



**FIDUCIARY DUTIES, ESG, AND  
CLIMATE GOVERNANCE IN INDIAN  
AIFS: A CORPORATE LAW  
PERSPECTIVE ON PRIVATE EQUITY  
REFORM**

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**Abstract**

This paper examines the confluence between rather distinct fields of study which includes Environmental, Social and Governance (ESG) principles, climate governance and contextualises in terms of understanding the regulatory framework governing Indian Alternative Investment Funds (AIFs). It explores the possibility of purposive interpretation of fiduciary obligations under Indian corporate and securities law particularly the SEBI (AIF) Regulations, 2012 and Section 166 of the Companies Act, 2013 to incorporate ESG and sustainability-aligned considerations into investment decision-making. It remains undisputed that global scholarship identifies the importance of ESG integration in private equity, however existing studies remain limited in their analysis and rather does not contextualise it in terms of the specific legal and institutional context governing Indian AIFs. Using a doctrinal methodology, the paper analyses the regulatory frameworks including the Stewardship Code, BRSR architecture, and emerging climate-risk disclosure standards to understand how fiduciary duties can evolve to address sustainability and climate-related risks. The paper puts forth a central argument that climate risks and sustainability dimensions are quintessential material considerations affecting

investor interest and not just mere externalities. Consequently, Alternative Investment Fund managers face looming legal, financial, and reputational exposure if they fail to integrate ESG and sustainability factors. The findings suggest that the fragmented Indian fiduciary standards possess immense potential for expansion through purposive interpretation, regulatory nudges, and comparative international guidance. To operationalize this paradigm shift, the paper recommends statutory clarification of sustainability-linked fiduciary duties, mandatory ESG disclosure requirements for AIFs and the development of a context-specific Indian ESG taxonomy.

By integrating AIF regulatory framework with sustainable development, the paper concludes that fiduciary duties, ESG integration hold the potential to be interconnected domains which mutually reinforce investor confidence essential to create robust capital markets and long-term societal value.

**Keywords:** *Alternative Investment Funds, Climate Governance, Corporate Law, ESG Integration, Fiduciary Duties, Sustainability*

**Introduction**

Environmental, Social, and Governance (ESG) investment has moved from the periphery of ethical finance to the core of risk assessment and value creation in international capital markets.<sup>1</sup> By 2020, ESG-aligned investments accounted for nearly one-third of global assets under management, exceeding USD 35 trillion.<sup>2</sup> CEOs in India and around the world are adopting a long-term perspective on ESG investments, with many anticipating notable returns in the next five to 10 years, according to KPMG's 2024 India CEO Outlook.<sup>3</sup> The European Union's

<sup>1</sup> Georgios Zairis, Panagiotis Liargovas and Nikolaos Apostolopoulos, 'Sustainable Finance and ESG Importance: A Systematic Literature Review and Research Agenda', *Sustainability* 2024, 16(7), 2878,1

<sup>2</sup> Global Sustainable Investment Alliance, 'Global Sustainable Investment Review 2020', (GSIR),

<<https://www.gsi-alliance.org/wp-content/uploads/2021/08/GSIR-20201.pdf>> accessed on 17 September 2025

<sup>3</sup> Namrata Rana, 'ESG and the Growth Imperative - For Indian companies', (KPMG, 21 January 2025),



Sustainable Finance Disclosure Regulation (SFDR) and the U.S. Securities and Exchange Commission (SEC) have expedited mandatory ESG disclosures and further formalized ESG requirements.<sup>4</sup>

India's adoption of ESG norms has been shaped by the combined influence of market expectations and evolving regulatory mandates.<sup>5</sup> The Securities and Exchange Board of India (SEBI) required the top 1,000 listed businesses to file Business Responsibility and Sustainability Reports (BRSR) in order to integrate ESG disclosures into compliance frameworks.<sup>6</sup> These disclosure requirements build upon earlier statutory interventions under the Companies Act, 2013, which formally linked corporate governance with social responsibility through mandatory CSR obligations.<sup>7</sup>

A critical gap in existing scholarship lies in the treatment of ESG integration within Indian Alternative Investment Funds (AIFs), where regulatory guidance remains fragmented and under-theorised. Current practice indicates that only a limited number of AIFs explicitly incorporate ESG principles, and where they do, disclosure and implementation standards vary significantly.<sup>8</sup> Regulatory attention to ESG in India has been concentrated on listed companies through Business Responsibility and Sustainability Reporting

(BRSR), leaving AIFs with weaker obligations to comply with. This regulatory silence is particularly consequential given the growing role of AIFs in India's private capital markets and their increasing exposure to long-term environmental and governance risks.

The Securities and Exchange Board of India (SEBI) imposes obligations on AIF managers to act in the best interest of investors, but there is uncertainty whether this includes long-term ESG considerations.<sup>9</sup> Globally, fiduciary duty has been interpreted in light of sustainability, as seen in OECD and UN reports, but Indian jurisprudence on this dimension is still embryonic and whether India will adopt such a purposive interpretation is yet to be seen.<sup>10</sup> This critical gap poses an imminent need for the doctrinal and policy analysis of fiduciary duties in the context of ESG integration in AIFs.

Key questions include: (i) How are ESG principles currently reflected in Indian AIF practice? (ii) To what extent do regulatory frameworks incentivize or mandate ESG adoption? (iii) Can fiduciary duty in fund law be reinterpreted to encompass ESG integration?

This paper argues that ESG and climate governance considerations must be understood as integral to

<<https://kpmg.com/in/en/blogs/2025/01/esg-and-the-growth-imperative-for-indian-companies.html>> accessed on 17 September 2025

<sup>4</sup> European Commission, Regulation (EU) 2019/2088 on Sustainability-Related Disclosures in the Financial Services Sector [2019] OJ L317/1; US SEC, Enhanced Disclosures by Certain Investment Advisers and Investment Companies about ESG Investment Practices (Proposed Rule, 2022).

<sup>5</sup> Gaurav Bhatia, 'Navigating ESG in India: Current Regulations and Future Outlook', (*ET LegalWorld*, May 07, 2025), <<https://legal.economictimes.indiatimes.com/news/opinions/navigating-esg-in-india-current-regulations-and-future-outlook/120963366>> accessed on 17 September 2025

<sup>6</sup> Securities and Exchange Board of India, Circular SEBI/HO/CFD/CMD-2/P/CIR/2021/562 dated May 10, 2021,

<[https://www.sebi.gov.in/legal/circulars/may-2021/business-responsibility-and-sustainability-reporting-by-listed-entities\\_50096.html](https://www.sebi.gov.in/legal/circulars/may-2021/business-responsibility-and-sustainability-reporting-by-listed-entities_50096.html)> accessed on 17 September 2025

<sup>7</sup> The Companies Act 2013, s 135

<sup>8</sup> Rachna Balyan, Anmol Kumar, 'The Role of Alternate Investment Funds in Sustainable Investing: Opportunities and Challenges', (2023) 5 IJAEM 6,307

<sup>9</sup> SEBI (Alternative Investment Funds) Regulations 2012, reg 20.

