SUSTAINABLE PAY:

HOW TSX 60 COMPANIES COMPENSATE EXECUTIVES FOR SUSTAINABILITY PERFORMANCE

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by

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1. FOREWORD

By Toby Heaps

April 20th, 2010 was the 'deepwatergate' moment for corporate governance. That was the day when BP's Deepwater Horizon drilling rig exploded, killing 11 people, spilling millions of barrels into the Gulf of Mexico, causing untold environmental harm and ultimately costing BP tens of billions of dollars in damages. Six months later, Bob Dudley, BP's newly minted group chief executive, wrote an internal memo to his staff declaring that safety would be the sole criterion for rewarding employee performance in its operating business for the fourth quarter. One wonders what would have happened had a savvy institutional investor taken a look at BP's financial sanctions from the US Environmental Protection Agency (EPA) and the Occupational Safety and Health Administration (OSHA) before the Deepwater Horizon explosion. In the five years leading up to the incident, BP had been hit with more EPA and OSHA fines and penalties than Shell, Chevron, Exxon Mobil and ConocoPhillips combined. If BP had felt heat from its investors and moved earlier to realign compensation incentives, could the lives lost, ecosystem damage and balance sheet destruction have been prevented?

We will never know for sure, but we do know that despite the predictable irrationality of humans in many contexts, pay remains a powerful motivator. What we pay people to do really matters and is at the absolute core of corporate governance. So it stands to reason that we should make sure we are paying people to do what really matters.

We live in a globalized era in which natural resources and reputation matter like never before. On the backs of the burgeoning billions of middle class consumers, real commodity prices have rocketed by 147 per cent in just the past 12 years, making natural resource productivity increasingly relevant to a company's ability to create value. In stark contrast to just a few decades ago, the majority (80 %) of a company's share price is now based on a bubble of intangible assets, which expands or contracts largely based on reputation. As a result, natural resource use and the social and environmental factors that impact reputations are strategic imperatives for public companies. That's why investors are beginning to demand that companies better align relevant sustainability factors with compensation.

Against this backdrop, Coro Strandberg's first-of-its-kind systematic study into the sustainable pay practices of TSX 60 companies is a welcome injection of coherence. Her finding that 57 per cent of companies already consider sustainability factors in the annual incentive plan shows that the Rubicon has been crossed. While sustainable pay is still a wild west, this report contains many sensible recommendations for harnessing its power to build better companies and a better world.

Toby Heaps is the co-founder and CEO of Corporate Knights, the company for clean capitalism. Corporate Knights publishes the world's largest circulation magazine focused on business sustainability, empowers investors with quantitative sustainability insights, and co-ordinates the Council for Clean Capitalism, a CEO-led group catalyzing smart and efficient public policy.

Sustainable Pay

How TSX 60 Companies Compensate Executives for Sustainability Performance (2011)

60

Canadian Public Companies Analyzed

Consider Sustainability in Annual Incentive Plan?

- **57%** DO
- **35%** DO NOT
- **8%** DO NOT DISCLOSE

24

Companies Bonus for Annual Sustainability Performance

20%

Is Average Weight for Sustainability Factors Compared to 80% for Financial Factors

0

Companies Bonus for Long-term Sustainability Performance

8

Companies Set Sustainability Targets for Executive Performance

Leaders and Laggards

2 Leading Sectors: Extractives and Financials

2 Lagging Sectors: Services and Consumer Goods & Services

6

Common Metric Categories

- Safety
- Environment
- Employees
- Customers
- CSR Brand
- Community / Stakeholders

Top 2 Metrics = Safety (injuries) and Environment (spills & leaks)

Unique Global Metrics for Sustainable Pay

- Energy Use and GHG Reductions
- Green Product Targets

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2. EXECUTIVE SUMMARY

Sustainability is an important global business driver and is making its way into corporate boardrooms. Mounting evidence shows firms that invest in improved sustainability practices outperform their competitors. There is growing awareness that emerging sustainability risks can have a material impact on company performance. Recognizing these links, companies increasingly integrate sustainability performance objectives and targets into their performance management systems.

To better understand this trend to integrating sustainability into performance management programs, Coro Strandberg of Strandberg Consulting conducted a review of the degree to which companies listed on the TSX 60 Index integrate sustainability factors into executive incentive compensation packages. There are no universal standards that link sustainability metrics to executive pay so boards, executives and their compensation advisors lack benchmarks and best practice to guide their efforts in this area.

In the Canadian context, this research will help bridge this gap and define a roadmap for improved practices in executive sustainability compensation. Over time, increasing disclosure, analysis and demonstrated results will help to advance practice in this emerging compensation field.

Strandberg Consulting compiled a database of the executive sustainability compensation approaches utilized by the 60 companies listed on the TSX 60 as of August 31, 2012.

Information was extracted from public 2012 management information or proxy circulars, which provided details pertaining to 2011 compensation practices[1]. Executive compensation information was found within the compensation discussion and analysis (CD&A) section which describes and explains the company's executive compensation approach and the basis on which compensation decisions are made.

The study focused on annual and long-term (typically beyond three years) incentive awards that provide financial/monetary bonuses when pre-established corporate sustainability performance goals are achieved. The research covered:

- The decision process. (Who makes the compensation decisions – committees or boards?)
- Sustainability (non-financial) factors included within the annual incentive plan, including the category, metric and weighting.
- Incentive plan eligibility.
- Use of a balanced scorecard approach.
- Sustainability (non-financial) factors included within the long-term incentive plan.

The study found that over half (57% or 34) of the listed companies referenced sustainability factors in executive compensation in their disclosures. This number drops to forty per cent (24)

[1] Note that the 2012 compensation programs will be disclosed in 2013 Management Information or Proxy Circulars in the coming months. Thus, this study focuses on corporate practices from two years ago.

for those who disclose use of pre-determined sustainability metrics, targets and/or weightings. The remaining 43 per cent of companies did not include (35%) or did not disclose (8%) sustainability (non-financial) compensation factors. None of the listed companies explicitly included non-financial factors in their long-term incentive programs.

Overall, extractive and financial sectors lead best practice in executive sustainability compensation within the TSX 60 Index, including setting metrics, targets and weightings in advance for both social and environmental performance improvement. Companies in the services and consumer-goods-and-services sectors have not moved to include sustainability (non-financial factors) in their incentive programs and stand out as lagging sectors in this study.

Six metric categories predominate:

- Safety
- Environment
- Employees
- Customers
- Brand/CSR performance, awards and rankings
- Community and stakeholders

Safety was the most frequent metric, followed by environment. Safety metrics most frequently focused on injuries. Environmental metrics focused significantly on spills. Overall, the most common metrics are:

- Total recordable-injury frequency and lost-time injury frequency/rate.
- Number of spills.
- Employee engagement.
- Customer satisfaction.

