

The impact of ESG performance on corporate misconduct: evidence from Chinese A-share listed companies

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ABSTRACT

As corporate misconduct remains a persistent governance challenge, increasing attention has been devoted to whether ESG practices can effectively restrain such behavior. This study examines the impact of ESG performance on corporate misconduct and further explores the mediating role of agency costs. Using panel data from Chinese A-share listed firms over the period 2014–2023, the results show that stronger ESG performance significantly reduces corporate misconduct. Further analysis indicates that this relationship operates through an internal governance mechanism whereby ESG performance lowers agency costs, which in turn restrains corporate misconduct. These findings contribute to a deeper understanding of ESG performance as an ex-ante governance mechanism and provide policy-relevant insights into improving corporate governance and promoting sustainable development in emerging economies.

Keywords: Corporate misconduct, ESG performance, Agency costs

1. INTRODUCTION

Corporate misconduct has become a persistent and complex governance challenge in global capital markets (Dyck et al., 2024). From the accounting fraud exposed in the collapse of Enron in the United States (Ailon, 2011), to the food safety crisis triggered by China's Sanlu Group milk powder incident (Song et al., 2018), and the emissions manipulation scandal involving Volkswagen in Germany (Li et al., 2018), a series of corporate scandals have continuously undermined market trust and regulatory credibility (Davies & Olmedo-Cifuentes, 2016). Whether manifested as financial violations, product quality failures, or environmental harm, corporate misconduct distorts resource allocation efficiency, erodes investor confidence, and generates substantial economic and social costs (Carberry et al., 2018; Ye & Hu, 2025). In response, regulatory frameworks worldwide have been progressively strengthened, ranging from the enactment of the Sarbanes–Oxley Act in the United States (Act, 2002) to the continuous refinement of securities regulation in China (Chen et al., 2005). However, the enhancement of regulatory and governance frameworks has not eliminated corporate misconduct. According to official statistics, 739 securities and futures violation cases were investigated and penalized in 2024, representing an increase of 22.6 percent compared with 2022 (China Securities Regulatory Commission [CSRC], 2025). This persistence suggests that while regulatory intensity has increased, the expansion of economic scale and the transformation of economic structures continue to generate complex governance challenges (Yuan et al., 2022), prompting scholars and practitioners (He et al., 2022; Liao et al., 2019; Chen et al., 2020) to explore whether internal corporate practices can complement traditional compliance-based regulation in restraining misconduct.

Amid growing global emphasis on sustainable development, environmental, social, and governance (ESG) has evolved into a comprehensive framework for evaluating firms' non-financial performance

and long-term sustainability (Li et al., 2021). In China's capital market, ESG has progressed from normative advocacy to more substantive corporate practice. The issuance of the Guidelines on Social Responsibility for Listed Companies by the Shenzhen Stock Exchange in 2006 marked an important institutional step toward embedding sustainability into corporate operations (Zhang & Yuan, 2023). Since then, ESG performance has increasingly translated into concrete corporate actions. For instance, more than 200 Chinese firms have joined the Science Based Targets initiative (SBTi, 2022), while companies such as Alibaba Group and LONGi Green Energy have publicly committed to carbon neutrality and clean energy development. Financial institutions have also supported this transition through instruments such as green bonds (ICBC, 2023). These developments suggest that ESG performance is becoming increasingly integrated into firms' strategic decision-making and is playing a growing role in risk management, sustainable growth, and responses to stakeholder expectations. Although research on ESG performance in the Chinese context has expanded rapidly in recent years (Zeng et al., 2024), its governance implications for corporate misconduct remain underexplored. Existing studies mainly examine specific forms of wrongdoing, such as corporate fraud (Gao et al., 2024; Li et al., 2024), financial irregularities (Liu & Jin, 2023), earnings management (Mao et al., 2024), managerial misconduct (He et al., 2022), and R&D manipulation (Chen, 2024), rather than broader manifestations of corporate misconduct. Consequently, the overall governance role of ESG performance in constraining opportunistic behavior has not been systematically evaluated. Regarding mechanisms, prior research has explored several transmission channels, including financing constraints (Gao et al., 2024; Li et al., 2024), information transparency (Wang et al., 2024; Li et al., 2024), internal control quality (Gao et al., 2024), managerial myopia (Su et al., 2024), and corporate innovation (Gao et al., 2024). However, these mechanisms are typically examined within narrowly defined misconduct contexts and in isolation. Few studies integrate them within a unified corporate misconduct framework, leaving unclear whether ESG performance exerts a coherent governance effect through identifiable mediating pathways.

