SOUTHLEA GROUP

2025 Global Trends in Stakeholder Incentives:

Climate Strategies and Incentives for Corporate Sustainability

Table of Contents

3 About This Report

4 Study Methodology

6 Executive Summary

7 Climate Strategies and Ambitions

19 Climate Incentives

33 Takeaways and Action Steps

Southlea Group

Southlea Group (www.southlea.com) is a national independent compensation advisory firm that provides global perspectives as a GECN Group company. We are headquartered in Toronto with offices in Vancouver and Montreal, with clients representing all industries and organization structures. Our team of advisors is multidisciplined with diverse backgrounds and experiences. We are proud to be a certified Women's Business Enterprise by WBE Canada and to be Rainbow Registered as an LGBT+ friendly organization.

The Global Governance and Executive Compensation (GECN) Group is comprised of leading independent firms in the U.S., Canada, the U.K., Continental Europe, South Africa, and Australia. We specialize in executive compensation, performance management, governance, and related topics. The GECN Group serves companies and other organizations in more than 35 countries, working with boards of directors, C-suite executives, investors, heads of public authorities, and other decision-makers to enhance stakeholder value.

FOREWORD

A Note from Gabe Shawn Varges

Chair, GECN Group
Senior partner, HCM

In our 2023-2024 report, we observed certain tensions in the environmental, social, and governance (ESG) movement. We noted that some companies might be rethinking how far, how quickly, or how public they wanted to be with ESG initiatives.

With our multinational reach, the GECN Group is well positioned to follow these important trends from a long-term, global perspective. This is the eighth consecutive report by the GECN Group to study compensation and remuneration trends and the fifth consecutive report to focus exclusively on ESG incentives.

In this year's report, we take a deep dive into one ESG dimension: climate. What metrics are companies using to measure their progress on climate mitigation? To what extent are they leveraging their compensation system to spark performance in this area? How do corporate approaches differ by industry or geography?

Despite the shifting contours of sustainability, we believe that it will remain a strategic priority for boards and corporate leaders regardless of their geography or sector (or, in some instances, perhaps because of their geography or sector). This makes our efforts to document trends in the use of ESG incentives in executive compensation even more imperative.

Among the companies covered in this report, 96% disclose their strategies to address climate change, including their impact on a warming planet, adoption of cleaner energy sources, and pursuit of business opportunities related to energy transition. Notably, global companies are often ahead of governments in tackling climate change.

On behalf of our leaders and teams across five continents represented by the firms in the GECN Group, I invite you to read our report and to reach out to us if this subject is of interest to you, your company, or your investors.

About This Report

Corporate efforts to address environmental and climate impacts using executive incentives are the focus of *2025 Global Trends in Stakeholder Incentives: Climate Strategies and Incentives for Corporate Sustainability*.

As the first multi-national group to collate and analyze executive ESG incentives globally, the GECN Group is uniquely positioned to assess ESG-based incentive trends. We have witnessed how these measures have evolved to reflect greater rigor and specificity. As climate action has become a global priority, we ask: *What specific choices are large companies making on environmental incentive measures and goals? How do size, industry, and geography affect decision-making?*

This report details environmental incentive trends across regions and industries, and provides timely insights and data useful for corporate decision-makers to align their environmental strategies with executive compensation.

Client Service Collaboration	Knowledge Sharing	Employee Exchanges	Data Exchange (pay, practices)	Client Publications

Study Methodology

Globally, this research covers large companies in Australia, Canada, Europe, Singapore, South Africa, the UK, and the US. The GECN Group analyzed data on environmental incentives from the 2024 public disclosures of all 500+ companies listed in the following stock indexes:

- Australia - ASX 100

- Canada - TSX 60

- Continental Europe
  - France - CAC 40

  - Germany - DAX 40

  - Switzerland - SMI 20

- Singapore - STI 30

- South Africa - JSE Top 40

- United Kingdom - FTSE 100

- United States - S&P 100

Data sources: compensation and environmental incentive measure data were sourced by our GECN Group firms in Australia, the UK, and South Africa for those markets. Data for Canada, continental Europe, and the US was sourced by ESGAUGE from publicly disclosed annual reports, compensation/remuneration reports, and ESG/sustainability reports. Data was sourced from public filings as of September 1, 2024.

Environmental Incentive Measures Sorted by Prevalence

All environmental measures were grouped into categories (below) and definitions with examples provided.

MEASURE	DEFINITION	EXAMPLES
Greenhouse Gas (GHG) Emissions	The release of certain gases into the Earth's atmosphere can create a "greenhouse effect" and warm the planet, typically measured in terms of carbon dioxide equivalents (CO2e). Incentive measures may include direct emissions reductions or activity-based goals	■ Reduction in GHG emissions from operations ■ Working with clients to reduce emissions from products
Renewable or Non-Renewable Energy Use	The use of Energy from renewable natural energy sources, including solar, wind, hydropower, bioenergy, and geothermal power or low-carbon sources like nuclear power vs. non-renewable carbon-based sources including fossil fuels (e.g., coal, oil, and gas)	■ Percentage of Energy from renewable sources ■ Deployment of renewable energy projects
Environmental Incidents / Hazardous Materials	Management of environmental incidents or hazardous waste to limit negative impacts, including efforts for compliance, remediation, disposal of toxic waste, and chemical containment	■ Diversion of hazardous waste from operating sites ■ Number of significant environmental incidents
Air, Land, and Water Management	Management of environmental externalities stemming from a company's operations that may impact air quality, land use and preservation, and local water systems	■ Reduction in water consumption ■ Reduction in the use of single-use plastics
Other Environmental	All other environmental objectives, which may include management of environmental risks and opportunities, unspecified environmental compliance, and other general and broad references to environmental objectives	■ Progress toward environmental sustainability ■ Disclosure of environmental standards

For many directors, discussions around corporate environmental strategies can be new, and they may present details and terminology the board, and particularly the compensation/remuneration committee, is not accustomed to reviewing. To aid that discussion, key environmental terms used in this report are defined below.

Key Terms and Definitions (Alphabetical Order)

TERM	DEFINITION
Emissions Intensity	A normalized measure of emissions relative to the intensity of a specific activity (e.g., per dollar of revenue generated)
Financed Emissions	Indirect emissions that are attributed to a financial institution's lending and investing activities
Greenhouse Effect	A process that occurs when gases in the Earth's atmosphere trap the Sun's heat, thus raising the planet's surface temperature
Greenhouse Gas (GHG) Emissions	The release of certain gases, including carbon dioxide, methane, nitrous oxide, and fluorinated gases, into the Earth's atmosphere can create a "greenhouse effect," typically measured in terms of carbon dioxide equivalents (CO2e)
Greenwashing	Deceptive messaging in which a company makes false or misleading claims about the environmental friendliness of its products/services, operations, or policies
Scope 1 GHG Emissions	Emissions from sources that an organization owns or controls directly, such as from company-operated vehicles
Scope 2 GHG Emissions	Indirect emissions associated with the purchase of electricity, steam, heat, or cooling
Scope 3 GHG Emissions	Indirect emissions from upstream suppliers and from the downstream use of a company's products by customers

Executive Summary

For years, the GECN Group has studied the use of ESG incentives across companies globally. We have noted the continued adoption of ESG measures among companies of all sizes and the steep adoption of environmental and climate measures. In this year's report, the GECN Group takes a deeper dive into the use of environmental measures, particularly those aimed at reducing GHG emissions.

Companies globally are facing immense pressure to respond to the physical and financial impacts of climate change risk. They are responding by adopting and disclosing climate strategies, setting long-term and near-term targets, and tying executive pay to those targets. This shift has been influenced by multiple factors including regulatory requirements, stakeholder pressures, and demands for greater transparency and accountability from investors and customers.

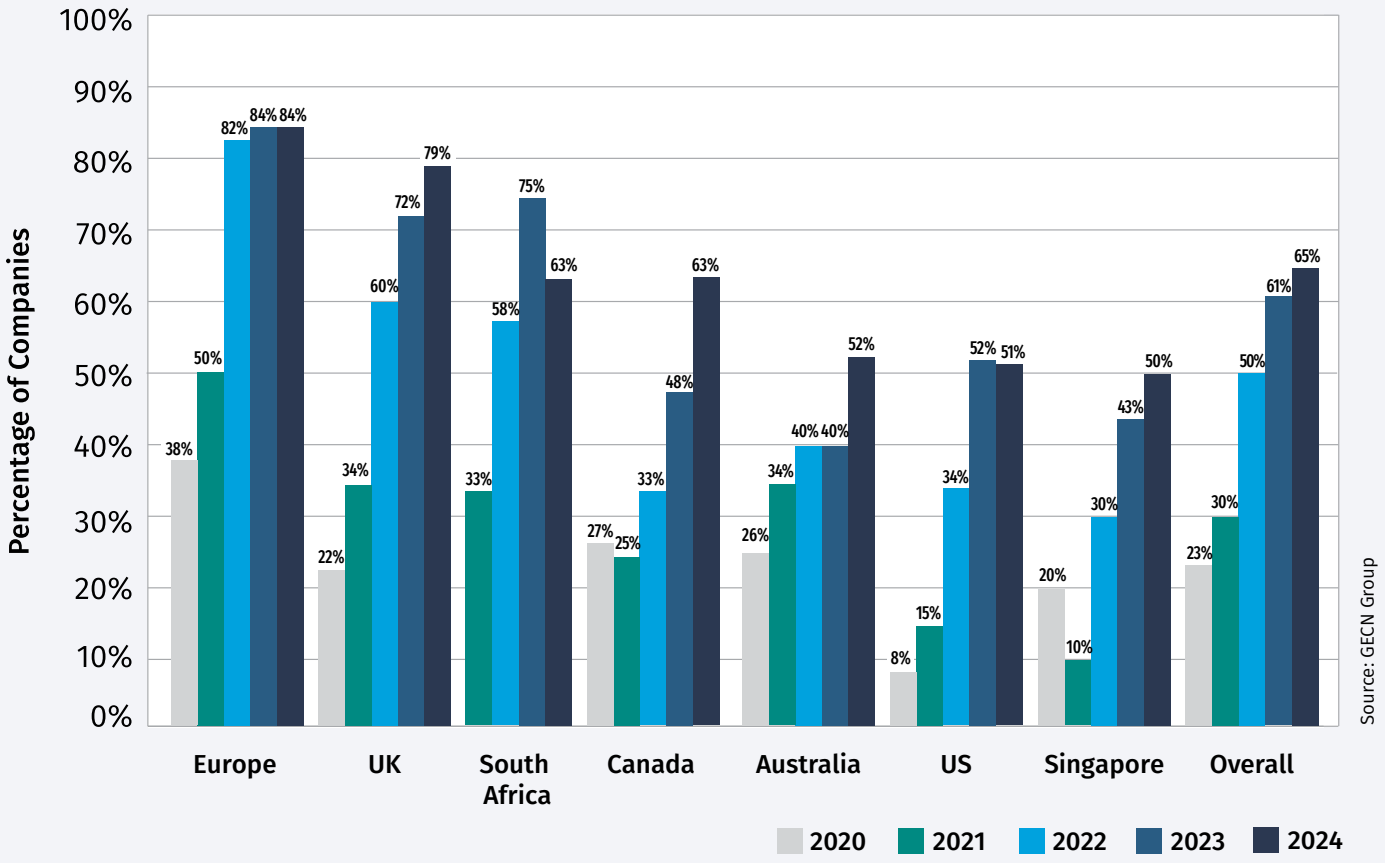
Key trends identified in corporate climate strategies and incentives include:

- **Climate strategies:** nearly all large global companies have developed an environmental and/or climate strategy, which is no longer a question but an expectation
- **Disclosures and targets:** almost all companies have disclosed their emissions across Scope 1 and Scope 2, while most have also made progress on Scope 3. A number of companies have also developed goals for reducing those emissions over the long-term and near-term
- **Sectoral differences:** different industries are at varying stages of adopting environmental and emissions measures and goals. Utilities lead in this area. Conversely, rapid growth and operational pressures have resulted in increased emissions among Information Technology firms
- **Role of incentives in driving progress:** the use of environmental measures in executive incentive plans has surged, indicating that companies are leveraging compensation structures to drive climate action. It appears as though such incentives are effective, as companies with emissions incentives also experience greater reductions in emissions
- **Short-term Incentives (STI) vs. Long-term Incentives (LTI):** while most companies use emissions measures in STI plans, there is increased adoption of environmental measures in LTI, with a majority of companies in Europe, the UK, and South Africa using them in the LTI
- **Challenges and criticisms:** companies face challenges in setting realistic and ambitious climate targets, particularly in incentives. They continue to use a mix of both quantitative and qualitative goals that can provide actionable levers while aiming for results that demonstrate progress against public commitments

As we enter 2025, certain conditions may hinder or slow progress. Political changes introduce uncertainty. However, it is clear that large companies have already made strides in addressing their climate impacts and continue to work toward a greener planet.

Future advancements will likely depend on regulatory support, technological innovation, infrastructure development, and sustained corporate commitments to climate goals. Climate incentive measures in executive pay programs can be part of an impactful environmental strategy that can help drive and demonstrate meaningful progress.

Prevalence of Environmental Incentives by Large Companies Globally



Climate Strategies and Ambitions

The rapid adoption of environmental incentive measures, particularly emissions, propelled the GECN Group to establish "climate" as the subject matter of this year's report. From 2020 to 2024, the prevalence of environmental measures increased from 23% of global companies to 65%. This pace of adoption has far exceeded that of Social or Governance measures in the broader arena of ESG incentives.

Companies globally recognize environmental imperatives such as reducing their external impacts and/or harnessing new "green" business opportunities as part of their broader corporate strategies. They are working to understand and often quantify the ways in which environmental factors impact their operations, including their supply chains and customers.

Additionally, large institutional shareholders continue to pressure companies to disclose their environmental data and demonstrate how they are harnessing or adapting to an energy transition in a way that makes them more resilient. This combination of strategic alignment and external pressures from stakeholders, including shareholders, has served as a catalyst for the adoption of environmental measures in incentive programs.

International Climate Action

Global action on climate change has been a major focus of corporations in the 21st century. Advancements in climate science and growing public awareness of the perils of a warming planet have pressured regulators, international bodies such as the United Nations (UN), and large investors to find ways to encourage companies to address their climate impacts. These groups and other stakeholders recognize that large companies in a globalized economy can have an outsized influence in the fight against climate change.

Corporate climate change efforts gained momentum after the 2015 Paris Climate Agreement, where 196 countries agreed to limit global warming to well below 2°C above pre-industrial levels while pursuing efforts to limit the increase to 1.5°C. The Paris Agreement followed a series of historical initiatives, including (i) the establishment of the Intergovernmental Panel on Climate Change (IPCC) at the UN in 1988; (ii) the IPCC's assessment that human activities are increasing greenhouse gases and causing global warming; and (iii) the 1997 Kyoto Protocol, which committed industrialized countries to limit their GHG emissions through individual targets.

Since the Paris Agreement in 2015, the UN has continued to develop strategies to deliver on its promises for climate action. A number of climate initiatives impacting corporations have developed, including broad efforts toward greater climate financing, disclosure, and target-setting. Chief among those efforts are net-zero pledges in which entities commit to cutting carbon emissions to an amount small enough to be absorbed by nature and other carbon removal measures, leaving zero net emissions in the atmosphere.

As of June 2024, 107 countries, responsible for approximately 82% of global GHG emissions, have adopted net-zero pledges. The UK was the first major country to pass a law committing to reduce GHG emissions to net-zero by 2050, with many countries following suit. Countries exempt include Singapore, South Africa, and the US, who all have net-zero commitments in policy documents but have not passed net-zero commitments into law.

An estimated 50% of the world's 2,000 largest companies have also committed to net-zero emissions. These commitments typically set long-term aspirational targets by 2050, although some companies are more aggressive and aim to reach net-zero by 2040 or earlier.

Net-Zero Commitments and Climate Disclosure Requirements by Region

Country	Country-Level Net Zero Target			Climate Disclosure Requirement (TCFD-Aligned)
	Political Pledge	Policy Document	Law	
France	✓	✓	✓	✓
Germany	✓	✓	✓	✓
Switzerland	✓	✓	✓	✓
United Kingdom		✓	✓	✓
South Africa		✓		Proposed
Canada	✓	✓	✓	Proposed
Australia	✓	✓	✓	✓
United States		✓		Proposed
Singapore		✓		✓

Source: ClimateWatchData, regulatory filings

In recent years, countries also have adopted rules that require companies to disclose their climate strategies and emissions. Many of these regulations closely follow the standards developed by the Task Force on Climate-Related Financial Disclosures (TCFD), which was established in 2015 following the Paris Agreement to drive transparency under a unified standard and increase reporting on climate-related financial information. For example, in 2024, Australia passed a law requiring mandatory climate-related reporting starting in 2025.

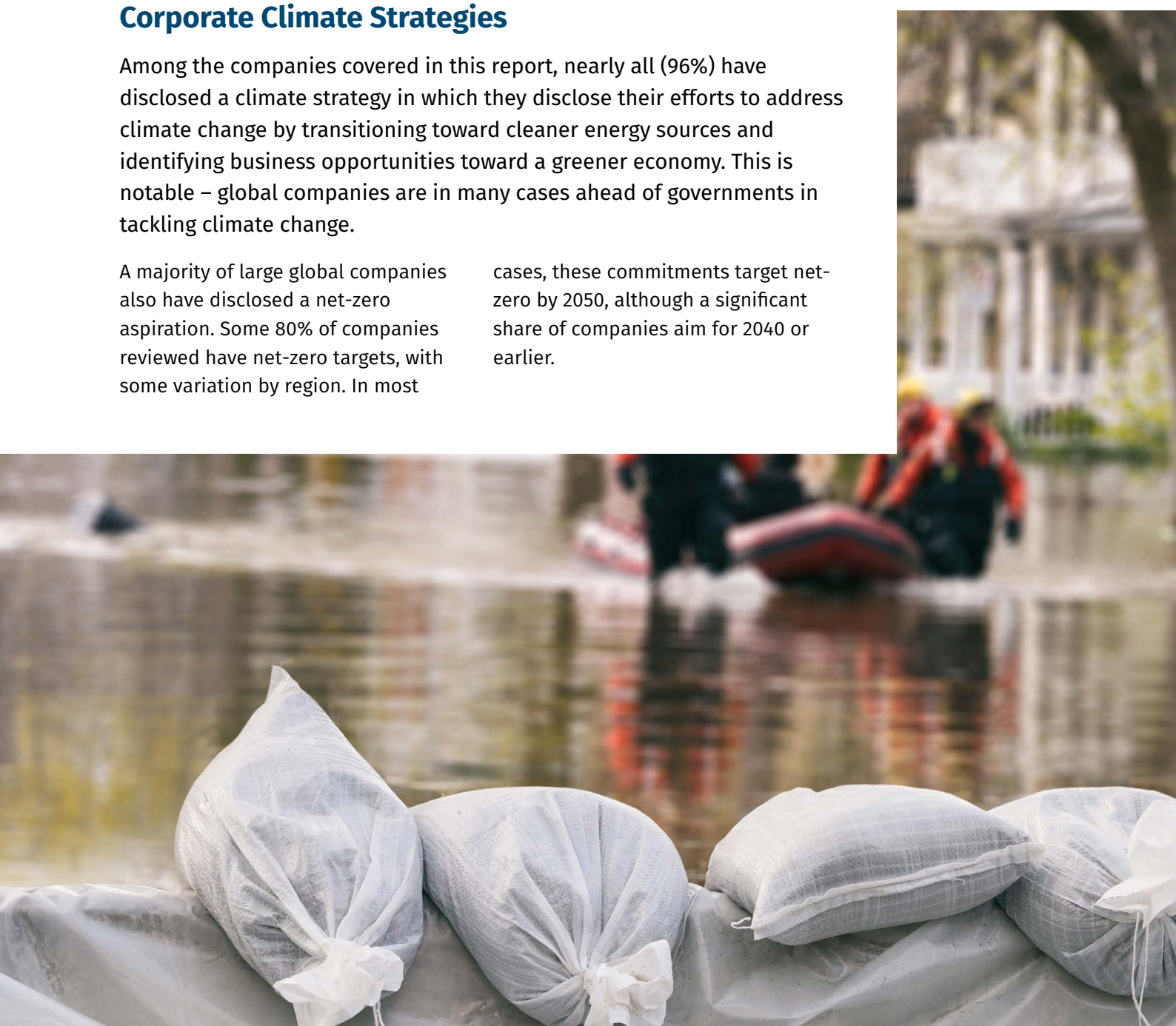
While progress is evident, there also has been pushback. In the US, while the Securities and Exchange Commission (SEC) passed a corporate climate disclosure rule in 2024 that was modelled after the TCFD, lawsuits have delayed its implementation, and there is speculation around whether a new US administration will cancel the rule.