<sup>10</sup> OECD Report, 'Investment governance and the integration of environmental, social and governance factors', (*OECD*, 01 January 2017) <[https://www.oecd.org/en/publications/investment-governance-and-the-integration-of-environmental-social-and-governance-factors\\_40a1430a-en.html](https://www.oecd.org/en/publications/investment-governance-and-the-integration-of-environmental-social-and-governance-factors_40a1430a-en.html)> accessed on September 17, 2025



fiduciary decision-making within Indian AIFs, rather than as discretionary ethical preferences. The paper will evaluate the extent of ESG integration and adoption into the Indian AIF ecosystem in light of SEBI Guidelines and market pressures including foreign Limited Partners (LPs). The study will also assess the fiduciary obligations of AIF managers and sponsors in embedding ESG within investment decision-making.

### I. Environmental, Social and Governance in Private Equity

ESG which stands for Environmental, Social, and Governance has emerged as one of the most notable trends in corporate governance in the past two decades.<sup>11</sup> ESG is a collection of criteria used to assess the social and environmental effect of a business.<sup>12</sup> Sustainable investing, responsible investing, impact investing, and socially responsible investing (SRI) are other names for ESG investing.<sup>13</sup> In the AIF or Private Equity context, the INSEAD report explains how investment committee decisions are increasingly including ESG considerations beyond compliance.<sup>14</sup> PE firms with higher voluntary ESG disclosures tend to see better ESG performance in their portfolio companies.<sup>15</sup>

It is imperative to analyse the nexus between ESG in the Private Equity space considering the role of PE/VC role in India's capital markets. With an average yearly investment volume of almost \$40 billion over the previous five years, the private equity sector in India has experienced impressive expansion in recent years.<sup>16</sup> With around 20% of all investments, India solidified its position as the second-largest PE-VC destination in the Asia-Pacific area, demonstrating increased investor trust in the macroeconomic stability of the nation.<sup>17</sup> India's fast growing startup ecosystem and advantageous regulatory environment have made it a popular and sought-after location for venture capital (VC) and private equity (PE) investments globally in recent years.<sup>18</sup>

The ESG considerations have become increasingly relevant in light of risk management and creation of long-term value. PE firms are realizing the importance of ESG due diligence in their deal-making, especially in light of this regulatory backdrop and the growing prevalence of climate-related hazards, as well as issues with employee and community relations and occupational health and safety concerns.<sup>19</sup> ESG has emerged as a crucial factor in decision-making as investors come under growing pressure from

<sup>11</sup> Elizabeth Pollman, 'The Making and Meaning of ESG' (2024) 14 Harv Bus L Rev 403, 403

<sup>12</sup> Tom Krantz, Alexandra Jonker, 'What is ESG?', (IBM, 24 January 2024),

<<https://www.ibm.com/think/topics/environmental-social-and-governance>> accessed 17 September 2025

<sup>13</sup> The Investopedia Team, 'Environmental, Social, and Governance (ESG) Investing: What It Is & How It Works', (Investopedia, 19 August 2025), <<https://www.investopedia.com/terms/e/environmental-social-and-governance-esg-criteria.asp>> accessed 17 September 2025

<sup>14</sup> White B., Zeisberger.C., 'ESG in Private Equity: A Fast-Evolving Standard', (INSEAD, May 2014), <<https://www.insead.edu/faculty-research/publications/reports/esg-private-equity-a-fast-evolving-standard>> accessed 17 September 2025

<sup>15</sup> Abraham et. al, 'ESG Disclosures in the Private Equity Industry', Journal of Accounting Research, Vol. 62 No. 5 December 2024

<sup>16</sup> Nils Rode et. al., 'The India growth story – the role of private equity and the 3D reset', (Schroders, 18 January 2024), <<https://www.schroders.com/en-ca/ca/professional/insights/the-india-growth-story-the-role-of-private-equity-and-the-3d-reset/>> accessed 17 September 2025

<sup>17</sup> Arpan Sheth et. al, 'India Private Equity Report 2025', (Bain & Company), <[https://www.bain.com/globalassets/noindex/2025/bain\\_report\\_india\\_private\\_equity\\_2025.pdf](https://www.bain.com/globalassets/noindex/2025/bain_report_india_private_equity_2025.pdf)> accessed 17 September 2025

<sup>18</sup> Dominic, James, and Anto Joseph, 'Dynamics of Venture Capital and Private Equity Investments in India: An Empirical Analysis', J. Risk Financial Manag. 2023, 16(11), 475,1

<sup>19</sup> EY India, 'How ESG Due Diligence is influencing Private-Equity Deal Making?' (EY, 05 September 2025),



international stakeholders to make sure their portfolios support ethical and sustainable practices.<sup>20</sup>

### Rise of ESG regulation

To increase openness on ESG-related risks, policies, and actions by listed businesses, SEBI launched the Business Responsibility Report (BRR) in its August 2012 circular.<sup>21</sup> At first, it applied to the top 100 listed businesses based on market capitalisation.<sup>22</sup> The BRR required disclosures aligned with the National Voluntary Guidelines (NVGs) on Social, Environmental and Economic Responsibilities of Business.<sup>23</sup> The BRR was based on the NVGs (2011) issued by the Ministry of Corporate Affairs (MCA), promoting responsible business conduct across 9 core principles such as environmental protection, human rights, and employee welfare.<sup>24</sup>

In May 2021, SEBI issued a circular mandating a shift from BRR to BRSR for the top 1000 listed companies (by market capitalization), starting from FY 2022–23.<sup>25</sup>

The BRSR introduced quantitative key performance indicators (KPIs) for environmental (e.g. GHG emissions, energy usage), social (e.g. gender diversity, employee training), and governance metrics. Starting FY25-26, the top 250 listed entities will need to report on their value chain, covering upstream and downstream partners that make up at least 2% of their purchases and sales.<sup>26</sup>

In 2021, SEBI introduced ESG disclosure and categorization norms for mutual funds, requiring schemes to classify as ESG, Social, or Sustainable funds. SEBI mandated mutual funds to classify schemes under “ESG funds,” “Socially Responsible Funds,” or “Sustainable Funds” categories. The 2023 amendments require mutual funds to provide detailed disclosures on ESG scoring methodology, data sources, and independent third-party verification to prevent misleading claims and improve comparability among ESG funds.<sup>27</sup>

<[https://www.ey.com/en\\_in/insights/private-equity/how-esg-due-diligence-is-influencing-private-equity-deal-making](https://www.ey.com/en_in/insights/private-equity/how-esg-due-diligence-is-influencing-private-equity-deal-making)> accessed 17 September 2025

<sup>20</sup> Green Buoy Consulting, ‘Why Private Equity is Prioritizing ESG in 2025’, (*Green Buoy Consulting*, 28 January 2025), <<https://www.greenbuoyconsulting.com/blog/why-private-equity-is-prioritizing-esg-in-2025>> accessed 17

September 2025

<sup>21</sup> Securities and Exchange Board of India, Circular CIR/CFD/DIL/8/2012 dated August 13, 2012, <[https://www.sebi.gov.in/sebi\\_data/attachdocs/1344915990072.pdf](https://www.sebi.gov.in/sebi_data/attachdocs/1344915990072.pdf)> accessed 17 September 2025

<sup>22</sup> EY India, ‘BRSR reporting and the evolving ESG landscape in India’, (*EY*, 21 April 2023), <[https://www.ey.com/en\\_in/insights/climate-change-sustainability-services/brsr-reporting-and-the-evolving-esg-landscape-in-india](https://www.ey.com/en_in/insights/climate-change-sustainability-services/brsr-reporting-and-the-evolving-esg-landscape-in-india)> accessed 17 September 2025

<sup>23</sup> Ministry of Corporate Affairs, ‘National Voluntary Guidelines (NVGs) on Social, Environmental and Economic Responsibilities of Business’, (MCA, July 2011),