Top findings include evidence that there is:

- An over-reliance on backward-looking and compliance-oriented sustainability metrics.
- A focus on protecting corporate value and mitigating risk. Few metrics focus on creating value and enabling new opportunities for a company's growth.
- A lack of metric consistency across sectors to enable comparison.
- An emergent area of practice in incentivizing overall sustainability performance. One third of companies use corporate social responsibility (CSR) or sustainability metrics per se, mostly measured by third-party standards such as rankings on sustainability indices.
- A dearth of metrics measuring stakeholder relations, sustainability embedment or strategic sustainability performance.
- An infrequent use of environmental metrics covering a range of environmental impacts.
- A trend to using internally designed indices to assess sustainability performance. These measure a suite of underlying sustainability achievements.

Finally, an ad hoc scan of the executive sustainability compensation approaches of 22 international companies in 2011 showed very similar practices in place globally. In this respect, Canada is neither ahead nor behind. The only distinction globally is the greater focus on metrics to reduce energy use and GHG emissions and the tendency to compensate executives for achieving green product goals.

This research shows that executive sustainability compensation is an emerging area in the intersection between sustainability outcomes and compensation practice. The years ahead will undoubtedly witness continued trial and error as companies, their leaders and those who advise them, better understand the right mix of metrics and incentives that can result in enhanced sustainability outcomes – and thus, shareholder value.

Who should read this report and why?

Boards and compensation committees

- To learn about emerging sustainability compensation trends.
- To understand how sustainability metrics can enhance sustainability and pay practices.
- To increase shareholder value for investors.

Executives

- To prepare for a potential new focus by boards and compensation committees on sustainability pay linkages.
- To understand how metrics associated with their own pay may shift to a greater focus on sustainability measures.
- To support board and compensation committee dialogue and questions regarding sustainability pay linkages and future trends.

Compensation advisors

- To be prepared for requests from board and compensation committees.
- To learn how to complement traditional financial/business metrics with a mix of sustainability metrics.

HR advisors

- To learn about emerging sustainability pay practices.
- To anticipate new metrics/weightings that may evolve in their organizations or in competing companies.
- To be equipped to proactively introduce this emerging trend and initiate dialogue.

3. INTRODUCTION

Increasingly company executives and boards consider the business risks and opportunities from sustainability megatrends. Whether to build the social license to operate and grow, to manage supply chain risks, maintain access to resources or meet changing customer preferences, companies set targets and seek the performance and product improvements necessary to conduct business in the twenty-first century. Importantly, companies recognize that for nine billion people to live well within planetary boundaries by 2050, business models need to be re-engineered.

For corporate sustainability goals and targets to be achieved, it is essential that boards incentivize executive sustainability performance along with traditional financial and business performance. To understand the current state of practice in this area, Coro Strandberg of Strandberg Consulting conducted a study of the executive sustainability compensation practices of top Canadian companies listed on the TSX 60.

As there are no universal sustainability-pay-link standards, Strandberg Consulting sought to determine a Canadian baseline from which future progress can be tracked. (See the Canadian Coalition on Good Governance guidance on executive sustainability compensation below.) This baseline can be the basis by which boards, executives and their compensation advisors can enhance their practices in this area. It will enable them to better manage the risks and opportunities from emerging sustainability trends and improve corporate performance overall. As more companies fine-tune and disclose their practices in this area, this compensation field of practice will mature to drive shareholder – and societal – value.

Institutional investors support alignment of relevant ESG measures and compensation

The Canadian Coalition for Good Governance (CCGG) is an association of 46 institutional investors, including pension funds, mutual funds and third party money managers that collectively manage nearly $2 trillion in assets on behalf of Canadian investors. Early this year the CCGG updated its "Executive Compensation Principles" from 2009 "to provide enhanced guidance to boards and to promote compensation decisions that are aligned with long-term company and shareholder success".

Among its six principles is Principle Two, which stipulates that "performance" should be based on key business metrics aligned with corporate strategy; that the board should determine these relevant performance metrics; and that compensation should be linked to their achievement. According to CCGG, metrics which public companies should use in performance-based compensation plans include "single and multi-year financial measures (both on an absolute and on a relative peer group basis), and *non-financial measures appropriate to the company, such as Environmental, Social and Governance (ESG) measures, corporate sustainability measures or other specific non-financial strategic measures. Such measures should reinforce an expectation of ethical behavior within the company".* (Emphasis added)

This guidance reflects the concerns of institutional investors, representing a sizable share of global capital markets, that their shareholder companies are effectively managing their sustainability performance across material drivers of shareholder value.

4. METHODOLOGY

The study involved compiling a database of the executive sustainability compensation approach of companies listed on the TSX 60 as of August 31, 2012.

For the purposes of this study, sustainability is defined as non-financial factors, typically including metrics pertaining to the following:

- Environment
- Employees

- Customers
- Communities
- Other stakeholders

The information was compiled from the 2012 Management Information or Proxy Circular, which provided details pertaining to 2011 compensation practices[2]. Executive compensation information was found within the Compensation Discussion and Analysis (CD&A) section, which describes and explains the company's executive compensation approach and the basis on which compensation decisions are made. For the purposes of this study, the terms sustainability and non-financial factors are used interchangeably.

The study focused on annual and long-term incentive awards that provide financial/monetary bonuses when pre-established corporate performance goals are achieved. Sometimes there was an individual performance component as part of the sustainability (non-financial) measures of the annual incentive plan. These were recorded when disclosed.

The study assessed the following:

- The decision process. (Who makes the compensation decisions – committees or boards?)
- Sustainability (non-financial) factors included within the annual incentive plan, including the category, metric and weighting.
- Incentive plan eligibility.
- Use of a balanced scorecard approach.
- Sustainability (non-financial) factors included within the long-term incentive plan.

The TSX 60 list, including sector classifications, was sourced from TMX Group which owns and operates the Toronto Stock Exchange and TSX Venture Exchange.

Twenty-one of the 60 companies (35%) did not consider sustainability factors in executive compensation; a further five (8%) did not disclose any compensation information, for a total of 26 (43%) companies excluded from further analysis.

Of the remaining 34 (57%) companies which referenced sustainability factors in executive compensation in their disclosures, only 24 (40% of 60) included pre-determined metrics, targets and /or weightings. The remaining 10 described sustainability achievements for the year, but without any indication that sustainability performance was incentivized. As a result, these 10 companies were not analyzed further for their approach to including sustainability factors within the annual incentive plan. However, they are analyzed for their decision process, coverage, the use of the balanced scorecard and inclusion of sustainability factors within the long-term incentive plan.

[2] Note that the 2012 compensation programs will be disclosed in 2013 Management Information or Proxy Circulars in the coming months. Thus, this study focuses on corporate practices from two years ago.

The following table lists the 24 companies which are analyzed in full.

