BEYOND PROFIT

Using ESG Metrics in Executive Compensation Plans

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Introducing Today's Speakers

Brett A. Herand is a managing director at Pearl Meyer. Specializing in executive compensation, he works with boards and management on issues related to performance measurement and value creation, incentive plan design, and technical advisory work with respect to tax, accounting, and SEC regulatory issues. Brett works with public and private companies across many industries, including financial and diversified services, technology, and manufacturing.

Prior to joining Pearl Meyer in 2008, Brett spent five years in Mercer's human capital practice, working in executive remuneration. He holds a bachelor's degree in finance from the W.P. Carey School of Business at Arizona State University.

Brooke Fernandez is the General Manager of Main Data Group (MDG), a provider of executive compensation benchmarking and corporate governance analytics. The MDG team continues to innovate upon a comprehensive proxy database and offers custom research services to top-tier companies and Executive Compensation firms worldwide. MDG’s mission is to empower executive compensation professionals with meaningful, comprehensive total rewards and corporate governance information through the industry’s most cost-effective and easy-to-use data platform. She holds a bachelor's degree from UCLA and a master's degree from the Stanford Graduate School of Business.

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What Does ESG Mean, Anyway?

A Primer on Key Environmental, Social and Governance Measures and Linkages to Executive Compensation Plans

A Quick Primer Regarding ESG Metrics

Environmental Social & Governance metrics used in executive compensation plans have been growing steadily

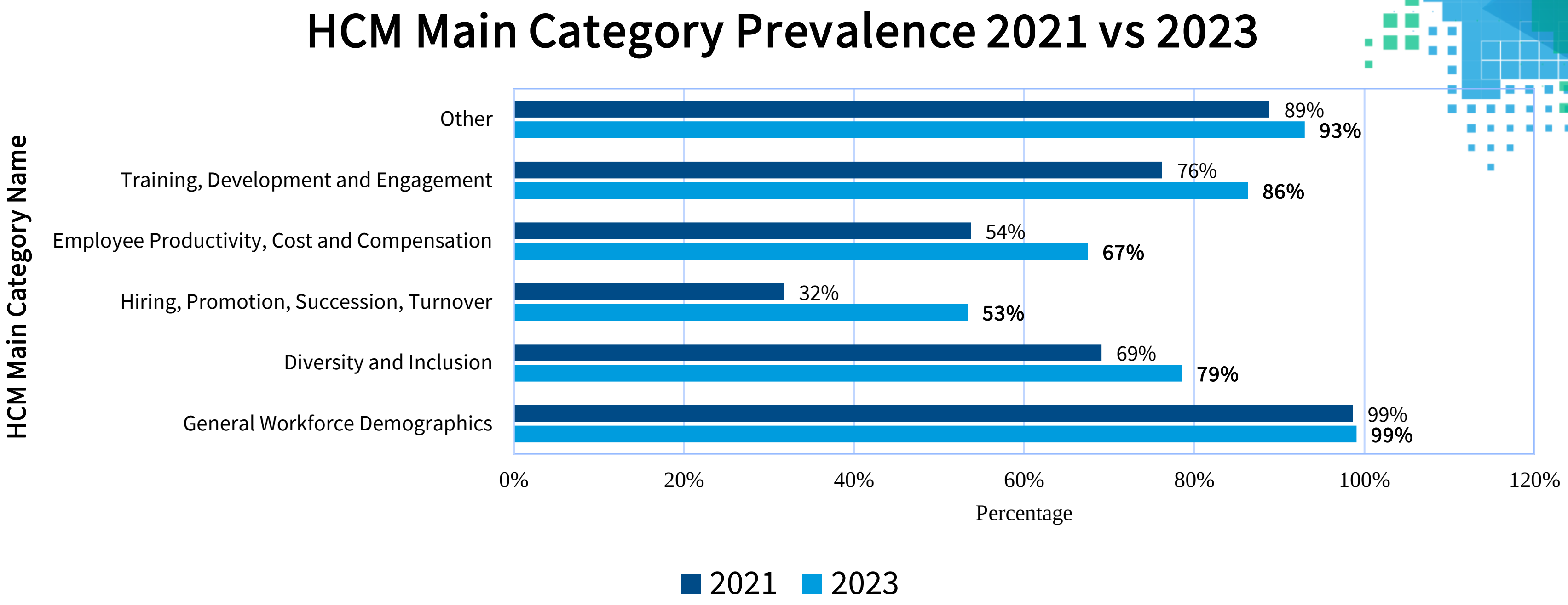
ESG Incentive Metrics are NOT new: Classic vs Contemporary ESG measures

- Classics: Safety, Customer Satisfaction
- Contemporary: Carbon Neutral by 2050
- Other examples: DEI, Turnover, etc.