As in other markets, companies in the US have already voluntarily disclosed considerable climate data for use by investors and other stakeholders. Large companies, in partnership with standard-setters and governance groups, often have led the charge on disclosure in the absence of local regulation. Market observers will be watching to see if the new regulatory regime in the US will change how companies report environmental information.

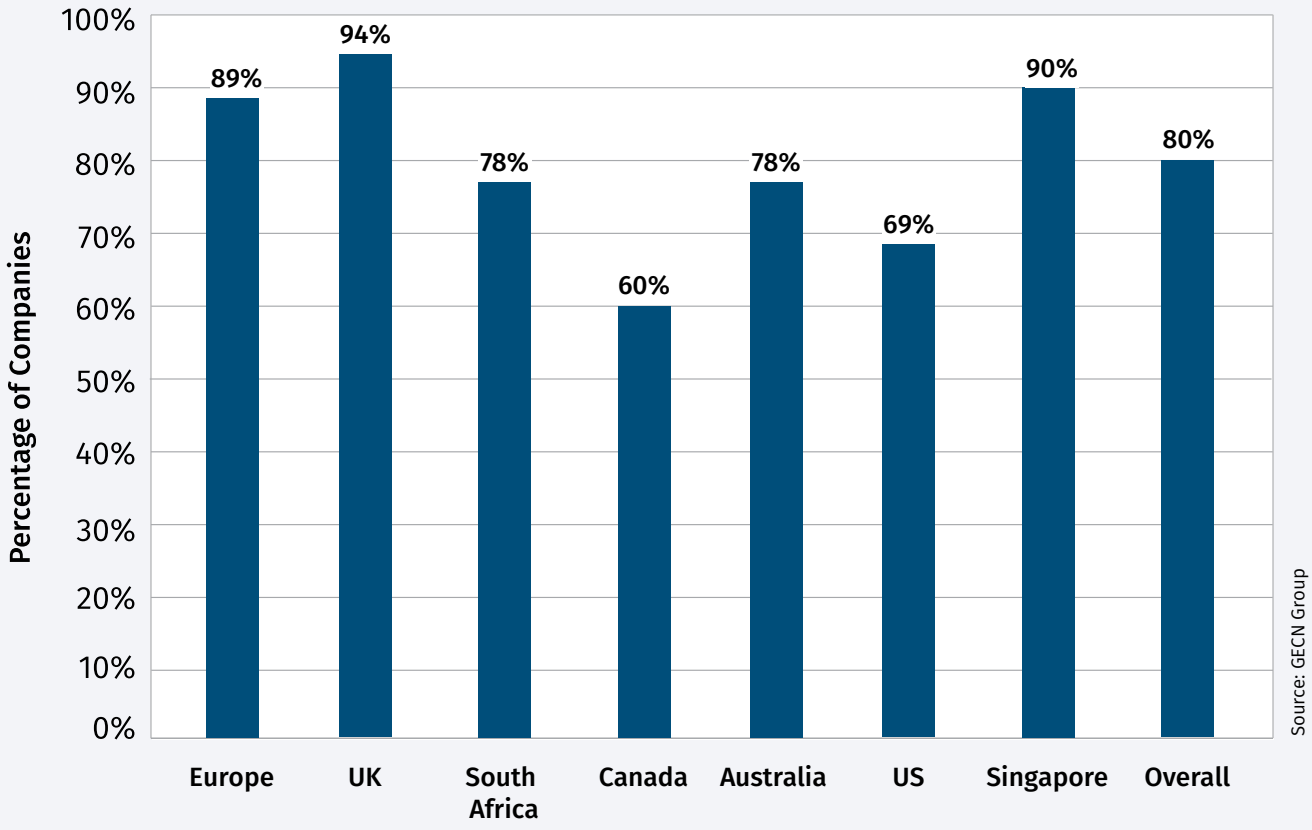
Corporate Climate Strategies

Among the companies covered in this report, nearly all (96%) have disclosed a climate strategy in which they disclose their efforts to address climate change by transitioning toward cleaner energy sources and identifying business opportunities toward a greener economy. This is notable – global companies are in many cases ahead of governments in tackling climate change.

A majority of large global companies also have disclosed a net-zero aspiration. Some 80% of companies reviewed have net-zero targets, with some variation by region. In most cases, these commitments target net-zero by 2050, although a significant share of companies aim for 2040 or earlier.



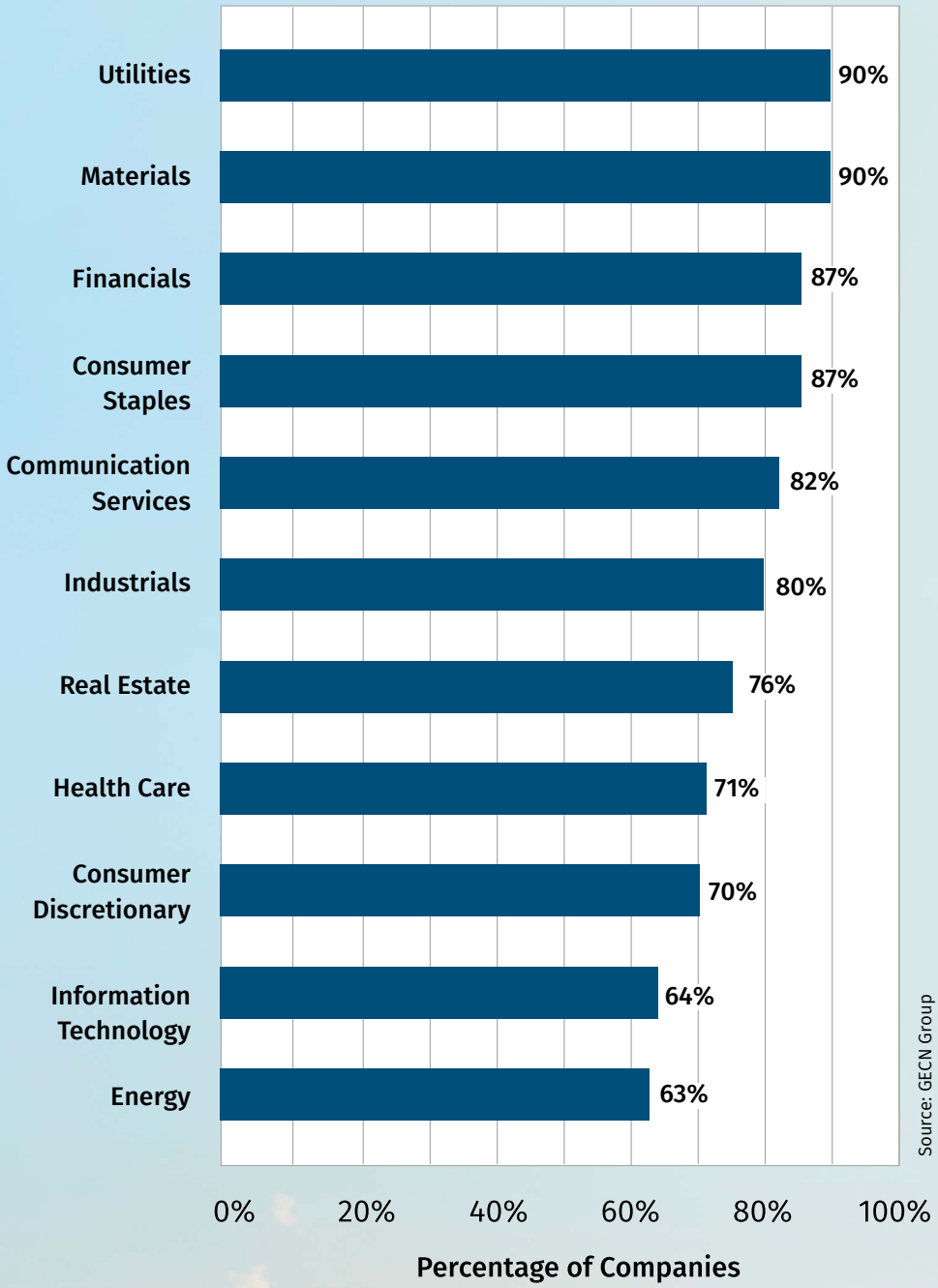
Prevalence of Disclosed Net-Zero Commitments by Region



- Companies in the UK (94%) and Europe (89%) are most likely to disclose alignment with net-zero. Companies in Canada (60%) are the least likely to disclose net-zero commitments, which probably is the result of companies reacting to recent anti-greenwashing regulations, which has caused some firms to remove their public goals to limit the risk of regulator or legal action. Most other countries covered also have anti-greenwashing rules, but reactions to those have not been as stark
- In the US, despite lagging efforts on climate action by regulators, 69% of large companies have committed to net-zero, likely due to pressures from stakeholders, particularly shareholders who have policies and expectations for their portfolio to address climate risks
- Companies in the Utilities and Materials sectors are the most likely to have net-zero commitments (90%), reflecting an acknowledgement of their sector's ability to impact climate. At the same time, Energy companies are least likely to have net-zero ambitions (63%) given that their business relies on fossil fuel production. Additionally, many Energy companies have yet to establish a pathway to lower or low-emissions products. As a result, for many Energy companies, a net-zero ambition is not a goal to which they can aspire

(See chart on next page)

Prevalence of Disclosed Net-Zero Commitments by Sector



Source: GECN Group

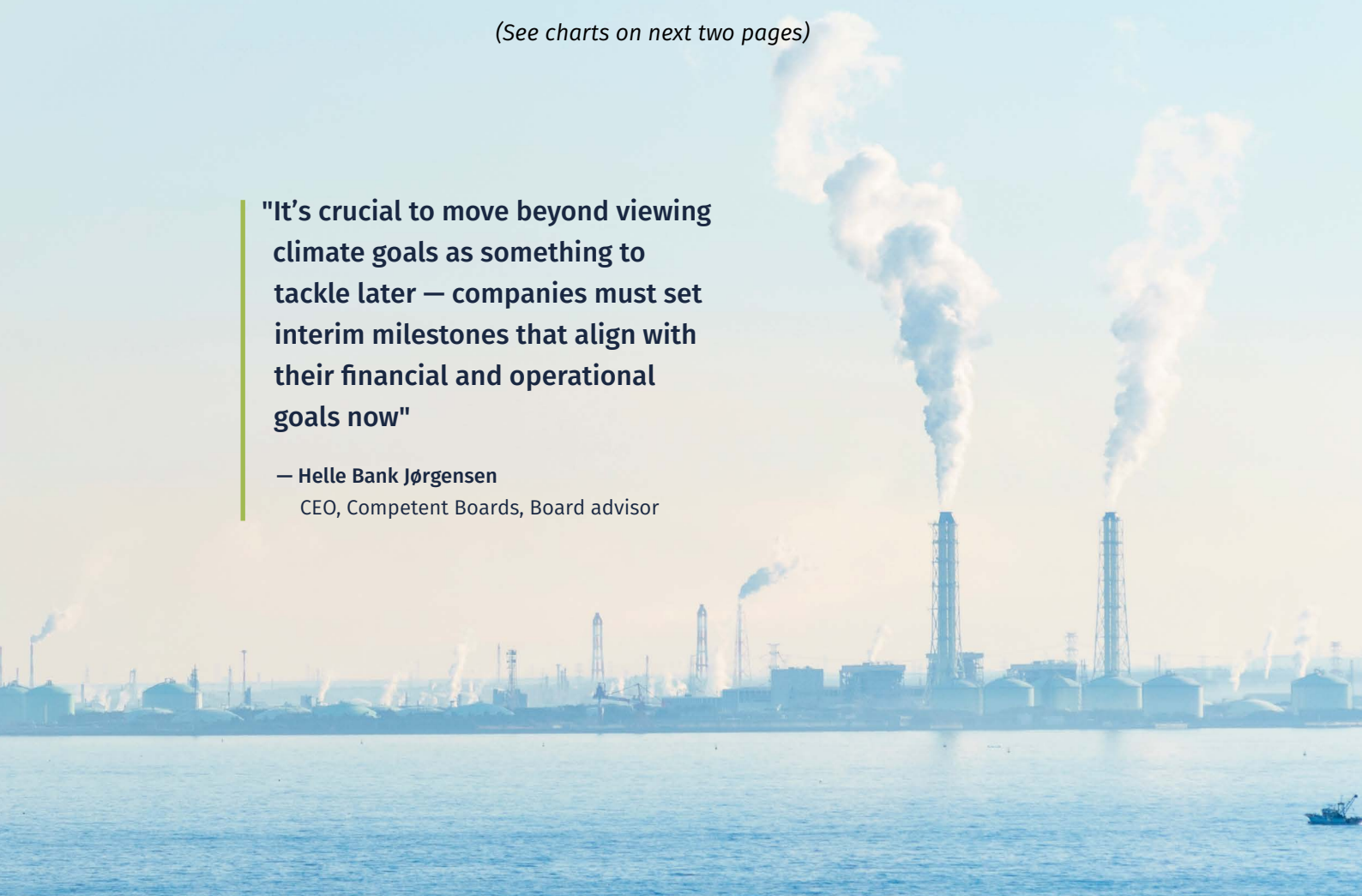
Emissions Disclosures

Companies also have made significant progress in reporting their actual GHG emissions. These disclosures were historically voluntary and generally aligned with ESG reporting standards, including the TCFD framework, the Global Reporting Initiative (GRI), and the CDP (formerly the Carbon Disclosure Project). More recently, climate disclosure regulations across countries have further pressured companies to measure and report their emissions. Today, 95% of large global companies report their Scope 1 and Scope 2 GHG emissions, while 84% disclose their Scope 3 GHG emissions.

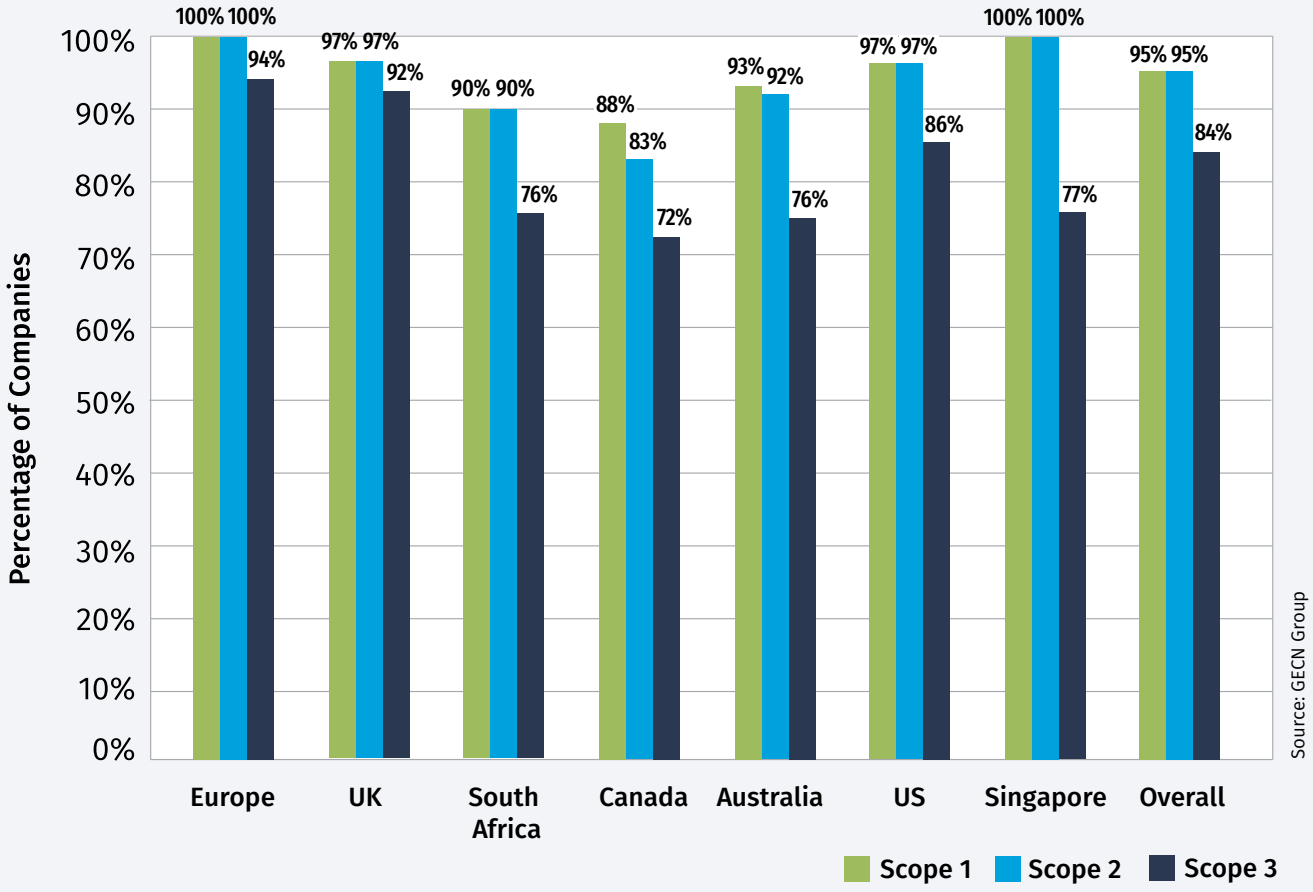
- Scope 1 and 2 GHG emissions, which measure direct emissions from a company's operations (Scope 1) and indirect emissions from purchased fuel and electricity (Scope 2) have generally been easier for companies to track and report. As such, the vast majority of companies across all countries and sectors reviewed disclose Scope 1 and 2 emissions
- Disclosure of Scope 3 emissions, which measures indirect emissions from a company's upstream suppliers and from the downstream use of a company's products, has been slower as it can take significant time and investment for a company to measure Scope 3. While companies can leverage existing standards for measurement from organizations such as the Greenhouse Gas Protocol and local regulators, the methodology can be complex and is dependent on suppliers also providing and disclosing their own emissions. Today, 84% of large global companies disclose Scope 3 GHG emissions, with the lowest disclosure being in Canada (72%)
- Across sectors, Energy has the lowest prevalence of Scope 3 disclosure (58%). Many Energy companies are likely reluctant to report on their Scope 3 emissions given that the use of their key products (oil and gas) is and has been a primary contributor to greenhouse gases in the Earth's atmosphere

(See charts on next two pages)

> **"It's crucial to move beyond viewing climate goals as something to tackle later — companies must set interim milestones that align with their financial and operational goals now"**
>
> **— Helle Bank Jørgensen**
> CEO, Competent Boards, Board advisor



