

# Role and composition of the nomination committee on banks' ESG controversies

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## **Abstract**

This study investigates the relationship between the nomination committee and bank's ESG disputes in a sample of 30 systemically important banks (G-SIBs) from 2015 to 2020. Using data from several sources (BankFocus, Refinitiv and Annual reports of banks), we find that nomination committee members who also join the sustainability committee contribute to reducing the ESG disputes of banks. This is in line with the main literature on the importance of miscellaneous skills of the board committee in the management of risks and board heterogeneity. Moreover, we find a negative relationship between the independence of nomination committee members and ESG controversies score, while a greater women representation on this committee does not produce any influence on banks' ESG disputes. We contribute to strengthening the role of the nomination committee for the board corporate governance policies and reviewing policies pertaining to public concerns, interactions with external organizations influencing the bank's reputation, and ESG issues.

**Keywords:** Board of Directors, Nomination Committee, Global Systemically Important Banks (G-SIBs), ESG controversies

**JEL Classification:** G21, G34

**EFM classification codes:** 150 - Corporate Governance

## 1. Introduction

In recent years, - especially in the aftermath of subprime and sovereign crises – the focus of Supervisory Authorities on directors' nomination processes has greatly increased given that having high-quality managers is an essential condition for a more effective and efficient corporate governance system. Banks are required to have a clear and rigorous process for identifying, assessing, and selecting board candidates and to promote an appropriate succession planning of all board members (BCBS, 2015). This selection process should aim to verify whether board candidates possess adequate knowledge, skills and experience, a good reputation and not present any conflicts of interests (BCBS, 2015) to fulfil their responsibilities. Moreover, board candidates should be able to promote a smooth interaction between all board members. To this end, banks need to establish a nomination committee (NC) to which such essential tasks are entrusted. Moreover, the NC should ensure that the board of directors is equally balanced in terms of members' gender and is not dominated by any one individual or small group of individuals.

Thus, the establishment of the NC can be considered a key attribute to fulfil objective assessment, to improve board effectiveness, control executive's behaviour and monitor operating in the duty of care. According to the agency theory perspective, the NC plays a key role in balancing interests between managers and shareholders. This body nominating both new directors and proper candidates for the board (Soana and Crisci, 2017) can reduce the influence of firm CEOs on the director selection process (Vafeas, 1999; Shivdasani and Yermack, 1999; Eminet and Guedri, 2010), ensure the independence and the quality of the nominees, improving both director's qualification and independence. Moreover, the selection process can settle the asymmetry between boards and management trying to align hired board members to collaborate to accomplish shareholder's interests (Ruigrok *et al.*, 2006).

In the light of these considerations, this research aims at extending the debate on corporate governance for financial institutions focusing on the role and composition of the NC considering several characteristics of its members such as CSR skills, gender, age, independence, and nationality. Also, the paper intends to verify whether such qualifications of NC members positively impact banks' ESG performance reducing the involvement of these companies in non-financial disputes.

For these purposes, we focus on Global Systemically Important Institutions (G-SIIs) selected by EBA for the period 2015-2020. We use different sources of data: financial data are retrieved from the BankFocus database, the information on the NC members is manually collected using the banks' Annual reports while the governance data and the ESG controversies score are retrieved from the Refinitiv database. The ESG controversies score measures a company's exposure to environmental, social and governance controversies and negative events reflected in global media. The empirical analysis is conducted from 2015 to 2020 because the main important regulatory initiatives on banks' board composition and directors' qualification were implemented just in these six years (EBA, 2020).

Despite the essential role of the NC to the board, literature on the aforementioned topic is scant especially on its influence on ESG, therefore, this research aims at filling the gap in the previous literature and at contributing to agency theory. Moreover, despite there is extensive body of literature on the relationship between different types of bank committees and financial performance, to our knowledge, little is known about the role of NC and bank's ESG controversies score.

The main finding of this study reveals that ESG controversies score can be reduced when there are specific skills of NC members, in particular when the share of members belongs also to the

Sustainably Committee. In addition, we find an inverse relationship between the independence of NC members and ESG controversies score. Finally, we do not find significant evidence on the crucial role of the female gender composition of NC on ESG disputes.

