Executive Compensation Key Driver for fulfilling India's Net Zero Commitment

As global momentum builds to tackle climate change, India has made big commitments for the same at the 2021 United Nations Climate Change Conference, which was recently held at Glasgow. The Prime Minister of India made important announcements related to India's climate action plan. One major commitment being that India would achieve Net-Zero target by 2070 which was backed by concrete measures to support this goal. The Indian Prime Minister also called on Indian corporates and foreign investors to bring investments and build capabilities around Net Zero initiatives. Simultaneously, the Government is undertaking public initiatives and supporting industries to reach net zero goals by developing solar energy capacity, committing Indian Railways to Net Zero by 2030, and through other social, health and governance initiatives.

Also, regulatory developments in the corporate sector seek to bolster reaching net zero targets. For instance, in line with the vision for greater sustainability, the Securities and Exchange Board of India (SEBI) introduced new requirements for the top 1,000 listed companies. These pertain to reporting on sustainability. The new reporting format called Business Responsibility and Sustainability Report (BRSR) aims to establish a comprehensive source of non-financial sustainability information relevant to all business stakeholders. While it is voluntary for FY2021-22, it is mandatory from next fiscal onwards.

The governments and other stakeholders growing concern about climate change isn't lost on India Inc. This is evident by the 17% increase from 2019 to 2020 in the number of Indian companies (220 organisations) that disclosed their climate change goals to investors and customers, as per a report by CDP India. Additionally, 52 Indian organisations have committed to the Science Based Target Initiative (SBTi) and submitted their GHG emissions reduction targets. Globally, India ranks sixth in terms of the number of companies that have committed to SBRi and higher than any emerging economy.

Large businesses like Reliance Industries, Mahindra Group, JSW Group, Tata Group, ITC and Wipro have made voluntary commitments to achieve carbon neutrality. Furthermore, all leading Indian organisations have adopted ESG goals in one way or another as part of their sustainability initiatives. And it would not be surprising should these commitments grow stronger and spread wider among different industries in the coming years.

It's crucial to note that to be effective, these ESG commitments cannot be stand-alone targets for organisations. Rather, they need to be tied to an organisations overall vision and business strategy. To tie ESG goals to business decisions, boards around the world are adopting ESG metrics and targets and linking them to executive pay and incentives.

What can company boards do – The role of executive compensation

Boards have the key role of setting expectations for the management and reward them for delivering the desired performance whilst demonstrating the right behaviours. One

big lever that they have to drive any agenda is through executive compensation.
Principle 6 of the World Economic Forum's principles for climate governance specifically calls out for executive incentivisation on climate-related targets and indicators.

An analysis conducted by Willis Towers Watson in 2020 shows that approximately 11% of top 350 European companies have disclosed linkages between CO2 emissions to their long-term incentive plans.

This issue is still in the early stages in India, but several progressive companies are considering adding explicit carbon-related targets in executive incentive plans. We expect to see many more companies purse this over the coming year.

Possible metrics to measure ESG goals
Boards can tie compensation to definitive metrics based on holistic ESG results. Possible metrics include:

- Environmental – tCO2e (or tonnes of CO2 equivalent). The metric is applied across direct and indirect resources consumed by an organisation.
- Governance metrics around whistle-blower policies, unethical behaviour tied to monetary losses, dismissal, and incentives against excessive risk-taking, roles of risk officers, etc.
- Social metrics: like pay-equity ratios, diversity, and representation targets, etc.

These may need to be calibrated to industry and relevant timeframes for them to be effective to drive the desired management behaviours.

On climate change, now is the time to act, or it might be too late
Organisations should focus on having relevant systems that can measure and track carbon emissions, set clear and stretched reduction targets and then align executive compensation plans to these goals. It is important to understand that substantial maturity is required when incorporating CO2 emission reduction targets in executive compensation.

This article was first published in Financial Express.

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