To address these limitations, this study examines the impact of ESG performance on corporate misconduct within a unified analytical framework. Grounded in the Resource-Based View (Barney, 1991), ESG performance is conceptualized as a strategic organizational capability that enhances governance quality and accumulates reputational and relational resources. Drawing on Fraud Triangle Theory (Cressey, 1953), such capability reshapes the behavioral environment underlying misconduct by influencing pressure, opportunity, and rationalization. Building on this integrated perspective, the study introduces agency costs as a key mediating channel, proposing that stronger ESG performance mitigates agency conflicts and managerial opportunism, thereby reducing the likelihood of corporate misconduct in the Chinese institutional context.

2. LITERATURE AND HYPOTHESES

2.1 ESG Performance and Corporate Misconduct

Corporate misconduct encompasses behaviors undertaken by corporations or their representatives that cause harm to individuals, organizations, or society by breaching legal requirements, ethical norms, or regulatory standards (Vaughan et al., 1999; Hersel et al., 2019; Palmer et al., 2016). Effectively curbing such misconduct calls for a multidimensional governance strategy, including improvements in corporate governance structures (Lu et al., 2023), strengthened regulatory supervision (Wang et al., 2024), and active societal participation (Wang et al., 2023). Amid rising public concerns regarding corporate influence and moral responsibility, Bowen (1953) first articulated the notion of corporate social responsibility (CSR), arguing that corporate decisions and

policies should be aligned with societal values and ethical expectations. With the advancement of economic globalization and the growing demand in capital markets for comparable and decision-useful sustainability information, this normative concept was institutionalized into the ESG framework in 2004. ESG offers a more systematic and evaluation-oriented structure by explicitly incorporating environmental, social, and governance dimensions into corporate assessment and strategic decision-making (Shen et al., 2023). Prior studies suggest that firms engaging in CSR are less likely to be involved in misconduct (He et al., 2022; Liao et al., 2019; Chen et al., 2020). Emerging evidence further indicates that strong ESG performance is associated with lower levels of fraud, managerial misconduct, financial irregularities, and R&D manipulation (Li et al., 2024; Sun et al., 2024; Su et al., 2024). As an extension of CSR, ESG performance embeds governance and monitoring functions that may constrain broader forms of corporate misconduct.

According to fraud triangle theory (Cressey, 1953), corporate misconduct is often driven by pressures arising from financial and non-financial factors. Strong ESG performance reflects firms' commitment to environmental responsibility, social obligations, and governance standards, enabling them to better meet the expectations of investors, regulators, employees, and other stakeholders (Daugaard & Ding, 2022). Firms with superior ESG performance are therefore more likely to obtain external financing (Eliwa et al., 2021), secure stable investments (Tang et al., 2024), and receive policy or market support (Zhang et al., 2023). From the perspective of the resource-based view (Barney, 1991), these supports constitute valuable organizational resources that enhance financial stability and competitive capability, thereby alleviating pressure and reducing incentives for corporate misconduct.

Opportunity represents another critical element in fraud triangle theory (Cressey, 1953), arising when internal controls and oversight mechanisms are weak. Strong ESG performance is associated with more robust governance structures and effective internal control systems extending from board supervision to operational management (Martiny et al., 2024). These governance arrangements enhance monitoring, standardize procedures, and strengthen risk management (Li et al., 2022), thereby limiting managerial discretion and reducing the scope for manipulation or concealment of misconduct (He et al., 2022). From the perspective of the resource-based view (Barney, 1991), firms with strong ESG performance possess greater organizational and financial resources to support investments in compliance infrastructure and control systems (Moffitt et al., 2024). Such resource advantages reinforce monitoring capacity and reduce opportunities for unethical behavior (Sun et al., 2024).

Another key component of fraud triangle theory is rationalization, which occurs when individuals justify misconduct as acceptable under certain circumstances (Cressey, 1953). Firms with strong ESG performance demonstrate sustained commitment to ethical standards, fair treatment, and responsible management practices (Daugaard & Ding, 2022). Such commitment fosters a positive organizational climate and strengthens the internalization of ethical values among managers and employees (Zhang et al., 2024). As ethical norms become embedded in daily operations (Sheehan et al., 2023), opportunistic or unethical behavior becomes increasingly difficult to justify. Consequently, strong ESG performance weakens the rationalization condition underlying corporate misconduct. Taken together, by alleviating pressure, constraining opportunity, and weakening rationalization, strong ESG performance reduces the likelihood of corporate misconduct.

H1: ESG performance has a mitigating effect on corporate misconduct.

