

ESG-LINKED EXECUTIVE REMUNERATION IN INDIAN BANKING AND FINANCE SECTOR: READINESS AND REALITIES

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ABSTRACT

ESG-linked remuneration faces the same problems as any ESG-related metrics in business settings. There is a feeling of emptiness and greenwashing that has created perception and foundational doubts in the minds of boards regarding the efficacy of ESG metrics in performance evaluations. In the banking and finance sector, there is the additional problem of regulation of executive compensation. This paper studies the existing legal, regulatory and market framework of ESG compensation in India in the banking and finance sector and makes policy recommendations on the requirement to make ESG one of the key performance evaluation metrics for executive compensation in BFSI.

Keywords: ESG-linked remuneration, ESG Framework, Business Responsibility and Sustainability Reporting, Corporate Social Responsibility.

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VIII. CONCLUSION78**I. WE BEGIN WITH A PARABLE**

In the 1990s, the growing ozone layer was a pressing global crisis, which caused scientists and economists worldwide to raise alarms. The major cause of the depletion of the ozone layer was the man-made compound known as chlorofluorocarbons (CFCs), which were used in aerosols or cooling devices.

Alarms gushed worldwide as the news of the discovery spread. Nobody questioned the scientific study or called it a hoax. Thankfully it was a world without conspiracy theory social media videos. Everyone acknowledged that the depletion of the ozone layer would severely impact people's health and the world's climate, leading to changes in every aspect of our lives. This, thereby, led to the adoption of the Montreal Protocol in 1987 to take immediate action - phasing out the chemicals, specifically CFCs. All nations of the world came together, regardless of whether they were a superpower or not, to put a halt to CFC use.¹

As of today, the ozone layer has stopped depleting and is, in fact, recovering, which is evidence of what can be accomplished when policy is informed by science and when there is shared accountability for immediate policy change.

In recent years, Environmental, Social, and Governance ("**ESG**") principles have evolved from a niche consideration to an important necessity for financial institutions worldwide. As a growing international pressure, there is a pressing urge for banks, firms and insurers to inculcate ESG principles into their operational and regulatory framework. The framework must address climate change, lessen social injustice and refine governance procedures. One of the most significant steps in this direction was the 2015 signing of the Paris Climate Change Agreement, which legally required 196 nations to take action to slow down climate change. In the age of social media and autocratic political forces worldwide, we

¹ Kira Walker, What happened to the world's ozone hole?, BBC (Mar.22, 2022) <https://www.bbc.com/future/article/20220321-what-happened-to-the-worlds-ozone-hole><https://www.bbc.com/future/article/20220321-what-happened-to-the-worlds-ozone-hole>.

are first struggling to have a consensus on whether climate change is a reality or a fallacy internationally. Such is also the case of ESG implementation from the lens of a South Asian economy. It is presently considered a ‘them’ problem and not an ‘us’ problem.

II. IS THE WORLD READY FOR ESG?

The question of whether the world is ready for widespread implementation of ESG principles within the banking, finance, and insurance (“**BFSI**”) sector emerges in India, a rapidly expanding market with a distinct regulatory environment and a variety of challenges. Regulatory bodies like the Securities and Exchange Board of India (“**SEBI**”), the Reserve Bank of India (“**RBI**”) and the Insurance Regulatory and Development Authority of India (“**IRDAI**”) have played a key role in promoting ESG adoption. There has been a profound change in the BFSI sector regarding the incorporation of ESG principles. Firms and companies are more open to accepting and incorporating these changes. Particularly in India, to respond to expanding regulatory requirements, stakeholder expectations, and sustainable global goals, the BFSI sector has begun to incorporate an ESG framework into its companies. Multinational companies with international commitments to ESG are the flag-bearers of this change. However, the complete integration of ESG into core operations continues to present difficulties despite these regulatory initiatives.

Incorporating ESG principles in financial organisations worldwide means more than just checking boxes on paper. It also means putting the principles into process, systems and, consequently, action. This assists the banking and finance industry in adopting sustainable development and developing purposeful economic strategies that balance environmental and social well-being without impacting bottom lines.