Companies with basic to strong practices in executive sustainability compensation

Sector	Company
Basic materials	Agnico-Eagle Mines Ltd.
	Agrium Inc.
	Barrick Gold Corporation
	Cameco Corporation
	IAMGold Corporation
	Inmet Mining Corporation[3]
	Kinross Gold Corporation
	Teck Resources Ltd.
Oil and gas	Canadian Natural Resources Ltd.
	Encana Corporation
	Enerplus Corporation
	Husky Energy
	Nexen Inc.
	Suncor Energy
	Talisman Energy Inc.
Financials	Bank of Montreal
	Bank of Nova Scotia
	Canadian Imperial Bank of Commerce
	Royal Bank of Canada
	Toronto-Dominion Bank Ltd.
Technology	BCE Inc.
	Rogers Communications Inc.
	TELUS Corporation
Industrials	Bombardier Inc.

A further 22 company reports were scanned of global public companies with sustainability incentive compensation practices for the 2011 year (including annual reports and proxy statements). This research revealed limited formal disclosure of sustainability compensation metrics similar to those in the Canadian companies profiled in this report. One company stood out for advanced practices: DSM. Their sustainability incentive program is profiled on page 32, along with BASF, which discloses notable carbon and energy reducing practices in its Carbon Disclosure Project report, and two others which CERES and Sustainalytics profile in their report "The Road to 2020: Corporate Progress on the Ceres Roadmap for Sustainability".

The Appendix includes the following information:

- Complete list of non-financial metrics.
- Spotlight on the financial sector.
- Case study of leading practices.
- International best practice.
- Executives eligible for participation in annual incentive plans.
- Balanced scorecard approach.
- Decision process for executive compensation.

[3] Note that Inmet Mining Corporation is no longer on the TSX 60 since the closing date of the study.

5. RESULTS

General

Over half of the companies referenced sustainability factors in their executive compensation disclosures (34 or 57%).

However, only 24 (40%) disclosed use of pre-established sustainability metrics, targets and/or weightings for incentive pay within their annual incentive plans. A number of companies also reported 2011 non-financial results although this practice was not analyzed for this study. (29 companies – nearly half of the TSX 60 – reported 2011 results, amounting to 85% of those with sustainability considerations in executive incentive pay.)

Over one-third of the TSX 60 (21 or 35%) did not include sustainability factors in at-risk pay schemes and a further five (8%) did not disclose sufficient financial or sustainability information for analysis for a total of 26 (43%) of companies with poor practices or poor reporting in this area. They are listed below.

Companies with no disclosed practices in executive sustainability compensation in 2011

Services	Canadian Tire Corporation Limited
	Loblaw Companies Ltd.
	Shoppers Drug Mart Ltd.
	Shaw Communications Inc.
	Tim Hortons Inc.
	George Weston Limited
Financials	Brookfield Asset Management Inc.
	Manulife Financial Corporation
	National Bank of Canada
	Power Corporation of Canada
Basic Materials	Eldorado Gold Corporation
	First Quantum Minerals Ltd.
	Silver Wheaton Corp.
Utilities	Fortis Inc.
	TransAlta Corporation
	TransCanada Corporation
Consumer Services & Goods	Gildan Activewear Inc.
	Magna International Inc.
	Saputo Inc.
Oil and Gas	Canadian Oil Sands Limited
	Imperial Oil Limited
Technology	Research in Motion Ltd.
	Thomson Reuters Corporation
Healthcare	Metro Inc.
	Valeant Pharmaceuticals International Inc.
Transportation	Canadian Pacific Railway Limited

Notably, none of the services and consumer services and goods companies (9) appears to include non-financial factors in executive compensation (as of 2011). Of further note, while basic materials and oil and gas companies tend to have good practices incentivizing sustainability performance (15 of 24), five companies in these two sectors are out of step with their peers: Eldorado Gold Corporation, First Quantum Minerals Ltd. and Silver Wheaton in basic materials and Canadian Oil Sands Limited and Imperial Oil Limited in oil and gas. As well, none of the utilities have practices in this area, although there are only three utilities listed on the TSX 60.

Sustainability Factors for Short-Term Incentive Plans

Twenty-four companies included one or more sustainability metrics, targets and weightings in their short-term incentive plans. As shown in the list below, six metric categories predominate.

Safety

The top metric category was safety: nearly two-thirds (15 or 63%) of companies included safety in their executive compensation program. The top safety metrics were total-recordable injury frequency (TRIF) (10) and lost-time injury frequency (LTIF) (9).

Environment

Environment was the next most frequent non-financial metric category (12). Of those companies, the most common metric was number of spills, leaks, containment losses or unintentional releases (8).

Employee Engagement and Customer Satisfaction

The third most common sustainability non-financial metric category was employee engagement and talent management, with 11 companies taking this approach. Customer satisfaction measures followed, with nine companies incorporating some aspect of the customer experience as a key performance factor for executives.

Brand/Corporate Social Responsibility (CSR) and Community/Stakeholder Relationships

Brand/CSR rankings and community and stakeholder relationships were used by seven and six companies respectively.

Number of sustainability metrics

The number of sustainability metrics ranged from one to nine, with Suncor and Cameco having the greatest number. Five was the most common number of metrics, used by six companies, followed by one sustainability metric at five companies. The average across all 24 companies is four metrics. At the five companies using only one metric, in four of five cases the metric was customer satisfaction.

The most common cluster (metrics in two or more categories) was safety and environment, used by eight companies, notably but not surprisingly all of which are in the basic materials (mining) or oil and gas sectors.

Altogether, about 44 different metrics were referenced across the 24 companies.

Weightings

Nine of the 24 companies (38%) did not disclose the weightings of the sustainability metrics. From the nature of their disclosures it would appear this was because weightings were not used to determine compensation awards, opening up an element of discretion in compensation practice.

Fifteen companies used/disclosed weightings in their annual incentive plans, reflecting best practice in executive incentive compensation. In six instances single sustainability metrics were given a weight of 10 per cent, and in five cases non-financial metrics were weighted 20 per cent. In one case the metric weighting (customer satisfaction) was 50 per cent. Other weightings included 25 per cent (4 companies); 15 per cent (3); 5 per cent (3); and 7.5 per cent (2).

The total weighting for non-financial performance used by these companies ranged from five per cent, used twice, to 60 per cent, also used twice. Three companies used 15 percent. Other weightings included:

- 10% (2)
- 13% (1)
- 20% (2)
- 25% (1)
- 30% (1)
- 55% (1)

20%

Is Average Weight for Sustainability Factors Compared to 80% for Financial Factors

Notably, Cameco, Kinross and TELUS weighted sustainability factors at 55 - 60 per cent, the highest amongst this group of companies.

8

Companies Set Sustainability Targets for Executive Performance

Targets

Eight companies disclosed measurable targets within their annual incentive plan for executives:

- Agnico-Eagle Mines Ltd
- Barrick Gold
- Bombardier
- Scotia Bank
- Cameco
- Canadian Natural Resources
- IAMGold
- Kinross Gold

Indices

There were nine sustainability indices referenced in the compensation disclosures including the following:

- Customer service/client excellence leadership/customer experience index (3)
- Safety performance index (2)
- CSR performance index (2)
- Employee commitment index (1)
- Quality index (1)

In a few cases, details were provided on the underlying metrics which make up the index.

