Video Segment 5: Executive Compensation and ESG Performance

NOTE-TAKING GUIDE

"We're at the cusp of pay policies getting infinitely more complicated for boards to manage." – Brian Stafford

Under the influence of ESG, the way that boards of directors decide how executives are paid for their performance is less about the financial value delivered to shareholders and more about the broader value to all stakeholders -- this idea of doing well by doing good. How do the following themes from the discussion connect to this idea of tying executive compensation to ESG performance?

Diversity, Inclusion and Sustainability Targets:

S&P 500:

Freeport-McMoRan:

Caroline Flammer Research:

According to Dr. McDonnell, the fact that CEOs and other executives get more credit for strong corporate performance leads to “real disparities” between top management and lower-level employees. What are some of the operational and societal problems that result from pay inequality within companies?

1.

2.

3.

4.

5.

If stakeholders (customers, employees, investors, and others) judge companies for how well they do meeting Environmental, Social and Governance goals, it likely makes sense to tie executive compensation to those goals. Professor McDonnell says, “I think it’s one of the most exciting potential tools that firms could use if they are truly committed to ESG performance over the long-term.” How do you feel about these types of financial incentives to encourage managers – and possibly even employees – to do the right thing for the environment and society? Do you think it’s a corporate step in the right direction or a capitalist cop-out?

THE LANGUAGE OF BUSINESS

Capitalism

CEO (Chief Executive Officer)

Company

Corporate Board of Directors

Corporate Culture

Corporate Governance

Corporation

Diversity

Executive Compensation

Executive Team

Inclusion

Industry

Operations

Organization

Performance

Public Company

Senior Leadership

Shareholder

Sustainability

Teams

Worker Output

Aspirational Targets: Goals that suggest a company is open to doing things differently.

Caroline Flammer: Associate Professor at Boston University who researches corporate governance.

Corporate Governance (*see video glossary links)* The rules, practices and processes used to direct and manage a company. A company's board of directors is the primary force influencing corporate governance.

Disparity: A social or economic condition that is considered unfairly unequal, like disparities in pay.

ESG: ESG stands for Environmental, Social and Governance and refers to a system for how to measure the sustainability of a company. It is an evaluation of a firm's beliefs and attitudes about social and environmental factors. Companies, and their corporate boards of directors, are thinking hard about how to incorporate ESG factors into their business strategies to appeal to investors, customers and other stakeholders. And investors are turning to ESG rating firms and others to screen their investments on these various factors. Effective and evolving governance is helping firms meet their ESG goals.

ESG Metric Scores: The scores used to assess a company's exposure to environmental, social and governance risks – for example, is a company positioned to perform well within the climate crisis or is this an area of risk?

ESG Performance Incentives: Motivational tools that might inspire an executive, for example, to strengthen a company's ESG commitment.

Firm: Another word for company.

Freeport-McMoRan: A public American mining company based is Phoenix. Arizona.

Greenhouse Gas Emissions: The rising levels of carbon dioxide and other heat-trapping gases that are emitted from factories, vehicles and other sources of fossil fuels and are thought to be damaging the planet.

Index Performance: A measurement of the price performance of a group of stocks representing a segment of the market.

Market Outperformance: When a stock outperforms a specific index or the overall market.

Market Price: The price at which an asset or a service can be bought or sold.

Metrics of Performance: Measurements of the behavior, activities and performance of a business.

Pay-for-Performance Compensation: A compensation program where employees are paid based on their performance in their role.

Pay Inequity: When one group in a company is compensated differently than another.

Performance Metrics: Goals specified by a company for which its executives will be rewarded – in this case, environmental or social objectives.

S&P 500: The Standard and Poor's 500 is a stock market index tracking the performance of 500 large companies listed on U.S. stock exchanges.

Stakeholder: A person with an interest or concern in a business, including owners, managers, board members, employees and investors.

Tobin's Q: Also known as "the Q Ratio," this is a measurement of whether a business is overvalued or undervalued.

Total Return to Shareholders: A measure of the performance of different companies' stocks and shares over time.

Worker Morale: The attitude and level of satisfaction an employee has on the job.

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