2.2 Mediating Effect of Agency Costs

Existing studies suggest that ESG performance can restrain R&D manipulation by reducing agency costs (Chen, 2024). Based on this view, ESG performance is expected to mitigate agency conflicts

within firms and thereby lower agency costs. The governance dimension embedded in ESG performance enhances overall governance quality by optimizing board structure, strengthening internal control systems, and improving disclosure practices (Moffitt et al., 2024). These institutional arrangements strengthen the overall governance framework, optimize decision-making processes, and enhance the efficiency of corporate governance (Boulhaga et al., 2022). In addition, firms with strong ESG performance are more likely to attract responsible long-term investors (Tang et al., 2024) and professional managers (Welch, K., & Yoon, 2023), which helps align the interests of managers and shareholders within the organization. Improved governance structures and better internal coordination reduce monitoring frictions and enhance the efficiency of internal supervision (Lin et al., 2009). As governance quality improves and interest alignment strengthens, agency conflicts between managers and shareholders are mitigated, leading to lower agency costs.

A reduction in agency costs weakens the institutional conditions underlying corporate misconduct. First, declining agency costs typically reflect improved resource allocation efficiency and enhanced operational performance (Houque et al., 2022), thereby alleviating performance-related pressures faced by managers, including compensation and target pressures (Gu et al., 2025). As financial and career concerns ease, incentives to engage in misconduct driven by performance distress are correspondingly reduced. Second, lower agency costs are generally associated with stronger internal controls and more effective monitoring mechanisms (Behbahaninia, 2024), which limit managerial discretion and reduce the space available to conceal opportunistic behavior (Hales et al., 2025). As oversight improves, opportunities for misconduct are substantially constrained. Third, when governance conflicts are mitigated and organizational interests become more aligned, managers are less able to justify self-serving actions as necessary responses to unfair treatment or institutional disorder (Wirtz, 2002). Strengthened ethical discipline diminishes the rationalization pathway that often bridges pressure and opportunity. Taken together, by simultaneously mitigating pressure, constraining opportunity, and weakening rationalization, lower agency costs exert a systematic deterrent effect on corporate misconduct. Based on this reasoning, we propose the following hypothesis:

H2: Agency costs mediate the relationship between ESG performance and corporate misconduct. That is, ESG performance reduces corporate misconduct by alleviating agency costs.

3. Research Design

3.1 Sample and Data Sources

The empirical sample comprises Chinese A-share listed companies over the period from 2014 to 2023. To enhance data reliability and ensure cross-sectional comparability, several filtering steps were implemented. First, firms operating in the financial sector were excluded because of their unique regulatory frameworks, capital structures, and operational models, which may introduce systematic bias into the analysis (Khalid et al., 2024). Second, companies labeled as “ST” or “*ST” were removed, as these firms are typically subject to financial distress and exhibit abnormal governance or performance characteristics that could distort empirical results (Zhou & Xie, 2016). Third, observations lacking key variables or sufficient longitudinal data were discarded to preserve data integrity and consistency (Little & Rubin, 2019; Schafer & Graham, 2002). Finally, all continuous variables were winsorized at the 1st and 99th percentiles to mitigate the influence of outliers (Anita et al., 2023). After applying these procedures, the final dataset contains 32,578 firm-year observations.

The data used in this study were compiled from multiple authoritative databases. ESG performance data were obtained from the Sino-Securities Index (SSI). Information on corporate misconduct was sourced from the China Research Data Services (CNRDS) database. All other firm-level financial and governance variables, including agency costs and control variables, were collected from the China Stock Market and Accounting Research (CSMAR) database.

3.2 Variable Measurement

3.2.1 Dependent Variable

Corporate misconduct is measured based on officially disclosed firm-level incidents involving violations of legal, ethical, or regulatory standards (Szwajkowski, 1992; Yang et al., 2021). Following Heese et al. (2022), we define corporate misconduct as the annual number of misconduct cases attributed to each firm. The data are obtained from the “Violation and Punishment of Listed Companies” sub-database of the China National Research Data Service (CNRDS) (Cheng et al., 2025). According to the official documentation, this sub-database is constructed from enforcement announcements issued by Chinese capital market regulators and systematically records administrative penalties imposed on listed companies. It provides detailed information on the timing and types of violations as well as the relevant regulatory authorities. The database covers various forms of misconduct, including fraudulent financial reporting, disclosure violations, insider trading, stock price manipulation, misappropriation of corporate assets, and illegal guarantees.

