Executive Compensation Guidebook for Climate Transition

Co-hosted by Willis Towers Watson and Climate Governance Initiative, a collaboration with the World Economic Forum

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Today’s speakers and agenda

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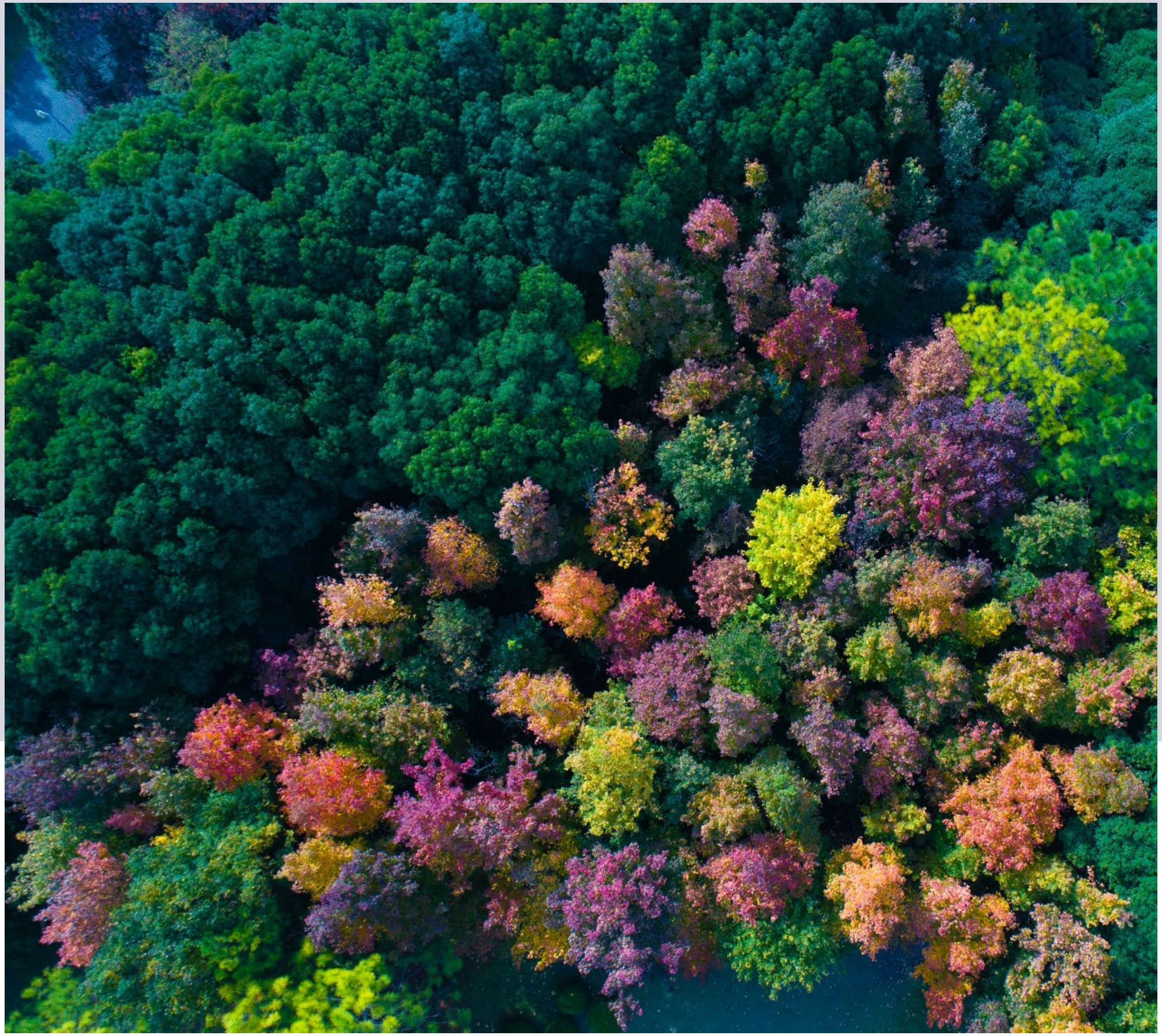
Agenda

▪ Opening remarks by Natasha Fortuin	▪ Business, investor and regulatory context ▪ Executive compensation guidebook overview ▪ Best practices, including incentive metrics ▪ Industry highlights	▪ Panel discussion moderated by Shai Ganu	▪ Closing remarks by Karina Litvack