It is a strong theory that the implications of ESG principles are associated with higher equity returns and fewer downside risks by improving credit ratings

and lowering loan default rates.²In India, the RBI has issued guidelines that support green financing efforts in the financial sector, including incentives to improve energy efficiency and mitigate climate change.³

III. REGULATORY FRAMEWORK FOR ESG IN INDIA

Companies in India are using ESG reporting frameworks to disclose data regarding their business operations, opportunities, and risks. Out of 100 top companies in India, around 79% publish separate or standalone ESG reports, which clearly shows a transition towards accountability and transparency.⁴ Various organisations, including stock exchanges, non-government organizations (NGOs), not-for-profit organizations (NPOs), think tanks, business groups and governments, have created such frameworks, but only a dozen or so are considered major.⁵ The legislative framework for ESG integration creates an entire framework controlling sustainable practices among different financial institutions.

A. EVOLUTION OF ESG REGULATIONS IN INDIA

Existing frameworks governing sustainability reporting, rating techniques, and green financing have been improved by India's financial regulatory bodies, such as the RBI, SEBI and IRDAI. It started when the Ministry of Corporate Affairs (“MCA”) issued ‘Voluntary Guidelines on Corporate Social Responsibility (“CSR”)’ in the year 2009 and “National Voluntary Guidelines (NVGs) on Social, Environmental, and Economic Responsibilities of Business” in 2011, which provided a structured framework for reporting.

² Sanya Gupta, ESG: Driving positive change in Finance & BFSI, POLESTAR (Jul. 18, 2023) <https://www.polestarllp.com/blog/esg-driving-positive-change-in-finance-bfsi>.

³ *Id.*

⁴ Jennifer Shulman, Richard Threlfall, The time has come: the KPMG survey of sustainability Reporting 2020, KPMG (Dec. 2020) https://assets.kpmg.com/content/dam/kpmg/be/pdf/2020/12/The_Time_Has_Come_KPMG_Survey_of_Sustainability_Reporting_2020.pdf.

⁵ IBM, What are ESG frameworks?, IBM THINK, https://www.ibm.com/think/topics/esg-frameworks#:~:text=Regulatory%20ESG%20reporting%20frameworks%20are,these%20frame works%20and%20reporting%20requirements_.

One of the most important developments in this area was SEBI's introduction of the Business Responsibility and Sustainability Reporting (“**BRSR**”) framework in 2021. By replacing the previous Business Responsibility Reporting (BRR) structure, it raised awareness of sustainability and brought India's corporate reporting procedures into compliance with international norms, promoting increased accountability and transparency in the way Indian companies handle their ESG obligations.⁶ Consequently, 1000 companies have voluntarily adopted this framework.⁷ The IRDAI has also issued “IRDAI (Corporate Governance for Insurers) Regulations 2024” and “Master Circular on Corporate Governance for Insurers 2024”, which require all Insurance Companies in India to have a Board-approved ESG framework and oversee ESG activities.⁸ Additionally, it has issued the “Master Circular on Reinsurance” for extending these obligations to Branches of Foreign Reinsurers and Lloyd's India.⁹ Green finance initiatives are also supported and promoted through proactive policy measures of the RBI, which include giving loans to small firms in the renewable energy sector under its Priority Sector Lending scheme of 2015.¹⁰ A government-backed agency like the Indian Renewable Energy Development Agency has also set up a ‘Green Window’ to enhance the financially underserved clean energy market.¹¹ Despite all these regulations and initiatives, there is currently a lack of uniformity and a standard framework for ESG reporting and disclosures, and there is no comprehensive

⁶ Securities and Exchange Board of India, BRSR-Core- Framework for assurance and ESG disclosures for value chain, Circular No. SEBI/HO/CFD/CFD-SEC-2/P/CIR/2023/122,) (Jul.12, 2023).

⁷ First Notes; Mandatory BRSR reporting for TOP 1,000 Listed companies from FY2022-23, KPMG(Jun.8, 2021) <https://assets.kpmg.com/content/dam/kpmg/in/pdf/2021/06/firstnotes-sebi-business-responsibility-sustainability-reporting-listed-companies.pdf>.

⁸ Insurance Regulatory and Development Authority of India, Master Circular on Corporate Governance for Insurers, Circular No. IRDAI/F&I/CIR/MISC/82/5/2024 (Issued on May 22, 2024).

⁹ Insurance Regulatory and Development Authority of India, Master Circular on Insurance Regulatory and Development Authority of India (Registration and Operations of Foreign Reinsurers Branches and Lloyd's India) Regulations, 2024, Circular No. IRDAI/REIN/MSTCIR/MISC/87/5/2024 (Issued on May 31, 2024).