Disclosure on 2012 metrics

Of companies using and disclosing an approach to executive sustainability compensation, only Inmet and Cameco reported on their current (2012) incentive program, not just their prior year (2011) approach.

It is notable that Inmet increased its allocation (weighting) to sustainability factors from 15 per cent in 2011 to 20 per cent in 2012. Further, the company went from:

- a general 15 per cent allocation across safety (lost-time injury frequency and total-injury frequency), environment (intensity of environmental incident) and a vague reference to sustainable development, community consultation and human rights projects in 2011;
- to 10 per cent each for safety based on a safety performance index and corporate responsibility (CR) based on a CR performance index.

These year-over-year changes (increasing the weight and clarifying the metrics) suggest the company has invested time to improve its approach to sustainability performance incentives. Of course, the use and disclosure of indices, rather than specific priority metrics, makes key targets less clear.

Among the TSX 60, Cameco demonstrated leading practices. Its approach to executive sustainability (non-financial) compensation is profiled in the appendix on page 29 along with four cases studies of leading international practices on page 31. The financial sector's sustainable pay practices are featured on page 26.

Long-Term Incentive Plans

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Companies Bonus for
Long-term Sustainability Performance

For the most part, none of the companies include non-financial factors in long-term (beyond three years) incentive performance. There was one somewhat vague reference to including a safety target within one business unit's long-term incentive plan. In another instance, the company disclosed that its long-term incentive grants followed the same guidelines and performance criteria used to determine the size of the short-term incentive plan. This means they include safety and fatality records, environmental and community incidents, environmental certification and "top 10" external sustainability ranking. Assuming this interpretation is accurate, 32 of 34 companies don't include non-financial factors in long-term incentives (94%).

6. ANALYSIS

Overall, the study indicates that the extractive and financial sectors lead best practice in executive sustainability compensation within the TSX 60. Best practice includes setting metrics, targets and weightings in advance for both social and environmental performance improvement. Companies in the services and consumer-goods-and-services sectors have not moved to include sustainability or non-financial factors in their incentive programs and stand out as lagging sectors in this study. Additionally, five companies are out of step with their extractive industry peers and lag best practice in non-financial compensation:

- Eldorado Gold Corporation
- First Quantum Minerals Ltd.
- Silver Wheaton Corp.
- Canadian Oil Sands Limited
- Imperial Oil Limited

Canadian companies demonstrate emerging good practice in the field of sustainability pay for executives. Approaches taken by these companies shed light on opportunities to enhance compensation practices. Twenty broad observations and findings from the study include:

1. Backward-Looking and Compliance-Oriented Metrics

The great majority of metrics are backward-looking, focused on reducing negative impacts such as injuries or spills. Very few set targets and metrics for positive performance impact, except in the case perhaps of employee engagement, where the focus is on improving engagement and customer satisfaction. Similarly, most of the metrics are compliance- and regulatory-oriented, especially in the case of safety and the environment. There is little evidence of compensation incentives focused on proactive measures to forestall regulation, apart from possibly "implementation of sustainable mining". No further details or metrics were provided as to how this outcome is measured or achieved.

2. Protecting Corporate Value/Mitigating Risk

Most of the metrics are focused on protecting corporate value and mitigating potential risks for the company. There are relatively fewer metrics targeted at creating value and enabling new opportunities for a company's growth.

When designing non-financial incentives, companies should consider both risk management (e.g. safeguarding shareholder value from accidents, reputational damage, supply chain or business disruption, loss of access to resources, scandals and fines) and growth opportunities to advance longer-term profitability. Examples of the former from this study include the bulk of the safety and environmental metrics and some examples of the latter include:

- Implementation of sustainable mining.
- Global and diverse workforce development.
- Implementation of a CSR policy to advance projects and secure support from indigenous communities.

The suite of 44 sustainability metrics used by the TSX 60 – whether focused on risk management or value creation – are potentially directed at sustainability issues of the last two decades: corporate reputation and regulatory compliance. Companies strategically managing for emerging material sustainability risks such as global population and middle class growth; resource, water and food scarcity; climate change; biodiversity and ecosystem decline; aging; obesity; growing income gap and changing customer preferences for example, would be expected to have incentive measures addressing this risk and opportunity suite. These are the issues most likely to have a material impact on firm performance and shareholder value in the coming period. Thus, the focus of some of the best-practice companies on GHG emission and energy reduction and low-carbon and low-impact products, shows an attempt to incentivize performance in areas of concern in the emergent realities of the global economy.

3. Metric Standardization

There is a remarkable lack of metric standardization across sectors. The most consistent metrics are:

- Total recordable injury frequency and lost-time injury frequency/rate.
- Number of spills.
- Employee engagement.
- Customer satisfaction.

Of these, only injuries appear to have measurement consistency, enabling a possible comparison between sectors and companies.

4. Sub-Themes

Two sub-themes within the employee metrics are talent management and diversity, the latter somewhat related to talent management insofar as diversity commitments can improve the talent depth in a company. Metrics associated with this aspect of employee relations include:

- Employee attraction, retention, engagement and development in support of current and future operations.
- Employee recruitment and retention.
- Global and diverse workforce development.
- Creation of a succession pool for key positions.
- Percentage of women new to the VP+ pool.

5. Corporate Social Responsibility (CSR) Metrics

About a third of companies have metrics pertaining to CSR or corporate sustainability per se, mostly measured by third-party standards such as awards or rankings on sustainability indices. One company, Inmet, has developed an internal CR (corporate responsibility) Index, comprised of a number of underlying CSR metrics to measure its CSR performance. However, the index components are not disclosed, so it is difficult to assess the quality of the index.

TELUS also reports use of a CSR Index for its CEO incentive program and describes the underlying metrics within the index. A noteworthy metric is "employee assessment of the company being a socially and environmentally responsible organization via survey". That TELUS tracks this indicator and includes it within the CEO's compensation program reveals a level of commitment to social and environmental responsibility which few companies display through their executive compensation programs. Further, TELUS includes broader community investment objectives within its CEO objectives, measured through participation rates for the employee giving and volunteering program and number of employee volunteer hours. No other company has this type of employee-related community metrics. This appears to indicate a higher degree of commitment to internal engagement on CSR than other companies within this study.

6. Use of Sustainability Index

The practice of incentivizing executives for a company's listing in a sustainability index or rating scheme such as the Dow Jones Sustainability Index (DJSI) is problematic. On the one hand, it is an objective performance measure due to its third-party nature and is one way of assessing sustainability reputation. On the other hand, awards and rankings are out of a company's control, and executives are limited in their ability to influence this outcome. As well, these indices are likely not accurate measures of a specific company's non-financial performance.

7. Non-Strategic Metrics

Given that corporate social responsibility and sustainability are increasingly becoming areas of corporate performance to be managed, it is surprising how non-strategic most of the metrics appear to be, with the exception, perhaps, of customer satisfaction and employee engagement. One would expect to gain better insights from reviewing a company's non-financial performance metrics as to how sustainability risks (apart from safety and environmental compliance) and opportunities are managed within the firm.