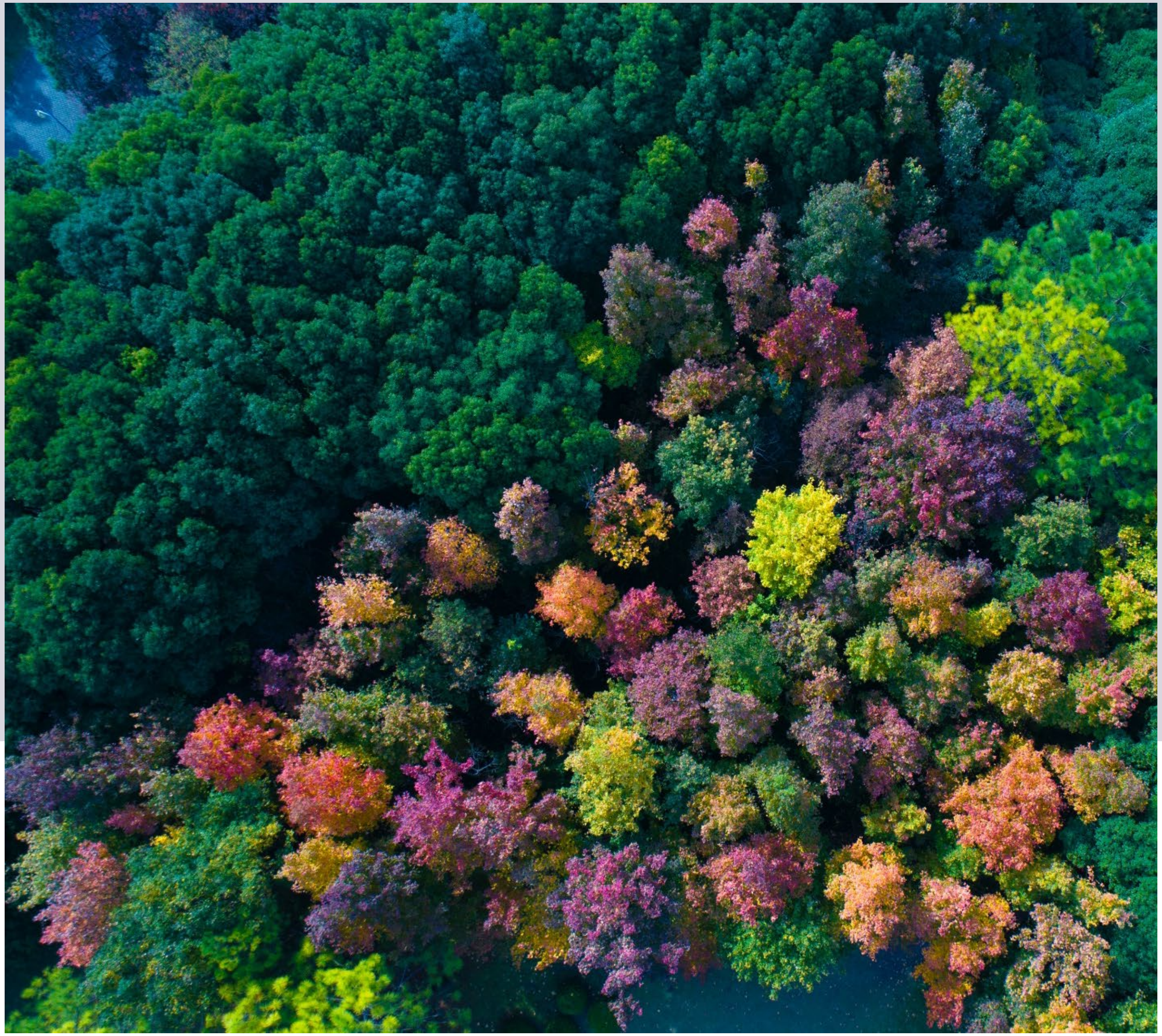
Executive Compensation guidebook



Guidebook overview

- Executive Summary
- Business, investor and regulatory context
- Best practices in driving climate objectives with executive compensation
- Market insights: Climate metrics in executive incentive plans
- Industry deep-dives

Business, regulatory and investor landscape



Act now, while you still have a competitive advantage

Business Context

- **Climate challenges present opportunities** for many businesses to innovate and offer zero-carbon alternatives
- **Customers and employees** are making climate-informed decisions
- Forward-thinking businesses transform opportunities into **competitive advantage**

"It is the board and the CEO that guide the direction. What has become apparent now is that climate needs to be embedded into strategy."