¹⁰ Abin Francis, Comparative Guides, ESG, MONDAQ (July 25, 2022), <http://mondaq.com/guides/results/54/1100/all/india-esg>.

¹¹ ESG, MONDAQ, *supra* note 10 at 72.

ESG-specific legislation.

B. CORPORATE GOVERNANCE AND CORPORATE SOCIAL RESPONSIBILITY

Corporate governance is an underlying principle of all policies that are rolled out in India either by SEBI or RBI or under the MCA under the Companies Act. So, there is heavy adoption of corporate governance in all the policies that are framed and laws that we issue. However, we will not find anything that says that this is corporate governance. Our corporate laws are based on common law principles, and the common law principles very heavily rely on corporate governance, which is very intrinsic in the Indian framework.

The ethics and morals in the business are enunciated by corporate governance and CSR. The idea that "*business of business is business*" is invalidated by them. It recognised the relevance of society and stakeholders by adding the touch of humanitarian and distributive aspects.¹² Corporate governance aims to balance the 4Ms—money, manpower, machinery, and management—to harmonise the interests of the corporation with those of its shareholders.¹³ Corporate governance is a system of rules and procedures created to manage and control the company. Such practices are based on principles of fairness, transparency, obligations, and risk management. However, challenges continue to arise in its implementation.

For instance, we are finding it difficult to define the role of independent directors and non-executive directors in companies. There is a recent slew of decisions at the High Court and Supreme Court level for banking and insurance companies where they have highlighted that the role of a non-executive director is to only attend the meetings of a company, and he cannot be held responsible for fraudulent actions of the company or other misconduct of the company which were not discussed at board meetings, and he was not a party to them.¹⁴

¹² A Sharma, Interrelationship between Corporate Governance and Corporate Social Responsibility, SSRN JOURNAL (Dec.19, 2022)https://papers.ssrn.com/sol3/papers.cfm?abstract_id=4294364.

¹³ *Id.*

¹⁴ K.S. Mehta v. M/s Morgan Securities and Credits Pvt. Ltd., 2025 SCC OnLine SC 492 (Ind.).

Whistleblower protection is also of paramount importance in the context of ESG concerns. Critical and sensitive information in connection to areas like environmental harm, labour exploitation, or governance failure can be provided through whistleblowers. However, independent directors and non-executive directors also find it difficult to report these issues due to the lack of proper implementation of the whistleblower protection mechanism. Along with revision in the policy perception of executive remuneration, an important ancillary aspect of empowering executives to take ESG based actions is strengthening whistleblower mechanisms and protections in India.

C. CORPORATE SOCIAL RESPONSIBILITY AND ITS CHALLENGES

A few years back, corporations realised their responsibility beyond maximising profits for shareholders and executives. They also have a social responsibility towards society at large, and this realisation has led the way for companies to be identified as socially responsible. According to UNIDO¹⁵ *“Corporate Social Responsibility is a management concept whereby companies integrate social and environmental concerns in their business operations and interactions with their stakeholders. CSR is generally understood as being the way through which a company achieves a balance of economic, environmental and social imperatives (“Triple-Bottom-Line- Approach”), while at the same time addressing the expectations of shareholders and stakeholders. In this sense, it is important to draw a distinction between CSR, which can be a strategic business management concept, and charity, sponsorships or philanthropy. Even though the latter can also make a valuable contribution to poverty reduction, will directly enhance the reputation of a company and strengthen its brand, the concept of CSR clearly goes beyond that”*. This concept is embedded in Section 135 of the Companies Act 2013, which mandated certain companies to contribute a certain amount towards CSR activities.¹⁶ Its applicability is on companies whose annual turnover is INR 1000 crore or above, a net worth

¹⁵ United Nations Industrial Development Organisation, Corporate Social Responsibility, UNIDO, Progress by innovation <https://www.unido.org/our-focus-advancing-economic-competitiveness-competitive-trade-capacities-and-corporate-responsibility-corporate-social-responsibility-market-integration/what-csr>.