<[https://www.mca.gov.in/Ministry/latestnews/National\\_Voluntary\\_Guidelines\\_2011\\_12jul2011.pdf](https://www.mca.gov.in/Ministry/latestnews/National_Voluntary_Guidelines_2011_12jul2011.pdf)> accessed 17

September 2025

<sup>24</sup> Press Information Bureau, ‘MCA releases national guidelines on responsible business conduct’, (PIB, 13 March, 2019), <<https://www.pib.gov.in/Pressreleaseshare.aspx?PRID=1568750>> accessed 17 September 2025

<sup>25</sup> Securities and Exchange Board of India, Circular SEBI/HO/CFD/CMD-2/P/CIR/2021/562 dated May 10, 2021,

<[https://www.sebi.gov.in/legal/circulars/may-2021/business-responsibility-and-sustainability-reporting-by-listed-entities\\_50096.html](https://www.sebi.gov.in/legal/circulars/may-2021/business-responsibility-and-sustainability-reporting-by-listed-entities_50096.html)> accessed 17 September 2025

<sup>26</sup> S&R Associates, ‘Regulatory Initiatives on ESG Disclosure Requirements in India’, (*S&R Associates*, May 21, 2025) <<https://www.snrlaw.in/regulatory-initiatives-on-esg-disclosure-requirements-in-india/>> accessed 17 September 2025

<sup>27</sup> Securities and Exchange Board of India, Circular SEBI/HO/IMD/IMD-I –PoD1/P/CIR/2023/125 dated July 20, 2023,

<[https://www.sebi.gov.in/legal/circulars/jul-2023/new-category-of-mutual-fund-schemes-for-environmental-social-and-governance-esg-investing-and-related-disclosures-by-mutual-funds\\_74186.html](https://www.sebi.gov.in/legal/circulars/jul-2023/new-category-of-mutual-fund-schemes-for-environmental-social-and-governance-esg-investing-and-related-disclosures-by-mutual-funds_74186.html)> accessed 17 September 2025



In 2023, Securities and Exchange Board of India (SEBI) issued a circular to the issuers of Green Debt Securities to disclose the decision-making process used to determine project eligibility, include a statement of the issue's environmental sustainability objectives in the offer document, and explain the system or procedures for tracking the deployment of proceeds to avoid greenwashing.<sup>28</sup> The same circular mandates that issuers of Green Debt Securities make continuous disclosures to avoid misrepresentation. These disclosures include (i) the use of proceeds in line with the tracking method revealed in the offer document and verified by an external auditor; (ii) details regarding proceeds that have not been used; (iii) a list of the projects and assets to which proceeds have been allocated with disbursement amounts; and (iv) qualitative performance indicators and, when feasible, quantitative environmental impact metrics.<sup>29</sup> The rules which came into effect on April 1, 2023, were developed to align the framework for green debt securities with the Green Bond Principles (GBP) authorized by IOSCO in response to the growing interest in sustainable finance in India and around the world.<sup>30</sup>

In order to manage the use of the proceeds from a green debt security after it is issued and to verify internal tracking and impact reporting, the issuer must also choose a third-party reviewer.<sup>31</sup> In light of this, it is

pertinent to examine SEBI's definition of "greenwashing" in its February 2023 circular. SEBI defines greenwashing as "making false, misleading, unsubstantiated, or otherwise incomplete claims about the sustainability of a product, service, or business operation", with the circular requiring issuers to avoid such claims.<sup>32</sup>

In August 2025, SEBI proposed revised norms for appointment of independent third-party reviewers/certifiers for Green Debt Securities which requires that the reviewer must be independent of the issuer, its directors, senior management, key managerial personnel and must possess specific expertise in assessing ESG debt securities.<sup>33</sup> While this is a draft circular and has not come into effect, it reflects the importance that SEBI gives to the issuance of Green Debt Securities and the ESG component of it.

It is pertinent to note that SEBI through its SEBI AIF regulations, 2012 does not explicitly incorporate ESG or any Green Debt disclosure or assurance requirement akin to SEBI's ESG debt securities framework. This is a clear regulatory gap considering the growing importance of AIF's that will be examined in the section below.

<sup>28</sup> Securities and Exchange Board of India, Circular SEBI/HO/DDHS/DDHS-RACPOD1/P/CIR/2023/023 dated February 06, 2023, <[https://www.sebi.gov.in/legal/circulars/feb-2023/revised-disclosure-requirements-for-issuance-and-listing-of-green-debt-securities\\_67837.html](https://www.sebi.gov.in/legal/circulars/feb-2023/revised-disclosure-requirements-for-issuance-and-listing-of-green-debt-securities_67837.html)> accessed 17 September 2025

<sup>29</sup> *Id.* paragraph 2 and continuous disclosure requirement

<sup>30</sup> PTI, 'Sebi puts in place operational guidelines on green bonds', (*The Economic Times*, 06 February 2023), <<https://economictimes.indiatimes.com/markets/bonds/sebi-puts-in-place-operational-guidelines-on-green-bonds/>> accessed 17 September 2025

<sup>31</sup> PTI, 'Sebi asks issuers for additional disclosure in guidelines on green bonds', (*Business Standard*, 06 February 2023), <[https://www.business-standard.com/article/markets/sebi-asks-issuers-for-additional-disclosure-in-guidelines-on-green-bonds-123020601146\\_1.html](https://www.business-standard.com/article/markets/sebi-asks-issuers-for-additional-disclosure-in-guidelines-on-green-bonds-123020601146_1.html)> accessed 17 September 2025

standard.com/article/markets/sebi-asks-issuers-for-additional-disclosure-in-guidelines-on-green-bonds-123020601146\_1.html> accessed 17 September 2025

<sup>32</sup> 'Greenwashing: SEBI February 3 Circular', (*Verist Law*), <<https://www.veristlaw.in/post/sebi-circular-on-greenwashing>> accessed 17 September 2025

<sup>33</sup> Securities and Exchange Board of India, Draft Circular for Public Comments dated August 01, 2025, 'Revised Norms for appointment of an independent third-party reviewer/ certifier for green debt security',

<[https://www.sebi.gov.in/reports-and-statistics/reports/aug-2025/revised-norms-for-appointment-of-an-independent-third-party-reviewer-certifier-for-green-debt-security\\_95767.html](https://www.sebi.gov.in/reports-and-statistics/reports/aug-2025/revised-norms-for-appointment-of-an-independent-third-party-reviewer-certifier-for-green-debt-security_95767.html)> accessed on 17 September 2025



## Overview of Indian AIF Landscape

### Growth and statutory recognition of Alternative Investment Funds (AIFs) in India

Alternative Investment funds (AIF's) are privately pooled investment vehicles that collect funds from sophisticated investors and invest based on a definitive policy for the investors' benefit.<sup>34</sup> Indian alternative investments are likely to see a more than five-fold growth to \$ 2 trillion over the next decade.<sup>35</sup> Over the last five years (ending September 30, 2024), the industry has expanded at a compound annual growth rate (CAGR) of 31.44%, indicating its increasing integration into India's larger financial ecosystem.<sup>36</sup> Given that a sizable portion of these investments come from overseas investors or India-focused offshore funds as foreign direct investment (or "FDI"), AIFs are becoming a more alluring investment option for both foreign and non-resident Indian investors.<sup>37</sup>