Incentive Plans are NOT the Only Way to Focus on ESG

- Established enterprise risk management policies
- Corporate focus through required disclosure and regulation
- Current HCM disclosure
- Proposed Environmental disclosure
- Non-US requirements
- Individual focus through career opportunity
- Board reporting and oversight

SEC HCM Disclosure Requirement Year 3



Trends in Social disclosures

- Lots of what, not a lot of "how"
- Rarely anything negative disclosed here (i.e. turnover)

Proposed Environmental Disclosure

On March 6, 2024, the US Securities and Exchange Commission (SEC) adopted new rules that require publicly listed companies to disclose climate-related risks that could significantly impact their business, operations, or financial condition. The rules also require companies to explain how they manage these risks and any related corporate targets.

The new rules include the following requirements:

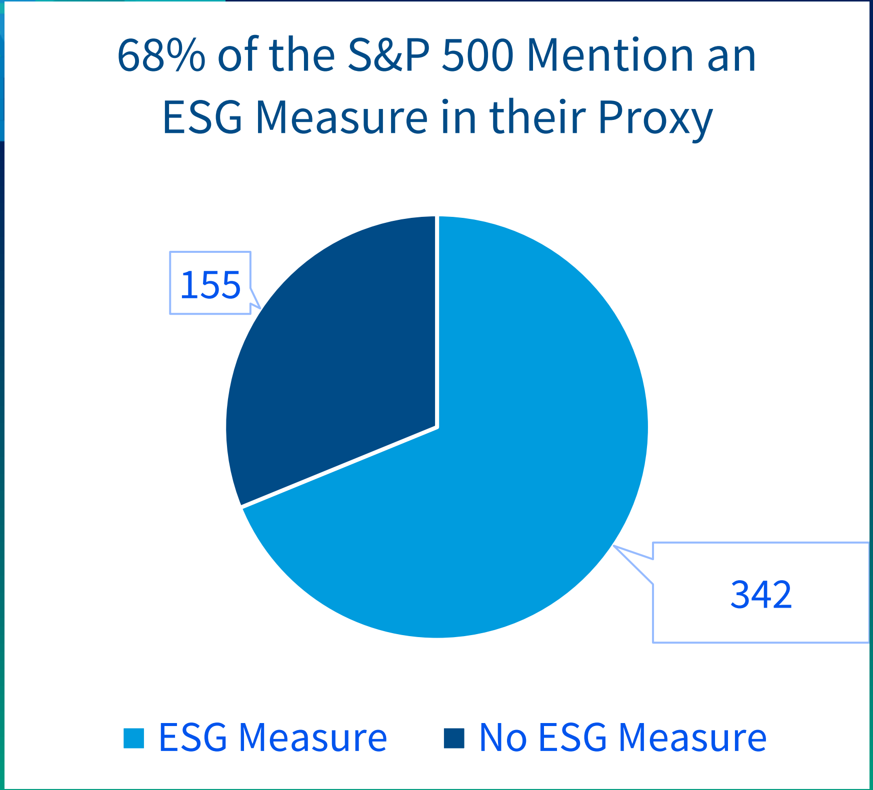
- Disclosures about climate-related risks that are likely to have a material impact on a company's business
- Disclosures about how companies are managing climate-related risks
- Disclosures about any related corporate targets
- Disclosures about activities to mitigate or adapt to climate-related risks, such as scenario analysis, transition plans, or internal carbon prices
- Oversight of climate-related risks by the board of directors
- A role for management in assessing and managing climate-related risks
- Disclosures about costs from severe weather events

