products-eurostat-news/w/ddn-20231222-2 (access 3.11.2024).
9. GlobalNAPS, (n.d.). *Small and Medium Enterprises (SMEs),* https://globalnaps.org/issue/small-medium-enterprises-smes/ (access 23.11.2024).
10. *Who Cares Wins: Connecting Financial Markets to a Changing World,* Swiss Federal Department United Nations of Foreign Affairs and United Nations, 2004, https://www.unglobalcompact.org/docs/issues_doc/Financial_markets/who_cares_who_wins.pdf (access 23.11.2024).
11. Helfaya, A., Morris, R. & Aboud, A., *Investigating the factors that determine the ESG disclosure practices in Europe*, Sustainability, 15(6), 5508,2023.
12. Davis, K., 1973. *The Case for and against Business Assumption of Social Responsibilities*. Academy of Management Journal, 16, p. 313.
13. Directive (EU) 2022/2464 of the European Parliament and of the Council of 14 December 2022 on Corporate Sustainability Reporting, https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A32022L2464 (access 2.11.2024).
14. *Delivering the European Green Deal*, 2021. European Commission,https://commission.europa.eu/strategy-and-policy/priorities-2019-2024/european-green-deal/delivering-european-green-deal_en (access 2.11.2024).
15. *Corporate Sustainability Reporting Directive (CSRD),* European Commission, 2021, https://finance.ec.europa.eu/capital-markets-union-and-financial-markets/company-reporting-and-auditing/company-reporting/corporate-sustainability-reporting_en (access 13.11.2024).

16. Önder, H.,*A new concept in sustainable development approach: circular economy*. Dumlupınar Üniversitesi Sosyal Bilimler Dergisi, 2018, 57, pp. 196-203. https://dergipark.org.tr/en/download/article-file/525632 (access 25.11.2024).
17. Khan, H., *A literature review of corporate governance. In International Conference on E-business, Management and Economics*, vol. 25, 2011. p. 1-5. Singapore: IACSIT Press, https://www.researchgate.net/publication/267773286_A_Literature_Review_of_Corporate_Governance (access 18.11.2024).
18. OECD, OECD Principles of Corporate Governance 2004, OECD Publishing, Paris.
19. Şeker, Y. & Şengür, E. D., *Environmental, social, and corporate governance (ESG) performance: An international study.* Muhasebe ve Vergi Uygulamaları Dergisi, 15(2), 2022, p. 349-387.
20. Onyiriuba, L., *Emerging Market Bank Lending and Credit Risk Control: Evolving Strategies to Mitigate Credit Risk, Optimize Lending Portfolios, and Check Delinquent Loans.* Academic Press 2016.
21. T.C. Sanayi ve Teknoloji Bakanlığı, *KOBİ tanımı güncellendi!* KOSGEB 2023. https://www.kosgeb.gov.tr/site/tr/genel/detay/8807/kobi-tanimi-guncellendi (access 19.11.2024).
22. Ang, V., *SMEs must adopt ESG reporting to get ahead, say industry experts.* The Business Times 2024, https://www.businesstimes.com.sg (access 23.11.2024).
23. Clark, G. L., Feiner, A. & Viehs, M., *From the stockholder to the stakeholder: How sustainability can drive financial outperformance.* SSRN 2015.
24. Grewal, J. & Serafeim, G., *Research on corporate sustainability: Review and directions for future research.* Foundations and Trends® in Accounting, 14(2), 2020, p. 73-127.
25. Gernego, I., Petrenko, L., Lavrenenko, V. & Dyba, M., *Challenges and opportunities of ESG investing. In New Trends in Contemporary Economics, Business and Management.* Selected Proceedings of the 14th International Scientific Conference "Business and Management 2024", p. 395-402.
26. Demir, Z., *Evaluation of sample country practices in anti-corruption studies and solution suggestions.* Kırklareli University Social Sciences Journal, 4(1), 2020, p. 153-183.

Emir Gürlevük - B.A. in Logistics Management with a double major in International Trade and Finance from Yaşar University, Turkey, e-mail: 22222204002@stu.yasar.edu.tr
ORCID: 0009-0007-5111-2992