India's regulatory framework for AIF's was established by the Securities and Exchange Board of India (Alternative Investment Funds) Regulations, 2012, which classifies AIFs into Category I (developmental/impact), Category II (private equity, debt funds, funds of funds), and Category III (hedge fund-style, employing complex or leverage

strategies).<sup>38</sup>

AIF's were introduced with an aim to encourage capital influx into areas that were not easily accessible through traditional investment channels such as early-stage startups, emerging markets or real estate which were not sufficiently encouraged by the erstwhile SEBI (Venture Capital Funds) Regulations, 1996.<sup>39</sup> According to the SEBI AIF Regulations, 2012 an AIF is defined as a privately pooled investment vehicle that is created or incorporated in India as a trust, corporation, limited liability partnership (LLP), or body corporate.<sup>40</sup> Under Regulation 2(1)(b), an AIF is defined as a "privately pooled investment vehicle which collects funds from investors (Indian or foreign)" for investing in accordance with a defined investment policy for the benefit of its investors.<sup>41</sup>

According to Regulation 3 of the Regulation, AIF in India can be registered under three categories:

a) Category I: This category includes infrastructure funds, Small and Medium Enterprise Funds (SME), venture capital funds, social venture funds, and such other AIFs that the Government may cite.<sup>42</sup> The government offers incentives and concessions for this money because of their "positive spill over effect" on the economy.<sup>43</sup> Category II: This category includes AIFs

<sup>34</sup> Repaka Pavan Aditya, 'Alternate Investment Funds (AIFs): An Overview', (ClearTax, 06 May 2025) <<https://cleartax.in/s/alternate-investment-funds>> accessed on 17 September 2025

<sup>35</sup> Khushi Keswani, 'India's Alternative Investment market to grow five-fold in next decade', (MoneyControl, 17 December, 2024) <<https://www.moneycontrol.com/news/business/markets/india-s-alternative-investment-market-to-grow-five-fold-in-next-decade-12891516.html>> accessed 17 September 2025

<sup>36</sup> BW Online Bureau, 'India's Private Equity And Venture Capital Markets: A Key Pillar For Long-term Investors', (BusinessWorld, 21 March 2025), <<https://www.businessworld.in/article/indias-private-equity-and-venture-capital-markets-a-key-pillar-for-long-term-investors-551281>> accessed 17 September 2025

<sup>37</sup> Sai Krishna Bharathan & Ganesh Rao, 'Alternative Investment Funds in India: Unlocking Sophisticated Investment' (2017) 3 NLS Bus L Rev 1,5

<sup>38</sup> Securities and Exchange Board of India (Alternative Investment Funds) Regulations, 2012

<sup>39</sup> Sakshi Bagdi & R. R. Pragnyath, 'Unlocking the Potential of the Indian AIF Regime and SEBI's Role in It' (2023) 3 Indian J Integrated Rsch L 1,5

<sup>40</sup> The Securities and Exchange Board of India (Alternative Investment Funds) Regulations, Regulation 2(b), Gazette of India, pt. III sec. 4, (2012)

<sup>41</sup> SEBI (Alternative Investment Funds) Regulations, 2012, Reg 2(1)(b).

<sup>42</sup> Regulation 3(4) (a), Securities and Exchange Board of India (Alternative Investment Funds) Regulations, Gazette of India, pt. III sec. 4, (2012)

<sup>43</sup> Ananya Shruti & Shashank Saurabh, 'Alternative Investments: Analysing Its Practical Application in



such as private equity funds or debt funds that engage in borrowing to meet the everyday practical functions. The Government does not provide incentives and concessions for this category of funds.<sup>44</sup> Category III: This category includes hedge funds, funds that trade to gain short term returns or open ended funds. These involve complex and diverse trading approaches. The government does not provide incentives and concessions for this category of funds.<sup>45</sup> According to the regulations, an AIF cannot accept an investment from an investor for less than ₹1 crore (one crore rupees), suggesting that investors must have substantial financial resources (e.g. HNWIs, institutional investors etc.).<sup>46</sup>

## II. The Role of Regulation in ESG Uptake Current SEBI Regulatory Framework SEBI (AIF) Regulations, 2012

As mentioned above, a clear regulatory gap exists as there is no explicit clause that requires AIFs or their managers to incorporate ESG criteria when making investment decisions or reporting performance. Although the Regulations do include Category I AIFs, like "Social Venture Funds" and "Infrastructure Funds," under categories deemed to have positive economic spillover effects, which may imply investment in socially or environmentally relevant sectors, the law does not impose any sustainability-

related obligations, impact metrics, or ESG-due diligence on those AIFs. The regulatory text does not impose any explicit ESG mandates as of its 2012 framing, even though there are implicit overlaps (such as social venture funds, infrastructure, and risk disclosures). Additionally, no amendment has added a legally binding ESG requirement to the core AIF Regulations until 2025. ESG principles may be introduced by investor demand rather than regulatory mandate if specific Limited Partners in AIFs, such as Development Finance Institutions or institutional investors with ESG mandates, voluntarily demand ESG considerations in investment decisions and reporting.<sup>47</sup>

### SEBI Stewardship Code, 2020

Effective from July 01, 2020, SEBI introduced a Stewardship Code applying to Mutual Funds (MFs) and Alternative Investment Funds (AIFs) investing in listed equities.<sup>48</sup> This was done to enhance corporate governance in India and align institutional investor behavior with global sustainability best practices.<sup>49</sup> SEBI Stewardship code is recognised as an instrument for strengthening ESG engagement by institutional investors, aligning with global investor trends and regulatory expectations.<sup>50</sup> SEBI's stewardship code has aided institutional investors in integrating and interacting with ESG by fostering greater transparency and better ESG practices among Indian firms.<sup>51</sup>

India' (2020) 7 RGNUL Fin & Mercantile L Rev 139,150

<sup>44</sup> Regulation 3(4) (b), Securities and Exchange Board of India (Alternative Investment Funds) Regulations, Gazette of India, pt. III sec. 4, (2012).

<sup>45</sup> Regulation 3(4)(c), The Securities and Exchange Board of India (Alternative Investment Funds) Regulations, Gazette of India, pt. III sec. 4, (2012).

<sup>46</sup> SEBI (Alternative Investment Funds) Regulations, 2012, Salient Features; also Reg 2(1)(b) read with the clause on minimum investment

<sup>47</sup> Divya Arvind Mahadule, 'Sustainable Finance: The Integration of ESG Criteria in Investment Strategies', IPE Journal of Management, Vol. 15, No 1, 146

<sup>48</sup> Securities and Exchange Board of India, Circular No.: CIR/CFD/CMD1/168 /2019 dated December 24, 2019, <<https://www.sebi.gov.in/legal/circulars/dec-2019/stewardship-code-for-all-mutual-funds-and-all>

categories-of-aifs- in-relation-to-their-investment-in-listed-equities\_45451.html> accessed 17 September 2025

<sup>49</sup> Securities and Exchange Board of India, 'Stewardship Code for Institutional Investors' (2020) <[https://www.sebi.gov.in/sebi\\_data/attachdocs/1599489795960.pdf](https://www.sebi.gov.in/sebi_data/attachdocs/1599489795960.pdf)> accessed 17 September 2025

<sup>50</sup> 'SEBI Funds Management adopts stewardship code as mandated by SEBI', The Economic Times (4 March 2020)

<<https://economictimes.com/markets/stocks/news/sbi-funds-management-adopts-stewardship-code-as-mandated-by-sebi/articleshow/74672530.cms>> accessed 20 September 2025

<sup>51</sup> Pandey A & Sharma B, 'Does a Stewardship Code Improve the Firm Valuation and ESG Scores? Evidence from India' (2024) 18(3) Australasian Accounting, Business and Finance Journal 146



### Business Responsibility and Sustainability Reporting (BRSR)

The Securities and Exchange Board of India (SEBI) established the Business Responsibility and Sustainability Reporting (BRSR) framework, which requires listed companies to report on their environmental, social, and governance (ESG) practices.<sup>52</sup> Although AIFs are not directly governed by BRSR, their investment strategies and due diligence procedures are indirectly impacted by the framework's relevance to listed investee companies.