8. New Sustainability Metrics

Undoubtedly, customer satisfaction, environmental compliance, safety and employee engagement have been managed areas of company performance for some time. The newer areas of non-financial corporate performance management are found in two of the metric categories: "CSR performance, awards and rankings" and "community and stakeholders".

Seven companies have "CSR performance, awards and rankings" metrics in their executive compensation plans, primarily focused on peer benchmarking via third party ratings and standards – a relative measure of sustainability performance, and not a measure of the company's sustainability performance per se. However, one company includes amongst its metrics "corporate responsibility programs implemented" although the corporate responsibility programs are not described.

Six companies have "community and stakeholders" metrics in their annual incentive plans. The community and stakeholder cluster is a mixed bag of metrics including:

- Community incidents.
- Donate minimum of one per cent of domestic pre-tax profits (five-year average) to charitable and not-for-profit organizations.
- Development of long-term relationships by engaging with regulators and other stakeholders important to our sustainability. Secure continued support from our employees, impacted communities, investors, governments and the general public through communications, community investment and business development (as measured by investor perception study, corporate trust ratings and CSR awards).
- Implement CSR policy to advance projects and secure support from indigenous communities.
- Community investment objectives (measured through participation rates for employee giving and volunteering program, number of volunteer hours, employee assessment of the company being a socially and environmentally responsible organization via survey).
- Sustainable development, community consultation and human rights projects.

Compared to safety, for example, there is much less clarity on how to measure and incentivize positive community and stakeholder relationships, which are so essential for building social license to operate and grow – a key factor for Canada's extractive sector, representing nearly half (45%) of the listed companies on the TSX 60. Overall, corporate social responsibility and community and stakeholder relationships are likely to be areas of growing executive compensation practice and differentiation in the years ahead.

9. Process-Oriented Metrics

There is a relatively small number (8 companies, or 18%) of "process oriented", qualitative metrics across the six main metric categories as follows:

- Implementation of sustainable mining.
- Implement CSR policy to advance projects and secure support from indigenous communities.
- Implement corporate responsibility programs.
- Sustainable development, community consultation and human rights projects.
- Employee attraction, retention, engagement and development in support of current and future operations.
- Global and diverse workforce development.
- Creation of a succession pool for key positions.
- Backlog on repair orders for safety-critical equipment and overdue safety-critical preventative maintenance man hours.

As much of CSR and sustainability is about embedding social and environmental considerations throughout business operations, one would expect to see more metrics focused on the qualitative measurement of this embedment process. This suggests that either companies:

- are not embedding sustainability into their operations,
- don't have benchmarks, metrics and targets for this, or
- are not compensating executives for performance in this area.

10. Stakeholder Engagement Metrics

Relatedly, a strong indicator of best sustainability and CSR practice is stakeholder engagement. Given the importance of successful stakeholder relations to all companies, it is surprising that few companies are including stakeholder relations metrics within their compensation programs (with the exception of employees and customers of course). The few noted in the study include:

- Development of long-term relationships by engaging with regulators and other stakeholders important to our sustainability. Secure continued support from our employees, impacted communities, investors, governments and the general public through communications, community investment and business development (as measured by investor perception study, corporate trust ratings and CSR awards).
- Implement CSR policy to advance projects and secure support from indigenous communities.
- Sustainable development, community consultation and human rights projects.
- Implementation of sustainable mining (which may include stakeholder considerations depending on how designed).

11. Comprehensive Environmental Metrics

In two of 12 cases, the environmental metric is comprehensive across a range of environmental impacts suggesting a more fulsome approach to, and focus on, overall environmental footprint reduction:

- Year-over-year improvement in environmental leadership indicators — i.e. treated water volume, treated water quality, energy intensity, GHG emissions, air emissions, waste to landfill, radioactive waste, unclaimed waste rock (Agrium).
- Site-specific objectives such as water quality, emissions, spill prevention, dust and closure (Teck).

12. Internal Indices

The use of internally designed indices is a growing practice area of mixed value. There were nine mentions of internal indices for customer satisfaction, employee engagement, safety performance, CSR performance and quality.

On the one hand, a composite index can represent an overall benchmark for improved performance across a range of related sustainability performance areas. On the other hand, they may be too diffuse an incentive, as they represent too many underlying variables. They risk introducing an element of vagueness to the executive team and a lack of focus on the key results expected. As well, non-disclosure of the underlying metrics reduces corporate transparency.

13. Number of Non-Financial Metrics

There is no common approach to the number of non-financial metrics included within executive sustainability compensation programs. The range is from one to nine amongst the 24 companies studied, with an average of four across the 24 companies, with six companies having five metrics and five companies having one metric. The best number of non-financial metrics will depend on the number and nature of the financial metrics and the nature of the company's sustainability strategy and targets. A select number of key metrics is probably preferred over a large assortment to prevent against dilution of incentives and to encourage clarity and focus towards meeting goals.

14. Weightings

Using and disclosing weightings for incentive compensation is not common practice, but it is best practice. Fifteen of the studied companies follow this approach. While the range went from 5 per cent to 60 per cent (67 per cent at Xcel Energy), 20 per cent was the average weighting for non-financial measures. Allocating weightings to non-financial factors is at least a sector specific, if not a company specific concern. For example, some sectors such as extractives have significant direct sustainability risks and impacts, suggesting these sectors would be expected to have greater weightings assigned to sustainability performance factors. Using an above average weight of 25 per cent or more, three of five companies compensating non-financial performance at that level are in the Extractive sector (Agrium, Cameco and Kinross; versus TELUS and CIBC).

15. Targets

Eight companies disclosed quantifiable targets for non-financial executive compensation, possibly revealing the number of companies which establish such targets. This is an area of underperformance for the TSX 60 companies overall.

16. Forward-Looking Disclosures

While only two companies (Inmet and Cameco) disclosed their current year (2012) metrics, it is expected there will be more forward-looking disclosures in future, as practice grows in this area. Such disclosure enables shareholders and others to see how executive priorities change over time and signals the company's current performance – as opposed to past performance – priorities. As such, these practices meet a higher test of transparency and accountability.

17. Coverage and Long-Term Incentive Plans

Most of the annual incentive plans with non-financial components covered both CEO and executive officers. However, in the case of long-term incentive plans, while there were two inconclusive cases where non-financial factors might have been included, the great majority (94 per cent) focused only on financial performance metrics. (One company in the international scan of 22 companies included GHG emission reduction in its long-term plan.)

18. Balanced Scorecards

The use of balanced scorecards was also analyzed. This is considered a strong management practice in that it elevates the significance of a mix of financial and non-financial performance factors and is usually cascaded across the organization into non-executive performance plans and incentive schemes. While this embedment practice was not considered for the study, four of the

34 companies explicitly followed this approach. A further 13 used a business or corporate scorecard model, with less explicit intention to include a balanced mix of financial and non-financial metrics.

