

SESSION: SUSTAINABILITY AND REPORTING

CAN CEO COMPENSATION DRIVE SUSTAINABILITY? EXPLORING INCENTIVES, ESG SCORES AND FIRM OUTCOMES

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How to cite: Tutino, M., & Capolini, F. (2025). Can CEO compensation drive sustainability? Exploring incentives, ESG scores and firm outcomes. In A. M. Gallo, U. Cornite, & A. Kostyuk (Eds.), *Corporate governance: International outlook* (pp. 33–37). Virtus Interpress. <https://doi.org/10.22495/cgiop6>

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Received: 28.04.2025
Accepted: 08.05.2025
Keywords: ESG, CEO Compensation, Sustainability, Corporate Governance
JEL Classification: M12, M14, M52
DOI: 10.22495/cgiop6

Abstract

One of the earliest attempts to integrate sustainability into corporate practices can be attributed to the concept of corporate social responsibility (CSR). Initially grounded in a primarily philanthropic perspective (Bowen, 2013), CSR has evolved to become a strategic component for businesses aiming to achieve sustainable development (Carroll, 1991; Elkington, 2004). Over the last decades, CSR has gained increasing relevance in both academic and public debates on corporate governance, with scholars recognizing the interplay between governance structures and socially responsible strategies (Tutino et al., 2019). Well-structured corporate governance systems are expected to align managerial incentives with those of stakeholders, in accordance with the triple bottom line approach (Elkington, 2006). Consequently, firms with effective corporate governance should prioritize the maximization of sustainable value over the long term (Jo & Harjoto, 2012).

Subsequently, the introduction of the environmental, social, and governance (ESG) concept broadened the key issues associated with sustainability. ESG factors represent a concrete operationalization of sustainability, providing measurable metrics to assess the environmental

and social impact of organizations, as well as the quality of their governance practices (United Nations, 2004).

Among the various corporate governance mechanisms, chief executive officer (CEO) compensation serves as a key governance tool aimed at aligning the interests of shareholders, non-shareholder stakeholders and chief executive officers (Walsh & Seward, 1990; Denis, 2001). Executive compensation has attracted significant attention from both academia and the corporate world, driven by the growing emphasis placed on effective governance mechanisms within firms (Pathak & Chopra, 2021).

While traditional studies on executive compensation have largely drawn on agency theory emphasizing the need to integrate divergent interests between principals and agents (Jensen & Meckling, 1976; Eisenhardt, 1989), more recent contributions suggest that this perspective may be too narrow to capture the complexity of sustainability-related objectives (Hill & Jones, 1992; Kock et al., 2012). Stakeholder theory offers a broader lens, proposing that compensation systems should also reflect the expectations of a wider set of actors, including employees, communities and environmental constituencies (Freeman, 1984; Donaldson & Preston, 1995). In this view, sustainable CEO compensation emerges as a mechanism not only for incentivizing financial performance but also for promoting ethical leadership and responsible corporate conduct (Eccles et al., 2014).

Recent empirical research suggests that compensation schemes with long-term components, such as equity-based incentives or deferred bonuses, are more conducive to CSR-oriented strategies and may help mitigate earnings manipulation practices (Bhaskar et al., 2023; Dakhli & Houcine, 2025). Notably, CSR-oriented business strategies are more likely to be adopted by CEOs whose compensation is tied to long-term incentives, rather than short-term rewards (Peng, 2020).

One way to enhance a company's sustainability profile is by integrating ESG criteria into the design of CEO compensation schemes. Some studies have highlighted that the presence of ESG-related expertise within the executive or board structure positively influences the adoption of such criteria in compensation frameworks (Mendiratta et al., 2022; Huang et al., 2025). Other scholars emphasize that the relationship between sustainability performance and CEO pay is strengthened by effective corporate governance mechanisms, particularly independent compensation committees, while it is weakened in cases of CEO duality, where excessive power concentration undermines alignment with sustainability goals (Shabbir et al., 2024).

In light of the current state of the literature, there remains a critical gap in understanding how CEO compensation policies are structured in response to firms' financial performance and sustainability achievements, particularly ESG performance. While previous research has examined the influence of sustainability on executive pay, much of this work has concentrated either on the presence of ESG-linked metrics

in compensation packages or on the symbolic adoption of sustainability-related discourse in corporate reporting (Flammer et al., 2019; Mishra, 2020). However, empirical evidence assessing whether and how such compensation mechanisms reflect firms' ESG outcomes, beyond financial performance, remains limited and inconclusive. Furthermore, a clear distinction between short-term and long-term incentive components in relation to sustainability commitments is often overlooked (Berrone & Gomez-Mejia, 2009; Gillan et al., 2021).

Building on this literature, the present study aims to contribute to the ongoing academic and policy debate by examining the extent to which CEO compensation is structured in relation to both traditional financial performance and ESG indicators. Specifically, the research has three main objectives: 1) to identify which types of incentive schemes are most frequently associated with higher ESG performance; 2) to explore how the interaction between ESG scores and financial results affects executive compensation; and 3) to evaluate whether firm-specific characteristics — such as industry sector, ownership structure, and board composition — moderate this relationship.

To achieve these goals, the study will adopt a quantitative empirical approach, relying on a panel dataset of publicly listed firms. The analysis will explore the relationships between CEO compensation, ESG performance, and financial results over time, controlling for relevant firm-level and governance characteristics. The methodological design will be tailored to ensure internal validity, accounting for potential endogeneity issues and unobserved heterogeneity. This framework aims to offer a comprehensive and evidence-based understanding of how compensation policies reflect and potentially drive firms' sustainability orientation.

Ultimately, this research aims to advance theoretical understanding by bridging agency and stakeholder perspectives within the domain of sustainability governance. It further seeks to provide empirical insights into the structural conditions under which ESG-linked compensation schemes are most effective. In doing so, it offers practical guidance for policymakers, boards of directors, and institutional investors striving to design incentive systems that promote executive conduct aligned with long-term financial performance and broader sustainability commitments.

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