3.2.2 Independent Variable

ESG performance refers to a firm’s performance across environmental, social, and governance dimensions as evaluated by third-party rating agencies (Martiny et al., 2024). Following prior studies (Wang et al., 2024; Su et al., 2024), this study measures ESG performance using composite ESG scores. Although mainstream international agencies such as Bloomberg, MSCI, Sustainalytics, and FTSE Russell provide widely recognized ESG ratings, their coverage of Chinese A-share listed firms is limited and relatively recent (Zhu et al., 2023). To ensure comprehensive coverage and longitudinal consistency, this study employs the Sino-Securities ESG ratings as the primary proxy.

The Sino-Securities ESG system builds upon international ESG principles while incorporating China-specific institutional features (Wu et al., 2022). It covers nearly all A-share listed firms and investable Hong Kong-listed companies, with market value coverage exceeding 95% (Sino-Securities Index, 2024). The framework comprises three primary pillars, multiple thematic layers, and a large set of underlying indicators, forming a structured and comprehensive evaluation system.

3.2.3 Mediating Variable

Agency costs arise from conflicts of interest between managers and shareholders and reflect inefficiencies associated with managerial discretion and resource consumption (Jensen & Meckling, 1976). In empirical research, agency costs are commonly proxied by expense-based measures that capture managerial consumption of firm resources (Ang et al., 2000; Singh & Davidson, 2003). Following prior studies (Chen, 2024), this study measures agency costs using the administrative expense ratio, calculated as administrative expenses divided by operating revenue. A higher ratio indicates greater managerial resource consumption and, therefore, higher agency costs.

3.2.4 Control Variables

To account for firm-level characteristics that may affect corporate misconduct, this study includes a set of control variables commonly adopted in the literature (Yuan et al., 2022; Zhou & Lei, 2025). Firm size (Asset) is measured as the natural logarithm of total assets. Financial leverage (Leverage) is calculated as total liabilities divided by total assets. Ownership concentration (Top1) is proxied by the shareholding ratio of the largest shareholder. Firm growth (Growth) is measured by the annual growth rate of operating revenue. Managerial ownership (Mhold) is defined as the proportion of shares held by senior executives. Board independence (Indept) is measured as the percentage of independent directors on the board. The book-to-market ratio (BTM) is computed as the book value of equity divided by its market value. Firm profitability is captured by return on assets (ROA), calculated as net income scaled by total assets. Detailed variable definitions and measurement methods are reported in Table 1.

Table 1

Measurement of Variables

Type	Variables	Symbol	Measurement
Dependent Variable	Corporate Misconduct	CM	The count of misconduct incidents involving a firm
Independent Variable	ESG performance	ESGP	Sino-Securities ESG ratings
Mediating Variable	Agency Costs	AC	Administrative expenses / Operating revenue
Control Variables	Firm Size	Asset	Ln (Total Assets)
	Financial Leverage	Leverage	Total Liabilities / Total Assets
	Ownership Concentration	Top1	Shares Owned by Largest Shareholder / Total Shares×100%
	Growth	Growth	Annual Percentage Change in Revenue
	Managerial Ownership	Mhold	Shares Owned by Executives / Total Shares×100%
	Board Independence	Indept	Number of Independent Directors / Total Number of Directors×100%
	Book to Market Value	BTM	Book Value of Equity/ Market Value of Equity
	Return on Assets	ROA	Net Income/ Total assets

3.3 Regression Model

Given the panel structure of the dataset, a Hausman test was conducted to determine the appropriate estimation approach. The test results ($\chi^2 = 292.79$, $p < 0.01$) reject the null hypothesis underlying the random-effects specification, indicating that the random-effects assumption is not satisfied. Therefore, fixed-effects models are employed to examine the relationship between ESG performance and corporate misconduct.

$$CM_{i,t} = \alpha_0 + \alpha_1 ESGP_{i,t} + \sum Controls_{i,t} + Firm\ FE + Year\ FE + \varepsilon_{i,t} \quad (1)$$

$$AC_{i,t} = \beta_0 + \beta_1 ESGP_{i,t} + \sum Controls_{i,t} + FirmFE + YearFE + \varepsilon_{i,t} \quad (2)$$

$$CM_{i,t} = \gamma_0 + \gamma_1 ESGP_{i,t} + \gamma_2 AC_{i,t} + \sum Controls_{i,t} + FirmFE + YearFE + \varepsilon_{i,t} \quad (3)$$

In the models, i denotes the firm and t denotes the year. All variables are defined in Table 1, and Controls represents the set of control variables. Firm FE and Year FE denote firm and year fixed effects, respectively, while ε represents the error term. Model (1) is used to test Hypothesis 1. Models (2) and (3) are employed to examine the mediating role of agency costs and thereby test Hypothesis 2.