19. Compensation Committees

It appears that of the 34 companies that include non-financial considerations in executive compensation, two-thirds of them have compensation-type board committees with mandates to make compensation recommendations to the board of directors. The compensation committee at 10 companies has more authority than this, with a mandate to approve either or both the CEO and executive officer compensation. It is arguably better governance practice to have the compensation committee recommend compensation packages for the entire executive.

20. Metric Verification

Not included within the scope of this study, but an important consideration for executive non-financial compensation, is whether the non-financial metrics used for compensation have been independently verified as accurate and authentic. Financial metrics go through a rigorous third-party audit, but typically non-financial information systems do not receive the same level of scrutiny. Companies that have their sustainability metrics independently audited will have more confidence in the results that inform executive compensation.

7. ADVICE FOR COMPENSATION COMMITTEES, COMPENSATION ADVISORS, EXECUTIVES AND CSR PRACTITIONERS

As there is no common blueprint for designing and constructing sustainability incentives, each company must design its own approach for setting up these systems. Companies need to consider:

1. Which material issues to focus on.
2. What metrics to develop.
3. Whether performance should be assessed at the individual, business unit or corporate level.

As this study has shown, there are emerging norms in some sectors, such as the extractives, around incentivizing safety and environmental compliance goals. Employee engagement and customer satisfaction are two other common metrics. However, there is lack of evidence of a strategic sustainability approach compensated for through incentive systems.

Arguably, companies should first have a corporate sustainability strategy with goals, targets and success measures. The strategy should be informed by emerging sustainability trends affecting corporate risks and opportunities. The top sustainability objectives should be integrated into the broader corporate strategy. This will enable the compensation team to identify which areas should be tied to executive compensation.

Corporate goals should be clear and measurable (following, for example, the “SMART” goal convention that metrics be Specific, Measurable, Attainable, Realistic and Time bound).

Sustainability metrics should be sufficiently diverse to reflect the corporate sustainability strategy, yet focused on its key metrics to ensure clarity and focus toward top goals, rather than diluting the incentive suite. Companies should also consider balancing metrics which create value with those that protect value. The tendency currently is for companies to reward measures that mitigate risk, which while important, needs to be balanced with measures that enable future growth. Executives should be focused on measures that safeguard shareholder value from business and supply chain disruption, volatile and increasing commodity prices, loss of access to resources and loss of community support, along with accidents, reputational damage, scandals and fines from law violations. But they should also pay attention to measures that enhance long-term profitability[4].

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8. CONCLUSION

Constructing and evaluating sustainability metrics promises to be a key task of boards, compensation committees and the C-suite in the years ahead. Companies that get this right are better positioned to generate short- and long-term value for stakeholders. This research shows that the majority of TSX 60 companies are on this path today. The coming years will see considerable experimentation and normalization as peers and competitors alike improve their approach to this important field of corporate practice.

[4] Adapted from "Integrating ESG Issues Into Executive Pay", UN Principles for Responsible Investment, accessed October 6, 2012 at www.unpri.org/files/Integrating%20ESG%20issues.pdf

9. APPENDIX

The following items are included in this appendix:

- Complete list of 2011 sustainability metrics.
- Spotlight on the financial sector.
- Case study of leading practices.
- Case studies of international best practice.
- Incentive plan eligibility.
- Balanced scorecard approach.
- Decision process for executive compensation.

Complete List of 2011 Sustainability Metrics

Safety (15)

- Total recordable injury frequency; employee and contractor recordable injuries (10)
- Lost-time injury frequency/rate (9)
- Number of fatalities (5)
- Radiation doses
- Motor vehicle incident rate
- Safety score
- Medical frequency rate
- Number of high risk incidents
- Backlog on repair orders for safety-critical equipment and overdue safety-critical preventative maintenance man hours

Environment (12)

- Number of spills, leaks, containment losses, unintentional releases (8)
- Environmental incidents (4)
- Environmental compliance (4)
- GHG emission intensity/energy intensity (2)
- Reclamation certificates/environmental certificates (2)
- Year-over-year improvement in environmental leadership indicators (treated water volume, treated water quality, energy intensity, GHG emissions, air emissions, waste to landfill, radioactive waste, unclaimed waste rock)
- Number of wells abandoned
- Remediation liability reduction
- Regulatory inspections
- Implementation of sustainable mining
- Site-specific objectives such as water quality, emissions, spill prevention, dust and closure

Employee engagement and talent management (11)

- Surveys (5)
- Turnover /voluntary attrition (2)

- Top 10 per cent of global financial institutions on employee engagement
- Employee attraction, retention, engagement and development in support of current and future operations
- Employee recruitment and retention
- Global and diverse workforce development
- Creation of a succession pool for key positions
- Percentage of women new to the VP+ pool
- Teamwork across departments or divisions measured by a survey

Customer satisfaction (9)
- Customer service/experience index (2)
- Index comprised of benchmarks and standards to measure ability to attract and retain customers
- Market share

Brand / CSR performance, awards and rankings (7)
- Inclusion in Dow Jones Sustainability Indices (3)
- Inclusion in Canada's Best 50 Corporate Citizens global benchmark
- Top 10 external sustainability ranking
- CSR survey score above global benchmark
- Corporate responsibility programs implemented and external recognition received
- #1 or 2 brand in Canada

Community and stakeholders (6)
- Community incidents
- Donate minimum of one per cent of domestic pre-tax profits (five year average) to charitable and not-for-profit organizations
- Development of long-term relationships by engaging with regulators and other stakeholders important to our sustainability. Secure continued support from our employees, impacted communities, investors, governments and the general public through communications, community investment and business development (as measured by investor perception study, corporate trust ratings and CSR awards)
- Implement CSR policy to advance projects and secure support from indigenous communities
- Community investment objectives (measured through participation rates for employee giving and volunteering program, number of volunteer hours, employee assessment of the company being a socially and environmentally responsible organization via survey)
- Sustainable development, community consultation and human rights projects

Spotlight on the financial sector

Financials represent 17 per cent of the TSX 60, with 10 companies listed. Of these 10 companies, four (Brookfield Asset Management, Manulife, National Bank of Canada and Power Corporation of Canada) do not include non-financial factors in executive compensation plans. One company – Sun Life – reports on sustainability achievements in its compensation disclosures, but does not appear to incentivize sustainability performance through establishing targets, metrics and weightings for sustainability achievements as profiled below.

Sun Life Financial discloses non-financial achievements considered in executive compensation, but does not specify metrics, weightings or targets (2011)

Sun Life Financial's Management Resources Committee considered six objectives when determining overall annual incentive compensation in 2011, including some reference to non-financial elements, as follows:

- Innovation: Named one of the "Global 100 Most Sustainable Corporations in the World"
- Customer Service: Built and leveraged stronger brand awareness through brand development, advertising, and marketing campaigns, including launching the Money for Life media campaign, becoming the inaugural sponsor of Celtics.com, and expanding its partnership with Cirque du Soleil
- Talent Management: Advanced the talent agenda through a structured process to assess talent in each business area, completed development plans and leveraged talent across the company. Successfully implemented a new Global Human Resource Information System across the company and a new payroll system in Canada

Acknowledging after-the-fact achievement as a component of annual incentive compensation lags best practice pre-determination of metrics, targets and weightings.