Prevalence of GHG Emissions Disclosure by Scope 1, 2, and 3, and by Region

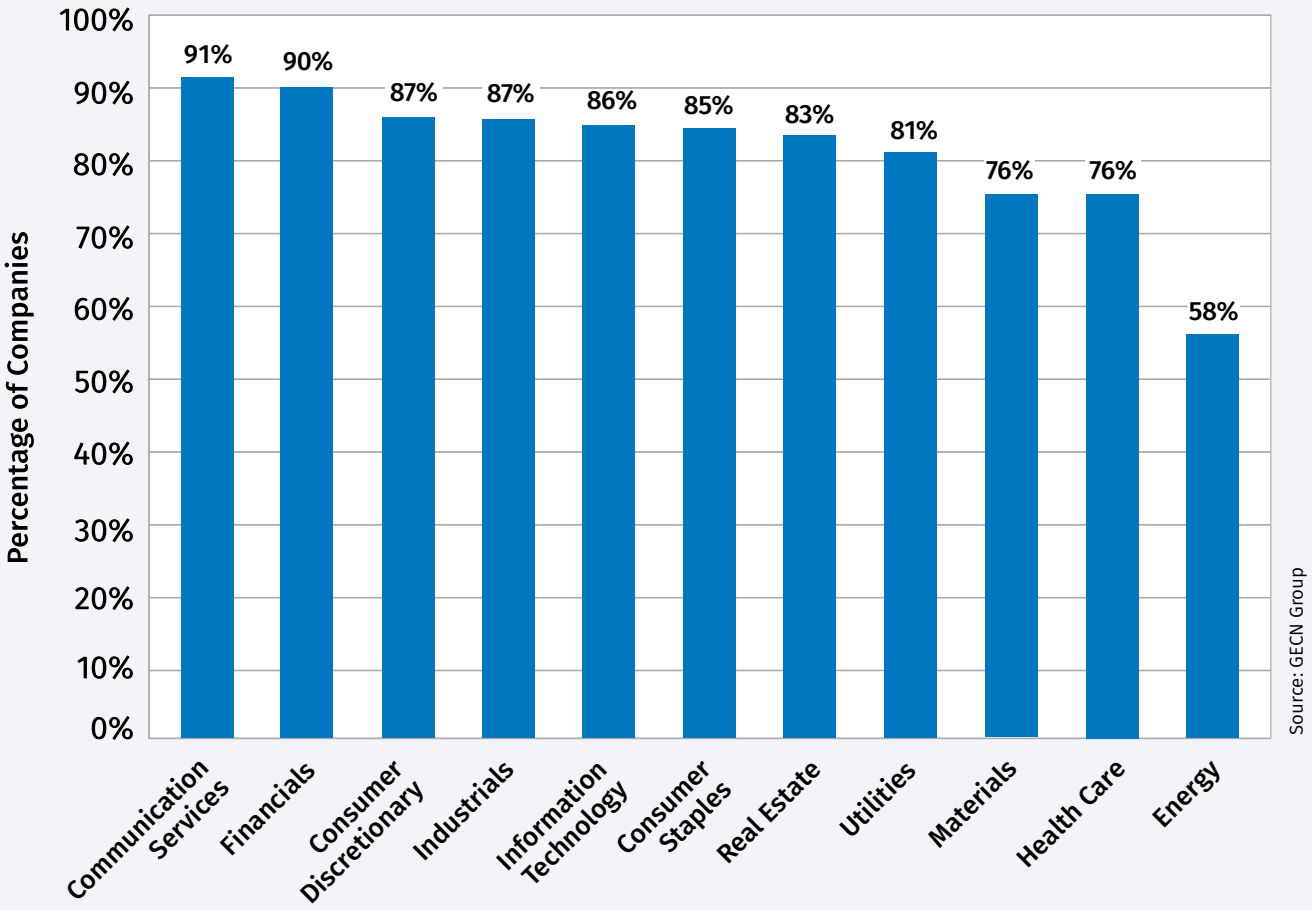


Emissions Reduction Targets

Disclosure provides transparency and accountability for climate progress, which is ultimately defined by GHG emissions reduction. In addition to long-term net-zero ambitions, many companies set near- or medium-term emissions reduction targets. Overall, 87% of large global companies have set near-term emissions reduction targets (defined as goals for reductions within the next 10 years). Most companies with near-term goals set them for 2030 or earlier.

- European (96%) and UK (93%) companies are the most likely to set and disclose near-term GHG emissions reduction targets. This prevalence reflects the longer history companies in these regions have with tracking and reporting their emissions performance and the pressure many companies face from their European and UK shareholders, who often have stringent expectations regarding climate progress
- Near-term targets are most often disclosed for Scope 1 and 2 emissions (82%), with the highest prevalence being in Europe and the lowest in Canada. In addition to regional differences in shareholder and stakeholder pressures and regulations, differences in the greening of a country's or locality's electricity grid can also hinder or facilitate a company's ability to reduce its emissions

Prevalence of Scope 3 GHG Emissions Disclosure by Sector

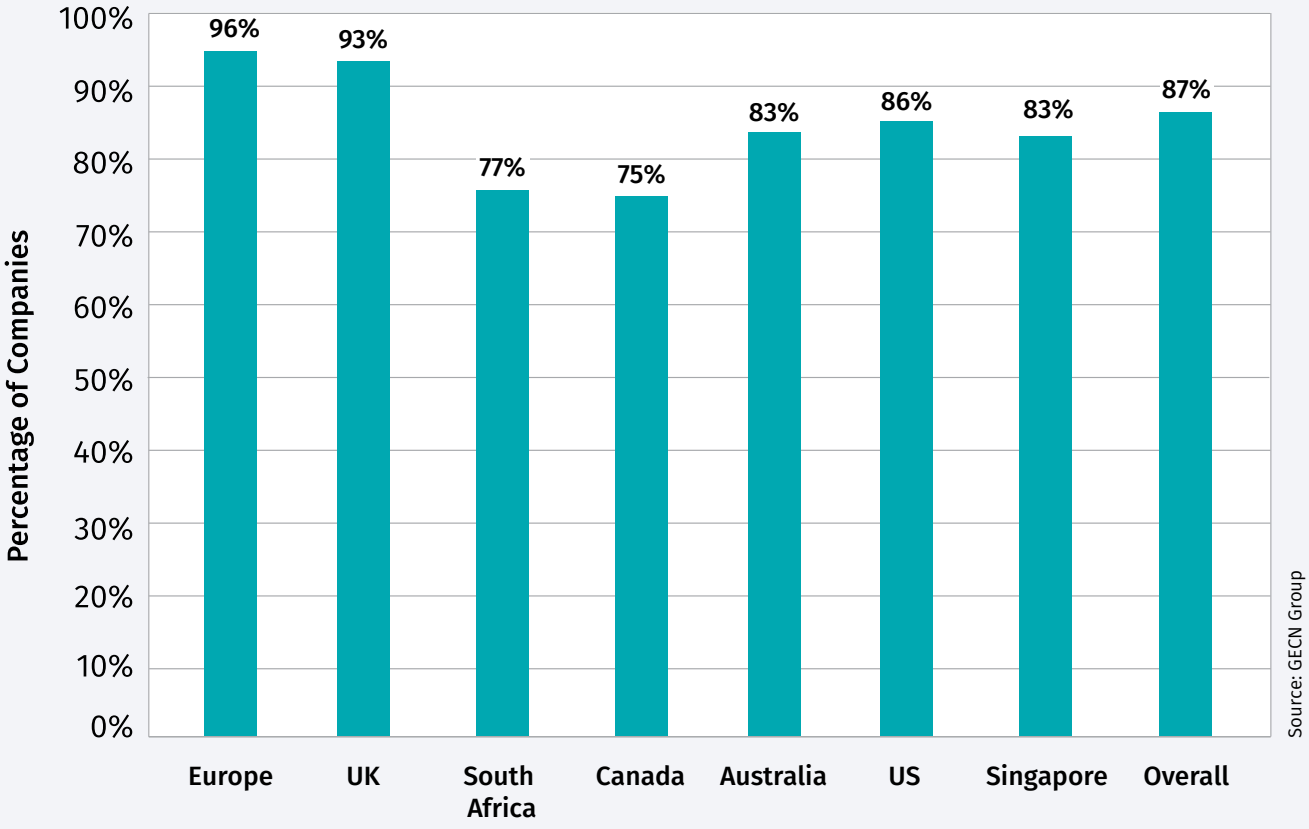


Source: GECN Group

- Although 84% of companies disclose Scope 3 emissions, only 53% set a Scope 3 emissions near-term target. Companies can be hesitant to publicly disclose Scope 3 targets given that they might not yet feel comfortable with the measure. Moreover, many companies continue to refine their Scope 3 methodologies and, in some cases, retroactively change historical numbers
- Utilities and Financial Services companies are the most likely to report a Scope 3 target, which is likely to reflect a combination of customer considerations for utilities and shareholder pressures for financial services firms. Energy companies are the least likely to disclose a Scope 3 target

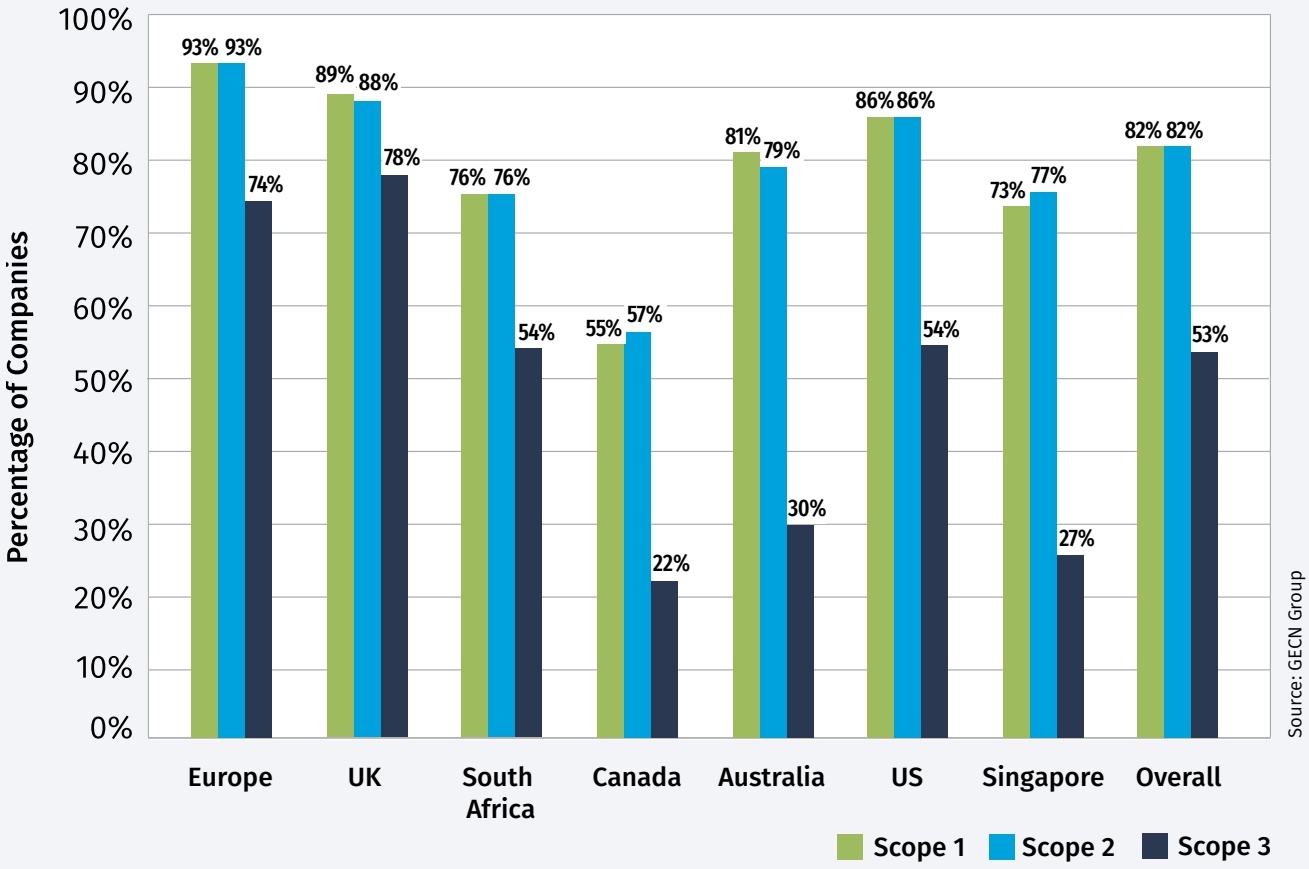
(See charts on next page)

Prevalence of Near-Term GHG Emissions Reduction Targets by Region



Source: GECN Group

Prevalence of Near-Term GHG Emissions Reduction Targets by Scope 1, 2, and 3, and by Region



Source: GECN Group

Two common criticisms of corporate GHG emissions targets, especially longer-term targets, have been that they are either (1) not realistic and too ambitious, or (2) not ambitious enough and insufficient to make a difference in the climate change trajectory. Companies face pressures to demonstrate how their goals align with efforts to limit global warming to 1.5 degrees Celsius.

To address this issue, companies are increasingly certifying goals from standard-setters, such as the Science-based Targets Initiative (SBTi). In addition, many companies disclose the pathway by which they plan to achieve those goals and the investments and other requisites needed to succeed. The Walt Disney Company is one example of a company disclosing its current historical emissions, the levers needed to achieve emissions reductions (e.g., using lower carbon fuels), and its specific SBTi-aligned targets on the path to net-zero.

Disney's Pathway to Net-Zero Emissions for Direct Operations

Source: The Walt Disney Company *2023 Sustainability and Social Impact Report*

Emissions Reduction Progress

Actual progress on corporate emissions reductions is mixed. Overall, in the most recent year, 46% of large global companies reported a decrease in their Scope 1 and 2 emissions, implying that 54% of companies increased their emissions.

- By sector, Utilities have shown the greatest progress in reducing their emissions, with 60% of companies in the sector reporting an emissions decrease in the most recent year
- Conversely, Information Technology companies are the least likely to be making progress on emissions, with only 29% reporting a decrease (i.e., 71% reported an increase in emissions). This reflects the sector's continued strong growth, which requires significant increases in computing power and emissions emanating from the energy needed for servers, infrastructure, and operations. Technological advancements like artificial intelligence (AI) computing and cryptocurrency also are known contributors to the need for increased energy use
- A lower proportion of companies disclose reductions in their Scope 3 emissions, as many companies are still reporting this measure for the first time and/or are adding new categories in their Scope 3 disclosures to account for upstream and downstream sources

(See chart on next page)

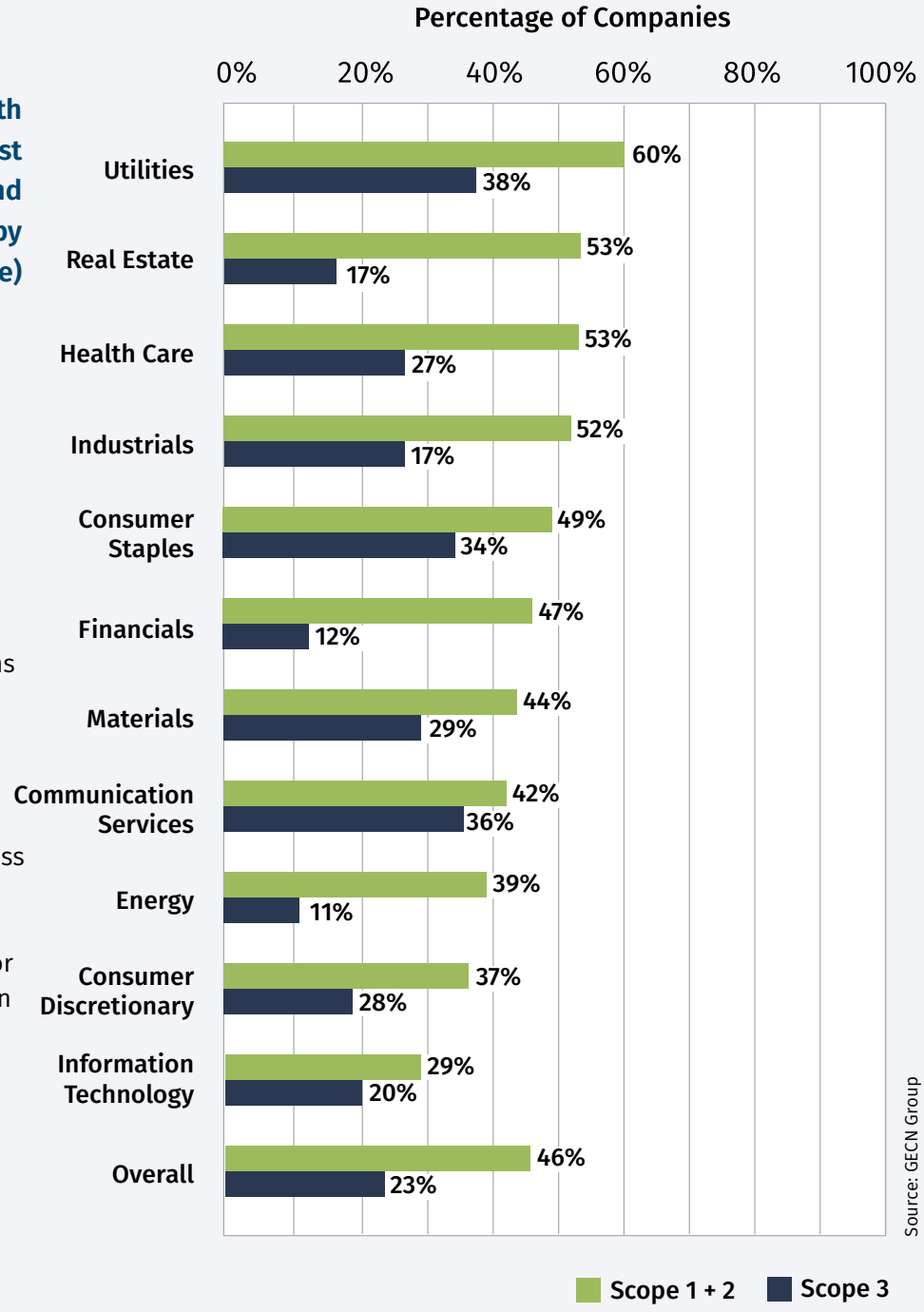
> "Look at your business purpose and your mission. Set climate goals that make sense in light of (1) where you want to be as a company and (2) what your specific investors (not all investors) want. Know your investors!"
>
> — **Anke Zschorn**
> Senior director, research
> Glass Lewis, Germany

Prevalence of Companies with Emissions Decrease in Most Recent Year by Scope 1, 2, and 3, and by Sector (Sorted by Scope 1 + 2 Prevalence)

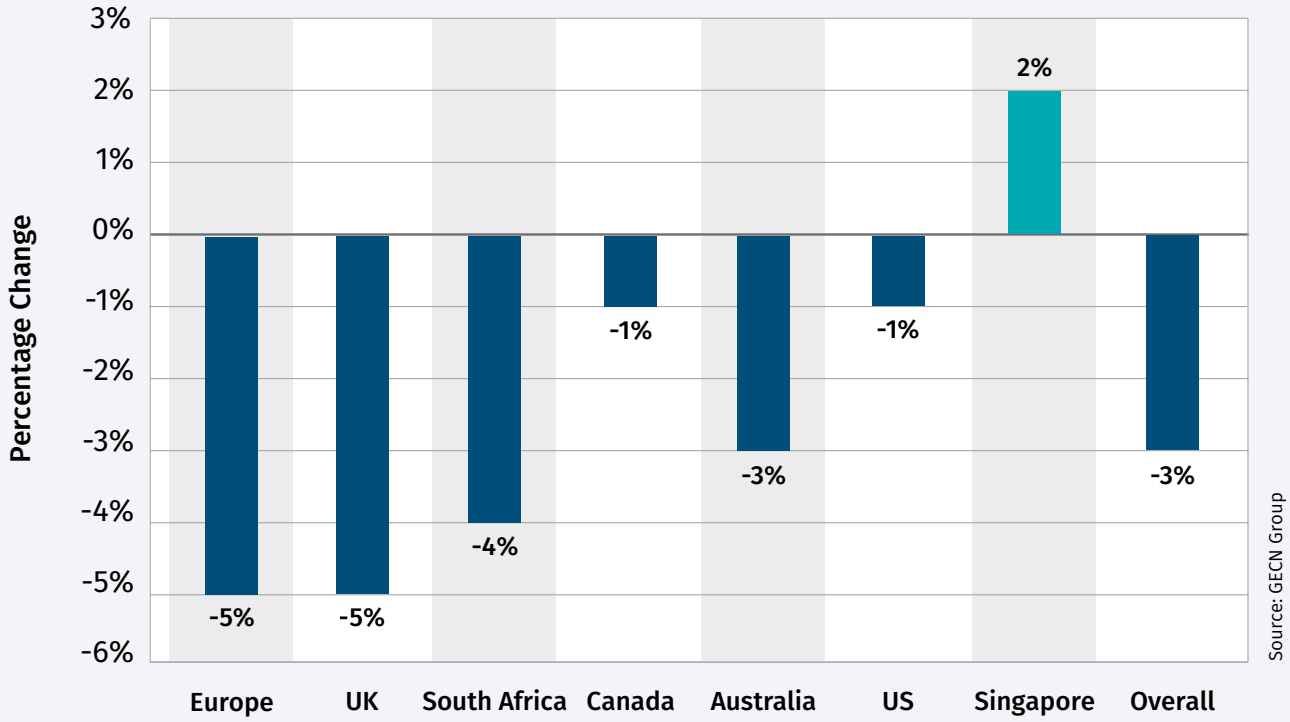
In the most recent year, the median change in Scope 1 and 2 emissions among large companies globally is -3%. In fact, the median change in emissions is negative across almost all countries, with the exception of Singapore, where the median change in emissions was an increase of +2%.

