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# The Role of Corporate Governance in Addressing Climate Change: The Case of India

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Climate change is forcing transformations in corporate governance. This is because large corporations have a dual relationship to climate change. On the one hand, mounting scientific evidence has established that the activities of corporations, such as emissions of greenhouse gases, cause climate change.[1] On the other hand, anthropogenic climate change poses a significant material financial risk to corporations, their shareholders, and other stakeholders. Hence, corporations and the law governing them play a vital role in addressing climate risk.

Until recently, the role of corporations in tackling climate change was embedded in the concept of voluntarism and social responsibility. This approach has nudged companies, generally by soft law, to have regard to matters pertaining to the environment. More recently, though, the discourse has taken a dramatic shift. No longer is climate change merely within the domain of voluntary conduct on the part of corporations. It is a material financial risk that corporations encounter, thereby imposing duties on the boards of directors to recognize and address it. Corporate boards can ignore the importance of climate risk only at the peril of reputational and legal consequences.

This essay focuses on two principal aspects of corporate governance pertaining to climate change that have received emphasis in the Indian context. The first is the duties of directors under corporate law to consider environmental matters pertaining to the business of a company. The second is the disclosure and reporting regime for environmental, social, and governance (ESG) issues and, in particular, climate change. The essay also briefly touches upon certain enforcement considerations that may open a wedge between substantive law and its implementation.

**Directors' Duties**

Since companies face greater scrutiny and responsibility in the context of climate risk, the nature of their governance gains prominence and the duties and liabilities of directors on corporate boards become pivotal. In India, Section 166(2) of the Companies Act, 2013 provides that a "director of a company shall act in good faith … in the best interests of the company, its employees, the shareholders, the community and for the protection of the environment." The jurisprudence surrounding this provision suggests that directors ought to consider the long-term interests of the company, which compels directors to identify and assess the risks emanating from climate change and implement strategies to address them. Conduct that involves sacrificing the long-term interests of the company in favor of short-term profitability would militate against the statute.

Furthermore, the fact that "the protection of the environment" commands its own space in Section 166(2) indicates that directors are obligated to turn their attention towards the topic regardless of any associated financial implications. The protection of the environment stands on an equal footing with catering to the interests of the shareholders or other stakeholders.[2] Hence, directors are not entitled to side-step issues of climate change in favor of other stakeholders such as shareholders. In a legal opinion issued to the Commonwealth Climate and Law Initiative (CCLI), senior advocate Shyam Divan and his colleagues opine that a "decision taken seemingly in the financial interest of the company and its shareholders, but which is detrimental to the environment, may transgress section 166."[3]

Corporate directors also bear a duty of competence. First, Section 166(3) of the Companies Act stipulates that directors shall exercise their "duties with due and reasonable care, skill and diligence and shall exercise independent judgment." Second, both the Companies Act and, in the case of listed companies, the listing regulations of the Securities and Exchange Board of India (SEBI), require boards to establish a framework for risk management. Given that climate change is not only a key risk for Indian companies but is one that is gaining greater prominence over time, directors' duties to account for climate risk can undoubtedly be found in the legal framework in India.

Hence, companies in general, and those that are vulnerable to the effects of climate change in particular, need to establish clear systems and processes to identify and address climate risk. This includes appropriately disclosing climate risks along the lines of well-known reporting frameworks and ensuring that they are represented in the financial statements, and more generally formulating strategies to ensure that the company will resiliently and sustainably operate in a net zero carbon global economy. All this is evident from the scope of directors' competence duties, although the details of the degree and nature of risk may vary from company to company. Due to the predominance of climate change as a leading risk that companies face, ignorance or inaction on the part of the directors to assess and deal with the risk would cause them to breach their duties under company law. In cases where companies are required to establish risk management committees, the directors on such committees arguably carry a greater responsibility to identify risks of climate change and deal with them.

