FUTUREPLUS

LINKING EXECUTIVE PAY TO ESG TARGETS

GUIDE

INTRODUCTION

Linking executive pay to sustainability targets aligns leadership incentives with long-term organisational goals related to environmental, social, and governance (ESG) priorities. This practice can help to ensure that executives are motivated to drive sustainable growth, reduce environmental impact, and promote social responsibility alongside financial performance.

It also signals to stakeholders (investors, employees, and customers) that the organisation is serious about embedding sustainability into its core strategy.

WHERE TO START?

The movement to tie executive pay to sustainability targets has been gradually gaining momentum. According to a Deloitte study, by 2022 more than 90 of the UK's FTSE 100 companies were incorporating ESG measures into their executive incentive packages.

DRIVERS

Executive compensation programmes are structured to not only attract and retain top talent but also to ensure their actions are closely aligned with the company's strategic priorities through a combination of rewards and incentives. Some of the leading drivers include:

- Signalling that ESG is a priority.
- Responding to stakeholder expectations.
- Achieving ESG commitments the business has made.
- Keeping pace with competitors.
- Responding to regulatory expectations or requirements.

MATERIALITY

Materiality is a measure of how important a piece of information is when making a decision. When we think about "what is material" in terms of sustainability factors for a business, what we really mean is: *what matters most, and how important are these issues to stakeholders?*

It's crucial that, when linking executive pay to sustainability outcomes, the selected ESG metrics are the ones that are most material for the business, i.e. those that will contribute to the largest, tangible real-world outcomes. Put well-defined ESG metrics in place before linking them to executive pay, ensuring you have the data and reporting capability in place to know *what* to measure, and *how* to measure it.

LOOK BEYOND THE C-SUITE

Setting company-wide targets, such as reductions in greenhouse gas (GHG) emissions, energy efficiency improvements, or improved anti-corruption outcomes, will also help to ensure that sustainability initiatives are prioritised throughout the business, not just by the Chief Sustainability Officer (CSO), with specific responsibilities allocated to the most appropriate teams.

When determining which roles should have their compensation tied to ESG goals, consider the alignment of these goals with the overall business strategy and the specific responsibilities of each role in achieving those goals.

THINK ABOUT TIME-SCALES

The timing of ESG goal inclusion in performance plans is crucial. While ESG initiatives often have long-term horizons, specific, short-term targets can and should be incorporated into annual plans. This approach ensures continuous progress, provides immediate feedback, and allows for adjustments to goals over time as the company's ESG journey evolves.

REVIEW GOALS REGULARLY

Regularly review ESG goals to ensure they continue to align with both financial and strategic objectives. Some goals may be achieved within a specific timeframe and subsequently removed from the compensation framework. Others, such as employee safety, may be considered evergreen and require ongoing monitoring. Dynamic goals, such as those related to Diversity and Inclusion (D&I), may need to be adjusted over time to reflect evolving best practices and organisational priorities.

From the outset, establish a clear understanding of the desired timeframe for achieving each ESG goal, if applicable

USING FUTUREPLUS TO LINK ESG OUTCOME WITH EXECUTIVE PAY

The FuturePlus scoring system and Roadmap provide the ideal solution for monitoring company targets and achievements. To speak to the team about using your FuturePlus dashboard to track progress, get in touch with the team: info@future-plus.co.uk.