4. RESULTS

4.1 Descriptive Analysis

Table 2 presents the descriptive statistics of the main variables used in this study. Corporate misconduct (CM) has a mean value of 0.181 and ranges from 0 to 3, indicating that misconduct is relatively common among firms (Dyck et al., 2024), with some firms experiencing multiple incidents within a single year. The variable ESGP has a mean value of 3.952, with values ranging from 0 to 6.25 and a standard deviation of 1.257, suggesting that the overall level of ESGP among sample firms remains relatively modest and may still have considerable room for improvement (Zhang & Yuan, 2023). Agency cost (AC) has a mean value of 0.084, with values ranging from 0.007 to 0.427, indicating noticeable variation in agency costs across firms. Overall, the control variables exhibit reasonable variation and distributions, which are broadly consistent with those reported in prior studies (Yuan et al., 2023; Zhou & Lei, 2025).

Table 2

Descriptive Statistics

Variable	Obs	Mean	Std. Dev.	Min	Max
CM	32,578	0.181	0.559	0	3
ESGP	32,578	3.952	1.257	0	6.250
AC	32,578	0.084	0.068	0.007	0.427
Asset	32,578	22.264	1.294	19.945	26.344
Leverage	32,578	0.411	0.205	0.055	0.920
Top1	32,578	33.245	14.562	8.370	73.560
Growth	32,578	0.145	0.372	-0.566	2.177

Mhold	32,578	15.155	19.921	0	68.764
Indept	32,578	37.755	5.285	33.330	57.140
BTM	32,578	0.618	0.249	0.118	1.201
ROA	32,578	0.040	0.068	-0.241	0.228

Note. Obs represents the number of observations; *Mean* indicates the average value; *Std. Dev.* refers to the standard deviation; *Min* and *Max* denote the minimum and maximum values, respectively. All variables are winsorized at the 1st and 99th percentiles.

4.2 Correlation Analysis

Table 3 reports the Pearson correlation coefficients among the main variables. ESGP is significantly negatively correlated with corporate misconduct (CM) at the 1% level, providing preliminary evidence that higher levels of ESG performance (ESGP) are associated with lower levels of corporate misconduct. Agency costs (AC) is positively correlated with corporate misconduct, suggesting that firms with higher agency costs may be more likely to engage in misconduct. Regarding the control variables, CM is negatively correlated with firm size (Asset), ownership concentration (Top1), managerial shareholding (Mhold), and profitability (ROA), while it is positively correlated with leverage. These correlations are generally consistent with prior studies (Yuan et al., 2022) on corporate governance and firm behavior. Overall, the correlations among the explanatory variables are moderate, and the highest pairwise correlation is well below the conventional threshold of 0.70, suggesting that multicollinearity is unlikely to pose a serious concern in the subsequent regression analyses.

Table 3

Correlation Analysis

Variable	CM	ESGP	AC	Asset	Leverage	Top1	Growth	Mhold	Indept	BTM	ROA
CM	1.000										
ESGP	-0.317***	1.000									
AC	0.084***	-0.143***	1.000								
Asset	-0.030***	0.182***	-0.312***	1.000							
Leverage	0.115***	-0.136***	-0.182***	0.493***	1.000						
Top1	-0.118***	0.091***	-0.138***	0.164***	0.013**	1.000					
Growth	-0.048***	0.001	-0.130***	0.050***	0.029***	-0.002	1.000				
Mhold	-0.076***	0.091***	0.022***	-0.372***	-0.309***	-0.053***	0.051***	1.000			
Indept	0.014*	0.071***	0.018***	-0.014***	-0.019***	0.046***	-0.014**	0.072***	1.000		
BTM	0.007	0.078***	-0.295***	0.534***	0.331***	0.137***	-0.083***	-0.129***	-0.032***	1.000	
ROA	-0.199***	0.221***	-0.246***	-0.010*	-0.379***	0.155***	0.275***	0.186***	-0.003	-0.171***	1.000

Note. ***, ** and * represent 1%, 5% and 10% significance levels, respectively.

4.3 Baseline Regression

Table 4 reports the baseline regression results examining the relationship between ESGP and corporate misconduct. Column (1) presents the fixed-effects regression including only the main explanatory variable while controlling for firm and year fixed effects. The coefficient on ESG performance is -0.1383 and statistically significant at the 1% level, suggesting that higher levels of

ESG performance are associated with fewer corporate misconduct incidents. Column (2) reports the main specification after incorporating firm-level control variables. The coefficient on ESG performance remains negative and statistically significant at the 1% level, with a value of -0.1311 , indicating that the negative association between ESG performance and corporate misconduct is robust after accounting for firm characteristics. Overall, the results provide evidence that higher ESG performance levels are associated with lower levels of corporate misconduct.