¹⁶ Companies Act, No. 18 of 2013, §135 (Ind.).

of INR 500 crore or above or a net profit of INR 500 crore or above.¹⁷

IV. HOW MUCH HAS THE WORLD REALLY INTEGRATED ESG PRINCIPLES INTO POLICIES?

Despite these regulatory requirements, several challenges persist in its effective implementation, including a lack of resources and specialised skills. The changing management culture can also be a challenge. Sometimes, it's difficult to report and measure the impact of CSR because quantifying the tangible results of CSR initiatives is not easy.¹⁸ Globally, ESG has evolved from a minor concern to a key corporate strategy. Investors are drawn to companies with strong ESG policies because they report higher equity returns and fewer risks.¹⁹ Boards of many BFSI companies are revising their agendas to incorporate sustainability goals and align investment decisions with mitigating climate risk.²⁰ Global CEOs have been tasked to implement country-specific ESG policies and targets.

India is at a key moment in incorporating ESG practices. Conversations with Indian business leaders reveal mixed views. Some businesses are staying quiet about their green initiatives due to financial constraints and concerns about being accused of false green claims. However, nearly half, 42%, of these leaders stress the importance of reducing carbon emissions and achieving net-zero goals in the next three years.²¹ While sustainability is recognised as crucial for business, the way sustainability is implemented in business systems varies owing to customised commercial considerations.

¹⁷ *Id.*

¹⁸ ESCE, What are the challenges of CSR for Companies?, ESCE (May 7, 2024) <https://www.esce.fr/en/faq-all-the-answers-to-your-questions/what-are-the-challenges-of-csr-for-companies/>.

¹⁹ Sean Brown & Robin Nuttal, The role of ESG and purpose, MCKINSEY (Jan.4, 2022) <https://www.mckinsey.com/capabilities/strategy-and-corporate-finance/our-insights/the-role-of-esg-and-purpose>.

²⁰ Tom Imbesi, Chair of the Future: The role of the Chair in the climate transition, DELOITTE, (2023) <https://www.deloitte.com/au/en/services/risk-advisory/analysis/role-chair-climate-transition.html>.

²¹ Amit Khandelwal, Indian CEOs adopt AI for future success: CEO outlook Pulse Survey 2024, (Jun.19, 2024) https://www.ey.com/en_in/ceo/indian-ceo-s-adopt-ai-for-future-success-ceo-outlook-pulse-survey-2024

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More Indian boards are spending time debating key ESG topics, including diversity and climate risks. Although India has a strong commitment to ESG standards, there are issues with the full implementation of these standards. A survey of 150 organisations indicates that only 27% of Indian firms are confident in meeting ESG standards. This poll points to a disconnect between their professed commitment to ESG values and their willingness to act. It was surprising to learn that only 15% of companies think their suppliers are ready to adapt to ESG standards. In the consumer goods industry, only 7% of companies say they are very ready, which is a sign of unpreparedness. However, sectors such as energy, resources, healthcare, financial services, and industrials show better preparedness levels.²²

Effective ESG integration requires robust leadership. Of late, concerns regarding climate change have compelled 91% of Indian companies to increase environmentally friendly investments. The report states that 87% of Indian CEOs are concerned about climate change, and 40% rank it even above issues such as economic trends or AI advancements. Also, 62% support ensuring an equitable and inclusive transition as part of their sustainability agenda.²³

V. ESG IN INDIA: ADOPTION, CHALLENGES, AND ECONOMIC REALITIES

A. CURRENT TRENDS IN ESG ADOPTION: INDIA AND WORLDWIDE

The 2025 Sustainalytics data emphasised that over 15,000 companies in 42 industries are adopting ESG frameworks in their daily operations and work. Out of which, 50 companies have accomplished “Top-Rated” status worldwide due to their implementation of robust ESG principles. Moreover, 77 % of G250

²² Jon Raphael & Kristen Sullivan, Sustainability action report: Survey findings on ESG disclosure and preparedness, DELOITTE (Dec. 2022) <https://www2.deloitte.com/content/dam/Deloitte/us/Documents/audit/us-survey-findings-on-esg-disclosure-and-preparedness.pdf>

²³ Jennifer Steinmann, Deloitte 2024 CxO sustainability Report: Signs of a shift in business climate action, DELOITTE (Sep. 2024) <https://www.deloitte.com/global/en/issues/climate/cxo-sustainability-report.html>

companies now align their sustainability reports with the Global Reporting Initiative (GRI) standards, as revealed by the Global ESG survey.