Sun Life Financial 2012 Management Information Circular

This leaves the five major Canadian banks – BMO, Scotia Bank, CIBC, RBC and TD – all of which include non-financial components within their annual incentive plans (though not within their long-term incentive plans consistent with their TSX 60 peers as described later).

Of the five banks, BMO stands out for having the least evidence of non-financial compensation, with only one metric, customer satisfaction, weighted at five per cent. However, it is one of only two of the five major banks which weighted non-financial performance, along with CIBC.

CIBC appears to have the strongest approach to non-financial incentive compensation amongst its peers, with the most robust metrics (customer satisfaction measured by market share and a customer service index; and employee engagement measured by an employee survey and employee turnover) and 30 per cent weighting (20 per cent for customer satisfaction and 10 per cent for employee engagement).

CIBC's 30 per cent weighting places it among the top four companies within this study, weighting non-financial factors at 30 per cent or more (the weightings for 11 companies for non-financial components was 25 per cent or less).

The following is a summary of the approach the five major banks take to integrating non-financial factors into executive incentive pay.

Canadian banks' approach to executive non-financial compensation in 2011

Bank	Non-Financial Metric	Weight
BMO	• Customer satisfaction	**5%**
Scotia Bank	• Customer satisfaction • Employee engagement (top 10% of global financial institutions) • Workforce diversity (% of women new to the VP+ pool) • Collaboration (teamwork across departments or divisions measured by a survey) • CSR awards/rankings • CSR survey score above global benchmark	**Not provided**
CIBC	Customer satisfaction • Customer service index • Market share Employee engagement • Surveys • Turnover	**20%** **10%**
RBC	Customer satisfaction Employee engagement Brand: • #1 or 2 brand in Canada • Inclusion in Dow Jones Sustainability Indices • Inclusion in Canada's Best 50 Corporate Citizens	**Not provided**
TD	Customer satisfaction • Improve customer experience index score Employee engagement • Improvements in employee engagement score Community • Donate minimum of 1% of domestic pre-tax profits (five year average) to charitable and not-for-profit organizations	**Not provided**

As the above table reveals, the most common banking metrics are customer satisfaction (used by all) and employee engagement (used by four – does not include BMO). Three of the banks (Scotia Bank, RBC and TD) included aspects of community or corporate social responsibility/ sustainability compensation, as follows:

- CSR awards/rankings (Scotia Bank)
- CSR survey score above global benchmark (Scotia Bank)
- Inclusion in Dow Jones Sustainability Indices (RBC)
- Inclusion in Canada's Best 50 Corporate Citizens (RBC)
- Donate minimum of one per cent of domestic pre-tax profits (five-year average) to charitable and not-for-profit organizations (TD)

Notably, from these metrics it would appear that RBC and Scotia Bank are rewarding executives for inclusion in CSR and sustainability awards and rating systems showing the relevance of a CSR or sustainability brand to these companies.

Case Study of Leading Practices

The following is a case study of leading practices in executive sustainability among the studied companies.

Cameco Corporation has leading approach to non-financial disclosure and compensation practices in 2011

- Annual incentive plan covers CEO and executive.
- Company uses balanced scorecard methodology.
- Human Resources and Compensation Committee makes compensation recommendations to the board.
- Discloses 2011 and 2012 metrics.
- Discloses 2011 results.
- Assigns weightings to four non-financial components (total 55 per cent).
- Most metrics are measurable and objectively quantifiable.
- Includes a range of non-financial metrics across safety, employee, environment, and stakeholder categories.
- Goes beyond environmental compliance metrics to include metrics on reducing overall environmental impact (although this is not repeated in 2012).
- Reveals three CSR goal areas: safe, healthy and rewarding workplace; clean environment; and supportive communities.
- Uses some consistent industry metrics to enable comparison.
- A unique reference to the implementation of a CSR embedment tool (CSR policy) at its operations.
- Year-over-year improvement in approach.

Annual incentive plan includes the following non-financial components:

Safe, Healthy and Rewarding Workplace

2011:

- Strive for no lost-time injuries at all Cameco-operated sites and, at a minimum, maintain a long-term downward trend in combined employee and contractor injury frequency and severity, and radiation doses; weight: 25%. Result: Lost-time incident frequency for employees and contractors was 0.3 per 200,000 hours worked compared to a target of 0.4, severity was 8.9 compared to a target of 25, and normalized full-time average radiation dose at operating sites was 2.0 millisieverts compared to long-time average of 2.1.

2012:

- Strive for no lost-time injuries at all Cameco-operated sites, and, at a minimum, maintain a long-term downward trend in combined employee and contractor injury frequency and severity, and radiation doses.
- **Attract, retain, engage and develop employees in support of current and future operations and establish succession pools for key positions.**

Clean Environment

2011:

- Strive for zero reportable environmental incidents, reduce the frequency of incidents and have no significant incidents at Cameco-operated sites. Result: There were 31 reportable environmental incidents, above 3-year average of 29, but within the range of statistical variation. There were no significant environmental incidents.

- Improve year-over-year performance in corporate environmental leadership indicators (treated water volume, treated water quality, energy intensity, GHG emissions, air emissions, waste to landfill, radioactive waste, unclaimed waste rock). Result: two of eight KPIs showed an improvement over 2010, while two were at the same level. Higher rates in two of the key indicators were largely influenced by the cleanup of historic waste. Higher rates in the remaining two key indicators were tied to increased activity at our operations. We need continuous innovation in our practices and technology to improve year-over-year.
- Weight for two environmental components: 25 per cent.

2012:

- Strive for zero reportable environmental incidents, reduce the frequency of incidents and have no significant incidents at Cameco-operated sites.

Supportive Communities

2011:

- Develop long-term relationships by engaging with stakeholders important to our sustainability. Ensure support from our employees, impacted communities, investors, governments and the general public through communications, community investment and business development; weight: five per cent. Result: Established and maintained positive relationships with groups affected by our operating activities. Received a higher management credibility rating of 74 per cent in our investor perception study compared to 64 per cent in 2010. Maintained strong corporate trust ratings in Saskatchewan (7.24/10 compared to 7.62 in 2010), Port Hope (7.98/10 compared to 7.58 in 2010) and the US (7.32/10 compared to 7.74 in 2010). These levels of support for our operations were achieved in the face of inherent challenges for mining companies, complicated by misperceptions of the nuclear industry. Named a Top 100 Employer and among the 10 Best Companies to Work For, and received awards for being one of Saskatchewan's Top Employers, Canada's Best Diversity Employers and a Top Employer of Canadians Over 40.