Table 4

Results of Baseline Regression

VARIABLES	CM (1)	CM (2)
ESGP	-0.1383^{***} (-29.23)	-0.1311^{***} (-28.42)
Asset		-0.0855^{***} (-6.85)
Leverage		0.2750^{***} (5.33)
Top1		-0.0034^{***} (-4.06)
Growth		-0.0304^{***} (-2.77)
Mhold		-0.0026^{***} (-4.73)
Indept		0.0036^{***} (2.97)
BTM		0.0156 (0.56)
ROA		-0.3151^{***} (-3.29)
Constant	0.5362^{***} (29.78)	2.3118^{***} (8.65)
Year FE	YES	YES
Firm FE	YES	YES
Observations	32,578	32,578
R ² (within)	0.0981	0.1090

Note, ***, **, and * indicate significance at the 1%, 5%, and 10% levels, respectively. Robust standard errors are clustered at the firm level, and t-statistics are reported in parentheses.

4.4 Mediating Effect

Table 5 reports the results of the mediation analysis. Column (2) shows that ESG performance is negatively and significantly associated with agency costs (AC) at the 1% level, with a coefficient of -0.0026 , indicating that higher ESG performance is associated with lower agency costs. Column (3) further indicates that agency costs are positively related to corporate misconduct at the 1% significance level, with a coefficient of 0.5704 , suggesting that firms with higher agency costs are more likely to engage in corporate misconduct. After including agency costs in the regression, the coefficient of ESGP on corporate misconduct remains negative and statistically significant at the 1% level, with a value of -0.1296 . However, its magnitude is slightly reduced compared with the baseline result reported in Column (1), where the coefficient is -0.1311 . This attenuation indicates that agency costs partially mediate the relationship between ESG performance and corporate misconduct. Overall, the results provide evidence that ESGP reduces corporate misconduct partly by lowering firms' agency costs.

Table 5

Results of Mediating Effect

VARIABLES	CM (1)	AC (2)	CM (3)
ESGP	-0.1311*** (-28.42)	-0.0026*** (-7.80)	-0.1296*** (-28.12)
AC			0.5704*** (4.85)
Asset	-0.0855*** (-6.85)	-0.0197*** (-10.40)	-0.0743*** (-6.01)
Leverage	0.2750*** (5.33)	-0.0142** (-2.29)	0.2831*** (5.47)
Top1	-0.00341*** (-4.06)	0.00021** (2.13)	-0.00353*** (-4.23)
Growth	-0.0304*** (-2.77)	-0.0182*** (-16.85)	-0.0200* (-1.83)
Mhold	-0.00258*** (-4.73)	0.00004 (0.58)	-0.00260*** (-4.79)
Indept	0.00359*** (2.97)	0.00008 (0.70)	0.00355*** (2.93)
BTM	0.01559 (0.56)	0.00183 (0.61)	0.01455 (0.52)

ROA	-0.3151*** (-3.29)	-0.1782*** (- 17.83)	-0.2134** (-2.19)
Constant	2.3118*** (8.65)	0.5456*** (13.07)	2.0007*** (7.51)
Year FE	YES	YES	YES
Firm FE	YES	YES	YES
Observations	32,578	32,578	32,578
R ² (within)	0.109	0.250	0.111

Note, ***, **, and * indicate significance at the 1%, 5%, and 10% levels, respectively. Robust standard errors are clustered at the firm level, and t-statistics are reported in parentheses.

To further assess the statistical significance of the mediation effect, we conduct a cluster bootstrap test with 1,000 replications. As reported in Table 6, the 95% bootstrap confidence interval for the mediating effect of ESG performance on corporate misconduct through agency costs ranges from -0.000636 to -0.000057 and does not include zero. This provides formal statistical support for the partial mediating role of agency costs.

Table 6

Bootstrap Test of the Mediating Effect

Mediating path	Mediating effect (ab)	Bootstrap method	Replications	95% CI
ESGP → AC → CM	-0.00148	Cluster bootstrap (firm)	1,000	[-0.00234, -0.00084]

Note, The table reports cluster bootstrap results for the indirect effect of ESG performance on corporate misconduct through financial constraints. Confidence intervals are based on 1,000 bootstrap replications.