The Global Sustainable Investment Alliance estimated that ESG investments will total \$35.3 trillion globally in 2024 in terms of investment trends. The figure accounts for about one-third of all the assets managed globally. But there are regional differences. The United States corporations are facing challenges due to varying legislation, while Spain and Italy are leading the way in Europe.²⁴

According to the reports, Indian MNCs or large companies have made notable strides in adopting ESG principles in their structures. The Indian government is said to be committed to ambitious targets, including becoming net-zero carbon by 2070 and launching initiatives like the Green Hydrogen Mission.²⁵ However, owing to a lack of knowledge and resources, mid-tier and smaller enterprises fall behind. Regulations like green deposits and climate risk disclosure guidelines have put the Indian BFSI industry at a turning point.²⁶

VI. ARE CORPORATIONS TRULY COMMITTED?

In the past, companies were evaluated just by their financial success. Now, they should consider ESG principles. This change reflects a shift towards being more socially responsible. Large corporations, known as MNCs, face pressure from new government regulations, investor demands, and societal expectations to adopt ESG practices. Because of this, 40% of the world's biggest companies are now tying executive pay to ESG goals.²⁷ They are adopting and constantly changing

²⁴ ESG in 2024 and Outlook for 2025 in the US and EU: A Tale of Two Regions, BARNES & THORNBURG (Jan. 7, 2025) <https://btlaw.com/insights/alerts/2025/esg-in-2024-and-outlook-for-2025-in-the-us-and-eu-a-tale-of-two-regions>

²⁵ Sanat Rao, *Esg in Indian Banking Sector: An Equation of Growing Importance*, Infosys Finacle <https://www.finacle.com/insights/blogs/esg-in-indian-banking-sector-an-equation-of-growing-importance/>

²⁶ ESG in the BFSI Sector, Breathe ESG, <https://www.breatheseg.com/resources/esg-in-the-bfsi-sector>

²⁷ John McCalla-Leacy & Dr. Jan-Hendrik Gnandiger, *The move to mandatory reporting: Survey of Sustainability Reporting 2024*, KPMG International (2024). <https://assets.kpmg.com/content/dam/kpmgsites/xx/pdf/2024/11/the-move-to-mandatory-reporting-web-copy.pdf.coredownload.inline.pdf/>.

their ESG strategies in their policies. The major attention will be on managing significant risks and opportunities, specifically in governing the companies. Thus, this trend indicates that companies are beginning to incorporate ESG into their core strategies instead of maintaining it as an independent initiative. Even with significant efforts made to implement ESG principles, there is a gap in doing so effectively due to various reasons, including the increase in inflation and the decline of the stock market. The consumer price index (CPI) is also very high, not only in India but in the rest of the globe as well. It can be especially difficult for small corporations and Non-Banking Financial Companies (NBFCs) because of a shortage of resources to implement comprehensive ESG principles, whereas the larger corporations have advanced technology to meet these principles.²⁸

A. BOARD EXPECTATIONS FOR ESG

Boards of directors have different expectations in the implementation of ESG. Some are concentrated on key sustainability targets, including net-zero emissions or renewable energy investments. These boards view ESG to enhance long-term value as well as deal with climate-related risks more effectively. Others do smaller things, such as arranging recreational activities or going paperless, which positively impact workplace culture but fail to address bigger environmental or societal concerns. This brings forth a critical question: *Have the companies/MNCs truly made ESG or sustainable measures an integral part of their business model, or have they just adopted these measures on the superficial level?*

A key element in enhancing the business plans of MNCs and corporations is that they are strongly advised to incorporate ESG strategies in their office environment. This also means that people who are interested in the company, like investors, customers, or even employees, want businesses to make money but also to do it in a way that matches society's values. This also indicates that stakeholders increasingly demand that companies not only generate profits but do so in a manner that aligns with broader societal values. Thus, while some organisations

²⁸ Akhil Puri, #NavigatingTheFuture- Key trends shaping India's BFSI sector in 2025, FORVISMAZAR (2025)<https://www.forvismazars.com/in/en/insights/market-insights/key-trends-shaping-india-s-bfsi-sector-in-2025>.

may adopt ESG practices at a minimal level, there is a growing expectation for comprehensive integration across all facets of operations.

VII. REGULATORY CONUNDRUM OF ESG REMUNERATION

The financial crisis of 2008 showed a perilous misalignment between the way insurers and bankers were rewarded. Their executives bet recklessly to fatten up profits in the short term, grabbing big bonuses long before the blowback from their actions manifested itself. When these bets then turned sour, by which time they had already vanished, the costs fell on the shareholders and the taxpayers.²⁹ This discontent between reward and responsibility highlighted a fundamental flaw in compensation structures, one that renowned economist Nassim Nicholas Taleb discusses in his book *Skin in the Game*. In it, Taleb argues that true accountability requires decision-makers to face the consequences of their actions, not just reap the benefits.³⁰ This led to the increasing use of clawback clauses in executive remuneration, especially in regulated sectors such as banking and insurance.