- Almost all sectors demonstrated emissions decreases, with Utilities showing the greatest progress with a median emissions change of -7%. Information Technology is the lone sector with an increase (+2%), again likely reflecting increased energy use stemming from sector growth and the development of new technologies (e.g., AI)

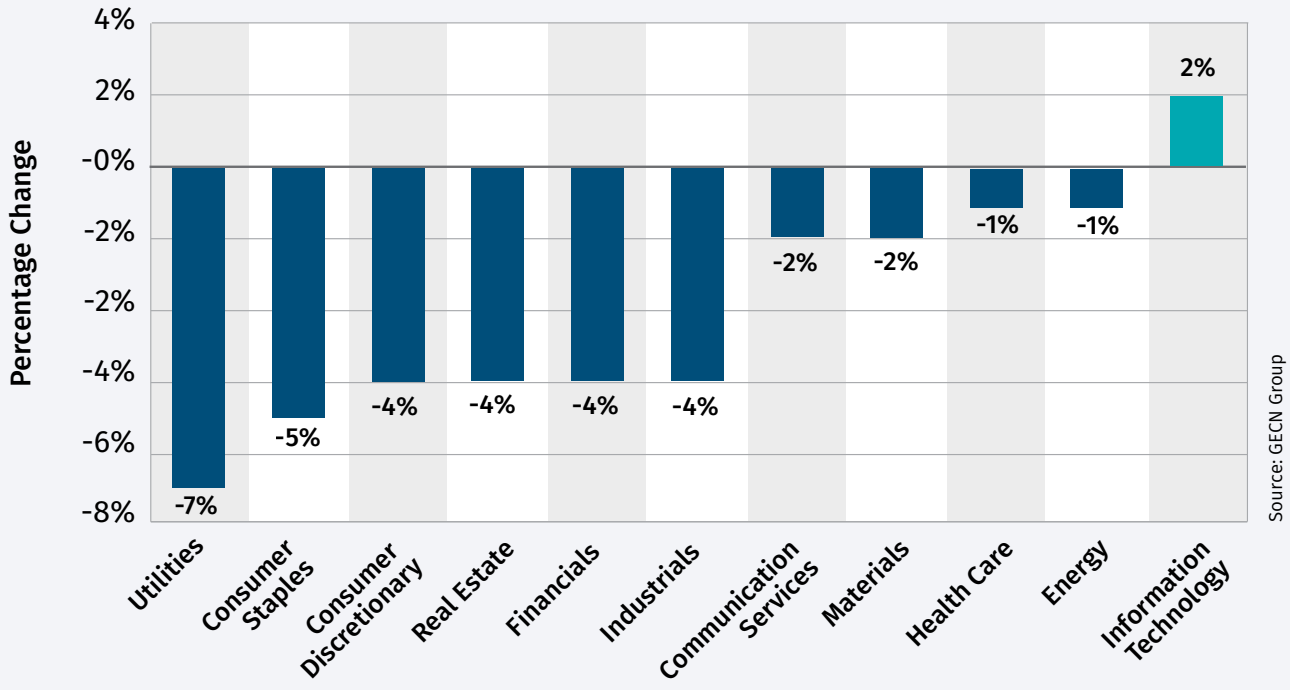
(See charts on next page)



Median Change in Scope 1 & 2 GHG Emissions in Most Recent Year by Region



Median Change in Scope 1 & 2 GHG Emissions in Most Recent Year by Sector



While progress is being made, more action is needed for companies to meet their goals. In many cases, progress will depend on external action by governments and regulators to help phase out fossil fuels through infrastructure development, greater availability of renewable energy sources, and other levers. For companies today, corporate action on climate change can take many forms, including the use of compensation/remuneration plans to incentivize behaviors and signal priorities for environmental action.

Climate Incentives

Tying corporate incentive programs to environmental and emissions targets can take many forms. While the adoption of such measures has increased rapidly in recent years, there are differences by region and sector that reflect the specific dynamics of each. Every company has a unique set of considerations influenced by their business mix, operational conditions, customers, investors, and other factors.

These differences, combined with the varying ways companies design incentive programs, are reflected in environmental incentive trends.

Use of Environmental Measures by Region

While 65% of companies globally use environmental measures in their incentive plans, Europe and the UK continue to lead (84% and 79% prevalence, respectively). This reflects a longer history of regional actors, including regulators and large shareholders, placing pressure on companies to address environmental externalities and demonstrate progress supporting climate ambitions, such as net-zero targets written into EU and UK laws.

Companies in the other regions use environmental measures at a rate of 50% to 63% but have demonstrated a rapid increase in adoption. In the US, for example, the use of environmental measures jumped from 8% to 51% in just four years, although it has plateaued more recently. In Canada, 63% of companies now use environmental measures, which continues to climb from prior years despite some headwinds following anti-greenwashing regulations.

While adoption rates for environmental incentives are climbing in aggregate, there has been some slowdown, particularly in Europe, the US, and South Africa. Some of this reflects market saturation, where the companies most likely to adopt these measures have already done so, and there is little additional room for growth. In the US, the slowdown may also be a function of pushback to ESG by some investors and a pullback by some companies as they address other priorities, including financial performance and operational matters.

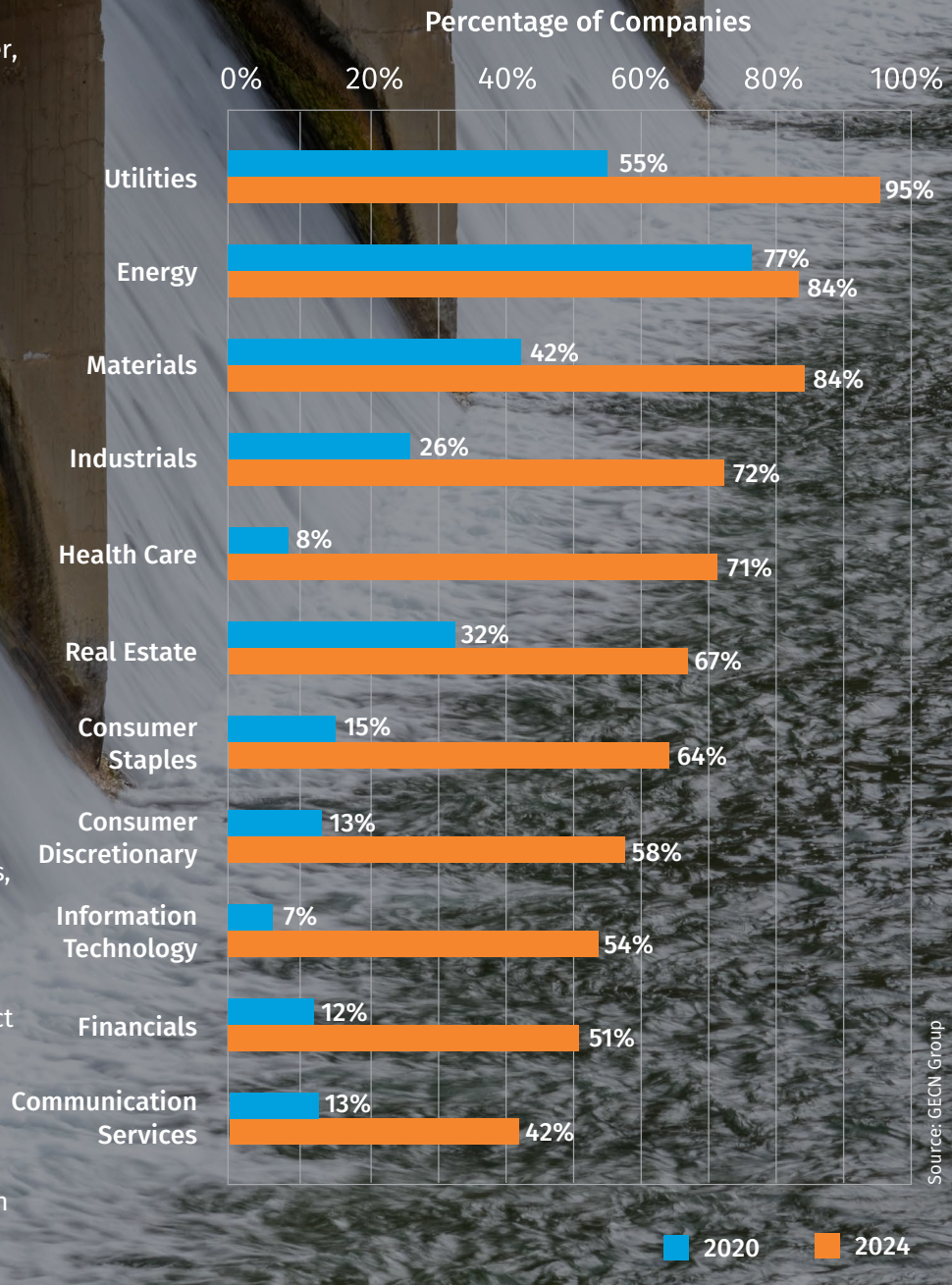
> **"Companies' exposure to climate change risk varies considerably based on numerous factors, especially industry, location, and respective regulatory bodies. Therefore, for companies whose risk is material, climate mitigation strategies are consistent with other risk mitigation initiatives, and investors will expect that such strategies are designed to mitigate those risks to protect shareholder value"**
>
> — **Bob McCormick**
> Executive Director, Council of Institutional Investors (CII)

Use of Environmental Measures by Sector

The use of environmental measures has increased across all sectors. While in prior years, such measures were majority practice for Utilities and Energy, they have gained prominence across the board.

- Utilities and Energy companies have long used environmental measures due to the nature of their operations, which often require compliance with local or national environmental laws that seek to protect habitats and people. Moreover, companies in these sectors often are expected to curtail the negative climate impacts of their operations by local governments and customers. As such, they maintain the highest prevalence of environmental measures
- Health Care and Consumer Staples have demonstrated the greatest change in the adoption of environmental measures. About 8% of health care companies used such measures in 2020 vs. 71% today; for this sector, the increase reflects a combination of factors, including stakeholder concerns, a recent focus by regulators on the waste produced by medical facilities, and energy cost pressures. The rapid adoption among consumer staples companies to 64% also reflects the impact of stakeholder pressures, i.e., customers who demand products that demonstrate positive environmental impacts and sensitivities, such as products that are made from recycled materials

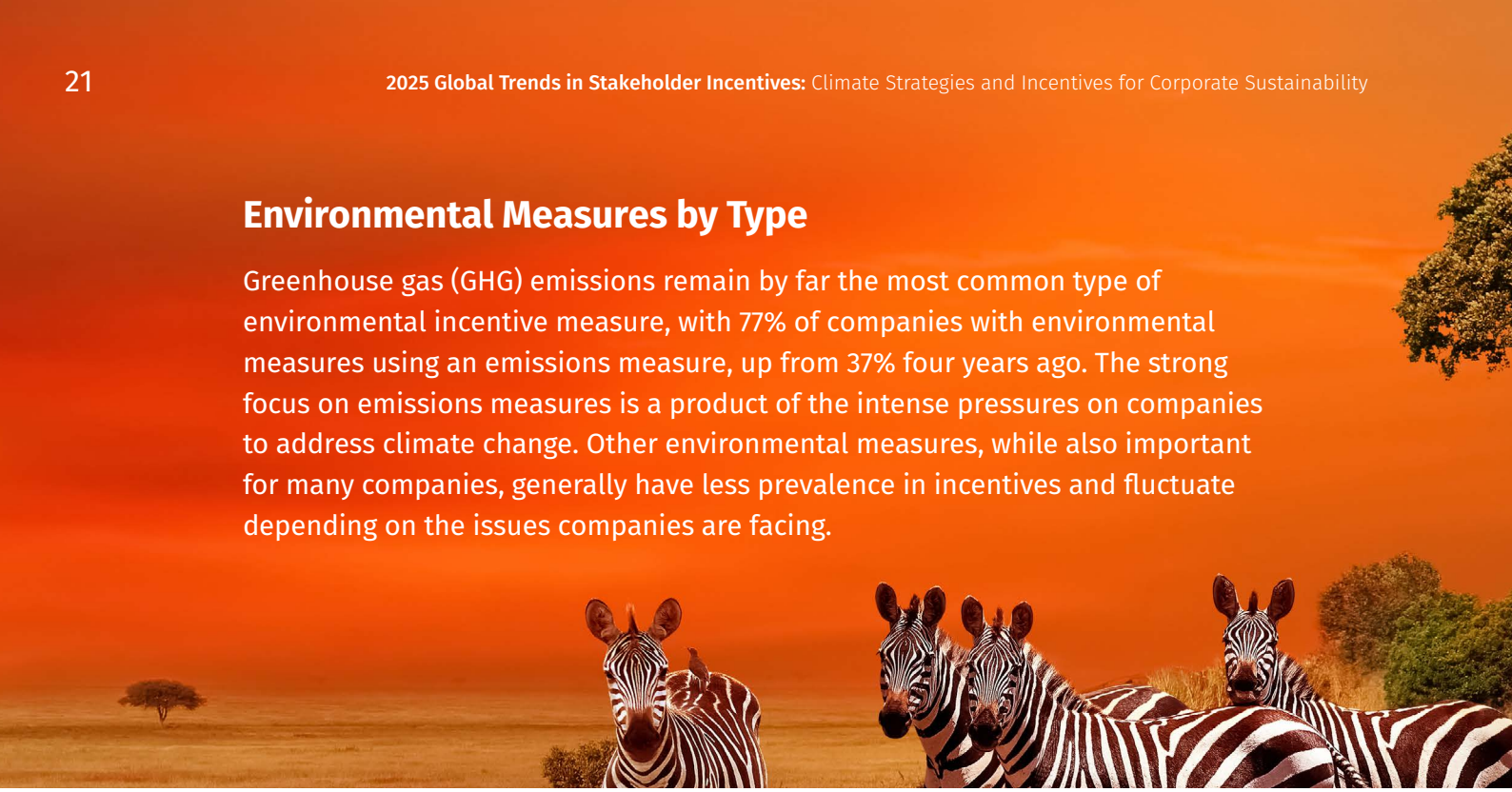
Prevalence of Environmental Incentives by Sector (Sorted by Prevalence 2024)



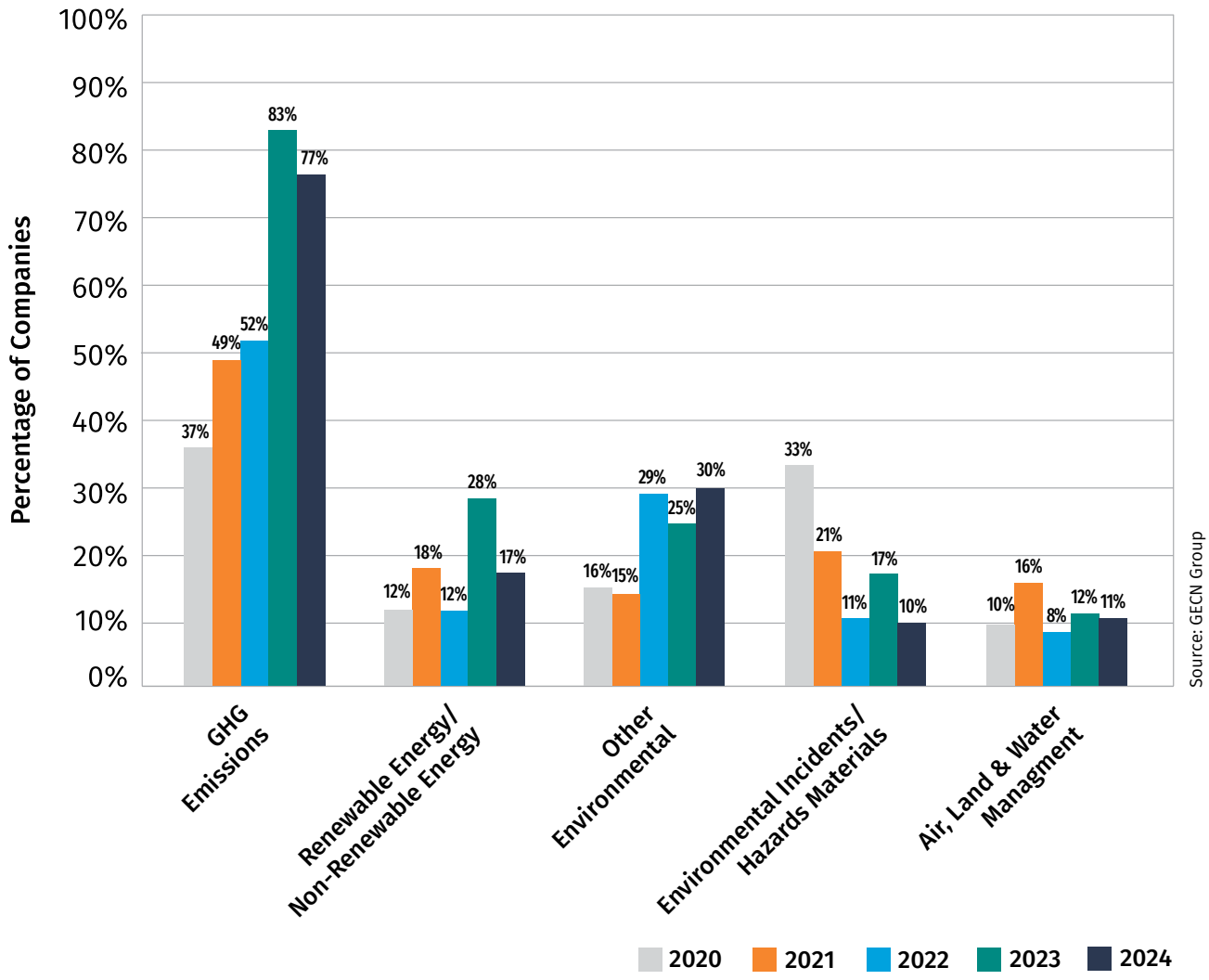
Source: GECN Group

Environmental Measures by Type

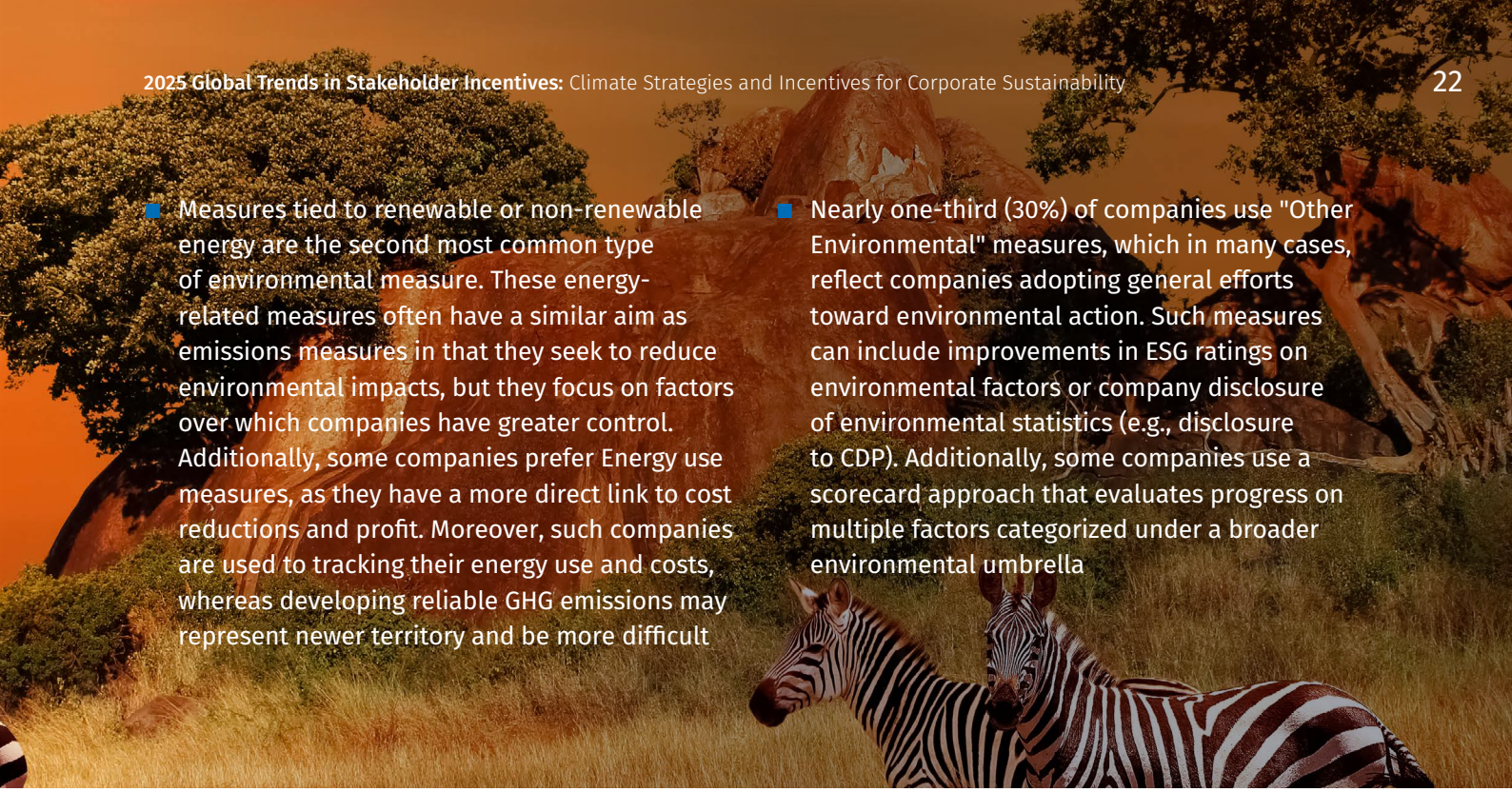
Greenhouse gas (GHG) emissions remain by far the most common type of environmental incentive measure, with 77% of companies with environmental measures using an emissions measure, up from 37% four years ago. The strong focus on emissions measures is a product of the intense pressures on companies to address climate change. Other environmental measures, while also important for many companies, generally have less prevalence in incentives and fluctuate depending on the issues companies are facing.



