ES Pay and Firms' Environmental and Social Conduct (joint with Thomas Schmid & Menghan Wang)

Abstract

This paper combines a novel hand-collected dataset with a machine learning (ML) classification approach to measure environmental and social targets in executive compensation ("ES Pay"). We find that one-third of public U.S. firms adopt ES Pay, which is under-estimated by commercially available data, increased substantially over time, is higher in polluting industries, and varies with firm characteristics such as size and CEO tenure. Although ES Pay does not affect compensation levels, it reduces pay-for-financial performance sensitivity and, at least temporarily, operating performance. Using four ES indices yields evidence that ES Pay increases index scores, especially if the targets are quantitative and linked to compensation via modifiers or formulas instead of discretion. However, there is no evidence for a reduction in emissions, possibly because executives focus on ES-related issues that are easier to improve.