Current Trends

Prevalence of ESG Measures Across the S&P 500

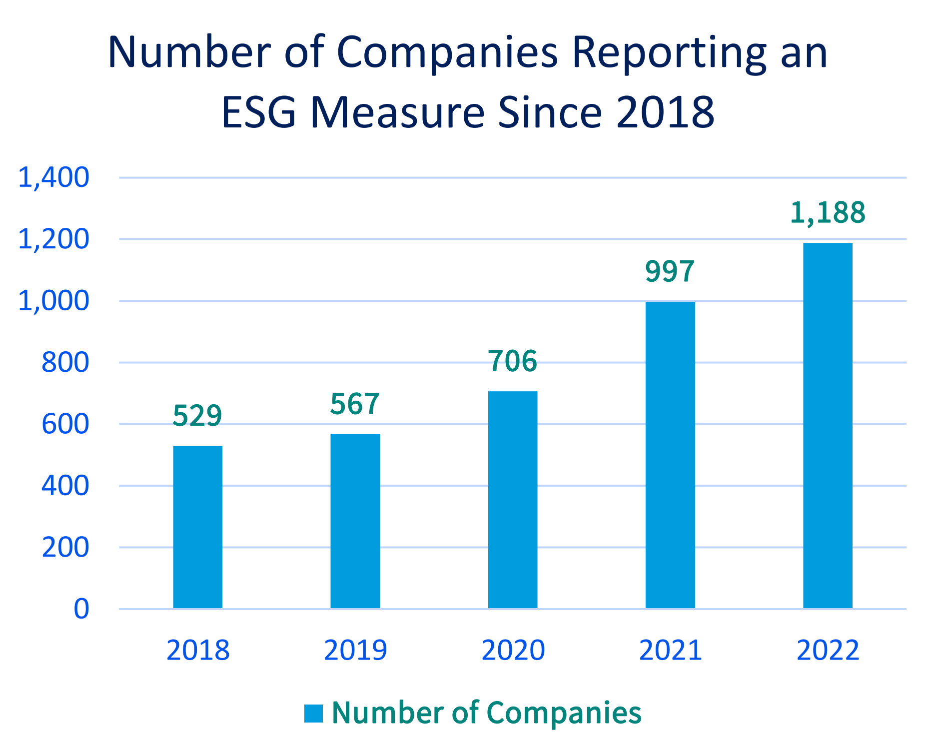
Drivers of Disclosure:

- Asset/Revenue size of company in public facing sectors like retail, CPG, energy, etc.
- Consumer-facing organizations (B2C) more prevalent than B2B
- Pressure to disclose is felt more keenly by employee/customer businesses under external forces



Prevalence of ESG Measures Across the Russell 3000

Smaller companies less likely to have ESG metrics in incentive plans

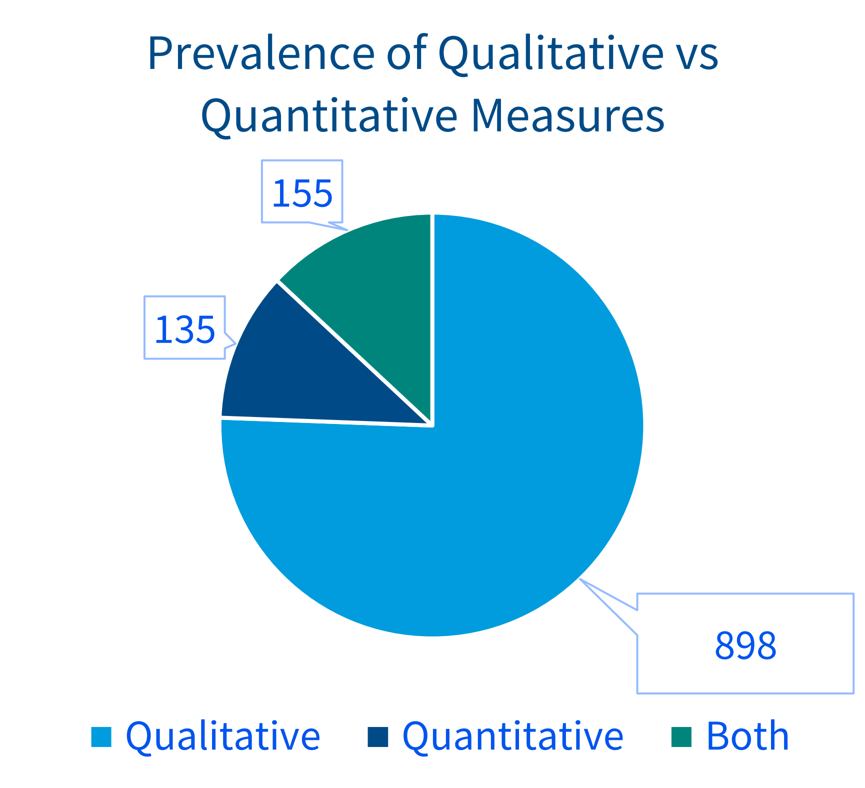


Prevalence By Type Across the Russell 3000

Qualitative Measures Still Rule the Day

Fact vs Fiction: designing an effective, measurable metric still proves challenging