This paper is organized as follows. Section 2 reviews the literature on the NC and develop the research hypotheses. Section 3 presents the sample and data collection. Section 4 provide the main results of the analysis. Finally, Section 5 illustrates the main contribution and conclusions.

## **2. Literature review and hypotheses development**

Banking regulation (BCBS, 2015; Capital Requirement Directive V; EBA, 2021), including many corporate governance codes and stock exchanges requirements (see, for example, the NYSE Listed Company Manual) unanimously recommend that the majority of the nomination committee members should be non-executive or independent directors. This is of great importance because, from the agency theory viewpoint, the independence of nomination committees represents a critical tool to reduce the influence of firm CEOs on the director selection process (Vafeas, 1999; Clune *et al.*, 2014). As a result, the quality of new directors' appointments will be at its highest when all nomination committee members are independent, and among them is not the CEO. In this vein, some studies reveal that both the designation and the composition of the nomination committee (in terms of independent directors, female members, woman chair of the committee, etc.) are associated with higher quality characteristics of the board of directors. For example, Hutchinson *et al.* (2015), focusing on the top 500 listed firms in Australia, find that female presence on the nomination committee is positively associated with increasing board gender diversity. However, the influence of the independence of nomination committees has not yet been in-depth explored in the literature, especially in the banking sector. A large number of studies analyzed the independence of banks' board of directors considering it to be the main board characteristic that can positively influence both the economic and non-financial performance of these companies. Indeed, there is a broad consensus by scholars on the key role of independent directors to increase effective board monitoring, to reduce agency conflicts and therefore to ensure better management quality (Birindelli *et al.*, 2018; Beji *et al.*, 2020). This occurs both because the independent directors do not play executive functions and their compensation is not related to the short-term financial performance of the company. These circumstances allow such directors to make objective and unbiased judgments about the manager performance in all stakeholders' interests. Indeed, both agency and stakeholder theories attribute to the board independence requirement an essential role in enhancing both a firm' economic and sustainability performance (Ortas *et al.*, 2017).

However, at the empirical level, there are mixed results, especially with regard to the firms' non-financial performance. If most studies confirm a positive relationship between independent directors and sustainability outcomes, other studies find no significant relationship between them (Walls and Berrone, 2017) or even a negative one (Haniffa and Cooke, 2005; Mallin *et al.*, 2013). Similarly, also studies on banks do not fully converge. Sharif and Rashid (2014), Kiliç *et al.* (2015) and Jizi *et al.* (2018) document that board independence is positively related to banks' CSR disclosure, but no significant linkage is found by Hossain and Reaz (2007). Conversely, Birindelli *et al.* (2018) and Tapver (2019) find a negative relationship between independent directors and ESG performance and CSR disclosure of banks, respectively. Finally, although these studies focus on the independence of the board, their outcomes can also be applied to the nomination committees as the

two bodies share the same directors. Hence, based on the above discussion, we state the following hypothesis:

**H<sub>p</sub> 1: The nomination committee independence can exert a positive/negative impact on banks' ESG controversies**

Section 124 of the recent joint ESMA and EBA Guidelines on suitability of members of the management body states that “*members of the nomination committee should have adequate collective knowledge, expertise and experience relating to the business of the institution to be able to assess the appropriate composition of the management body*” (ESMA and EBA, 2021:52). Moreover, Section 63 of the same guidelines affirms that “*when assessing the knowledge, skills and experience of a member of the management body, consideration should be given to theoretical and practical experience relating to – among several aspects – all main types of risk of an institution including environmental, governance and social risks*”. Together, these two recommendations include a clear reference to the need for bank nomination committees' members to have, among several competencies, specific expertise on sustainability and ESG risks in the financial sector to carry out their functions effectively. Equally, the recent revised ECB' Guide to fit and proper assessments stress the importance the management body possess adequate collective knowledge of climate-related and environmental risk, given the increasing relevance of these issues as an area of supervisory attention (ECB, 2020 and 2021).