In 2025, SEBI included Green Credit Program under BRSR framework wherein principle 6 of BRSR states that companies should respect and make efforts to protect and restore the environment, green credits produced by the listed company and their top ten value chain partners can be added as a leadership indicator.<sup>53</sup> This is in line with the Environment Audit Rules, 2025 issued by the Ministry of Environment, Forests, and Climate Change, which aims to incorporate environmental factors into corporate reporting.<sup>54</sup>

<<https://www.uowojournals.org/aabfj/article/id/1040/download/pdf/>>, accessed 20 September 2025

<sup>52</sup> Securities and Exchange Board of India, Circular No.: SEBI/HO/CFD/CFD-SEC-2/P/CIR/2023/122 dated July 12, 2023, <[https://www.sebi.gov.in/legal/circulars/jul-2023/brsr-core-framework-for-assurance-and-esg-disclosures-for-value-chain\\_73854.html](https://www.sebi.gov.in/legal/circulars/jul-2023/brsr-core-framework-for-assurance-and-esg-disclosures-for-value-chain_73854.html)> accessed 17 September 2025

<sup>53</sup> PTI, 'Sebi includes Green Credit Program under BRSR framework', (*Business Standard*, 28 March 2025), <[https://www.business-standard.com/markets/news/sebi-includes-green-credit-program-under-brsr-framework-125032801374\\_1.html](https://www.business-standard.com/markets/news/sebi-includes-green-credit-program-under-brsr-framework-125032801374_1.html)> accessed 17 September 2025

### ESG Policy Instruments

#### Corporate Social Responsibility Mandate under Companies Act

According to Section 135 of the Companies Act of 2013, any company that meets any of the following thresholds in the previous fiscal year—net worth of at least ₹500 crore, turnover of at least ₹1,000 crore, or net profit of at least ₹5 crore—must allocate at least 2% of its average net profits (calculated over the three fiscal years prior) to Corporate Social Responsibility (CSR) initiatives.<sup>55</sup>

#### RBI's climate-related disclosure guidelines – implications for lenders to AIF-backed entities

According to RBI's Draft Disclosure Framework on Climate-Related Financial Risks, 2024, Regulated Entities (REs), such as Scheduled Commercial Banks (SCBs), All-India Financial Institutions (AIFIs), and major non-bank financial companies (NBFCs), must reveal information in the "Governance; Strategy; Risk Management; Metrics & Targets" pillars, which includes the financed emissions of counterparties and investees.<sup>56</sup> Under the metrics & targets disclosure regime, any exposure by lenders to AIFs or downstream exposure of an AIF to a company, may be relevant because many AIF-backed companies are among those

<sup>54</sup> Shreya Verma, 'India notifies Environment Audit Rules, 2025 to bolster environmental compliance & governance', (*Down To Earth*, 08 September 2025) <<https://www.downtoearth.org.in/environment/india-notifies-environment-audit-rules-2025-to-bolster-environmental-compliance-governance>> accessed 17 September 2025

<sup>55</sup> The Companies Act, 2013, s 135(1)–(2), Schedule VII

<sup>56</sup> Reserve Bank of India, 'Draft Disclosure framework on Climate-related Financial Risks, 2024', RBI/2023-24/DOR.SFG.REC./30.01.021/2023-24 dated 28 February 2024, <[https://www.rbi.org.in/Scripts/bs\\_viewcontent.aspx?Id=4393](https://www.rbi.org.in/Scripts/bs_viewcontent.aspx?Id=4393)> accessed 17 September 2025



investees/counterparties.<sup>57</sup> This is because such exposure may need to be measured and reported. The RBI changed the rules in March 2024 to require REs to make provisions only for the part of their investment in an AIF scheme that the AIF then invests in the RE's debtor company.<sup>58</sup>

### MCA National Guidelines on Responsible Business Conduct (NGRBC)

The Ministry of Corporate Affairs (MCA) updated the 2011 National Voluntary Guidelines (NVGs) in March 2019 with the National Guidelines on Responsible Business Conduct (NGRBC), which is in line with the Sustainable Development Goals (SDGs), the UN Guiding Principles on Business & Human Rights, and other international standards.<sup>59</sup> The NGRBC set out nine principles, including that “businesses should conduct and govern themselves with integrity, and in a manner that is ethical, transparent and accountable”, “provide goods and services in a manner that is sustainable and safe”, “respect and make efforts to protect and restore the environment”, and “promote inclusive growth and equitable development”.<sup>60</sup>

### Regulatory or governmental incentives for ESG for green-aligned AIFs in India

The government amended Section 2(14) of the Income Tax Act in the 2025 Indian Budget to guarantee that income from AIF investments in securities will be treated as capital gains (rather than possibly being treated as business income) for investors.<sup>61</sup> In terms of tax rate expectations, this gives investors more certainty and is advantageous for them, especially in ESG/green AIFs. Certain tax and regulatory benefits are available to AIFs established in the International Financial Services Centre (IFSC), such as GIFT City. For instance, Category I and II AIFs in the IFSC have tax pass-through status for Indian income tax purposes (with the exception of business income), and in certain situations, business income is eligible for a 100% tax holiday for up to fifteen years.<sup>62</sup> For ESG-aligned funds that domicile or structure through IFSC, this can be leveraged. However, there are no explicit tax incentives for ESG / green-aligned AIF's in terms of tax deductions, lower tax rates, accelerated depreciation, or subsidies. While the 2015 Budget clarifies the tax treatment of AIF's, there is no specificity with respect to ESG.

<sup>57</sup> Saptaparno Ghosh, ‘RBI’s proposal for disclosure framework to ascertain climate-related financial risks | Explained’, (*The Hindu*, 12 March 2024), <<https://www.thehindu.com/business/Economy/rbis-proposal-for-a-disclosure-framework-to-ascertain-climate-related-financial-risks-explained/article67938041>> accessed 17, September 2025

<sup>58</sup> The Hindu Bureau, ‘RBI modifies norms for lenders having exposure into AIF’s’, (*The Hindu*, 27 March 2024), <<https://www.thehindu.com/business/rbi-modifies-norms-for-lenders-having-exposure-into-aifs/article67998937>> accessed 17 September 2025

<sup>59</sup> Press Information Bureau, ‘MCA releases national guidelines on responsible business conduct’, (*PIB*, 13 March 2019), <<https://www.pib.gov.in/Pressreleaseshare.aspx>> accessed 17 September 2025

<sup>60</sup> Lexplosion, ‘MCA releases National Guidelines on Responsible Business Conduct to assist businesses in

complying with requirements of regulatory compliance’, (*Lexplosion*, 20 March 2019), <<https://lexplosion.in/mca-releases-national-guidelines-on-responsible-business-conduct-to-assist-businesses-in-complying-with-requirements-of-regulatory-compliance/>> accessed 17 September 2025