2012:

- Develop long-term relationships by engaging with regulators and other stakeholders important to our sustainability. Secure continued support from our employees, impacted communities, investors, governments and the general public through communications, community investment and business development.
- Implement Cameco's corporate social responsibility policy to advance Cameco projects in all locations and secure support from indigenous communities affected by our operations.

Cameco 2012 Proxy Circular

International Best Practice

The following are four examples of globally leading practices in executive sustainability pay.

Four Case Studies

Executive sustainability compensation practices of 22 global public companies from Sustainalytics'[5] database were assessed for best practices. Of these 22 public disclosures, only one stood out for "best practice", with the rest having similar practices to the TSX 60: DSM. Their approach is drawn from their 2011 Integrated Report and is profiled below. As well, Sustainalytics collaborated with CERES to produce a progress report on 600 publicly traded companies to assess their performance on CERES' Sustainability Roadmap. Two of their profiled companies, Intel and Excel, have some best practices and are described below. Finally, BASF discloses some interesting approaches to executive incentive compensation as revealed in their Carbon Disclosure Product report.

DSM

DSM is a Dutch-based multinational life sciences and materials sciences company. DSM's products include food and dietary supplements, personal care, feed, pharmaceuticals, medical devices, automotive, paints, electrical and electronics, life protection, alternative energy and bio-based materials. DSM employs over 22,000 people worldwide and delivered annual net sales of around €9 billion in 2011. The company is listed on NYSE Euronext in Amsterdam.

It is considered best practice because its compensation metrics include the development of environmental products (ECO+ products) and because it includes greenhouse gas (GHG) reduction targets in its long term incentive plan.

Annual Incentive Plan

20 per cent of the annual incentive bonus is based on shared sustainability targets as summarized below. (A further 10 per cent is based on individual sustainability targets, the details of which are not disclosed.)

1) ECO+ products: percentage of successful product launches that meet ECO+ criteria.
2) Energy-efficiency improvement − linked to target of 20 per cent increase in energy efficiency in 2020 compared to 2008.
3) Employee Engagement Index − related to the High Performance Norm in the industry.

These three components are further described as follows:

1) ECO+ products: ECO+ solutions are products and services that, when considered over their whole life cycle, offer clear ecological benefits compared to the mainstream solutions they compete with. These ecological benefits can be created at any stage of the product life cycle − from raw material through manufacturing and use to potential re-use and end-of-life disposal.

2) Energy-efficiency improvement: Reduction of the amount of energy that is used per unit of product (known as energy efficiency) on a three-year rolling average basis.

[5] Sustainalytics is a global responsible investment research firm specialized in environmental, social and governance (ESG) research and analysis. www.sustainalytics.com

3) Employee Engagement Index: An Employee Engagement Survey is conducted annually, focusing on a combination of perceptions that have a consistent impact on behavior and create a sense of ownership.

Long-Term Incentive (LTI) Plan

Executives are also eligible to receive performance-related shares, which are conditionally granted and ultimately vested on the achievement of certain predetermined performance targets during a three-year period. Two performance targets apply for the vesting of performance shares:
- Comparable Total Shareholder Return (TSR) performance versus a peer group
- Greenhouse-gas emissions reduction over volume related revenue

In the LTI plan, 50 per cent of the performance-shares grant is based on GHG emission reduction.

Intel

Since 2008 "Intel has linked the variable compensation package of each of its employees, including executives, to the company's achievement of environmental sustainability metrics in three areas: energy efficiency of products, reductions in greenhouse gas emissions and energy use and improvements in its reputation as an environmental leader"[6]. Collectively, employee satisfaction, corporate reputation, environmental impact leadership and energy savings is worth 10 per cent of the annual incentive package.

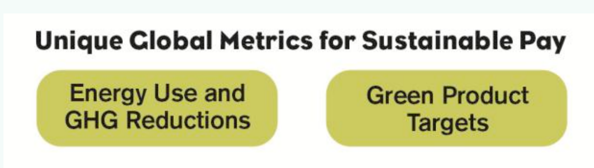
Xcel Energy

Xcel Energy's executive compensation package is based on a number of performance measures including safety targets and environmental performance targets "such as increasing the amount of renewable energy available for commercial operation, reducing emissions, improving energy efficiency and integrating new technologies"[7]. In 2011 environmental leadership was worth one-third of the annual incentive bonus and safety performance was worth another third, for a total of 67 per cent of compensation directed at sustainability factors.

BASF

BASF is a global chemical company. Its incentive performance measures, as disclosed in its 2012 carbon disclosure project report include: GHG emission reduction, energy efficiency, development and sales of climate products, climate related projects or activities and implementation of carbon reducing technologies.

Summary



These four best-practice companies reward target achievement in the following notable areas (in addition to employee engagement and safety):

[6] From http://www.ceres.org/roadmap-assessment/key-findings/governance-for-sustainability/executive-compensation
[7] From http://www.ceres.org/roadmap-assessment/key-findings/governance-for-sustainability/executive-compensation

- Environmental products (including energy efficiency of products and renewable energy products) (4 companies)
- GHG emission reductions (4)
- Energy reductions (4)
- Implementing new technology, e.g. carbon reducing technology (2)
- Climate related projects or activities (1)
- Reputation as environmental leader (1)

Executive Compensation Methods

Three compensation methods were studied to better understand executive incentive plan eligibility, the use of balanced scorecards as a performance management tool and the process by which compensation decisions were made by the studied companies:

- Incentive plan eligibility
- Balanced scorecard approach
- Decision process for executive compensation

Incentive Plan Eligibility

CEOs and executive officers are both covered by 30 of the 34 short-term/annual incentive plans (88%). Three companies did not disclose this detail and one company reported that its CEO, CFO and CRO were not included in its annual incentive plan.

Balanced Scorecard Tool

A balanced scorecard (BSC) is a performance management tool which includes a mix of both financial and non-financial measures for performance monitoring. Of the 34 companies included in this analysis, only four (12%) explicitly used a balanced scorecard approach, intentionally including financial and non-financial metrics, leading to the assumption that the metrics would cascade across the company and influence non-executive compensation rewards. A further 13 (38%) used a business or corporate scorecard approach, similar to a balanced scorecard model, but without intentions to include a mix of financial and non-financial performance. Half of the group made no reference to any form of balanced or corporate scorecard in their disclosures (17 or 50%).

Decision-Making Processes

Four decision processes predominated amongst the 34 companies analyzed in this area.

Compensation Committee[8] makes CEO and executive officer compensation recommendations to the Board of Directors	**23(68%)**
Compensation Committee approves executive officer compensation and recommends CEO compensation to the Board of Directors	**6 (18%)**
Compensation Committee approves both CEO and executive officer compensation	**4 (12%)**
Compensation Committee approves executive officer compensation; does not have a CEO	**1 (3%)**

In the majority of companies, the compensation committee (or its equivalent) recommends CEO and executive officer compensation to the board of directors for approval (23 companies, or 68%). For nearly a third of the companies (10 companies, or 29%) the compensation committee approves either or both the CEO and executive officer compensation.

[8] The committees had different names, but common compensation mandates.