Having adequate competencies and skills by directors is considered important also by scholars. Many studies in corporate governance show that a higher level of education by board' members is a key determinant of the involvement in CSR (Vives, 2006; Gadenne *et al.*, 2009) or environmental activities (Shahgholian, 2017). In the same vein, other studies find that the presence of a CSR committee – thus of directors with expertise on sustainability issues - is positively associated with the extent and/or the quality of sustainability disclosure (Amran *et al.*, 2014; Cucari *et al.*, 2018, Adnan *et al.* 2010; Liao *et al.*, 2015; Helfaya and Moussa, 2017) or the CSR performance (Spitzeck, 2009). These considerations together allow us to formulate the second research hypothesis, that is:

**H<sub>p</sub> 2: The percentage of sustainability-educated directors on the nomination committee is negatively associated with banks' ESG controversies**

A board diversity issue investigated in depth by scholars concerns the women representation on the board of directors. In the banking literature, the board gender diversity (BGD) has been analysed from various points of view. Although most studies have focused on the relationship between women directors and banks' economic performance, another strand of studies has aimed to investigate the relationship between BGD and banks' sustainability performance. In this context, García-Sánchez *et al.* (2018), focusing on a sample of 159 banks in nine countries during the period 2004–2010, find that the greater the BGD, the better the CSR performance of banks. Similarly, focusing on the 30 largest banks in Europe in terms of market capitalisation, Gallego-Sosa *et al.* (2021) show that for “Climate Action” and “Sustainable Cities and Communities” SDGs, bank commitment is stronger when there is greater female board representation. Finally, Shakil *et al.* (2020), drawing on the resource dependence and legitimacy theories, identify a significant positive relationship between board gender diversity and bank ESG performance. Finally, Birindelli *et al.* (2018), focusing on a sample of 108 listed banks in Europe and the US for the period 2011–2016,

show that the relationship between board gender diversity and a bank's ESG performance is an inverted U-shape. This means that after reaching a critical mass of women on the board, the increasing presence of female directors does not have a positive impact on a bank's sustainability performance. In sum, this study finds no support for the critical mass theory, confirming that only gender-balanced boards positively impact a bank's ESG performance. Other studies focus on bank CSR disclosure. On the whole, also this research confirms the existence of a positive linkage, that is a greater presence of women on board of directors positively impacts the CSR reporting of banks (Barako and Brown, 2008; Kiliç *et al.*, 2015; Tapver *et al.*, 2020). Based on this evidence, we formulate the third research hypothesis:

**Hp. 3: More women directors as a member or chair of the nomination committee leads to fewer banks' ESG controversies**

### 3. Research design and methodology

#### 3.1 Sample and Data collection

To examine the relation between NC and bank's environmental, social and governance (ESG\_C) controversies we focus on all Global Systemically Important Banks (G-SIBs) selected by the EBA over the period 2015-2020. We choose these years because the main important regulatory initiatives on banks directors' qualification (EBA, 2020) and sustainability goals (SDGs of United Nations, 2016) were implemented in this period.

Information on NC composition (% of non-executive board members; % of women directors; woman chair of NC) and NC members (nationality, age, and having CSR skills) are collected from the banks' Annual reports. All others governance data and the ESG controversies score are retrieved from the Refinitiv database. The ESG controversies score measures a company's exposure to environmental, social and governance controversies and negative events reflected in global media.

In line with the recent studies (Alberici and Querci, 2016; Hussain *et al.*, 2018; Alazzani *et al.*, 2017), we add several bank-specific financial variables retrieved from the BankFocus database and the Economic Sentiment Indicator collected from the Eurostat database.

#### 3.2 Model

To investigate the relationship between the NC characteristics and the ESG controversies score, we estimate the following panel data models with fixed effects, clustering heteroscedasticity standard errors at the bank level to account for the serial correlation of the dependent variables for each bank:

$$\begin{aligned}
 ESG\_C_{it} = & \alpha_i + \beta 1 NCINDEP_{it} + \beta 2 NCSTUSMEMBER_{it} + \beta 3 NCWOMEN_{it} + \beta 4 NCWOMANCHAR_{it} + \\
 & + \beta 5 NCMEANAGEMEMEBER_{it} + \beta 6 NCMEMBERNATIONALITY_{it} + \beta 7 BOARDSIZE_{it} + \beta 8 BANKSIZE_{it} + \beta 9 CINC_{it} + \beta 9 TIER_{it} \\
 & + \beta 9 ECONOMICSENT_{it} + \delta_i + \epsilon_{it}
 \end{aligned}
 \tag{1}$$

Employing panel regression, we are able to analyse data over a longer period. Indeed, this methodology has been implemented in many recent banking studies (Birindelli *et al.*, 2018; Buallay, 2019; Shakil *et al.*, 2020; Galletta *et al.*, 2021).