Investor Perspectives

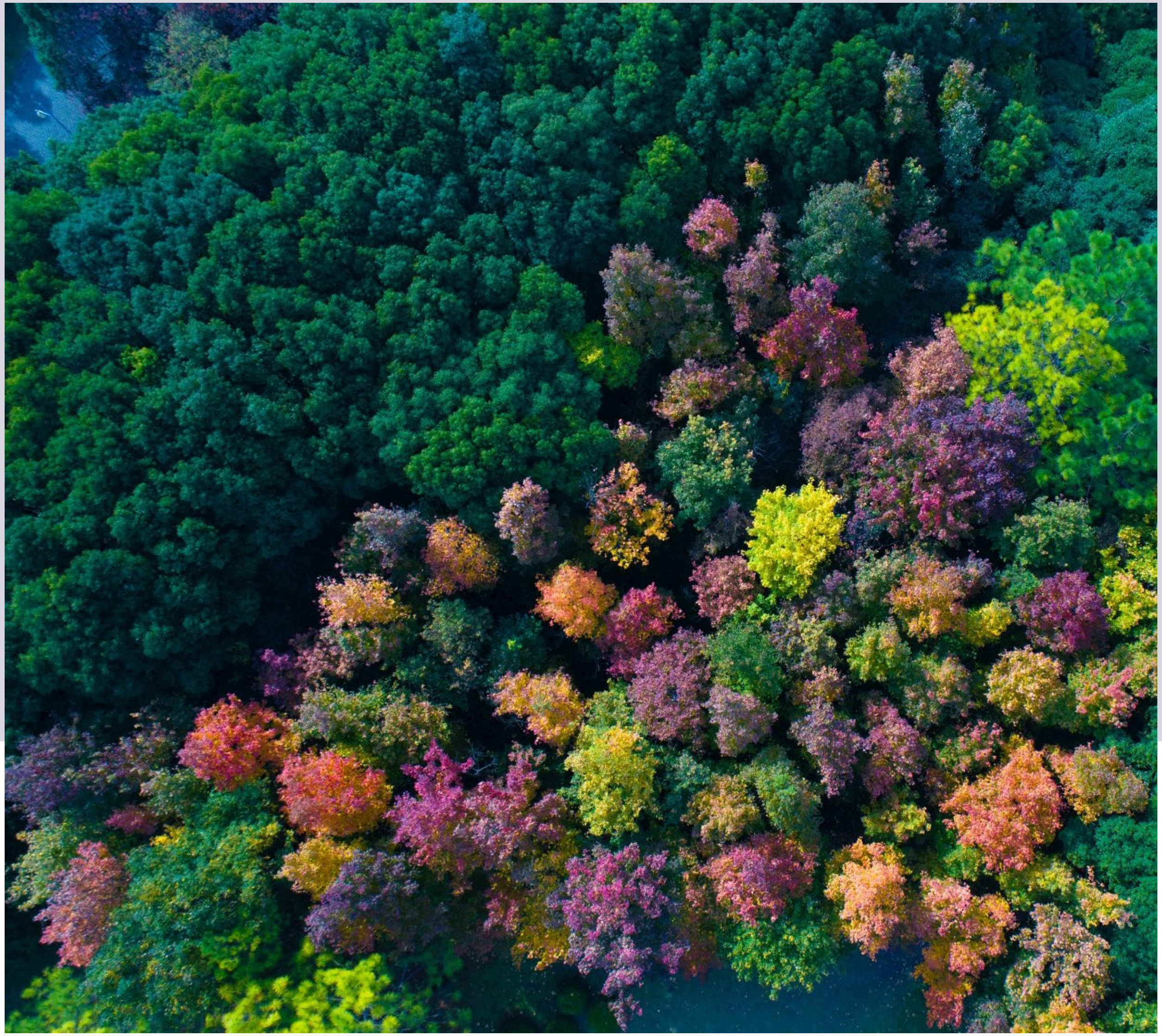
- Investors perceive climate transition as **investment risk and opportunity**
- Business viability in a low-carbon economy is key in assessing sustainable value creation
- Incentive compensation is viewed as a **driver of climate transition**

If you have a 2030 or 2050 plan [on emissions reduction] and it's meaningful for the company, then why shouldn't the plan be broken down into shorter-term targets and anchored into the incentive remuneration plans? Your CEO won't be here in 2050, but they can certainly shape the roadmap to get there."