Prevalence of Environmental Measures by Type of Measure Among Companies Using Environmental Measures



Source: GECN Group



- Measures tied to renewable or non-renewable energy are the second most common type of environmental measure. These energy-related measures often have a similar aim as emissions measures in that they seek to reduce environmental impacts, but they focus on factors over which companies have greater control. Additionally, some companies prefer Energy use measures, as they have a more direct link to cost reductions and profit. Moreover, such companies are used to tracking their energy use and costs, whereas developing reliable GHG emissions may represent newer territory and be more difficult
- Nearly one-third (30%) of companies use "Other Environmental" measures, which in many cases, reflect companies adopting general efforts toward environmental action. Such measures can include improvements in ESG ratings on environmental factors or company disclosure of environmental statistics (e.g., disclosure to CDP). Additionally, some companies use a scorecard approach that evaluates progress on multiple factors categorized under a broader environmental umbrella

Environmental Measures in STI vs. LTI Plans

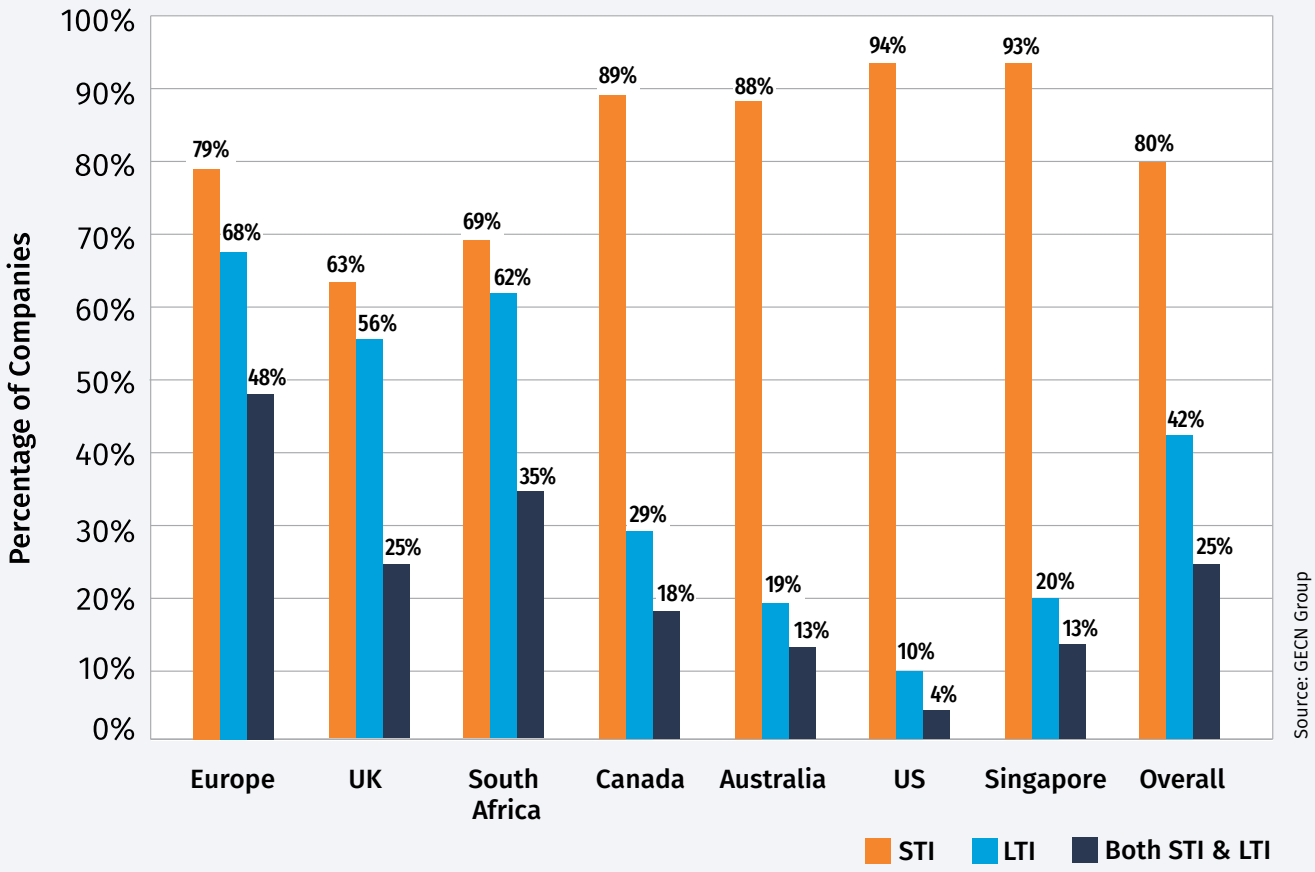
Although environmental incentive measures tend to relate to much longer-term sustainability goals, 80% of companies use these measures in the STI plan. The STI plan has been the preeminent home for environmental, and environment-specific and ESG measures more broadly, due to strategic measures historically being used in annual incentive plans. Given the relative newness of ESG measures, many companies still feel more comfortable using these measures in annual incentives, as they can adjust measures and goals every year as methodologies and/or focus areas shift.

Nevertheless, environmental goals tend to lend themselves better to the LTI plan because changing a company's environmental footprint is a multi-year endeavor and is rarely a straight line. As a result, companies are increasingly adopting these measures in their LTI plan, with 42% of large global companies now using environmental measures in their long-term plan. As noted earlier in this report, many companies have set net-zero ambitions and goals that are extremely long-term, and breaking those goals down further by shorter time periods can be easier for many companies to accomplish in an LTI plan, in which performance periods are generally 3 years.

- Companies in Europe (68%), South Africa (62%), and the UK (56%) are the most likely to use environmental measures in their LTI plan, although many use the measures in their STI plan as well. In Europe, 48% of companies use environmental measures in both their STI and LTI plans
- US companies demonstrate the lowest use of environmental measures (10% prevalence) in their LTI plan. However, this prevalence is expected to continue increasing over time as US companies gain confidence in working with environmental data and setting quantitative longer-term goals tied to their environmental priorities

(See chart on next page)

Prevalence of Environmental Measures in STI, LTI, or Both Plans by Region



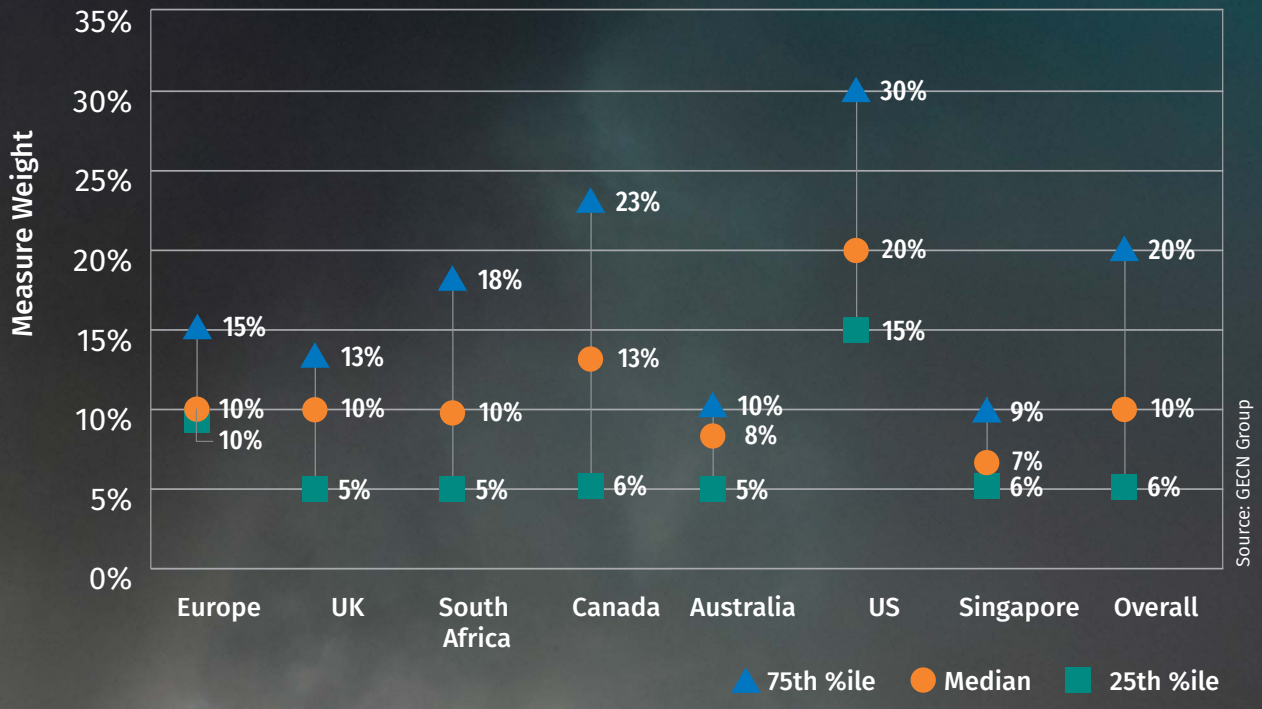
Environmental Measure Weighting

When used on a weighted basis, the median weight of environmental measures is typically 10% when used in the STI plan and 15% when used in their LTI plan. Differences by region generally reflect variations in incentive program design, such as the typical mix of fixed vs. variable compensation and the use of non-financial measures in STI vs. LTI plans.

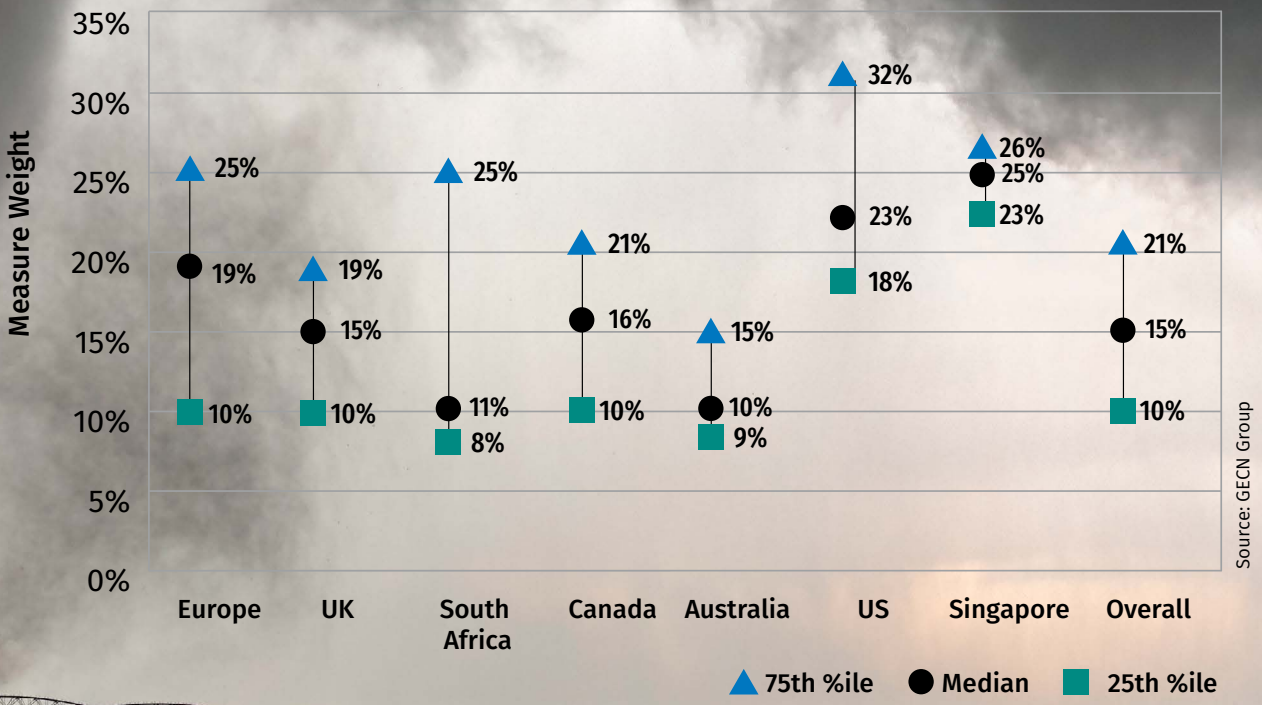
Companies must evaluate their strategic objectives to determine the appropriate weight for environmental measures in their incentive plan. For any given year, the focus may need to shift to financial measures or other non-financial goals. Some firms design ESG measures to pay out only if a minimum level of financial performance is first achieved.

(See charts on next page)

Weight of Environmental Measures in STI Plans by Region Among Companies Using Environmental Measures



Weight of Environmental Measures in LTI Plans by Region Among Companies Using Environmental Measures

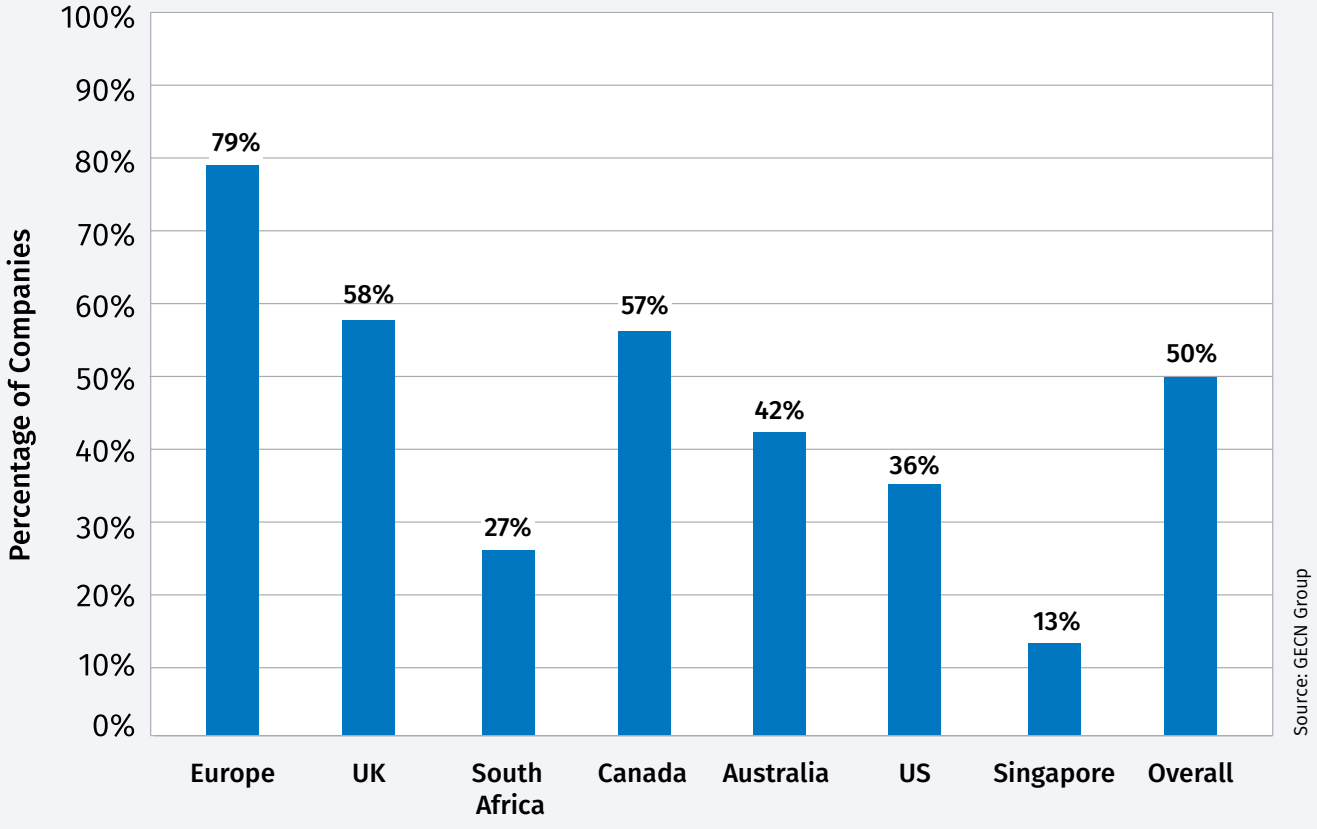


GHG Emissions Measures

There are some significant differences by region in the use of GHG emissions-specific measures. Among large global companies, emissions incentives are most common in Europe (79%), the UK (58%), and Canada (57%). Companies in South Africa (27%) and Singapore (13%) are the least likely to use emissions-based incentives for executives. These differences stem from the sectors prominent in each region and variations in regional stakeholders. In Europe, for instance, stakeholder engagement, regulatory actions, and climate groups have pressured companies on emissions more so than in other regions.