#### 3.3 Dependent Variable

To test our hypothesis, in this section we present the dependent variable. We use the ESG controversies score (ESG\_C) from the Refinitiv Eikon database (formerly called Thomson and Reuters). The ESG\_C is created on twenty-three controversial topics on recent controversies. These topics are labelled into the following seven categories: “Community”, “Human rights”, “Management”, “Product responsibility”, “Resource use”, “Shareholders” and “Workforce”. ESG controversies is a percentile score that takes into account litigation or disputes related to environmental, social and governance issues. The score ranges between zero and one hundred: companies that present the lowest number of controversies will get closer to 100%, while those that presents zero controversies will get a score of 100%. To maintain the database updated, Refinitiv revises ESG news and controversies continuously, i.e., when disputes or scandals occur. Concerning the controversies count, Refinitiv in the computation process includes all recent controversies in the latest closed fiscal year, doing so no controversy is double-counted. To integrate and account for industry materiality and company size biases, ESG controversies are benchmarked on industry groups. Moreover, the score addresses the market cap bias that is an issue involving companies with large capitalization. This is linked to their exposure to media and their active scrutiny from the stakeholders.

The percentile rank formula is applied as a scoring methodology to determine the ESG controversies score. It is based on the following three factors: 1) How many companies are worse than the current one? 2) How many companies have the same value? 3) How many companies have value at all? (Refinitiv, 2021).

$$\text{score} = \frac{\text{no. of companies with a worse value} + \frac{\text{no. of companies with the same value included in the current one}}{2}}{\text{no. of companies with a value}}$$

### 3.4 Independent Variables

We include three independent variables in our econometric models. First, the share of independent directors on the nomination committee (Vafeas, 1999; Ruigrok *et al.*, 2006; Kesner, 1988; Bilimoria and Piderit, 1994). It is expressed as a percentage of non-executive board members on the nomination committee on the total number of board members. The second independent variable expresses the joint membership of NC members in the Sustainability/CSR committee. Indeed, companies with a CSR Sustainability committee are seen as more ESG compliant (Cucari *et al.*, 2018; Helfaya and Moussa, 2017; Hussain *et al.*, 2018). In this study, we use the joint membership of a NC member to the CSR sustainability committee as a proxy of possessing ESG competencies from NC members. It is a dummy variable equals 1 if a member of NC is also a member of the Sustainability or CSR committee, and 0 otherwise.

Following the corporate governance stream of research, as the third independent variable, we add a gender component to our model, namely, we control for the presence of female NC directors by including their percentage over the total number of directors of the NC (Cucari *et al.*, 2018; Glass *et al.*, 2016). Moreover, we also add a variable that accounts for the presence of a woman chair in the NC, by including a dummy variable that takes a value of 1 if there is a woman chair and zero otherwise (Glass *et al.*, 2016; Huang, 2013). It is widely believed that the inclusion of women on boards improves banking to manage and mitigate risks as well as to take a more conservation position on economic decisions (Palvia *et al.*, 2015). Therefore, on the positive relationship between sustainability and low riskiness, the inclusion of CEO women can have a beneficial effect for banks to reach ESG targets (Karl, 2015).

### 3.3.1 Control Variables

To avoid model misspecification, we control for additional variables that could influence the ESG controversies score. Indeed, we control for NC age and nationality. In particular, we include the average age of NC members and a dummy variable accounting for NC members nationality which is equal to 1 if at least one NC member has a different nationality from its bank, and 0 otherwise. This allows us to verify the degree of heterogeneity in terms of nationality. Board size is also included as a control variable to account for board dimension. Literature on this top is still mixed since on the one hand large boards might be more disorganized and thus inefficient, on the other hand, a larger board can take advantage of several information and a broader pool of multiple skills and knowledge (Post *et al.*, 2011).