Regulatory Progress

- **Europe is leading** global transition to net-zero by 2050
- Significant progress has been made since 2020, particularly in North America, albeit progress and commitment by country varies
- TCFD recommends:
  - Disclosing metrics used to assess climate risks and opportunities, and performance against targets
  - Including scopes 1-3
  - Embedding climate risk in broader organizational ERM

Best practices in driving climate objectives



Step-by-step guide to driving net-zero ambitions through executive pay

1 Align climate priorities with business strategy

2 Climate goals tied to the net-zero vision

3 Select the right metrics

4 Fit-for-purpose incentive design

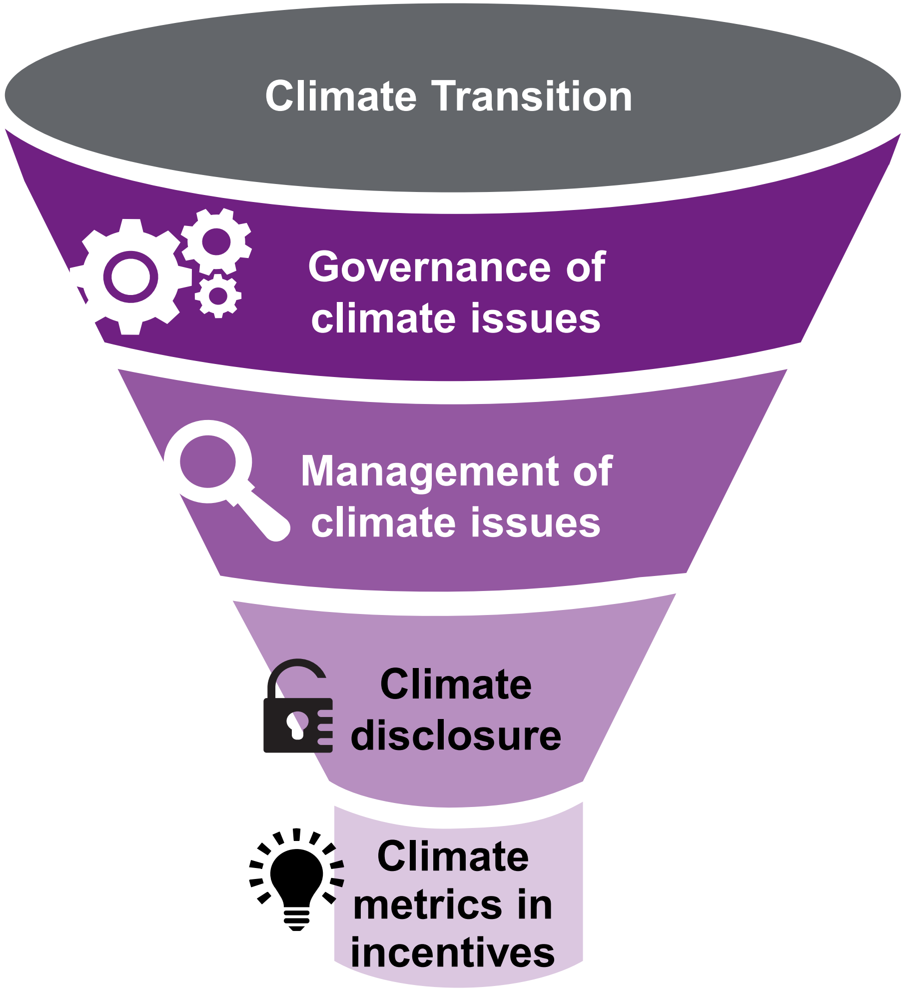
5 Tell the story with disclosures

6 Evolve and learn over time

The board's governance role is to challenge management each step of the way and ensure engagement of all key stakeholder groups