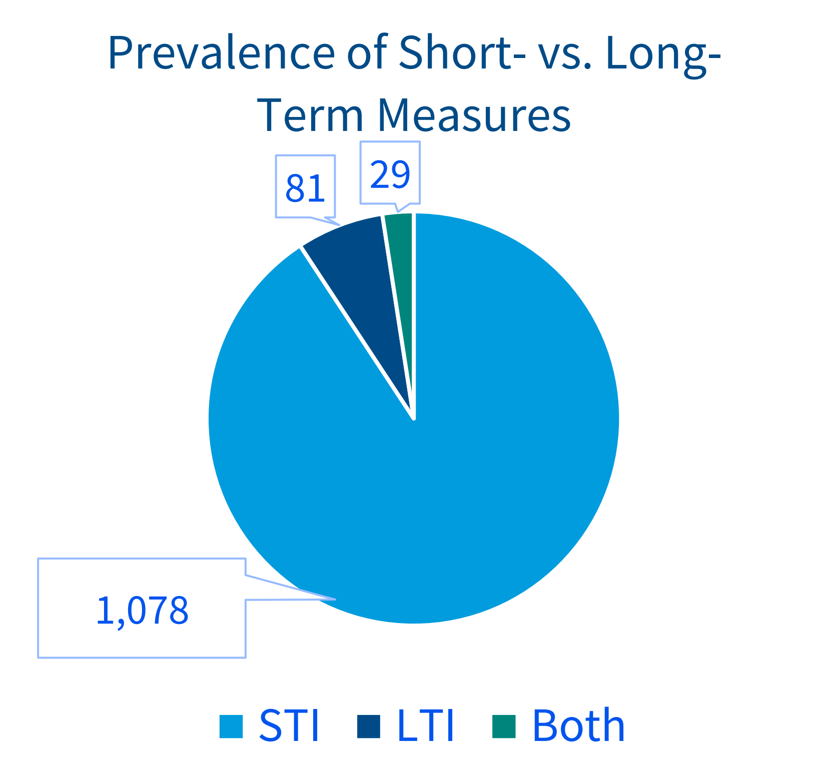
- Quantitative measures are riskier
- Companies revert to qualitative measures to reduce risk
- Is it a signaling exercise?



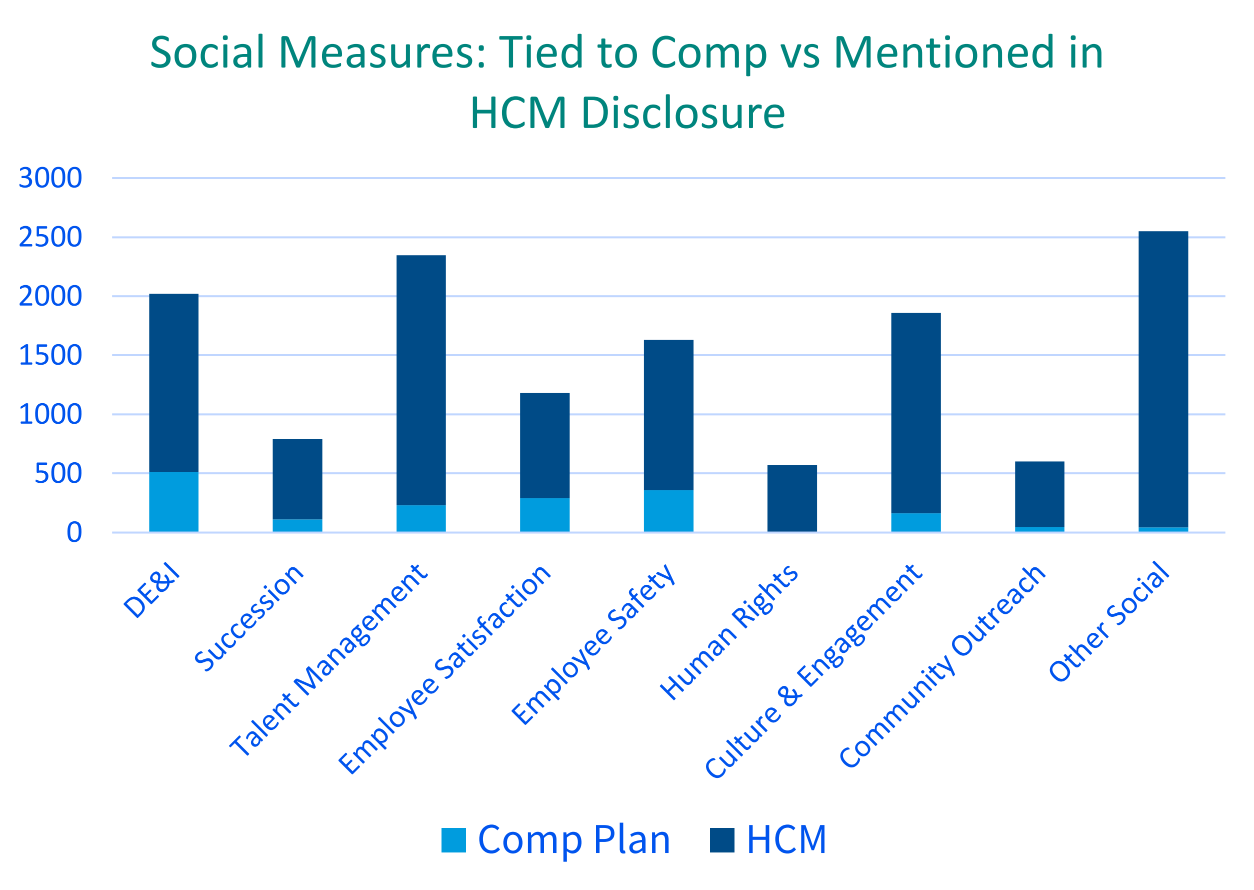
Prevalence – Long-term, Short-term or Both?