Moreover, we add several bank-specific financial variables retrieved from the BankFocus database. Indeed, we include the bank's total asset as a proxy of size (BANKSIZE). Because large companies are more exposed to public scrutiny and have more resources available for sustainability efforts than smaller companies, they should be more concerned about their ESG standards (Alberici and Querci, 2016; Cornett *et al.*, 2016; Kiliç *et al.*, 2015). Since banks with a higher level of profitability are more like to invest in ESG projects and initiatives (Hussain *et al.*, 2018), in our model we account for bank viability by adding return on assets (ROA). We control also bank core equity assets, namely Tier 1 (TIER) and the cost-to-income ratio for efficiency (CINC). Finally, we include a variable to control for country-firm specific factors namely, the Economic Sentiment Indicator (ECONOMICSENT) created by the European Commission based on economic sentiment surveys. The surveys are carried out in all member states of the European Union and the goal of the indicator is to get insight into economic agents' attitudes on both the demand and supply sides of the economy. Consumers and businesses may increase consumption and production if they are optimistic about the current and future economic conditions (Gelper and Croux, 2010).

## 4. Descriptive Analysis

Table 1 presents the means standard deviations minimum and maximum of the selected variables. The mean of the ESG Controversies score is 58%. Since companies with no controversies will get a score of 100%, a mean of 58% indicates that there is a medium exposure to environmental, social and governance controversies from the selected banks. NC independence has a mean of nearly 76% indicating that there is a high presence of NC members who are non-executive board members. The average of women on the NC is 10.23 %, which shows a low presence of female gender into board committees of the selected banks. The same applies to female CEO, which shows very low values on average, i.e., 0.24%. The average age of NC members is 60.5 % showing that the composition of NC is affected by a higher presence of elder directors rather than younger ones. In addition, more than half of the NC directors are of different nationalities than the bank's country of headquarters, which could be a positive factor in terms of the degree of board heterogeneity in the influence of the NC decision-making process. About banks, profitability measure return on assets (ROA) presents a minimum negative value which underlines the impact of the economic distress faced by banks in the previous years.

**Table 1 Descriptive Statistics**

|                     | <b>Obs</b> | <b>Mean</b> | <b>Std. Dev.</b> | <b>Min</b> | <b>Max</b> |
|---------------------|------------|-------------|------------------|------------|------------|
| ESGC                | 150        | 58.00396    | 36.9937          | 0.505051   | 100        |
| NCINDEP             | 142        | 76.32382    | 33.46237         | 0          | 100        |
| NCSUSTMEMBER        | 198        | 0.136364    | 0.344044         | 0          | 1          |
| NCWOMEN             | 193        | 10.23123    | 20.19027         | 0          | 78         |
| NCWOMANCHAIR        | 194        | 0.242268    | 0.429564         | 0          | 1          |
| NCMEANAGEMEMBER     | 196        | 60.56756    | 4.043067         | 49.75      | 72.2       |
| NCMEMBERNATIONALITY | 197        | 0.609137    | 0.489187         | 0          | 1          |
| BOARDSIZE           | 156        | 14.4359     | 3.890733         | 7          | 23         |
| BANKSIZE            | 183        | 20.05694    | 1.038169         | 14.73779   | 21.61193   |
| ROA                 | 182        | 0.4069      | 0.298813         | -0.58967   | 1.060841   |
| CINC                | 183        | 62.63796    | 12.58121         | 35.38329   | 98.09275   |
| TIER                | 181        | 16.9611     | 4.13951          | 11         | 33.7       |
| ECONOMICSENT        | 216        | 6.898148    | 15.78079         | -39.4      | 33.1       |

Before carrying out our estimation, we perform the correlation between the variables implemented in the econometric model. Results are displayed in Table 2. Correlation coefficients with stars are significant at the 5% level and they are mostly  $< |0.5|$ , suggesting a small or medium-strength correlation. Therefore, a severe multicollinearity issue does not exist in our data. More specifically, the correlation matrix coefficients demonstrate that the ESG controversies score of banks is significantly and negatively associated with the independence, the average age and the nationality of NC members. Moreover, it shows that banks with larger size by total assets should reduce ESG controversies. Conversely, the ESG controversies score is significant and positively associated with bank profitability. From the correlation matrix values we can affirm that in our regression model, multicollinearity does not occur between the independent variables. This result is also corroborated by the VIF test computed on the pooled OLS version of our models (Table 2, column VIF).