A practical approach to selecting the appropriate metrics

1. Prioritize the spectrum of issues the company needs to be addressing
2. Determine approach and level of oversight required at the Board vs. Committee level
3. Collaborate with Management on strategy and plan for addressing climate priorities
4. Educate investors and the public on the issues – why addressing them is key to ensuring sustainability and long-term value creation, and how the company plans to deliver on its goals
5. Demonstrate commitment to initiatives by incorporating metrics that are specific and measurable and goals that are stretch but achievable, and time-bound



Principles to consider when selecting the right metrics

Materiality ✓	▪ Select metrics that are material to the business; those that contribute to long-term value creation and risk mitigation, and are central to the climate strategy ▪ They must also be material to the individual participants in order to be effective in incentivizing behavior/action
Measurability ✓	▪ Use metrics that can be reliably measured, quantified and scaled; potentially also allowing for independent audit of performance achievement ▪ This also allows for comparison across peers and industries, and to track meaningful progress over time.
Breadth ✓	▪ Take a broader view of climate performance beyond simply capturing carbon emissions, aligning to company's net-zero strategy, such as tying into industrial or commercial milestones
Comparability ✓	▪ Where possible, metrics should be defined using standard or widely adopted methodologies (e.g., definitions validated by third parties for greater comparability) ▪ Climate metrics that are captured in ratings and indices published by reputable organizations are a good starting point
Clarity ✓	▪ Important to provide clarity, transparency and consistency ▪ Seek independent verification for measurement ▪ Increasing convergence around core set of Scopes 1, 2 and 3 indicators, as mandatory reporting gains support (e.g., IFRS Foundation mandating sustainability reporting) and leading actors collaborate to develop a common set of metrics

WTW's design spectrum to incorporate metrics into executive compensation

Lower impact to organization, easier to implement

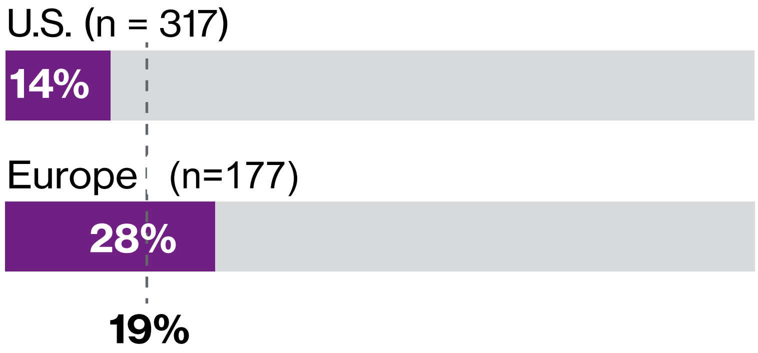
	Incentive Design Description
Underpin	Include threshold or basic level of performance required for some or all of the payout under other metrics to occur — STI or LTI
Individual performance rating modifier	Include a climate modifier under the individual elements of the STI or LTI to modify the payout up/down by a certain percentage
Company performance modifier	Include a climate modifier to overall STI or LTI formula that modifies the payout up/down by a certain percentage for all participants
Weighted metric in STI	Include a quantitative metric (e.g., carbon emissions) into the STI payout formula
Weighted metric in LTI	Include a quantitative metric (e.g., carbon emissions) into the LTI payout formula
Incentive funding formula	Incentive pool derived from financial measure adjusted for carbon charge (e.g., carbon cost added to cost of capital in economic profit calculation)
Standalone incentive plan	Introduce a separate incentive plan (e.g., hyper-long term aligned with sustainability strategy, or plan with timeless emissions goals)

Greater impact to organization, more disruptive

There is significant room for improvement in the adoption of climate metrics

All plans

19%
of **companies** incorporate climate and broader environmental measures in their incentive plans.

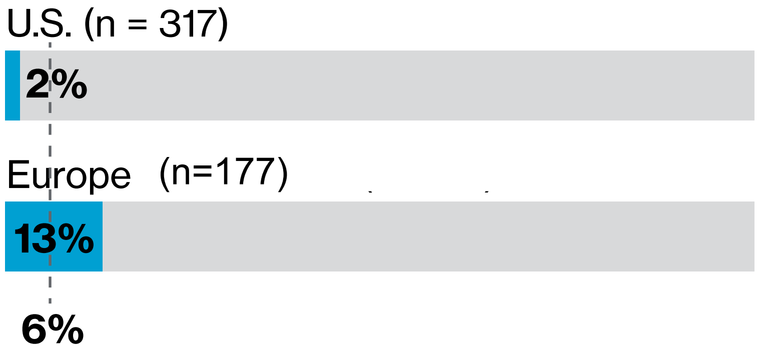


STI plans

16%
of **companies** incorporate climate and broader environmental measures in their STI plans.

