A TIME OF OPPORTUNITY

By Peter Swabey

An area on which we, as a professional body, have focused in recent weeks has been the way in which organisations have been trying to address the impact of COVID-19 on their sustainability activities and, given ProShare's interest in share plans, the associated impact on these.

One of the changes that we have all seen in recent years is the rise of the board's focus on sustainability. This is the result of both internal and external factors. To some degree it is a function of changes in boardroom composition, with many boards having younger members, with different social interests and, in particular, with experience in different corporate cultures. But it is also a function of changes outside the boardroom. The impact of the press and social media commentary on ESG issues, coupled with the activities of activist investors has been unmissable and even the least aware directors cannot have been unaware of the breath of the winds of change.

This has been exacerbated by the fact that, as Chris Hodge noted in the Institute's paper on Untangling Corporate Governance in February 2017, "policymakers in the UK and internationally have too often been guilty of assuming that a requirement to report on something would be sufficient to bring about change. As a result, I think reporting has been overused as a policy solution."

Consequently, one of the changes in the role of the reward professional has been to ensure that the board's desire to remain on the front foot in these areas, increasingly the subject of legislation and regulation, remains on the agenda of the executive team and, in particular, those in the one or two levels immediately below ExCo. For the share plan professional, this has increasingly manifested itself through the inclusion of sustainability metrics in corporate KPIs and, in particular, in share plan performance triggers.

This is a great way of getting management engagement, but the challenge is to develop appropriate metrics. One of the consistent issues in the executive pay debate has been that around the

relevance of metrics and the degree to which they ensure that pay outcomes reflect investor experience. This is not easy with non-financial measures, particularly those around sustainability where targets are often longer-term and individual year performance can only be considered as progress towards, rather than achievement of, a goal.

And these do not always reflect investment manager's own targets, which can be heavily driven by portfolio performance over the previous period, rather than the promise of 'jam tomorrow'. Investors want measurable results, not fluffy words but although some are interested in good sustainability metrics, there are others who are only really concerned by Total Shareholder Return and/or Earnings Per Share. These are relatively easy to calculate, harder to 'game' and contrast sharply with many sustainability KPIs which can all too easily be woolly and overly subjective. The only way to try to overcome this is with clear explanations of why these measures are critical to the company and how they are assessed.

But even that will not satisfy some investors – current feedback from Institute members is that there are many who regard sustainability metrics as 'emperor's new clothes' and expect focus on the numbers.

All of which brings me to COVID-19. Because the pandemic has had an enormous impact on the sustainability of so many organisations and on the way in which sustainability issues are addressed. For example, a site visit to familiarise a new director or executive with an aspect of the company's business can very well be made virtual; one where people have been sent because 'something smells funny' will be much less effective without feet on the ground.

And there are balances to be struck. Many companies may now be delaying structural and operational changes that they might perhaps have been introducing, or vice versa, and these may be captured in non-financial targets. But there are also issues about how the company treats its various stakeholders; about the degree to which it is focussed on financial or non-financial targets. For example, many suppliers are small businesses, reliant on cashflow. Delaying payment may help the corporate balance sheet, but if suppliers are put out of business the future sustainability of the company is put at risk.

I keep telling company secretarial colleagues that COVID has created a huge opportunity for them to demonstrate their commercial acumen. The same is true of share plan professionals and advisers.