**Table 2 Correlation matrix**

|                     | <b>VIF</b> | <b>1</b>     | <b>2</b>     | <b>3</b>     | <b>4</b>     | <b>5</b>     | <b>6</b>     | <b>7</b>     | <b>8</b>     | <b>9</b>     | <b>10</b>    | <b>11</b>    | <b>12</b> | <b>13</b> |
|---------------------|------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|-----------|-----------|
| ESGC                |            | 1            |              |              |              |              |              |              |              |              |              |              |           |           |
| NCINDEP             | 3.22       | <b>-0.22</b> | 1            |              |              |              |              |              |              |              |              |              |           |           |
| NCSUSTMEMBER        | 1.67       | -0.12        | 0.09         | 1            |              |              |              |              |              |              |              |              |           |           |
| NCWOMENPRESENCE     | 1.34       | -0.02        | <b>0.22</b>  | <b>0.29</b>  | 1            |              |              |              |              |              |              |              |           |           |
| NCWOMANCHAIR        | 1.31       | 0.09         | <b>-0.31</b> | <b>0.22</b>  | <b>0.18</b>  | 1            |              |              |              |              |              |              |           |           |
| NCMEANAGEMEMBER     | 1.64       | <b>-0.20</b> | <b>0.20</b>  | 0.09         | -0.14        | 0.02         | 1            |              |              |              |              |              |           |           |
| NCMEMBERNATIONALITY | 1.89       | <b>-0.33</b> | 0.33         | -0.04        | -0.030       | -0.07        | 0.11         | 1            |              |              |              |              |           |           |
| BOARDSIZE           | 2.19       | -0.15        | <b>0.26</b>  | 0.07         | 0.07         | -0.02        | <b>0.17</b>  | <b>-0.16</b> | 1            |              |              |              |           |           |
| BANKSIZE            | 2.33       | <b>-0.55</b> | <b>0.37</b>  | -0.04        | <b>0.24</b>  | 0.01         | <b>0.29</b>  | <b>0.47</b>  | <b>0.31</b>  | 1            |              |              |           |           |
| ROA                 | 3.27       | <b>0.48</b>  | <b>-0.28</b> | -0.02        | -0.01        | <b>0.14</b>  | -0.09        | <b>-0.21</b> | <b>-0.36</b> | <b>-0.23</b> | 1            |              |           |           |
| CINC                | 5.12       | <b>-0.44</b> | <b>0.58</b>  | -0.00        | 0.08         | <b>-0.21</b> | 0.13         | <b>0.23</b>  | <b>0.57</b>  | <b>0.23</b>  | <b>-0.72</b> | 1            |           |           |
| TIER                | 2.82       | 0.10         | <b>-0.64</b> | <b>-0.17</b> | <b>-0.21</b> | <b>0.07</b>  | <b>-0.28</b> | <b>-0.37</b> | <b>-0.53</b> | <b>-0.34</b> | <b>0.18</b>  | <b>-0.36</b> | 1         |           |
| ECONOMICSENT        | 1.75       | <b>0.37</b>  | <b>-0.23</b> | <b>-0.15</b> | -0.12        | <b>-0.03</b> | <b>-0.27</b> | -0.09        | 0.06         | <b>-0.19</b> | 0.28         | -0.06        | -0.14     | 1         |



## 5. Results

Table 3 presents the results of the dynamic panel data model. The main findings show that the independence score of the NC members does not impact the ESG controversies score; however, when we introduce the lagged variable (column 4) the coefficient presents a negative and statistically significant coefficient at a 1% level. Thus, this confirms our first hypothesis that a higher share of independent directors might negatively influence the score of ESG controversies. In line with the literature review, when the board is dominated by a large proportion of shareholders - who may control the board in choosing their representatives (Shleifer and Vishny, 1997)- the independent directors might suffer from the scarcity of transparency or the lax statutory criteria thus their influence is severely constrained (Aluchna *et al.*, 2020).

Moreover, we can confirm H2 about the joint membership of the nomination and sustainability committee (NCSUSTMEMBER) as a proxy of NC members' specific knowledge which allows them to implement more appropriate decisions regarding ESG. Indeed, the positive and statistically significant coefficient shows that whenever a NC member belongs also to the sustainability committee this will increase the score of ESG controversies by 1% confidence level. Considering the lagged dependent variable, the magnitude of the coefficient is even higher. This result is in line with the stream of literature that support the theory that multiple skills by board committee members might positively influence banks' performance (Jensen, 1993; Anderson *et al.*, 2011; Minton *et al.*, 2014).