LTI plans

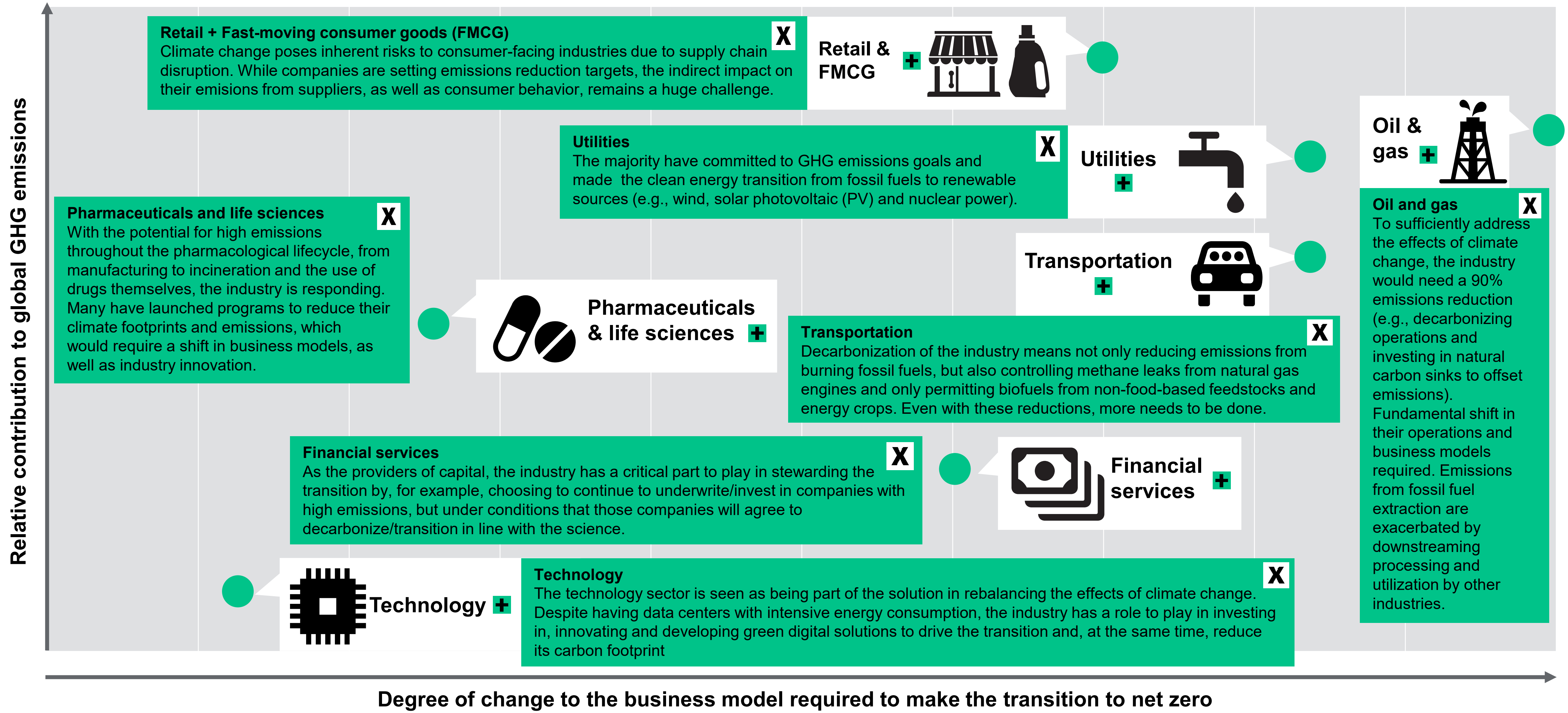
6%
of **companies** incorporate climate and broader environmental measures in their LTI plans.