> **"We believe there are material ESG characteristics that improve the long-term sustainability of a company. It's industry specific, especially where the transition to a low-carbon economy is important. We don't think they (ESG incentives) should dominate the compensation plan"**
>
> **— Fund manager (requested anonymity)**
> Large institutional investor

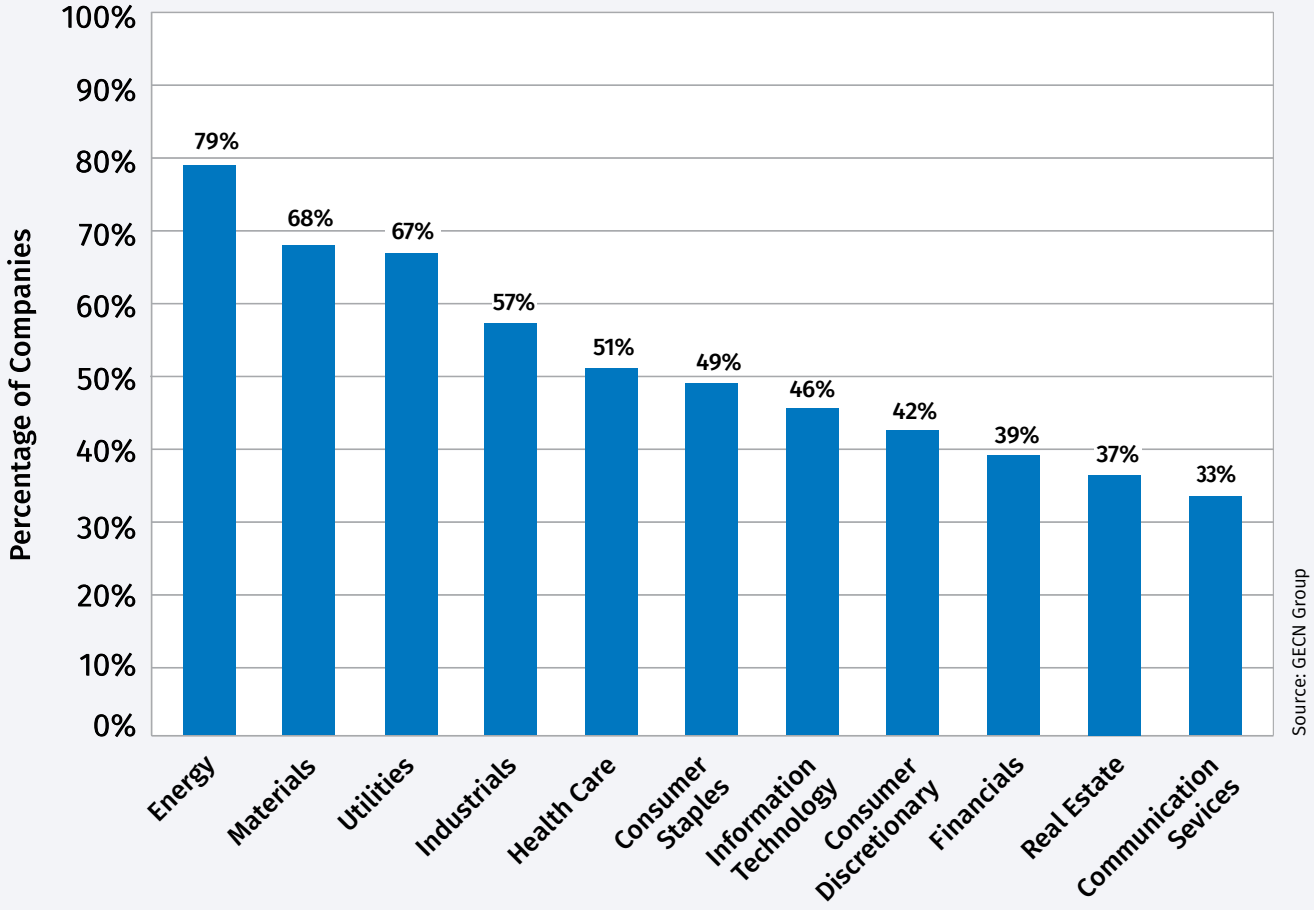
Prevalence of Emissions Incentives by Region



- Energy (79%), Materials (68%), and Utilities (67%) companies demonstrate a higher prevalence of using emissions measures as companies in these industries produce significant emissions through the inherent nature of their operations in the production and distribution of energy, electricity, and raw materials. As such, they face pressure from customers and regulators to reduce emissions and mitigate their environmental impacts. These companies were down 47% in the first half of 2023 compared to the same period the prior year
- Communication Services (33%), Real Estate (37%), and Financial Services (39%) demonstrate the lowest use of emissions-related measures. While many companies in these sectors use environmental measures, those tied to emissions are sometimes less of a concern because these businesses tend to have lower rates of emissions. Among Financials, for instance, companies using environmental incentives often tie goals to downstream customers rather than direct emissions targets

Many companies also use measures targeting GHG emissions intensity, which is a normalized measure of emissions relative to a specific activity. Intensity is calculated by dividing emission measures by a unit of volume or "work," such as revenue, number of products sold, or operating area, with the denominator varying by industry. Emissions intensity allows companies to track and target emissions reductions without sacrificing their growth ambitions; nevertheless, some environmental groups and investors prefer that companies measure absolute, rather than intensity-adjusted, emissions.

Prevalence of Emissions Incentives by Sector

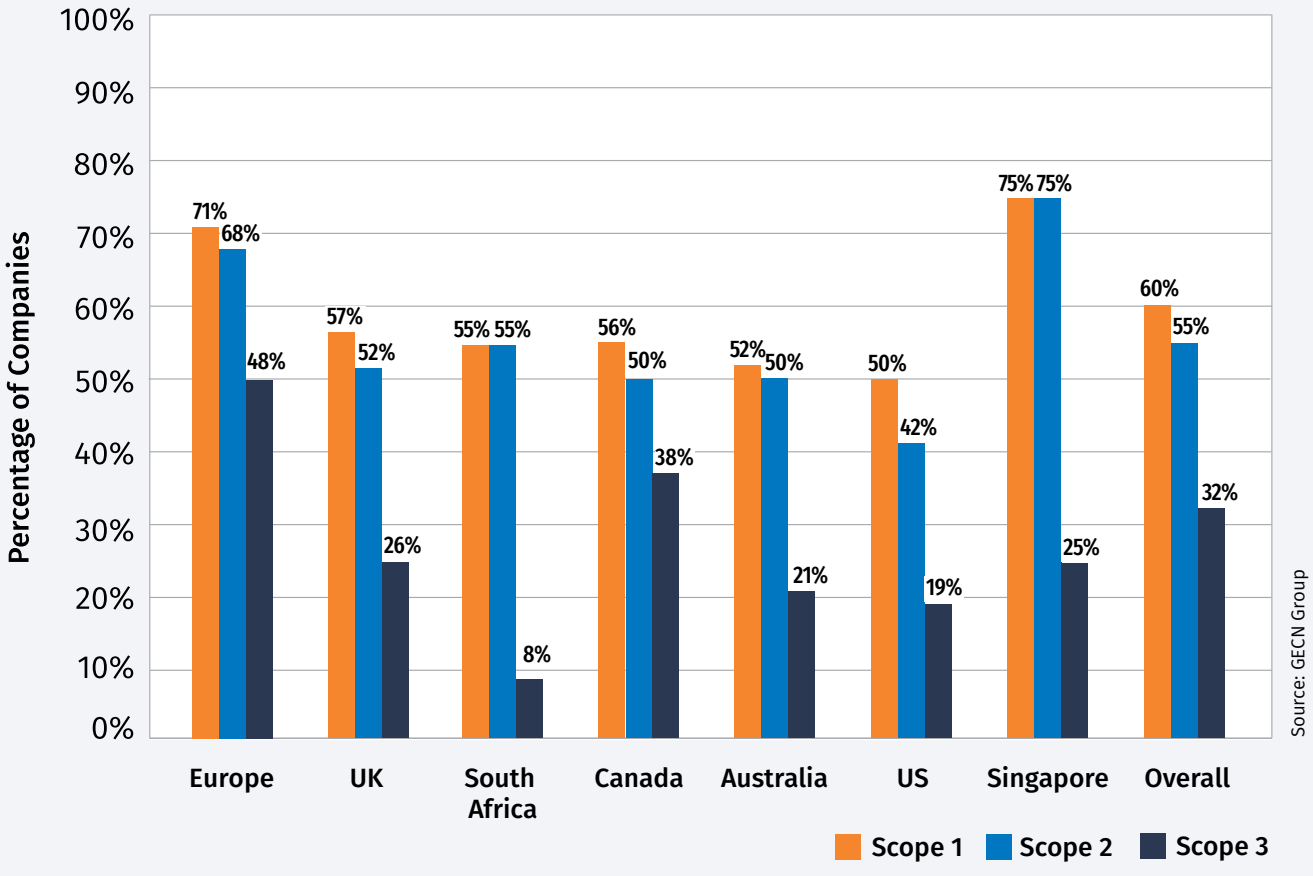


Emissions Measures by Scope

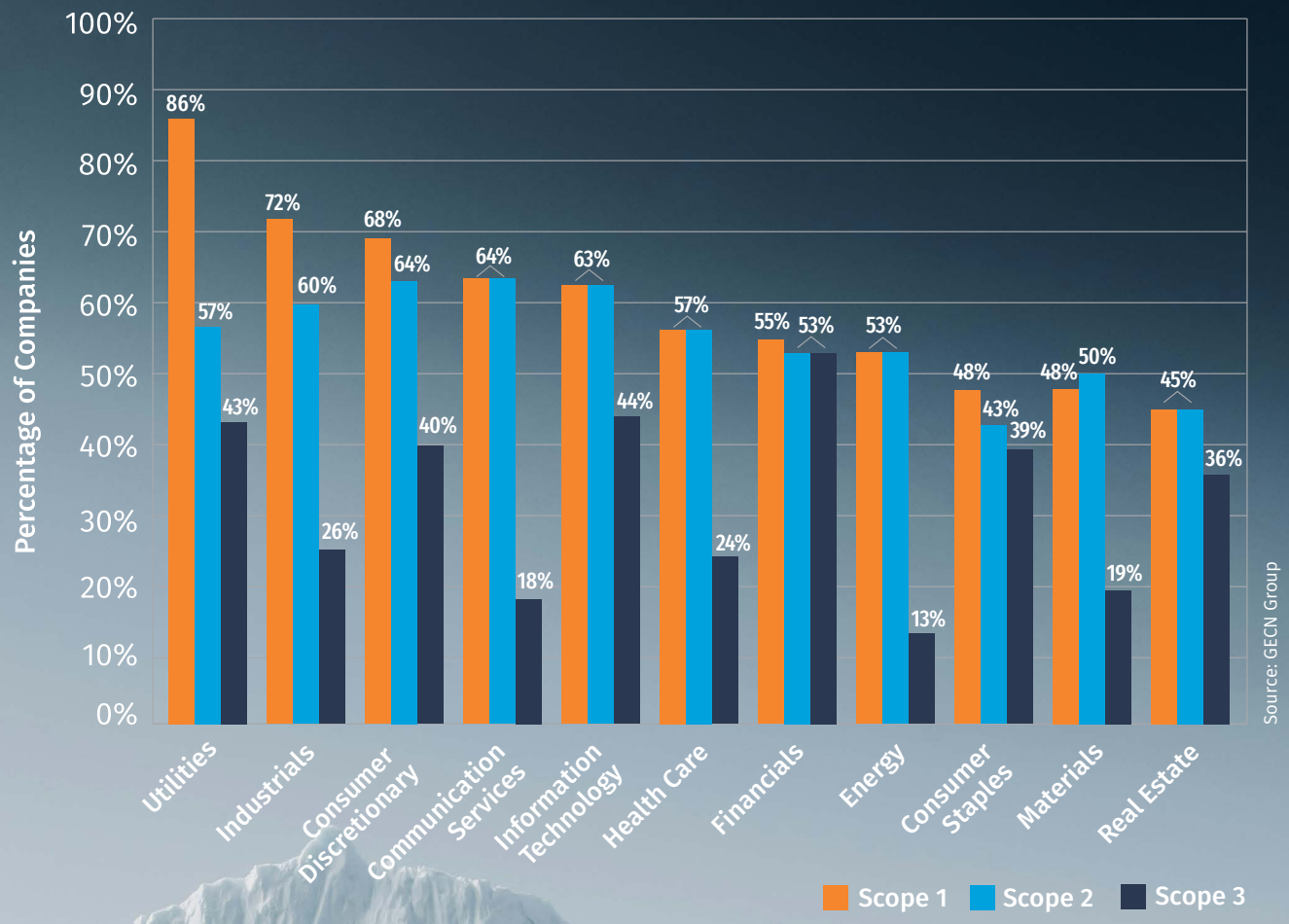
Companies using emissions incentive measures have had to determine whether to establish goals based on Scope 1, Scope 2, or Scope 3 emissions, or some combination thereof. Among companies using emissions measures, 60% use Scope 1, 55% use Scope 2, and 32% use Scope 3 measures.

The definition of emissions goals is important as the choice will drive different actions. For example, a Scope 1 target will inherently focus on company operations, which could mean, for example, changing a vehicle fleet to reduce direct emissions. A Scope 2 goal relates to emissions from purchased energy and may target investments in energy efficiency or renewable energy sources. Scope 3, which measures emissions across a company's supply chain, may be more complex in both measurement and performance tracking. Companies with Scope 3 goals might look for ways to reduce the downstream emissions of the products or switch to more sustainable suppliers.

Prevalence of Emissions Incentives by Scope 1, 2, and 3, and by Region Among Companies with Emissions Incentives



Prevalence of Emissions Incentives by Scope 1, 2, and 3, and by Sector Among Companies with Emissions Incentives



- While a majority of companies' emissions measures target Scope 1 and 2, the use of Scope 3 is more variable. The highest prevalence of Scope 3 is among European firms at 48%. The lowest prevalence is in South Africa at 8%. Regional differences in Scope 3 incentive adoption are partly a reflection of the amount of time companies in each region have measured and worked with Scope 3 data. Moreover, the concentration of certain sectors in each market is likely to impact adoption, as certain sectors are more likely to focus on reducing their Scope 3 vs. Scope 1 or 2 emissions
- On a sector basis, the highest prevalence of Scope 3 is Financials (53%), as many large banks have established targets for "financed emissions," i.e., indirect emissions resulting from a financial institution's lending and investment activities. Energy companies rarely target Scope 3 emissions (13%), likely because they may find it difficult to reduce the absolute emissions of their products in a meaningful way while seeking to grow their businesses

Quantitative vs. Qualitative Measures

Although strategic emissions targets are generally quantified, companies adopt emissions measures in incentives in both quantitative and qualitative forms. In some cases, companies' goals are tied to activities or milestones that aim to reduce emissions in the long term, such as goals aimed at calculating and disclosing Scope 3 emissions or making certain operational investments for future reductions.

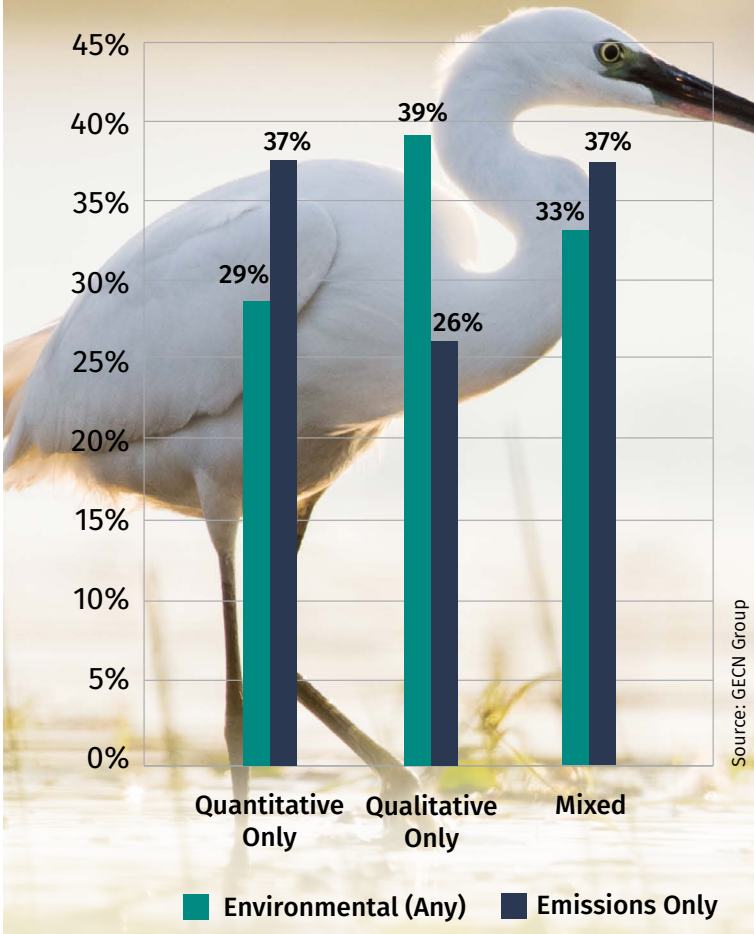
Among companies using emissions measures, 37% use only quantitative goals, 26% use only qualitative goals, and 37% use a mix of quantitative and qualitative goals. Notably, companies using environmental measures generally (not just emissions), tend to use a higher mix of qualitative goals, indicating emissions measures lend themselves to quantitative targets. Companies adopting emissions measures typically set goals that are aligned with public commitments, which tend to be quantitative and aim for a percentage reduction in emissions over a specified period of time (e.g., by 2030). The incentive goal, in turn, often aims to reduce emissions over a shorter timeframe (e.g., 3 years).

Emissions Goal Disclosure

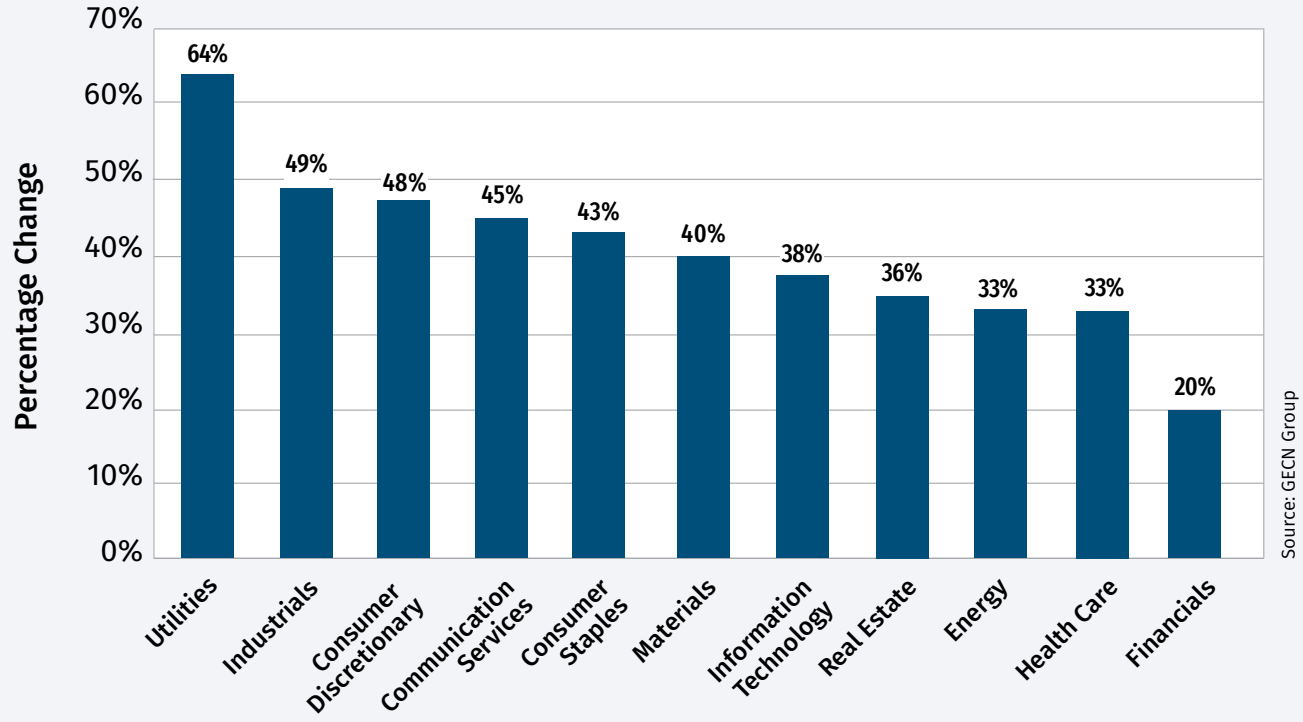
Among companies using emissions measures, only 39% disclose a specific goal as part of the incentive plan disclosure. Companies that do not disclose specific goals are often more likely to use qualitative measures. Many companies refer to their broader climate aspirations and their ESG/sustainability reporting to provide direction of what they aim to achieve, sometimes without reporting specific incentive goals publicly. However, investors and proxy advisors often expect more robust disclosure of goals, especially when evaluating whether goals are rigorous and incentive payouts are merited.