<sup>61</sup> Sneha Shah, Ranjani Raghavan, ‘Budget 2025 I Tax clarity for AIF’s as income will now be treated as capital gains’, (*Mint Markets*, 01 February 2025), <<https://www.livemint.com/market/budget-2025-tax-relief-for-aifs-as-income-will-now-be-treated-as-capital-gains-11738407920343.html>> accessed 17 September 2025

<sup>62</sup> GIFT CFO, ‘Alternative Investment Funds (AIFs) in GIFT City IFSCA’, (*GIFT CFO*, 03 January 2025), <<https://www.giftcfo.com/post/unlocking-opportunities-in-investment-funds-a-guide-to-ifsc-fund-management-regulations-2022>> accessed 17 September 2025



### Limitations of the Current Framework

As of now, AIFs are not required by the SEBI (AIF) Regulations, 2012 to include environmental, social, or governance considerations in their investment strategies, disclosures, or reporting requirements.<sup>63</sup> Even for large AIFs with substantial institutional or foreign LP exposure, there is no comparable ESG-specific disclosure, screening, or reporting framework for AIFs, despite SEBI having released ESG-related guidelines for mutual funds and listed companies.<sup>64</sup> This regulatory void exists even though SEBI encourages "institutional investors like AIFs" to encourage ESG practices among their investee companies, especially in the unlisted sector.<sup>65</sup>

India is yet to formally adopt a sustainable finance taxonomy that applies to private capital vehicles such as AIFs.<sup>66</sup> AIFs are not currently required to publish sustainability-related disclosures in the same manner as listed entities, nor does SEBI run a centralized ESG monitoring framework for them.<sup>67</sup> In contrast to listed companies that are required to disclose BRSR Core information and obtain third-party assurance from FY 2023–2024, AIFs are exempt from the ESG compliance certification, audit, and assurance requirements under Indian law.<sup>68</sup> As a necessary consequence, enforcement

risks for ESG violations or misstatements by AIFs remain low and ESG mislabelling is not subject to specific penal provisions under SEBI AIF regulations.<sup>69</sup> It is pertinent to note that the SEBI (Alternative Investment Funds) Regulations, 2012, do not contain any explicit ESG mandates, nor do they require ESG-related disclosures which makes the regulatory landscape nascent for ESG integration in AIF's. Since SEBI's Business Responsibility and Sustainability Reporting (BRSR) framework applies to the top 1,000 listed entities, ESG expectations in the AIF space are primarily shaped by indirect regulatory nudges and soft law tools.<sup>70</sup> Despite this disjointed structure, India's ESG regulatory environment seems to be heading towards harmonisation with global sustainable finance taxonomies, and enhanced supervisory frameworks with AIF's role in spearheading ESG in unlisted firms.<sup>71</sup>

### III. Theoretical Foundations of Fiduciary Duty and Fiduciary Duties in Indian Fund Law

The traditional legal underpinnings of fiduciary duty are based on the duties of loyalty, caution, financial prudence and care, especially as they relate to fund managers and general partners (GPs) in private capital

<sup>63</sup> SEBI (Alternative Investment Funds) Regulations 2012, *see also* Schedule IV (no ESG clause).

<sup>64</sup> Securities and Exchange Board of India, 'New category of Mutual Fund schemes for Environmental, Social and Governance ("ESG") Investing and related disclosures by Mutual Funds', Circular no. SEBI/HO/IMD/IMD-I – PoD1/P/CIR/2023/125 dated 20 July 2023, <[https://www.sebi.gov.in/legal/circulars/jul-2023/new-category-of-mutual-fund-schemes-for-environmental-social-and-governance-esg-investing-and-related-disclosures-by-mutual-funds\\_74186.html](https://www.sebi.gov.in/legal/circulars/jul-2023/new-category-of-mutual-fund-schemes-for-environmental-social-and-governance-esg-investing-and-related-disclosures-by-mutual-funds_74186.html)>

<sup>65</sup> Ridhima Bhatnagar, 'SEBI encourages AIFs to push ESG compliance among their investee companies', (*Business Today*, 15 July 2025), <<https://www.businesstoday.in/latest/corporate/story/sebi-encourages-aifs-to-push-esg-compliance-among-their-investee-companies-484787-2025-07-15>> accessed 17 September 2025

<sup>66</sup> Sarthak Shukla, 'Sustainable Finance Taxonomy for India: Just another taxonomy or a 'just' taxonomy?', (*Heinrich-Böll-Stiftung*, 01 August 2024), <<https://in.boell.org/en/sustainable-finance-taxonomy>> accessed 17, September 2025

<sup>67</sup> SEBI (Alternative Investment Funds) Regulations 2012, *see also* SEBI (LODR) Regulations 2015, which mandate ESG/BRSR disclosures for top 1,000 listed entities.

<sup>68</sup> *Supra* note 52

<sup>69</sup> SEBI Act 1992 s 15HB (general penalty for contravention with no specific penalty).

<sup>70</sup> *Supra* note 52.

<sup>71</sup> BS reporter, 'AIFs must lead ESG push in unlisted firms, says Sebi's Ruchi Chojer', (*Business Standard*, 15 July 2025), <[https://www.business-standard.com/markets/news/aifs-must-lead-esg-adoption-in-unlisted-space-says-sebi-official-125071501185\\_1.html](https://www.business-standard.com/markets/news/aifs-must-lead-esg-adoption-in-unlisted-space-says-sebi-official-125071501185_1.html)> accessed on 17 September 2025



structures like Alternative Investment Funds (AIFs).<sup>72</sup> When taken as a whole, these responsibilities create a fundamental goal: to maximize risk-adjusted financial returns for the beneficiaries, guaranteeing that capital is allocated effectively and without jeopardizing LPs' financial interests.<sup>73</sup>

In countries like India, where fund agreements, SEBI regulations, and common law principles all influence fiduciary standards in private funds, the question of whether fiduciaries have the right to incorporate non-financial considerations like ESG emerges.<sup>74</sup> However, the treatment of ESG under fiduciary norms for AIFs remains a theoretically contentious and practically cautious area in India due to the lack of clear legal clarification or regulatory guidance.<sup>75</sup>

#### Companies Act, 2013 – Section 166: Directors as Fiduciaries

The fiduciary duties of company directors are codified in Section 166 of the Companies Act, 2013, which mandates that they behave in the best interests of the business, shareholders, employees, the community, and the environment.<sup>76</sup> Using independent judgement, avoiding conflicts of interest, avoiding undue benefits or advantages, and operating in good faith are some of these obligations.<sup>77</sup>

When Alternative Investment Funds (AIFs) purchase substantial or controlling shares in portfolio companies,

usually through private equity or venture capital strategies under Category I or II AIFs, Section 166 becomes relevant. In these situations, the AIF may nominate directors to the investee company's board or obtain board representation, establishing a dual role whereby the nominee director must act in the AIF's (and its investors') best interests while also adhering to Section 166.<sup>78</sup> SEBI guidelines and Indian jurisprudence confirm that nominee directors are required to act as the company's fiduciaries and are not merely representatives of their appointing shareholders.<sup>79</sup> When the long-term interests of the business or its wider stakeholders clash with the AIF's investment objectives, like exit-driven returns, this could lead to conflict.<sup>80</sup>

Furthermore, Section 166(2) is frequently read to allow, directors to take into account interests other than shareholders—like the effects on the environment and society.<sup>81</sup> This is conceptually consistent with ESG integration. However, the fiduciary balancing act faced by AIF-linked directors is still unclear, though, as there is still a lack of judicial guidance in India regarding how to balance ESG priorities with the requirement to maximize returns for AIF beneficiaries (LPs).<sup>82</sup>

<sup>72</sup> Stephen Cork, 'Understanding the Role of a Fiduciary in Fund Management', (*Cork Gully*, 16 March 2024),

<<https://corkgullyassetmanagers.com/understanding-the-role-of-a-fiduciary-in-fund-management-3/>> accessed on 17 September 2025

<sup>73</sup> Benjamin J Richardson, 'Fiduciary Law and Responsible Investing' (2013) 36(2) *University of British Columbia Law Review* 205, 207

<sup>74</sup> SEBI (Alternative Investment Funds) Regulations 2012, *see also* Regulation 21; Limited Partnership Agreements (LPAs) govern fiduciary obligations contractually

<sup>75</sup> Tanvi Soni and Umakanth Varottil, 'Fiduciary Duty and ESG Integration in India's Investment Funds' (2023) 15 *NUJS Law Review* 45, 49.