Short-term Incentives by far the most prevalent

- Incentivize incremental progress and add medium-term benchmarks
- Disconnect between long-term incentives being financially driven, quantitative measures and short-term qualitative measures that are more palatable to adopt



Greenwashing?
Virtue Signaling?



Where Do We Go From Here?

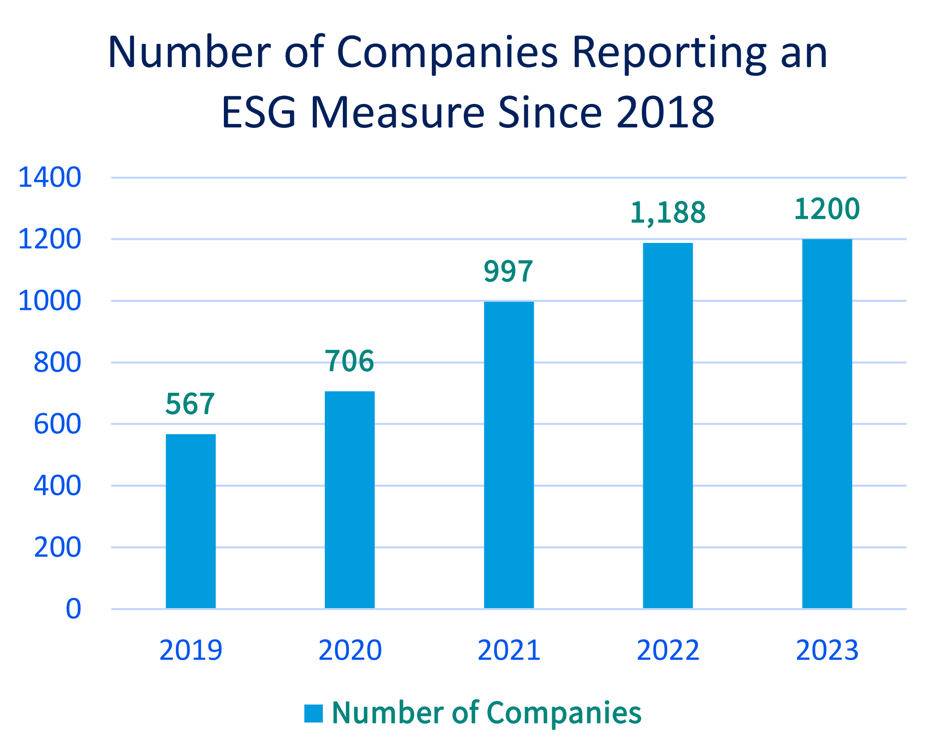
Has the Backlash Begun?

- Harvard admissions
- Undesirable press coverage and boycotts
- State-based legislation
- Political campaigns

What does the data say?

Early look at filers for 2024 season

- Early findings for 2024 indicate a flattening of the curve
- Hovering around 40%



Q&A

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POLL QUESTION

Does your company track and externally report some element of its ESG impact?

1. Yes
2. No
3. Not applicable

POLL QUESTION

Does your company include ESG as an incentive compensation metric?

1. Yes
2. No
3. No. But it’s been discussed it at the Board level
4. Not applicable

POLL QUESTION

What percentage of the Russell 3000 will have an ESG measure in their comp plan in 5 years?

- <30% (less than today)
- Flat with today
- At or near 50%
- More than 50%