- US is based on companies in the S&P 500; Europe is based on companies in the following indices: FTSE 100 (UK), IBEX 35 (Spain), BEL 20 (Belgium), DAX 30 (Germany), AEX 25 (Netherlands), CAC 40 (France), SMI 20 (Switzerland), ISEQ 20 (Ireland) and MIB 40 (Italy)
- Including the following industries: Fast Moving Consumer Goods, Financials, Health Care, Information Technology, Oil & Gas, Retail, Transportation, Utilities
- All analyses are based on FYE between June 2020 – May 2021 (except where latest proxies have not yet been published)

n = number of companies

The impact by industry varies notably, but all have a marked role to play



One size does not fit all – best practice examples

Standard Chartered

- **STI Metric (10%): "Purpose and people"** – a strategic metric within the bonus scorecard. One of the three targets is: "Exceeded our 2020 target in financing services for renewable energy projects and on track to the sustainability aspiration target of $35B; all other sustainability measures also at or above target.
- **LTI Metrics (15%):**
  - **"Sustainable finance"**
    - Develop and implement a framework to **align our financial services with net zero emissions by 2050**, and deliver 2023 targets consistent with that plan
    - **Provide $35B (cumulative) worth of project financing services**, M&A advisory, debt structuring, transaction banking and lending services **for renewable energy** that align to our verified green and sustainable product framework
    - **Only provide financial services to clients that are less than 80% dependent on earnings from thermal coal** (% corporate EBITDA)).
  - **"Responsible company"**
    - Reduction in property emissions of 10% annually
    - Reduction of flight emissions of 25%
    - Offset 95% of all residual emissions from our operations

AstraZeneca

- **LTI Metric (10% - Performance Share Plan): CO_2 Emissions (Delivery of Ambition Zero Carbon commitments)**
  - Reduction of **Scope 1 and Scope 2 greenhouse gas (GHG)** emissions by 2025, measured against 2016 baseline.
  - The **threshold target is 60% reduction** and the **maximum is 68% reduction**.
  - Targets and assessment of performance to be determined in line with the World Resources Institute/World Business Council for Sustainable Development GHG Protocol methodology for accounting and reporting of emissions footprint
  - Introduced following CEO's announcement at the World Economic Forum in January 2020 of their Ambition Zero Carbon programme: the commitment to have zero carbon emissions from operations across the world by 2025 and ensure our entire value chain is carbon negative by 2030.

Source: Company public disclosures on executive incentive design.

One size does not fit all – best practice examples *(continued)*

Unilever

Example of climate and broader environmental targets within a scorecard, with a material weight in the LTIP

- **LTI Metric (25%):** detailed scorecard weighted 25% of the LTIP called the Sustainability Progress Index, which the Committee uses to assess the company's progress against the Unilever Sustainability Living Plan (USLP). This captures targets such as:
  - Reduce carbon dioxide emissions from energy from factories per tonne of production vs 2008 baseline (%)
  - Purchase crude palm oil from physically certified sustainability sources (%)
  - Achieve Leader/A ratings (number) — relating to a number of global rating providers (e.g., DJSI, CDP Climate, CDP Water, CDP Forests, GlobeScan).

Xcel energy

Example of a clear and quantifiable emissions reduction metric with a material weight in the LTIP

- **LTI Metric (30%):** weighted 30% of Performance Shares
  - The metric is based on reduction in Carbon Dioxide emissions below 2005 levels associated with electric service.
  - 2019-2021 performance is measured at the end of a 3-year performance period as follows (straight-line interpolation in between):

	Threshold	Target	Maximum
	43% reduction	47% reduction	51% reduction or above
Payout	30%	100%	200%

Source: Company public disclosures on executive incentive design.

In summary

Do's	Don'ts
Continuously monitor and evolve measurement of goals	Add climate metric to incentive plans as a "check-the-box" exercise
Consider company-specific climate transition strategy and metrics	Blindly follow market practices and what "leading companies" do
Measure short-, medium- and long-term progress towards net-zero	Set annual goals with no tie-in to the overall net-zero vision
Select metrics and goals that are science-based, clear, ambitious, transparent and consistent	Use judgment-based or ambiguous metrics or goals
Tell the story of how executive compensation drives climate transition with robust disclosures	Manage annual reports, executive compensation disclosures and ESG/climate reporting in silos

Panel Discussion

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