However, the gender composition of the NC does not impact the ESG controversies score, thus we do not confirm H3 about the positive impact of women members or chair of NC in dealing with ESG issues.

For what concern the average age of NC members, results show that is a detrimental factor for ESG controversies score because an increase in the average age of members might be expression of less risky decisions from the board which results in lower exposure to sustainability investments. This is because according to the main literature review on the topic older board members are more risk-averse than younger proactive members that in turn are more inclined towards the short-term results of the banks at any level of risks.

Furthermore, concerning NC members' nationality, a higher grade of heterogeneity of the NC positively impacts on ESG controversies score. Indeed, a board committee that presents members with a nationality different from the country of headquarters of the banks can benefit from different backgrounds, culture, skills, experience and education. These characteristics unique for each member can merge into the final decision of the committee by highlighting different points of view and simplifying the decision-making progress (Harjoto *et al.*, 2018).

For what concern the other control variables, as inefficiency increases, ESG controversies increase, and higher capitalisation leads to higher ESG controversies scores.

**Table 3. Dynamic Panel Data Results**

|           | ESGC<br>(1)         | ESGC<br>(2)         | ESGC<br>(3)         | ESGC<br>(4)          | ESGC<br>(5)         | ESGC<br>(6)          |
|-----------|---------------------|---------------------|---------------------|----------------------|---------------------|----------------------|
| NCINDEP   | -0.1044<br>(0.1240) | -0.1363<br>(0.1650) | -0.0785<br>(0.1736) |                      |                     |                      |
| L.NCINDEP |                     |                     |                     | -0.5678<br>(0.2651)* | -0.5400<br>(0.3022) | -0.5795<br>(0.2909)* |

|                       |                        |                        |                        |                        |                        |                        |
|-----------------------|------------------------|------------------------|------------------------|------------------------|------------------------|------------------------|
| NCSUSTMEMBER          | 18.6666<br>(3.1945)*** | 15.2017<br>(4.6673)*** | 15.8913<br>(4.2182)*** |                        |                        |                        |
| L. NCSUSTMEMBER       |                        |                        |                        | 46.8306<br>(6.2663)*** | 48.3489<br>(6.1329)*** | 47.7302<br>(5.9169)*** |
| NCWOMEN               | 0.4368<br>(0.3180)     |                        | 0.3620<br>(0.2536)     |                        |                        |                        |
| L. NCWOMEN            |                        |                        |                        | -0.2682<br>(0.3663)    |                        | -0.2625<br>(0.3728)    |
| NCWOMANCHAIR          |                        | -20.3466<br>(13.2866)  | -19.1828<br>(12.7767)  |                        |                        |                        |
| L. NCWOMANCHAIR       |                        |                        |                        |                        | 4.9212<br>(12.7864)    | 4.6253<br>(12.9663)    |
| NCMEANAGEMEMBER       | -2.9654<br>(1.8709)    | -4.0751<br>(1.1693)*** | -3.4402<br>(1.3430)**  |                        |                        |                        |
| L. NCMEANAGEMEMBER    |                        |                        |                        | -3.8381<br>(1.8294)*   | -3.3607<br>(1.3622)**  | -3.8412<br>(1.8499)*   |
| NCMEMBERNATIONALITY   | 10.8576<br>(10.2933)   | 6.3696<br>(11.1130)    | 9.8331<br>(10.1690)    |                        |                        |                        |
| L.NCMEMBERNATIONALITY |                        |                        |                        | 25.1659<br>(10.1450)** | 28.5496<br>(10.9301)** | 25.9892<br>(10.1072)** |
| BOARDSIZE             | 1.0695<br>(1.5724)     | 1.1643<br>(1.4081)     | 1.1510<br>(1.4536)     |                        |                        |                        |
| L.BOARDSIZE           |                        |                        |                        | -1.1668<br>(2.2487)    | -1.2816<br>(2.2188)    | -1.2380<br>(2.2386)    |
| BANKSIZE              | 6.3865<br>(47.1900)    | 9.4700<br>(45.8287)    | 11.6498<br>(47.4963)   |                        |                        |                        |
| L.BANKSIZE            |                        |                        |                        | -11.8587<br>(60.6546)  | -14.0235<br>(65.3865)  | -14.6053<br>(63.6039)  |
| ROA                   | 11.7607<br>(16.2571)   | 13.6940<br>(15.5958)   | 13.8031<br>(16.1408)   |                        |                        |                        |
| L.ROA                 |                        |                        |                        | 34.3877<br>(29.5827)   | 33.5718<br>(29.0647)   | 34.6806<br>(29.5668)   |
| CINC                  | 0.0468<br>(0.8209)     | 0.1641<br>(0.7880)     | 0.0830<br>(0.8245)     |                        |                        |                        |
| L.CINC                |                        |                        |                        | 1.9429<br>(0.7495)**   | 1.8711<br>(0.7337)**   | 1.9192<br>(0.7886)**   |
| TIER                  | -0.3124<br>(0.6637)    | -0.7665<br>(0.5679)    | -0.8432<br>(0.6289)    |                        |                        |                        |
| L.TIER                |                        |                        |                        | 3.7941<br>(1.4204)**   | 3.8759<br>(1.4035)**   | 3.8787<br>(1.4087)**   |
| ECONOMICSENT          | 0.0515<br>(0.4382)     | 0.0342<br>(0.4113)     | 0.0787<br>(0.4362)     |                        |                        |                        |
| L.ECONOMICSENT        |                        |                        |                        | -0.6460<br>(0.4085)    | -0.6260<br>(0.4070)    | -0.6374<br>(0.4178)    |
| Observations          | 135                    | 135                    | 135                    | 114                    | 114                    | 114                    |
| r2                    | 0.2826                 | 0.2996                 | 0.3065                 | 0.3783                 | 0.3762                 | 0.3794                 |
| r2_a                  | 0.1854                 | 0.2047                 | 0.2057                 | 0.2832                 | 0.2808                 | 0.2770                 |
| Time Dummies          | Yes                    | Yes                    | Yes                    | Yes                    | Yes                    | Yes                    |
| Fixed Effects         | Yes                    | Yes                    | Yes                    | Yes                    | Yes                    | Yes                    |