This is part of a wider understanding that sustainable banking and insurance growth relies on incentivizing long-term stability rather than short-term profits. With ESG considerations increasingly in the spotlight, these reforms to compensation assume greater importance, ensuring executives are incentivized not only by profit but by resilience and responsibility.

A. PERFORMANCE METRICS AND RESPONSIBILITY

The subject of ESG performance and executive pay has been an area of contention, with way too many examples of packages deemed “excessive”, whether by company shareholders or activists. In the present global financial ecosystem, the ESG has become a critical benchmark for evaluating the

²⁹ David C. Broadstock, Kalok Chan, Louis T.W. Cheng & Xiaowei Wang, The role of ESG performance during times of financial crisis: Evidence from COVID-19 IN China, SCIEDIRECT (Jan. 22, 2021) <https://www.sciencedirect.com/science/article/pii/S1544612320309983>

³⁰ Nassim Nicholas Taleb, *Skin in the Game: Hidden Asymmetries in Daily Life* (Random House 2018) <https://philosophiatopics.wordpress.com/wp-content/uploads/2018/10/skin-in-the-game-nassim-nicholas-taleb.pdf>

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sustainability and impact of financial institutions on various stakeholders.³¹ Furthermore, ESG has shifted from being discretionary to a high priority in Indian boardrooms, thus redefining how banks and other financial institutions strategize their future growth. Investors, customers and even regulators like the RBI increasingly expect more accountability and sustainable practices from the industry.

With the increasing significance of ESG factors, there is increasingly strong backing to experiment with executive compensation for ESG performance. Executive compensation has traditionally been driven by financial outcomes and share price performance. The inclusion of ESG measures into compensation arrangements might increase accountability and promote long-term strategic planning focusing on sustainability. Current market information indicates that ESG-tied compensation is still novel. Also, in the EU member states, 17% of the public companies have implemented such measures, but in the USA and Canada, it is only 13%.³² However, despite this, there is a noticeable shift towards including nonfinancial goals in compensation plans, with 57% of 500 companies now incorporating at least one ESG-linked compensation.³³ Additionally, new financial regulations are compelling financial institutions to embrace ESG strategies. Yet emerging markets encounter peculiar challenges in enacting these initiatives because of resource shortages, poor infrastructure, and socioeconomic disparities. Such obstacles can derail ESG investments, which makes it important to devise innovative strategies to provide sustainable development.

Recent studies have shown the connection between executive pay and financial

³¹ Agyeya Tripathi, Exploring the dimensions of ESG in banks, TOI ECONOMY Dec.22, 2024 <https://timesofindia.indiatimes.com/blogs/agyeya/exploring-the-dimensions-of-esg-in-banks/>.

³² Ranjitha Ajay & Surendranath Rakesh Jory, Advancing understanding of ESG score and executive compensation relationships in the Indian context, 62 Global Finance Journal <https://www.sciencedirect.com/science/article/abs/pii/S1044028324000656>

³³ Adam Gorley, What is ESG and Why It's Important for Risk Management, SUSTAINALYTICS, (Mar. 02, 2022) <https://www.sustainalytics.com/esg-research/resource/corporate-esg-blog/what-is-esg-why-important-risk-management#:~:text=Broadly/>.

performance; however, they have also highlighted the growing influence of ESG.³⁴ Researchers have demonstrated that a strong CSR initiative lowers a firm's cost of equity, as investors view such companies as less risky. Further, it has been revealed that ESG Linked compensation policies can moderate the relationship between pay and carbon performance.

After the 2008 financial crisis, it was mandatory to incorporate a clawback clause in executive compensation frameworks to ensure accountability and long-term stability. A clawback clause allows an entity to recover previously paid compensation, such as bonuses or stock options, from directors and CEOs under certain circumstances, such as financial misstatements or misconduct.³⁵ By enforcing financial repercussions for short-term recklessness, the clawback clause aligns executive rewards with reducing performance, protecting shareholders, customers and the broader economy from systematic fallout.