4.5 Robustness Checks

4.5.1 Alternative Measures

ESG ratings provided by different agencies often diverge due to variations in indicator selection, weighting schemes, and evaluation scope (Berg et al., 2022; Chatterji et al., 2016). To ensure that the baseline results are not driven by the specific measurement of ESG performance, we conduct a robustness test by replacing the original ESGP measure with ESG ratings from another major Chinese provider, Wind. The Wind ESG rating system classifies firms' ESG performance into seven categories ranging from AAA to CCC, which are converted into a standardized 10-point scale for empirical analysis. As reported in Table 7, when ESG performance is proxied by the Wind ESG score, the coefficient on ESGPw remains negative and statistically significant at the 1% level, with an estimated coefficient of -0.0549. Both the sign and magnitude are broadly consistent with the baseline results, suggesting that the findings are robust to alternative ESG rating measures and are not driven by the choice of rating provider.

Table 7

Results of Robustness Checks

VARIABLES	CM
ESGP _W	-0.0542*** (-10.19)
Asset	-0.1431*** (-5.26)
Leverage	0.5045*** (5.61)
Top1	-0.0025 (-1.36)
Growth	-0.0214 (-1.16)
Mhold	-0.0029*** (-3.01)
Indept	0.0046** (2.34)
BTM	-0.0311 (-0.66)
ROA	-0.1406 (-1.01)
Constant	3.3914*** (5.65)
Year FE	YES
Firm FE	YES
Observations	22,674
R ² (within)	0.019

Note, ***, **, and * indicate significance at the 1%, 5%, and 10% levels, respectively. Robust standard errors are clustered at the firm level, and t-statistics are reported in parentheses.

4.5.2 Addressing Endogeneity Concerns

To address potential endogeneity concerns, we adopt an instrumental variable approach following prior studies (Zhou & Lei, 2025). Specifically, we construct an instrument based on the average ESGP of other firms operating in the same industry in a given year. This instrument captures industry-level

ESG performance patterns shared by firms within the same year while excluding firm-specific influences, thereby providing plausibly exogenous variation in a firm's ESGP that is unlikely to be directly related to its own misconduct behavior (Li et al., 2024).

Table 8 reports the results of the instrumental variable analysis. In the first-stage regression, the instrumental variable is positively and significantly associated with ESGP at the 1% level, with a coefficient of 0.6489, indicating strong instrument relevance. The Kleibergen–Paap rk LM statistic equals 464.65, rejecting the null hypothesis of underidentification. The Kleibergen–Paap rk Wald F statistic is 536.71, far exceeding conventional critical values, suggesting that the instrument does not suffer from weak identification. In the second-stage regression, ESGP remains negatively and statistically significantly associated with corporate misconduct at the 1% level, with a coefficient of -0.0657 . This result is consistent with the baseline estimates and suggests that the negative relationship between ESGP and corporate misconduct is robust to concerns about endogeneity. Overall, the instrumental variable estimates provide further support for the robustness of the main findings.

Table 8

Results of Endogeneity Test

VARIABLES	First Stage: ESGP	Second Stage: CM
Instrument (iv_ind_loo)	0.6489*** (23.17)	
ESGP		-0.0657*** (-3.46)
Asset	0.3175*** (12.24)	-0.1087*** (-7.67)
Leverage	-1.2024*** (-13.19)	0.3585*** (6.35)
Top1	0.0013 (0.81)	-0.0034*** (-3.96)
Growth	-0.0795*** (-4.28)	-0.0242** (-2.13)
Mhold	0.0055*** (4.82)	-0.0029*** (-5.22)
Indept	0.0114*** (5.02)	0.0028** (2.27)
BTM	0.0178 (0.30)	0.0133 (0.47)

ROA	0.5133*** (3.37)	-0.3539*** (-3.59)
Firm FE	YES	YES
Year FE	YES	YES
Observations	32,366	32,366
Kleibergen–Paap rk LM	464.65	
Kleibergen–Paap rk Wald F	536.71	

Note, ***, **, and * indicate significance at the 1%, 5%, and 10% levels, respectively. Robust standard errors are clustered at the firm level, and t-statistics are reported in parentheses
ESG ratings provided by different.

5. DISCUSSION AND CONCLUSION

The empirical results based on model (1) provide strong support for Hypothesis 1, indicating that firms with higher levels of substantive ESG engagement are less likely to engage in corporate misconduct. This finding is consistent with prior studies suggesting that firms with stronger corporate social responsibility or ESG performance tend to exhibit lower incidences of misconduct (He et al., 2022; Liao et al., 2019; Chen et al., 2020). While existing research has mainly focused on specific forms of misconduct, such as financial fraud or regulatory violations (Li et al., 2024; Gao et al., 2024; Su et al., 2024; Liu & Jin, 2023; Wang et al., 2024), our results suggest that the governance effect of ESG engagement extends to corporate misconduct in a broader sense.