(See charts on next page)

Prevalence of Quantitative, Qualitative, or Mixed Measures Among Companies Using Environmental (Any) vs. Emission Incentives



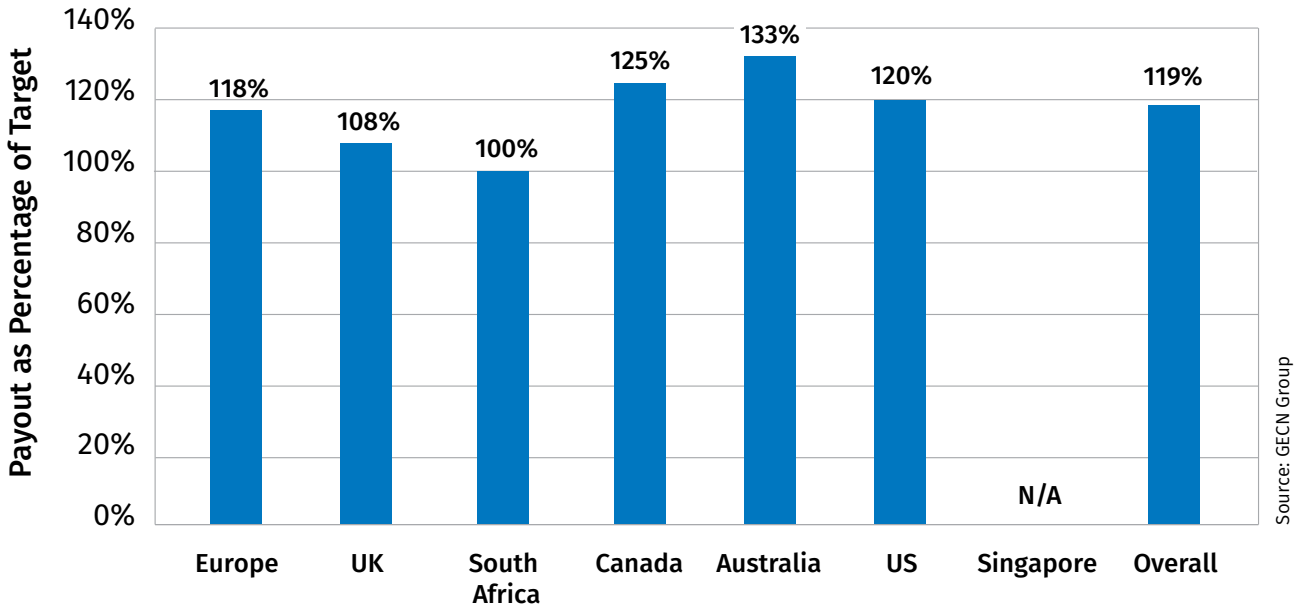
Prevalence of Disclosure of Specific Emissions Incentive Goals by Sector Among Companies with Emissions Incentives



Payouts on Emissions Incentives

The average payout on emissions incentives in the most recent year of disclosures was 119% of target. Across all regions, payouts averaged between 100% and 133%. This suggests that, on average, executives are achieving their emissions goals. This somewhat contradicts the fact that most companies increased their emissions in the most recent year. However, the discrepancy can be explained by the fact that many goals are based on activities rather than outcomes. For example, emissions goals may relate to disclosure or initial investments aimed at progress over the longer term.

Average Payout as a % of Target by Region Among Companies with Emissions Incentives

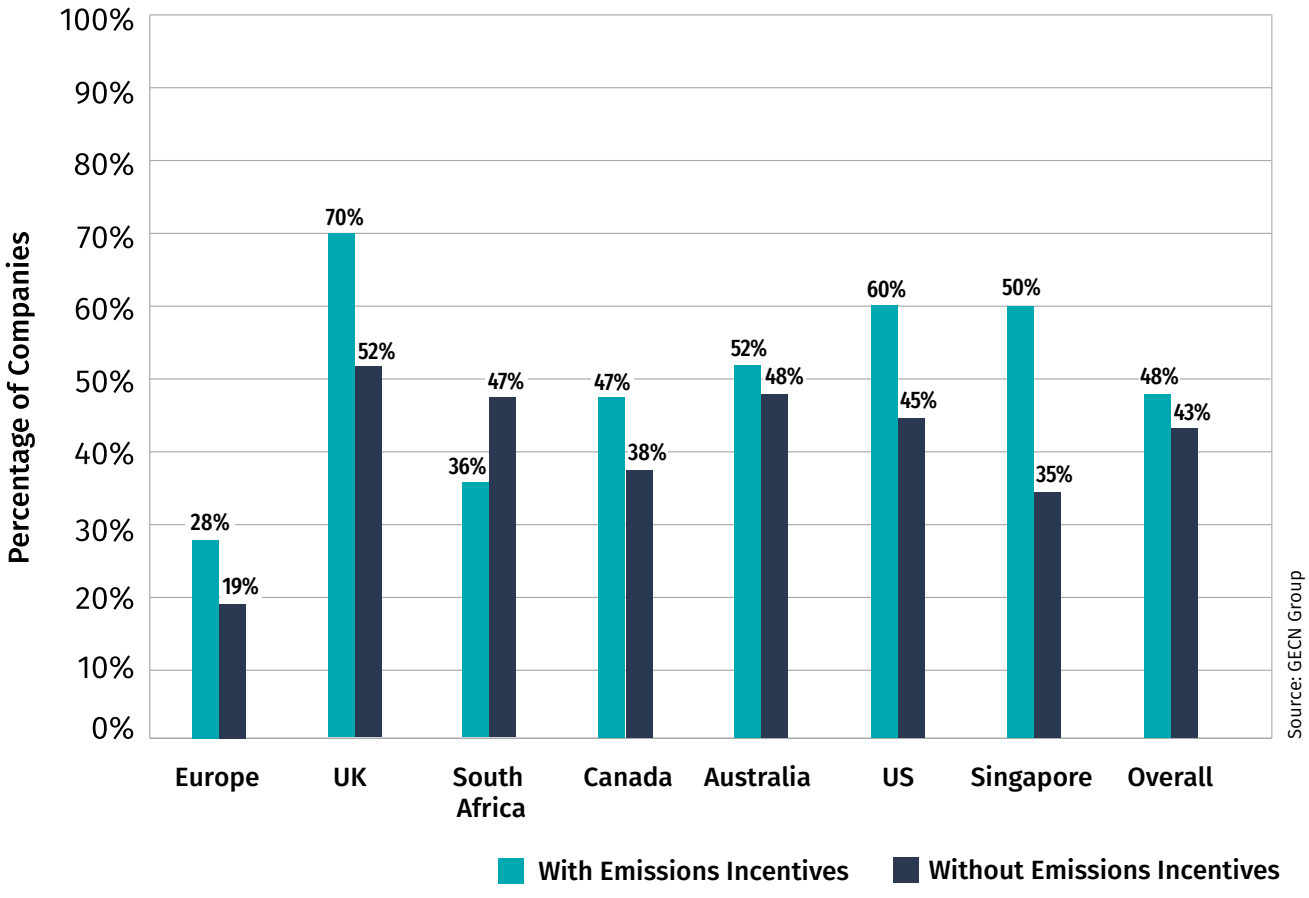


The Case for Emissions Incentives

Overall, companies with emissions incentives were more likely to reduce their emissions compared to companies without emissions incentives. In the UK, 70% of companies with emissions incentives decreased their emissions compared to 52% of companies without those incentives. In the most recent year, companies with emissions incentive measures in most markets had a higher likelihood of emissions reductions compared to those without emissions incentive measures. While there are individual company and regional exceptions, in general, emissions incentives are correlated with emissions reductions.

While a causal relationship has not been proven, the correlation suggests that emissions incentives work. Companies embarking on efforts to measure and track emissions and set credible goals linked to public commitments can effectively use incentives as a tool to drive progress against those goals.

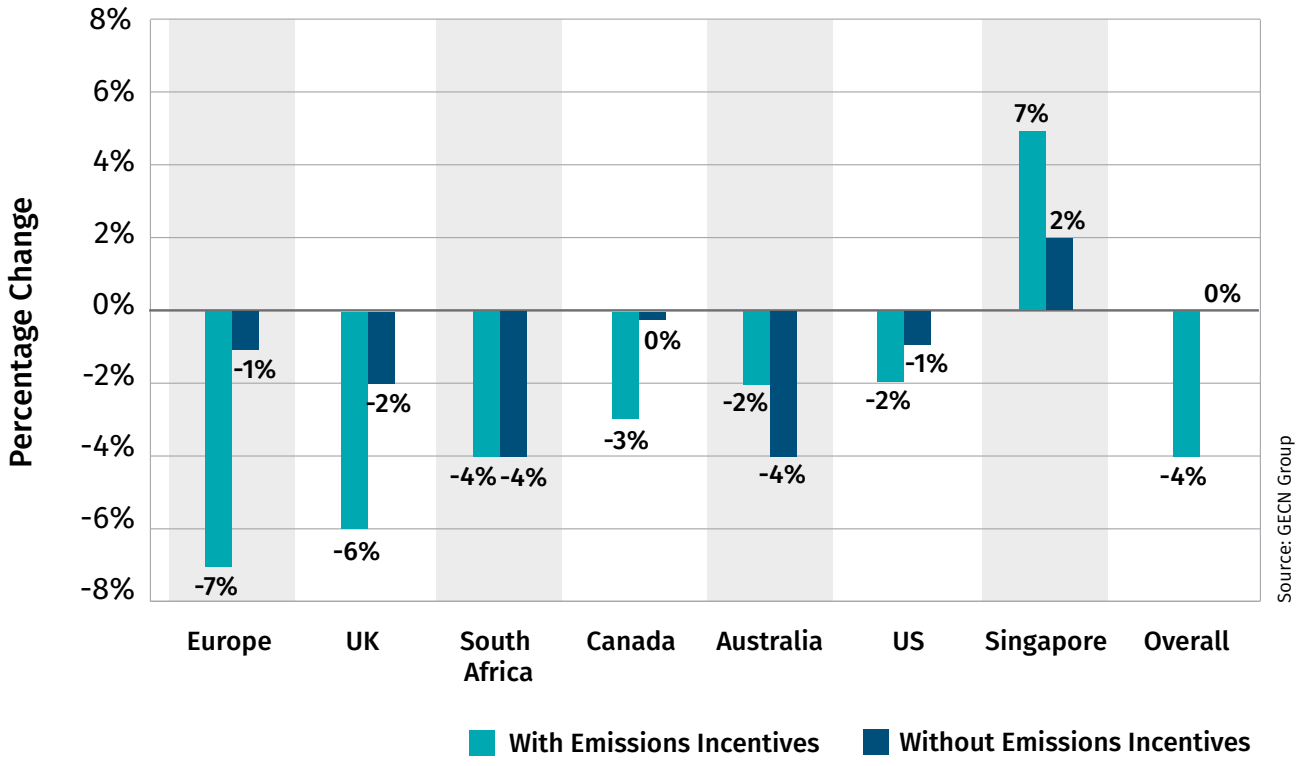
Prevalence of Companies with Scope 1 & 2 Emissions Decrease in Most Recent Year by Region Among Companies with and without Emissions Incentives



Companies with emissions incentives accomplished a median decrease (-4%) in their Scope 1 and 2 emissions in the most recent year, whereas companies without emissions incentives experienced a median of no change (0%) in their emissions. European companies with emissions incentives saw the strongest drop in their emissions, with a median of -7%, compared to European companies without emissions incentives, with a median of -1%.

In Australia and SIngapore, the trend was reversed so that companies with emissions incentives performed at the median worse than those without such incentives. For example, in Singapore, the median emissions change was +7% for companies with emissions incentives and +2% for those without.

Median Change in Scope 1 & 2 Emissions Among Companies with and without Emissions Incentives



Source: GECN Group

Takeaways and Action Steps

Large corporations are taking a lead in forging ahead on their sustainability initiatives, regardless of which way the political winds are blowing. To strengthen their efforts, companies are making greater use of environmental, especially climate-related, incentives. While the use of such incentives remains a choice point, there appears to be a positive correlation between the amount of progress a company makes on its reduction of GHG emissions and its use of climate-related incentives.

Corporate board directors and management teams play a critical role and in fact have an obligation to guide their organizational strategy with climate goals, and if appropriate, link performance to sustainability incentives.

TAKEAWAYS	ACTION STEPS FOR DIRECTORS AND MANAGEMENT
Climate Strategies and Ambitions	
Climate Strategies are an Expectation ■ Nearly all global companies have a climate strategy. This is no longer a consideration — it is an expectation and obligation ■ GHG emissions are a key focus area for investors, regulators, customers, employees, and other constituencies ■ Specifically, stakeholders want to understand what role their companies are playing in mitigating climate change ■ While mitigating climate change is a long-term game, there is urgency to making tangible progress	**Systematically Oversee, Maintain, and Update the Company's Climate Strategy** ■ Ensure the board has a definitive "home" (i.e., a committee and/or the full board) for overseeing environmental strategies, goal-setting, and monitoring progress toward achieving those goals ■ Regularly review the company's environmental and climate strategies in the context of corporate strategy and business dynamics (e.g., customer behaviors, regulatory changes, technological changes, and other forces) ■ Maintain an environmental roadmap and current-state dashboard for assessing progress. Systematically review the company's Scope 1, 2, and 3 emissions measurement methodologies, goals, and performance against those goals ■ Analyze competitive progress and comparative ratings by independent agencies to augment performance assessments ■ To the extent possible, disclose goals externally so investors and other external constituencies understand the company's progress; in addition, communicate goals and progress internally so employees understand their role in achieving those goals

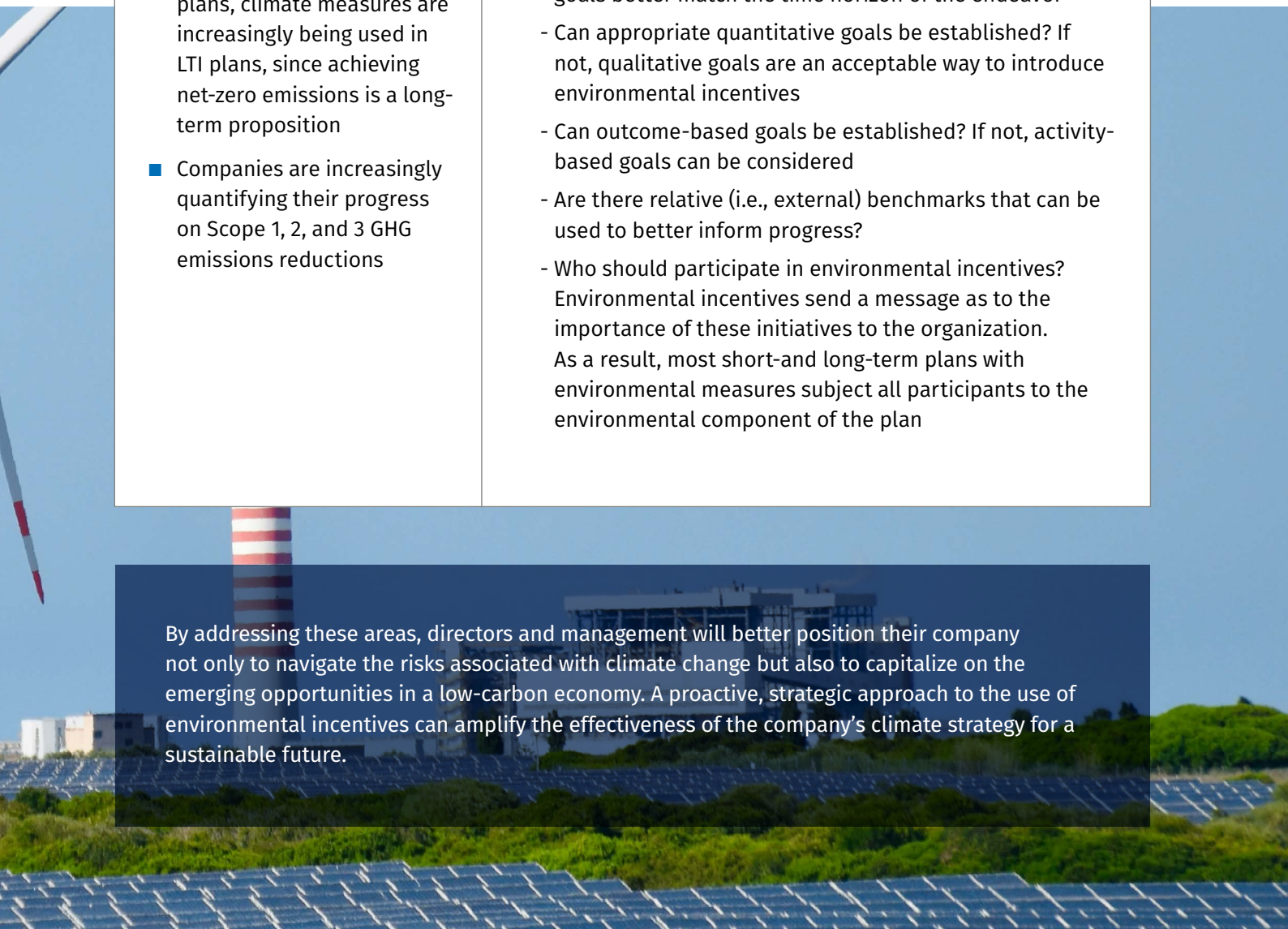
TAKEAWAYS	ACTION STEPS FOR DIRECTORS AND MANAGEMENT
Climate Incentives	

Environmental Incentives Have Surged in Prevalence and are Correlated with the Rate of GHG Reduction

- Among ESG incentives, the prevalence of environmental incentives are the most rapidly growing and have surpassed the tipping point. Now, the majority of large companies have adopted environmental incentives in all regions
- GHG reduction incentives appear to be effective in contributing to the reduction of GHG emissions
- While primarily used in STI plans, climate measures are increasingly being used in LTI plans, since achieving net-zero emissions is a long-term proposition
- Companies are increasingly quantifying their progress on Scope 1, 2, and 3 GHG emissions reductions

Evaluate Whether Incentives Could Help Achieve Climate Objectives; If So, Make Company-Specific Incentive Design Choices

- Consider adopting environmental/climate incentives if:
  - Environmental objectives are part of the company's core strategy
  - There is a need to improve performance on environmental/climate measures
  - Wins on sustainability goals also produce wins financially over the long term
- Tailor the approach to the company's sustainability strategy and circumstances to ensure alignment; no one is looking for a one-size-fits-all approach. Address the following issues and questions:
  - Is the company prepared to set long-term environmental incentive goals? Setting long-term goals is often more challenging than setting short-term goals, but long term goals better match the time horizon of the endeavor
  - Can appropriate quantitative goals be established? If not, qualitative goals are an acceptable way to introduce environmental incentives
  - Can outcome-based goals be established? If not, activity-based goals can be considered
  - Are there relative (i.e., external) benchmarks that can be used to better inform progress?
  - Who should participate in environmental incentives? Environmental incentives send a message as to the importance of these initiatives to the organization. As a result, most short-and long-term plans with environmental measures subject all participants to the environmental component of the plan

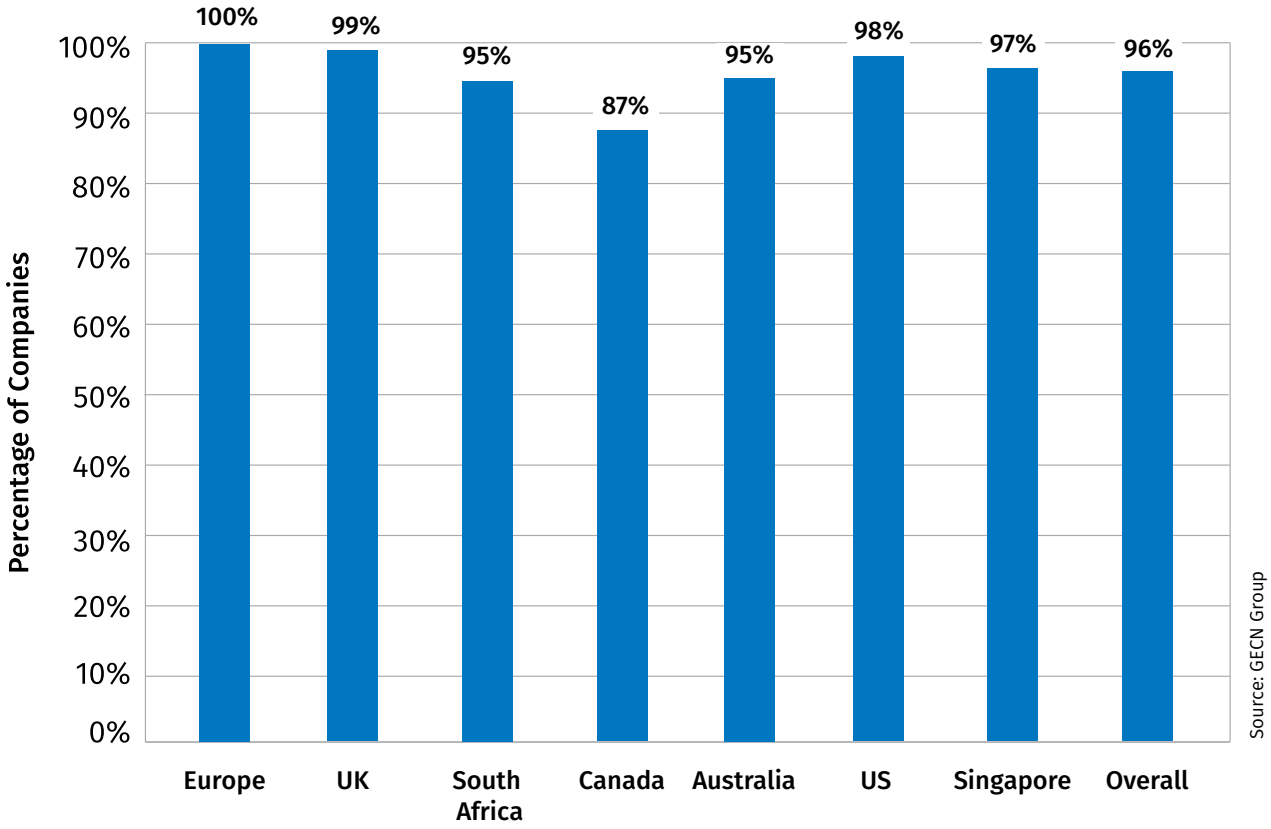


By addressing these areas, directors and management will better position their company not only to navigate the risks associated with climate change but also to capitalize on the emerging opportunities in a low-carbon economy. A proactive, strategic approach to the use of environmental incentives can amplify the effectiveness of the company's climate strategy for a sustainable future.

