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Press Release

Sustainability not an important criterion in top executives’ remuneration

International research team analyzes data on European top executives’ pay – Sustainability criteria have only minimal influence on performance-related compensation

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A study by an international team of researchers from the University of Tübingen and the HEC business school in Paris has shown that the payment of bonuses to executive board members in large European corporations is only minimally influenced by whether the top executives made decisions to reduce emissions, increase diversity in the company or improve product safety in the past financial year. According to the study, just five percent of executives’ performance-related remuneration is linked to binding criteria for measuring sustainable corporate behavior.

The researchers evaluated a data set on the remuneration of 674 executives at 73 companies listed in the two major European stock market indices EUROSTOXX 50 and STOXX Europe 50. The data covers the period from 2013 to 2020.

However, the study also found that 60 percent of executives had integrated at least one of the ESG (environment, social, governance) criteria into their remuneration. “Companies, investors and regulators are increasingly promoting the potential of these metrics in executive remuneration to align the interests of executives with broader societal goals such as environmental protection and diversity,” says Professor Patrick Kampkötter, co-author of the study and Head of the Managerial Accounting Department at the University of Tübingen. “But to do this, they would also have to provide real financial incentives. But they don't, because ESG performance metrics are largely symbolic. So, for most companies, appearances are more important than real actions,” he adds.

The researchers distinguished between “binding” and “discretionary” ESG indicators, enabling them to analyze whether the incentives are effective or not. Binding metrics are included in board members’ remuneration contracts at the beginning of the financial year, with a fixed weighting and providing clear and reliable targets. If executives meet or exceed these targets, they receive a payout based on the predetermined weighting of those metrics. Discretionary ESG metrics, on the other hand, are more flexible. Supervisory boards or compensation committees can adjust the weight or importance of these metrics at the end of the fiscal year as they see fit, creating uncertainty about the extent to which an executive's ESG performance affects his or her compensation. As a result, executives may feel less pressured to prioritize these goals throughout the year.

Large companies, particularly in the financial sector, often have a variety of largely discretionary ESG metrics in their compensation plans but lack significant weightings, according to the study. “This combination suggests that for many companies, the inclusion of ESG metrics may be a form of greenwashing - signaling commitment to sustainability without actually promoting substantive improvements or sacrificing shareholder value,” says Professor Matthias Efing of the HEC business school in Paris and co-author of the study. “In practice, non-ESG performance metrics such as financial results or share price development continue to dominate the calculation of executive bonuses.”

Implications for policy and practice

“For ESG metrics to drive real business change, they need to stop being a side note in remuneration plans and become a central part of how executives are assessed and rewarded,” says Kampkötter. “Investors and regulators could play a crucial role in pushing companies towards more robust ESG remuneration systems.” The researchers stressed that greater transparency on the true weight of ESG metrics and clearer reporting standards would help ensure that companies are held accountable for their ESG commitments to both shareholders and the public.

Publication:

Efing, Matthias and Ehmann, Stefanie and Kampkötter, Patrick and Moritz, Raphael, All Hat and No Cattle? ESG Incentives in Executive Compensation. HEC Paris Research Paper No. FIN-2024-1506, Available at SSRN: https://ssrn.com/abstract=4974204

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