One possible explanation lies in the resource advantages generated by substantive ESG engagement. Strong ESG performance enhances firms' access to external financing, investor recognition, government support, and reputational capital (Eliwa et al., 2021; Tang et al., 2024; Zhang et al., 2023; Zou et al., 2025), which can alleviate performance pressure and reduce incentives for misconduct. At the same time, ESG engagement strengthens governance structures and monitoring mechanisms, including improved board oversight and standardized operational procedures, thereby limiting managerial discretion and reducing opportunities for misconduct (Li et al., 2022; Moffitt et al., 2024). Moreover, sustained ESG practices help embed ethical norms and social responsibility within organizational culture (Daugaard & Ding, 2022; Sheehan et al., 2023), making it more difficult for managers to rationalize opportunistic behavior. Taken together, these mechanisms suggest that ESG engagement constrains corporate misconduct by alleviating pressure, limiting opportunity, and weakening rationalization.

The mediation analysis based on Models (2) and (3), together with the bootstrap test, indicates that agency costs play a significant mediating role in the relationship between ESG performance and corporate misconduct, thereby supporting Hypothesis 2. Higher ESG performance contributes to lower agency costs by improving overall governance quality. The governance dimension embedded in ESG practices helps optimize board structure, strengthen internal control systems, and enhance disclosure practices (Moffitt et al., 2024). These institutional arrangements improve oversight, information transparency, and internal coordination, thereby mitigating agency conflicts between managers and shareholders and reducing agency costs (Boulhaga et al., 2022). Lower agency costs further weaken the institutional conditions underlying corporate misconduct. Reduced agency costs often reflect more efficient resource allocation and improved operational performance (Houqe et al.,

2022), which alleviates performance-related and compensation pressures faced by managers (Gu et al., 2025). At the same time, stronger internal controls and monitoring mechanisms associated with lower agency costs constrain managerial discretion and reduce opportunities to conceal opportunistic behavior (Behbahaninia, 2024). Moreover, when governance conflicts decline and organizational interests become more aligned, managers are less able to rationalize self-serving actions as responses to perceived unfairness or institutional disorder (Wirtz, 2002). Taken together, these findings suggest that agency costs constitute an important transmission channel through which ESG performance restrains corporate misconduct.

This study examines the governance effect of ESG performance on corporate misconduct using firm-level panel data. The empirical results consistently show that higher ESG performance is associated with a lower incidence of corporate misconduct. Further analysis reveals that this relationship operates through an internal governance mechanism. Specifically, ESG performance reduces agency costs, which in turn contributes to the decline in corporate misconduct. These findings suggest that ESG practices enhance governance effectiveness and organizational efficiency, thereby weakening the conditions that give rise to misconduct. The results remain robust across a series of robustness tests. Overall, this study provides empirical evidence that ESG performance functions as an important governance mechanism in restraining corporate misconduct, with agency costs serving as a key transmission channel.

This study contributes to the literature in several ways. First, it extends existing ESG–misconduct research, which has largely focused on specific forms of financial misconduct (Liu & Jin, 2023) or fraud (Gao et al., 2024; Li et al., 2024; Su et al., 2024), by examining corporate misconduct in a broader and more comprehensive sense. Second, the study integrates the resource-based view (RBV) and Fraud Triangle Theory (FTT) to explain how ESG performance constrains corporate misconduct, highlighting how improvements in firms' internal resource environments and governance conditions influence the pressure, opportunity, and rationalization underlying misconduct. Third, the study identifies agency costs as an important transmission mechanism linking ESG performance to corporate misconduct. By demonstrating that stronger ESG performance reduces agency costs and thereby restrains misconduct, the findings provide new insight into the internal governance channels through which ESG practices influence corporate behavior.

From a policymaker's perspective, the findings are particularly relevant in the context of China's dual-carbon goals (Qian, 2024) and its pursuit of high-quality development (Pan et al., 2021). Encouraging stronger ESG performance among firms can simultaneously support the green transition and improve corporate governance. By promoting the integration of environmental, social, and governance considerations into corporate decision-making, policymakers can foster more sustainable resource allocation and strengthen internal governance mechanisms. In doing so, ESG-oriented policies can not only help firms align with national sustainability objectives but also contribute to restraining corporate misconduct and improving the overall quality of economic development.

From a firm-level perspective, proactively improving ESG performance carries important managerial implications. Firms that actively integrate ESG considerations into their strategic and operational decisions can enhance governance effectiveness and improve internal resource allocation efficiency. Strong ESG performance strengthens internal control systems and promotes alignment of organizational interests, thereby reducing agency conflicts and governance inefficiencies. Through these mechanisms, ESG practices support firms' long-term sustainability objectives while also contributing to more stable and responsible corporate development.

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