Appendix

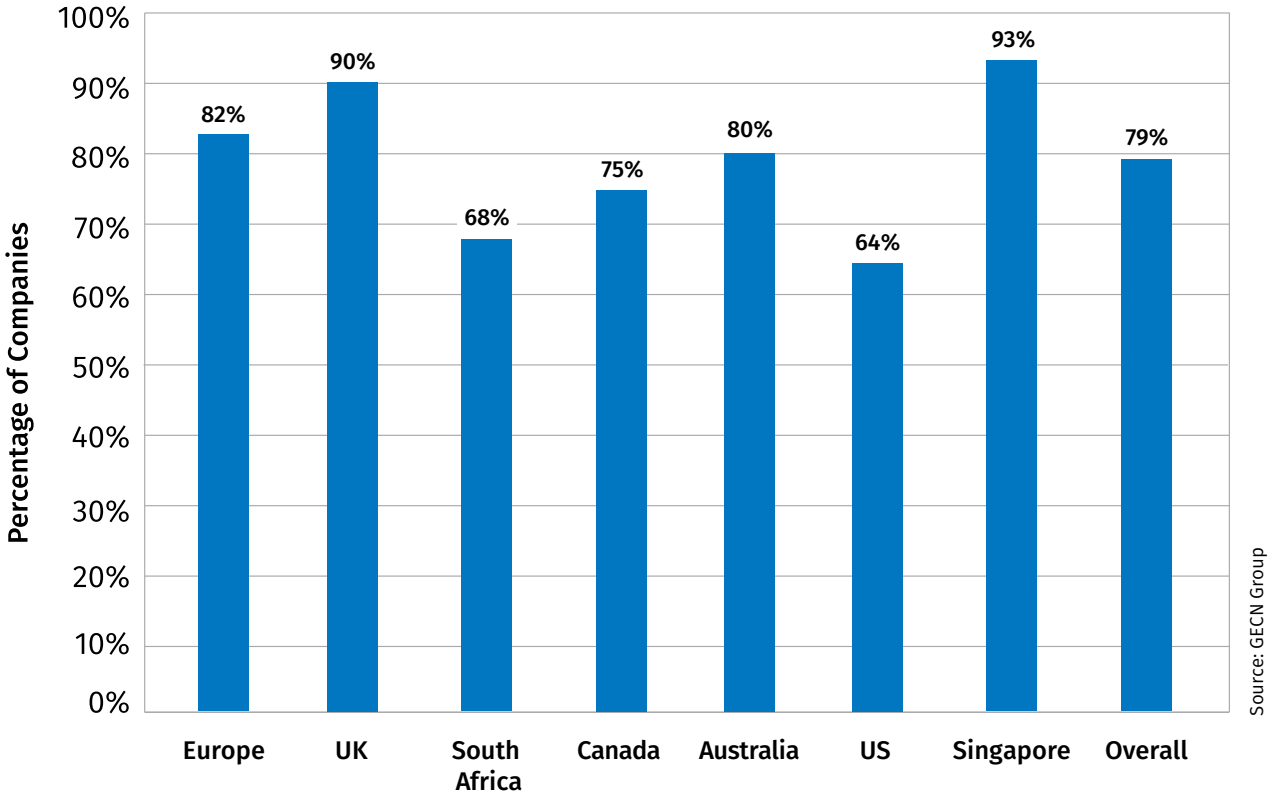
This Appendix includes additional data analysis on climate strategies and incentives not included in the body of the report but which may be of use in guiding a company's climate journey.

Prevalence of Disclosed Climate Strategy by Region



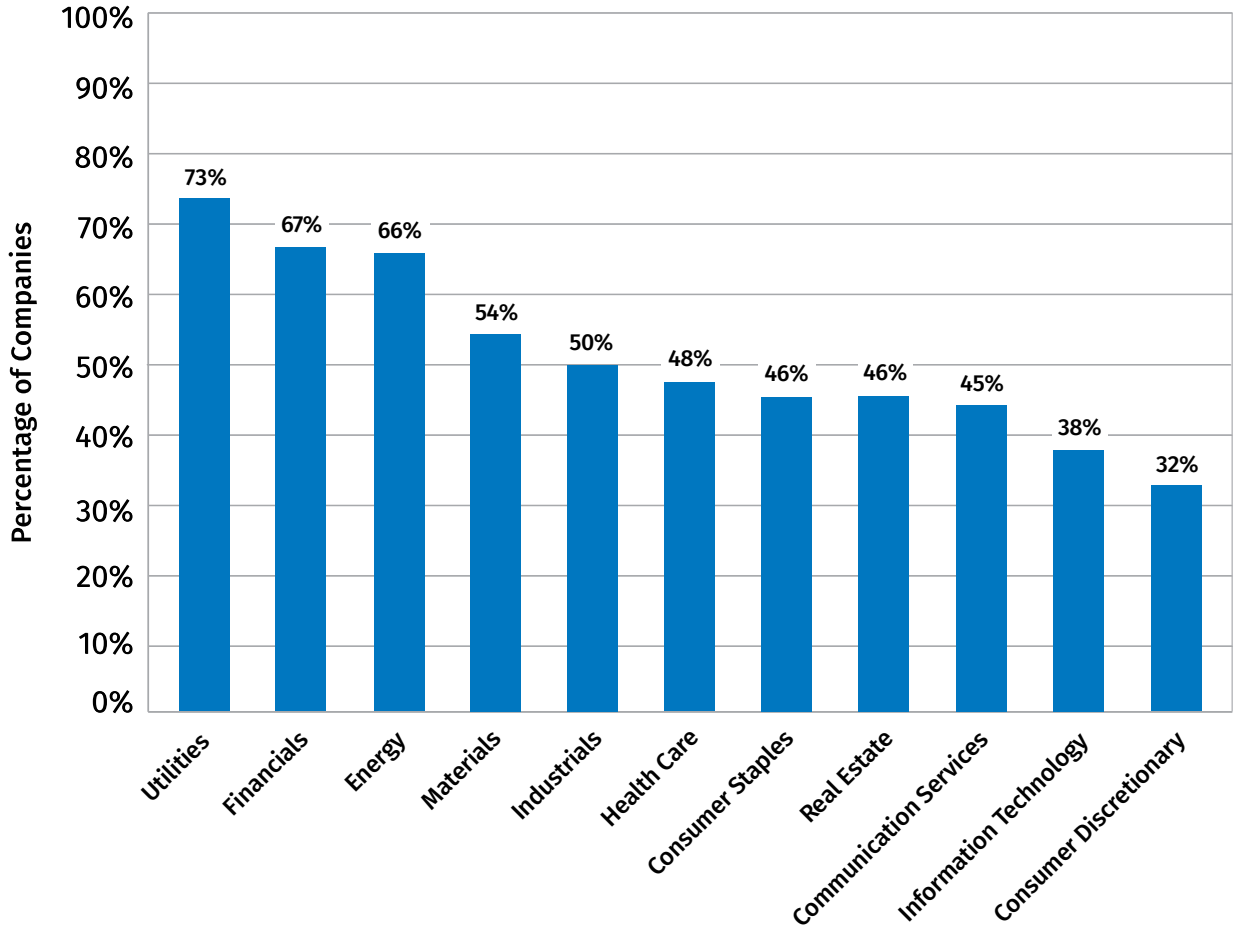
Source: GECN Group

Prevalence of Emissions Intensity Disclosure by Region



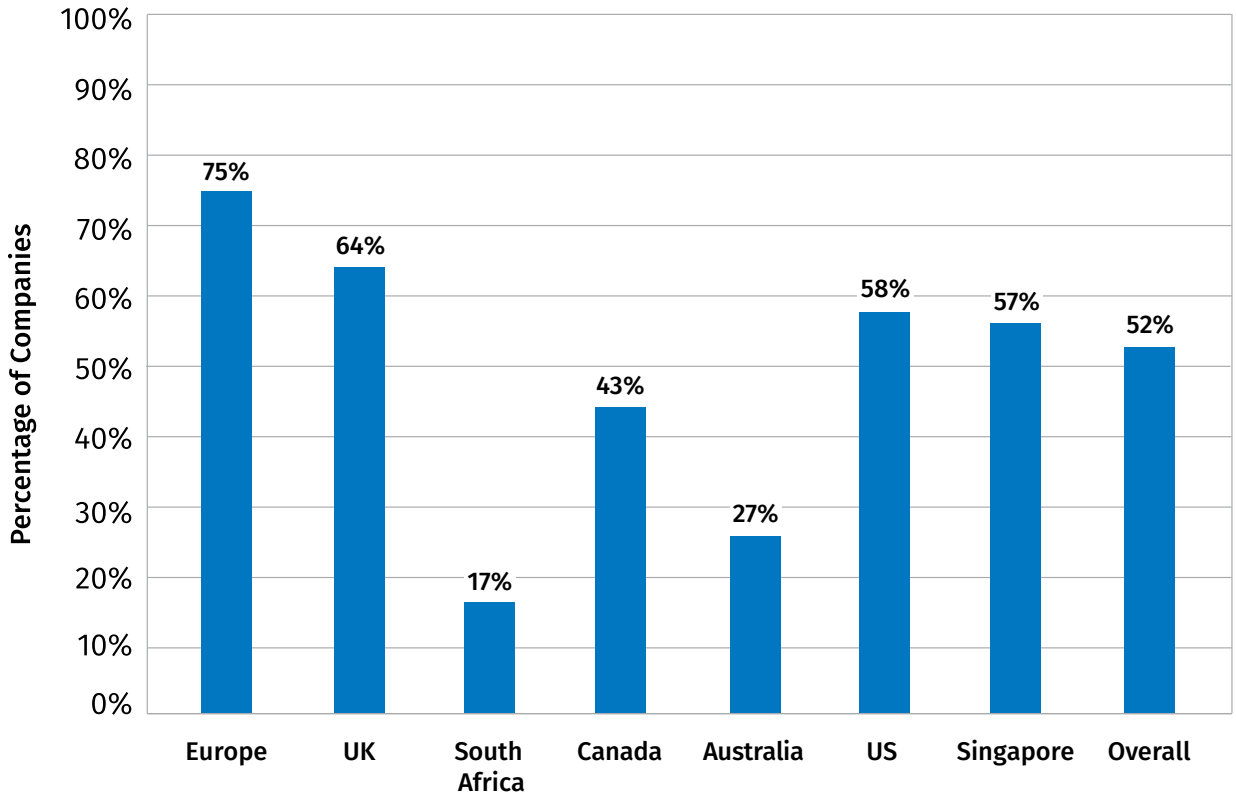
Source: GECN Group

Prevalence of Near-Term Scope 3 GHG Emissions Reduction Targets by Sector



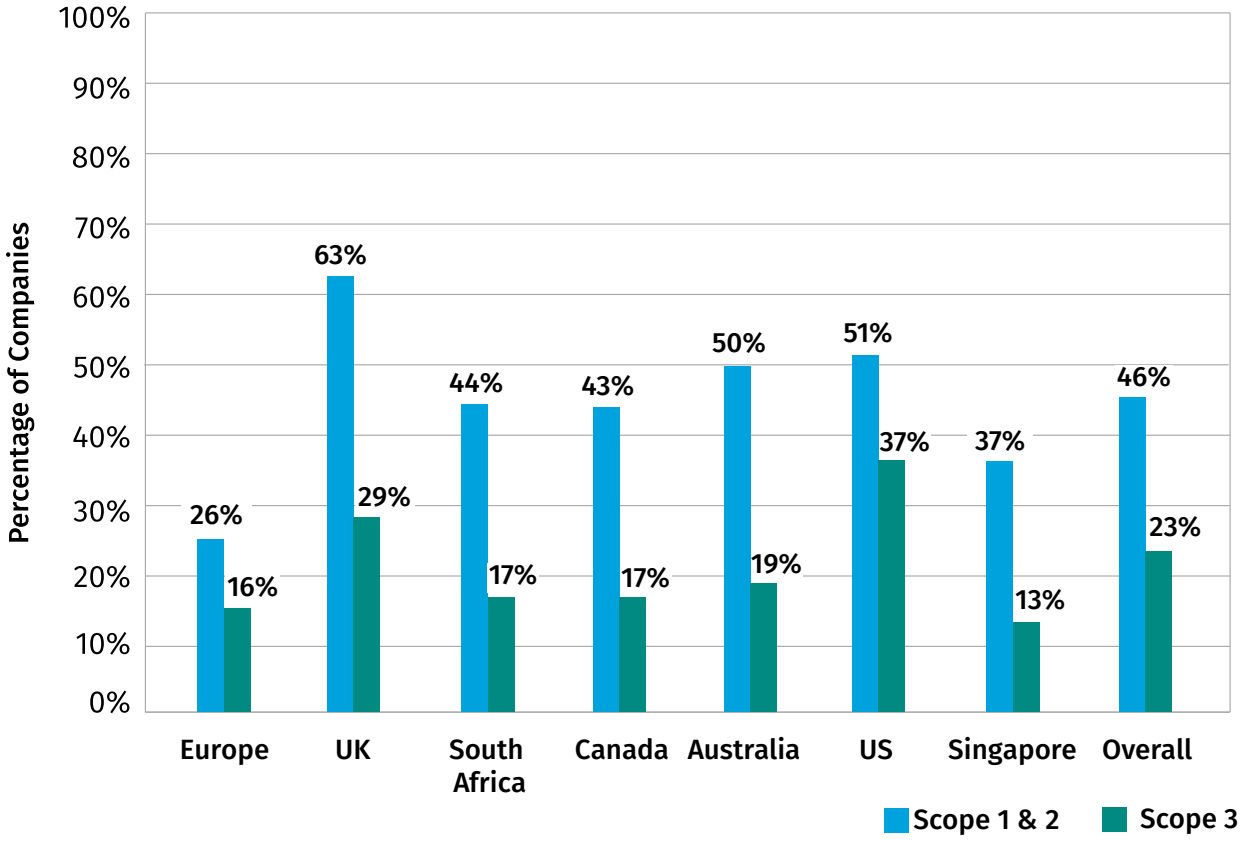
Source: GECN Group

Prevalence of Emissions Goal Alignment with SBTi by Region



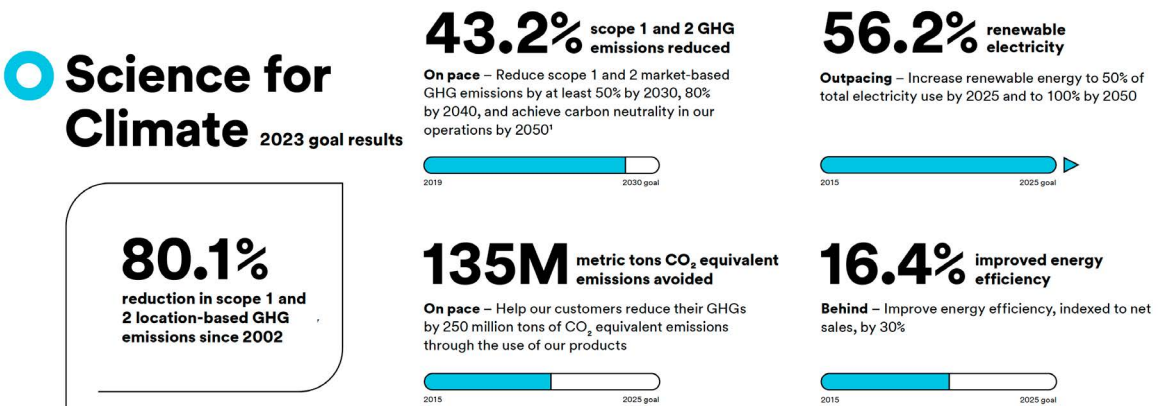
Source: GECN Group

Percent of Companies with Emissions Decrease in Most Recent Year by Scope 1, 2, and 3, and by Region



Source: GECN Group

3M Climate Performance Dashboard vs. 2030 Goals (Disclosed in 3M's 2024 Global Impact Report)



Source: 3M 2024 Global Impact Report

Vodafone ESG Performance Dashboard vs. Near-Term Goals (Disclosed in Vodafone's 2024 Annual Report)

Source: Vodafone Group Plc 2024 Annual Report

Contact Us

We hope this research contributes to the advancement of ESG measures and stakeholder engagement.

We invite your questions and comments. Feel free to directly contact any of the firms in the GECN Group or write to info@farient.com

United States

Farient Advisors LLC
Robin A. Ferracone (robin.ferracone@farient.com)
Brian Bueno (brian.bueno@farient.com)

United Kingdom

Farient Advisors Ltd.
Stephen Cahill (stephen.cahill@farient.com)
Simon Patterson (simon.patterson@farient.com)

Australia, Asia and New Zealand

Guerdon Associates
Michael Robinson (michael.robinson@guerdonassociates.com)

Europe and Middle East

HCM International
Stephan Hostettler (stephan.hostettler@hcm.com)
Gabe Shawn Varges (gabe.shawn.varges@hcm.com)

Canada

Southlea
Ryan Resch (ryan@southlea.com)
Amanda Voegeli (amanda@southlea.com)

South Africa

21st Century
Chris Blair (cblair@21century.co.za)
Dr. Mark Bussin (drbussin@21century.co.za)

SOUTHLEA

a GECN GROUP company