However, there is growing concern regarding the 'emptiness of ESG metrics' per se that has become a barrier in the widespread adoption of ESG as a business parameter in the first instance and to determine variable executive compensation in the second instance. As the Western world implements ESG governance beyond its realm, the realities of greenwashing practices adopted to date have become a stark reality facing South Asian executives reporting on ESG compliance. If viewed from this angle, ESG-linked remuneration has the same systemic implementation problems as any other metrics in the context of ESG. This problem is doubled in the banking, finance and insurance sector where executive compensation is regulated and approved by the regulators.

B. REGULATIONS IN BANKING AND FINANCE

Executive remuneration in the banking, finance and insurance sectors is

³⁴ Namrata Rana, ESG and the Growth Imperative-For Indian companies, KPMG, (Jan. 21, 2025) <https://kpmg.com/in/en/blogs/2025/01/esg-and-the-growth-imperative-for-indian-companies.html>.

³⁵ Johanna Stark, Clawback Provisions in Executive Compensation Contracts, BUSINESS LAW BLOG (Aug. 25,2020) <https://blogs.law.ox.ac.uk/business-law-blog/blog/2020/08/clawback-provisions-executive-compensation-contracts>.

regulated by RBI, SEBI and IRDAI in India. Primarily, they are based on the International Financial Stability Forum(FSF)Principles for Sound Compensation Practices (“**FSF Principles**”) dated April 02,2009 to redress deficiencies in compensation practices that contributed to the global financial crisis that began in 2007and further Implementation Standards for the Financial Stability Board (FSB) Principles for Sound Compensation Practices (“**FSB Principles**”)³⁶ on September25, 2009 which were designed to support the implementation of the principles.³⁷ Executive compensation especially variable components are heavily regulated in terms of when such remuneration may be paid and if so how much. It is compulsory for regulated entities to have a Nomination and Remuneration Committee that decides executive compensation based on board approved principles.³⁸ The key issue with this policy approach is that the FSF Principles and the FSB Principles where not policy rollouts as a measure of risk mitigation prevent.³⁹

They were a knee-jerk reaction to the fallout of the global economic crisis on ‘what ought to have been’. ⁴⁰The principles were well considered. They also have a traditional tone. But when we examine executive compensation regulations in

³⁶ Implementing the FSB Principles for Sound Compensation Practices and their Implementation Standards; Fourth Progress Report, FSB FINANCIAL STABILITY BOARD (Nov. 10, 2015) <https://www.fsb.org/uploads/FSB-Fourth-progress-report-on-compensation-practices.pdf>.

³⁷ Vittoria Cerasi, Sebastian M. Deininger, Leonardo Gambacorta & Tommaso Oliviero, How post-crisis regulation has affected bank CEO compensation, BANK FOR INTERNATIONAL SETTLEMENTS (Apr. 2017) <https://www.bis.org/publ/work630.pdf>.

³⁸ Companies (Appointment and Qualification of Directors) Rules, 2014, Rule 4. Number of Independent directors.

Securities and Exchange Board of India (Listing Obligations And Disclosure Requirements) Regulations, 2015, Rule 19, Nomination and remuneration committee.

³⁹ Guido Ferrarini and Maria Cristina Ungureanu, Flexibility of the FSB Principles for Sound Compensation Practices at Financial Institutions, HARVARD LAW SCHOOL FORUM ON CORPORATE GOVERNANCE (Mar. 31,2011). <https://corpgov.law.harvard.edu/2011/03/31/flexibility-of-the-fsb-principles-for-sound-compensation-practices-at-financial-institutions/>.

⁴⁰ Abhijit Sen, Arjun Sengupta, B.B.Bhattacharya, Gurbachan Singh, Jagdish Shettigar, Prasenjit Bose, Manish Tiwari, Atul Anjan, Mythili Bhusnumath, Avoid Knee-jerk Reaction to Tackle Inflation, ORF REPORT <https://www.orfonline.org/public/uploads/posts/pdf/inflation.pdf>.

banking and finance, there is one question that counts above all. That is: how will the executive's behaviour impact the financial stability or risk of the regulated firm? In this manner, the rules consider only one side. But a lot of ESG-related actions impact financial outcomes not only in the short run, but also in the mid-term. Due to this, BFSI executives might just continue to pay lip service to ESG. Their true concern might just remain focused on fulfilling financial goals set forth by the regulators and the board.