<sup>76</sup> The Companies Act 2013, s 166.

<sup>77</sup> The Companies Act 2013, s 166(3)–(6).

<sup>78</sup> V Umakanth, 'Nominee Directors and Corporate Governance' (2010) 22(2) *National Law School of India Review* 28, 32.

<sup>79</sup> *LIC of India v Escorts Ltd* (1986) AIR 1370 (SC); *see also* SEBI, 'Corporate Governance for Listed Entities' (LODR Regulations 2015) reg 25

<sup>80</sup> Vikramaditya Khanna, 'Nominee Directors and Corporate Governance: Managing the Dual Role Dilemma' (2017) 9 *NUJS Law Review* 89, 91

<sup>81</sup> The Companies Act 2013, s 166(2)

<sup>82</sup> Risham Garg, 'ESG and Directors' Duties: India's Emerging Framework' (2023) 4(1) *Journal of Business Law and Policy* 15, 22



### SEBI (AIF) Regulations, 2012: Duties of investment managers and trustees

The SEBI (Alternative Investment Funds) Regulations, 2012, place a fiduciary duty on the investment managers and trustees (or sponsors) of AIFs who "shall act in a fiduciary capacity towards its investors and shall disclose to the investors all conflicts of interest as and when they arise or seem likely to arise."<sup>83</sup> The duty of loyalty is encapsulated in this provision, which mandates that the manager actively manage or disclose any potential conflicts of interest and put the interests of investors, usually limited partners, above its own or related parties.<sup>84</sup>

According to Regulation 2(1)(w), the trustee or sponsor is principally in charge of supervision and governance, which includes making sure the AIF is run in accordance with fund documents and relevant laws.<sup>85</sup> Regulation 4(g) imposes a duty of competence and diligence on the sponsor or manager by requiring them to have the infrastructure and personnel needed to carry out an AIF's operations.<sup>86</sup> Regulation 20 establishes a duty of consistency and transparency by requiring the manager to make sure that the AIF's investments are made in line with its declared investment strategy and restrictions as communicated to investors.<sup>87</sup> The regulations clearly lay down the fiduciary duties of managers or sponsor in the context of AIFs.

### Private Placement Memorandums and Limited Partnership Agreements

The Limited Partnership Agreement (LPA) and the Private Placement Memorandum (PPM) are the main contractual tools used in the Indian AIF ecosystem to operationalize fiduciary duties and, frequently, to customize them above and beyond the SEBI-mandated minimum.<sup>88</sup> At the time of registration, all AIFs are required by the SEBI (Alternative Investment Funds) Regulations, 2012, to submit a PPM that includes information on their investment strategy, governance structure, fee arrangements, conflict-of-interest policies, and risk factors.<sup>89</sup>

Regulation 11(2)(a) incorporates a duty of transparency and informed consent into the PPM itself by requiring investors' consent for any significant changes to the fund's strategy or governance.<sup>90</sup>

### Fiduciary duties: Tension or Compatibility with ESG?

Particularly in the context of private capital structures like Alternative Investment Funds (AIFs), the question of whether Environmental, Social, and Governance (ESG) integration is compatible with fiduciary duty has generated an ongoing legal and financial debate.<sup>91</sup> While the fiduciary duties have been traditionally viewed only in the financial sense, some commentators view ESG as a diversion from the financial mandate, particularly when ESG initiatives have immediate financial consequences or are seen as ideologically aligned.<sup>92</sup>

<sup>83</sup> The SEBI (Alternative Investment Funds) Regulations, 2012, Reg 21

<sup>84</sup> Umakanth Varottil, 'Fiduciary Duties of Investment Managers in India: A Functional Approach' (2021) 14(2) NUJS Law Review 115, 118.

<sup>85</sup> SEBI (Alternative Investment Funds) Regulations 2012, reg 2(1)(w); *see also* reg 4(b).

<sup>86</sup> *Id.* reg 2 (g)

<sup>87</sup> *Id.* reg 20

<sup>88</sup> Umakanth Varottil, 'Private Equity and Fiduciary Governance in India' (2020) 13(1) Indian Journal of Law and Technology 42, 45.

<sup>89</sup> SEBI (Alternative Investment Funds) Regulations 2012, reg 3(4); Vinod Kothari Consultants, 'SEBI introduces enhanced disclosure and standardized reporting for AIFs', (*Vinod Kothafri Consultants*, 24 February, 2020),

<[https://vinodkothari.com/2020/02/standard-reporting-for-aifs/#\\_ftn3](https://vinodkothari.com/2020/02/standard-reporting-for-aifs/#_ftn3)> accessed 17 September 2025

<sup>90</sup> SEBI (Alternative Investment Funds) Regulations 2012, reg 11(2)(a)

<sup>91</sup> *Supra* note 84 at 81.

<sup>92</sup> Stephen Bainbridge, 'The Case Against Fiduciary ESG' (2020) 87(1) University of Chicago L Rev 45, 48.



However, a growing corpus of legal and economic literature acknowledges that because ESG factors impact portfolio risk, valuation, and long-term performance, they are clearly within the purview of fiduciary duty when they are financially material.<sup>93</sup>

### Global Legal Approaches to the nexus between ESG and fiduciary duties

#### United Kingdom, United States and European Union

Fiduciaries are not only allowed but also required, when financially significant, to take ESG factors, particularly climate-related risks, into account when performing their duties, according to the Law Commission's 2014 report.<sup>94</sup> The report made it clear that trustees must act sensibly and in the best long-term interests of their beneficiaries, which may include considering environmental and social risks when financially relevant, rather than trying to maximize returns at all costs.<sup>95</sup> Crucially, the Commission confirmed that systemic risks, including climate change, can be considered fiduciary concerns if they have the potential to impact long-term investment results.<sup>96</sup> For institutional investors who incorporate ESG into their investment decisions as part of risk management and value preservation strategies rather than as a matter of moral preference, this nuanced interpretation offers legal comfort.<sup>97</sup>

Due to divergent interpretations of the Employee Retirement Income Security Act (ERISA), the discussion surrounding ESG and fiduciary duty has become more heated in the US.<sup>98</sup> Under various administrations, the Department of Labor (DOL) has issued varying regulations, first prohibiting ESG unless it was financially justified and then, more recently, in 2022, confirming that ESG could be taken into account when it aligned with fiduciary principles.<sup>99</sup> The Securities and Exchange Commission (SEC) announced on June 12, 2025, that it was rescinding a number of proposed rulemakings with respect to the Commission's 2022 proposal, "Enhanced Disclosures by Certain Investment Advisers and Investment Companies About Environmental, Social, and Governance Investment Practices," where business development companies, registered investment companies, registered investment advisers, and some exempt advisers would have had to submit more details about how ESG considerations affect their investment choices.<sup>100</sup>