## 6. Conclusions, limitations, and suggestions for future research

In recent years, the topic of board diversity has attracted more interest from scholars, regulators, and practitioners. In this vein, a special focus is placed on the relationship between this issue and financial outcomes and corporate social responsibility of firms (Harjoto *et al.*, 2015; Ferrero-Ferrero *et al.*, 2015, García-Meca *et al.*, 2015).

This study verifies whether exists a relationship between NC composition and bank's ESG controversies score in a sample of global system important banks (G-SIBs) over the period from 2015 to 2020. The objective of the analysis is to shed a light on the importance of the NC to reduce

the likelihood of the bank incurring in Environmental, Social and Governance (ESG) disputes. We do not consider the establishment of the NC, but its effective functioning and the qualities of its members as a key attribute to fulfil objective assessment, to improve board effectiveness, control executive's behaviour and monitor operating in the duty of care.

Among the main results, we find that the ESG controversies score can be reduced when there are specific skills of NC members, in particular when the share of members belongs also to the Sustainability Committee. In addition, the main results show that there is an inverse relationship between the independence of NC members and ESG controversies score. However, we do not find significant evidence on the crucial role of the female gender composition of NC on ESG controversies.

Despite there is an extensive body of literature on the relationship between different types of bank committees and financial performance, to our knowledge, little is known about the role of NC and bank's ESG controversies score. Despite the essential role of the NC to the board, literature on this topic is limited especially on its influence on ESG controversies. Therefore, this research aims at filling the gap in the previous literature and at contributing to agency theory.

Our findings are particularly useful during periods such as the current one, where there is growing attention to environmental issues with banks. In this context, important synergies between bank managers and environmental policymakers could be created (Kassinis *et al.*, 2016).

Despite significant contributions in theoretical and practical fields, the current study has certain boundaries and limitations. First, the number of observations is not very high due to the presence of several missing values. Therefore, in future research, we intend to extend the sample by including the Other Systematically Important Institutions (O-SIIs).

Second, in the current study endogeneity is only controlled by lagging explanatory variables. Therefore, we intend to increase the number of observations and we can also perform dynamic models more effectively (e.g., GMM).

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