It is critical to highlight that India has taken significant regulatory steps to promote ESG transparency. In 2015, SEBI mandated BRRs for the 500 listed entities, thereby enhancing non-financial disclosures.⁴¹ This was expanded in 2021 with BRSR, asking the top 1,000 entities to disclose ESG metrics aligned with global standards.⁴²

Moreover, in the Companies Act 2013, the word “remuneration” means any money or its equivalent given or passed to any person for services rendered by him and prerequisites as defined under the Income Tax Act, 1961.⁴³ Section 197 of the Companies Act, 2013 states that the maximum remuneration for directors is governed by specific regulations that companies, including financial institutions, must comply with in order to meet limits while determining director pay. It is pertinent to mention that companies should also comply with the guidelines outlined in Section 200, read with Rule 6 of the Companies (Appointment and Remuneration of Managerial Personnel) Rules 2014 while setting the remuneration. Section 135 of the Companies Act further mandates that Indian companies above a certain financial threshold⁴⁴ shall spend at least 2% of their

⁴¹ Securities and Exchange Board of India, Format for Business Responsibility Report, 2015, SEBI Circular No. CIR/CFD/CMD/10/2015, (Nov. 04, 2015).

⁴² Dr Rajeev Singh & Chaitanya Kalia, Business Responsibility and Sustainability Reporting (BRSR) The evolution of sustainability reporting in India, ERNST & YOUNG ASSOCIATES LLP (2023), <https://www.ey.com/content/dam/ey-unified-site/ey-com/en-in/insights/climate-change-sustainability-services/documents/ey-business-responsibility-and-sustainability-reporting.pdf>.

⁴³ Companies Act, No. 18 of 2013, §2 (Ind.).

⁴⁴ Section 135 of the Companies Act, 2013 provides for Corporate Social Responsibility (CSR) for such companies which, in the previous financial year, have a net worth of ₹500 crore or more, a turnover of ₹1,000 crore or more, or a net profit of ₹5 crore or more.

profits on CSR activities, focusing on areas such as education, healthcare, and environmental protection, thereby reinforcing corporate accountability. It is also important to note here that although the CSR provision under the Companies Act, 2013 began with a lot of enthusiasm, the provision has lost its lustre. This is because the provision is not mandatory and the only consequence of not spending the prescribed amount in CSR expenditure is making a note of why this was not spent in the directors' report.

VIII. CONCLUSION

Considering what the Environmental, Social, and Governance (ESG) values stand for us, the journey to effectively integrating ESG is not easy. Thus, the primary concern is whether we are ready for the integration of ESG. Firms are more interested in integrating ESG principles into their office setup, but several obstacles remain to be overcome.

Achieving a board-level consensus is one major hurdle. Most decision-makers are concerned that ESG projects might contradict expansion, profit, or overall financial success. This misconception serves as a hindrance to fully accepting ESG as an integral part of business strategy. This misconception holds back the full integration of ESG as a basic element of corporate strategy. In addition, identifying clear-cut criteria for measuring ESG performance adds more complexity. The term 'ESG' encompasses a wide range of elements, making boards grapple with how best to prioritize environmental, social, and governance issues. The 2008 crisis underlined the risks of a bonus culture that paid for short-term dangerous risk-taking but protected executives from accountability.

Today, linking executive compensation to ESG goals offers a pragmatic solution, as it rewards sustainable, long-term performance. Globally, the pace is slow; in India, though, the leadership has been forthcoming with mandatory ESG disclosures and CSR mandates. The path forward is clear: compensation design must balance returns with accountability. Properly applied the clawback clause and ESG-based remuneration can initiate a change. Despite these difficulties, it is important to note that multinational companies are putting serious efforts into incorporating ESG into their organisational cultures. While we are playing around

with the concept of embracing ESG principles in totality, we are not yet prepared for its implementation in all industries.

For ESG remuneration to truly become mainstream, there is a need to reconsider policy decisions made in relation to executive compensation in banking and finance after the global financial crisis of 2007 and realign them towards the impending environment, social and governance crisis the world is on the brink of facing. The true lesson we can learn from the FSF Principles and the FSB Principles in the context of ESG is that we should not wait for a global crisis to kickstart policy making. Uniting international forces for consensus and worldwide implementation is important to see any movement in this area. Change of regulatory mindset and consequent change to regulatory policies is also important. Macro-economic stability is presently based on financial and economic stability. Bringing ESG into the picture shall require making social and environmental stability two indispensable pillars in financial policy making.