Even if directors acknowledge climate risk, the competence duties they owe require them to make further investigations to obtain adequate information, appoint experts and obtain their advice, and oversee and supervise management to whom they may have delegated tasks for identifying, strategizing, and implementing a framework to address climate risk. For example, this would include making appropriate levels of disclosure under recognized frameworks such as the Task Force on Climate-related Financial Disclosures, undertaking scenario modelling to assess the viability of the business under different carbon price and temperature settings, and formulating strategies to ensure that the business of a company can sustainably operate in a net zero globalized economy. Along with broader efforts, both globally as well as locally within India, to address concerns pertaining to climate change, the competence duties of directors will also operate in a dynamic manner to keep pace with developments.

**Climate Risk Disclosure**

Companies and their directors also carry duties under the Companies Act, 2013 and the SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015 (the LODR Regulations) to make disclosures of matters pertaining to climate risk. The nature and extent of disclosure required usually depend on the materiality of the risk. Disclosure norms that deal with the financial risks of climate change as well as those that relate to ESG have proliferated both internationally and within India. For instance, the board's annual report should carry details of material changes affecting the financial position of the company that may have occurred during the period to which the financial statements relate. This includes the financial impact of climate change, such as any physical risk, transition risk, or litigation risk that may have materialized during the period. More specifically, the annual report must include steps taken by the company towards conservation of energy, which would also incentivize boards to treat it as an opportunity in the transition towards clean energy. SEBI's listing rules require immediate disclosure of events that are, in the opinion of the board, material in nature. These would include climate events that result in disruptions to the company's operations or its supply chain.

More importantly, the concept of business responsibility and sustainability reporting has become a mainstay of Indian securities regulation.[4] This requires companies to report on how their businesses are being conducted “in a manner that is sustainable and safe” and what efforts they are expending “to protect and restore the environment.” These developments have brought about a considerable increase in the awareness regarding sustainability issues as well as the incidence of sustainability reporting by companies in recent years. The existing disclosure practices indicate that, within the gamut of sustainability reporting, there is a greater focus on environmental issues.

Disclosure obligations on corporate boards are key because they compel directors to turn their attention towards climate change as a material financial risk and as a matter of business responsibility and sustainability. The expectation is that this will naturally require boards to acknowledge and address climate risk, while acting overall in the long-term interest of the company. In that sense, disclosure and transparency requirements may have a significant impact in altering corporate behavior in the context of climate change.

**Enforcement of Governance Norms**

When it comes to enforcement mechanisms, shareholders have a number of avenues through which they can bring claims for breach of directors’ duties to deal with climate risk, including the duty to make adequate disclosures. These avenues include both private and public enforcement measures. While the private enforcement tools seem wide in nature and, in certain cases such as class actions, wider than other Commonwealth jurisdictions, severe constraints plague the effective use of such remedies. Exorbitant costs, colossal delays, and the lack of litigation funding mechanisms are some factors that impede effective private enforcement of directors’ duties. Such enforcement measures are likely to be taken only when there are significant shareholder disputes and where the petitioning shareholder has a sufficiently high economic stake as to be able and willing to incur the hefty costs of litigation.

Even though the substantive law goes as far as requiring directors of companies to act in the interest of stakeholders, this provision is not justiciable by the stakeholders. This is because duties are owed to the company, which alone can bring an action. A derivative action or other forms of claims enumerated under the Companies Act can be brought only by shareholders, and not other stakeholders. It remains unclear whether shareholders can do so for anyone’s benefit other than their own.

In the overall analysis, the corporate governance regime in India in relation to climate change can be best described as combining a robust set of duties under substantive law with considerable limitations as regards enforcement. This could lead to a gap between the law on the books and law in action. Hence, there is a need for a balanced assessment of directors’ duties and the disclosure regime on the one hand and their enforcement on the other.

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**Notes**

[1] Richard Heede, “Tracing anthropogenic carbon dioxide and methane emissions to

fossil fuel and cement producers, 1854-2010," (2014) *Climate Change* 229, 230.

[2] See e.g., *M.K. Ranjitsinh v. Union of India*, 2021 SCC OnLine SC 326.

[3] Shyam Divan, Sugandha Yadav & Ria Singh Sawhney, "Legal Opinion: Directors' obligations to consider climate change-related risk in India" (Sept. 7, 2021).

[4] Regulation 34(2)(f), LODR Regulations.

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