Legislation in the European Union has strengthened the fiduciary integration of ESG. Treating ESG as a crucial part of responsible risk management, the Sustainable Finance Disclosure Regulation (SFDR) requires asset managers and institutional investors to reveal how they

<sup>93</sup> Max M Schanzenbach and Robert H Sitkoff, 'Reconciling Fiduciary Duty and Social Conscience: The Law and Economics of ESG Investing by a Trustee' (2020) 72 Stanford L Rev 381, 412

<sup>94</sup> Law Commission (England and Wales), 'Fiduciary Duties of Investment Intermediaries' (Law Com No 350, 2014) paras 6.69–6.81

<sup>95</sup> *Id.* paras 6.80–6.81

<sup>96</sup> *Id.* para 6.79

<sup>97</sup> Benjamin J Richardson, 'Fiduciary Law and Responsible Investing' (2013) 36(2) UBC L Rev 205, 213

<sup>98</sup> Jed S Rakoff, 'Fiduciary Duty in the Age of ESG: ERISA's Evolving Boundaries' (2022) 45(3) Harvard Journal on Legislation 341, 343

<sup>99</sup> U.S Department of Labour, 'Final Rule on Prudence and Loyalty in Selecting Plan Investments and Exercising Shareholder Rights', (U.S DoL, 22 November 2022)

, <<https://www.dol.gov/agencies/ebsa/about-ebsa/our-activities/resource-center/fact-sheets/final-rule-on-prudence-and-loyalty-in-selecting-plan-investments-and-exercising-shareholder-rights>> access 17 September 2025

<sup>100</sup> Latham & Watkins LLP, 'SEC Withdraws Proposed Rule on ESG Disclosures for Investment Advisers and Investment Companies', (Latham & Watkins LLP, 26 June 2025), <<https://www.lw.com/en/insights/sec-withdraws-proposed-rule-on-esg-disclosures-for-investment-advisers-and-investment-companies>> accessed 17 September 2025



incorporate sustainability risks into investment decision.<sup>101</sup>

When combined, these global trends show a growing understanding that fiduciary duty and ESG are not mutually exclusive, but rather that they are increasingly required, especially in cases where ESG risks are systemically or financially significant. For countries like India, where institutional investing and AIF fiduciary standards are still developing, these precedents are persuasively relevant.

### Arguments for Reinterpreting Indian Fiduciary Law

A purposive interpretation of Section 166 of the Companies Act, 2013 provides a coherent doctrinal basis for incorporating ESG considerations within Indian fiduciary law.<sup>102</sup> Section 166(2) of the statute requires directors to act "in good faith in order to promote the objects of the company for the benefit of its members as a whole, and in the best interests of the company, its employees, the shareholders, the community, and for the protection of environment."<sup>103</sup> This clear mention of environmental and community protection already establishes a legal framework for integrating ESG principles into corporate governance, setting Indian law apart from models that are solely focused on shareholders.

Climate-related risks are therefore best understood as financially material investment risks, rather than externalities lying outside the scope of fiduciary concern.<sup>104</sup> The idea that ESG falls within, not outside, fiduciary boundaries has been further supported by the growing reference to sustainability by Indian courts and regulators when interpreting corporate responsibility,

such as in relation to Business Responsibility and Sustainability Reporting (BRSR) and CSR obligations.<sup>105</sup>

Investment managers, directors, and trustees—particularly those operating within the AIF ecosystem—face increasing legal, financial, and reputational exposure where foreseeable ESG risks are excluded from fiduciary decision-making.<sup>106</sup> The legal risk of omission, which holds fiduciaries accountable in future lawsuits for neglecting to take into account or take action on predictable ESG-related risks, especially those related to climate change, is one of the most significant new threats.<sup>107</sup> Therefore, failing to develop fiduciary standards not only erodes the legitimacy of governance but also goes against the fundamental fiduciary duty principle outlined in Section 166 of the Companies Act, 2013: acting in the long-term interests of beneficiaries.<sup>108</sup>

### Conclusion and Suggestions

This analysis demonstrates that incorporating Environmental, Social, and Governance (ESG) considerations into the regulation of Indian Alternative Investment Funds is not merely permissible, but fiduciary-consistent. ESG integration has become indispensable to AIF regulation due to its direct impact on financial risk, regulatory compliance, and long-term investor value. ESG factors, especially those related to climate change, can and should be regarded as financially significant and, as such, fall within the purview of a fiduciary's duties to act in the long-term interests of beneficiaries, according to a purposive interpretation of fiduciary duties under Section 166 of

<sup>101</sup> Regulation (EU) 2019/2088 on sustainability-related disclosures in the financial services sector [2019] OJ L317/1 (SFDR), arts 3–7

<sup>102</sup> The Companies Act 2013, s 166.

<sup>103</sup> *Id.* s 166 (2)

<sup>104</sup> Umakanth Varottil and Vikramaditya Khanna, 'Climate Governance and Corporate Law in India' (2023) 14 *Indian Journal of Corporate Law* 21, 30

<sup>105</sup> *Supra* note 6; see also The Companies Act, 2013, s 125

<sup>106</sup> *Supra* note 84 at 85

<sup>107</sup> Sarah Barker, 'Directors' Duties and Climate Risk: Australia's Emerging Legal Framework' (2020) 39 *Environmental and Planning Law Journal* 12, 15

<sup>108</sup> The Companies Act 2013, s 166(2)



the Companies Act, 2013 and the SEBI (AIF) Regulations, 2012.<sup>109</sup>

In terms of ESG, the Indian legal system that oversees AIFs is still disjointed and undeveloped. Private fund managers are not subject to legally binding ESG requirements, and relevant soft-law tools (like the SEBI Stewardship Codes) are still optional and only partially enforced. Accordingly, fiduciary duties and ESG integration should be understood as mutually reinforcing mechanisms for investor protection and sustainable capital formation.

The paper broadly proposes four major suggestions and policy recommendations:

(a) **Legal Clarification of Fiduciary Duty to Include ESG**

Financially material ESG risks, especially those with systemic or long-term relevance, are explicitly included in fiduciary obligations under Section 166 of the Companies Act and SEBI regulations, according to interpretive guidance issued by Parliament or SEBI.

(b) **Mandate ESG Disclosure for AIF Managers**

In accordance with developing international standards like TCFD and SFDR, the paper proposes that SEBI should provide unlisted investee companies and AIF managers with Business Responsibility and Sustainability Reporting (BRSR) or a customized ESG disclosure regime.

(c) **Develop an India-Specific ESG Taxonomy**

To direct fund-level ESG alignment, India requires a standardized, legally binding ESG taxonomy that is in line with global best practices but customized to national development priorities

(d) **Create Stewardship Responsibilities for Private Fund Managers**

The SEBI Stewardship Code for Mutual Funds and Insurers should serve as the model for a mandatory stewardship code for AIF managers that calls for accountability to LPs, transparency in voting, and involvement on ESG issues.

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<sup>109</sup> The Companies Act 2013, s 166(2); SEBI (Alternative Investment Funds) Regulations 2012, reg 21.



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