1 FUNCTION DESCRIPTION

Traditionally structured as two separate sub-functions within the broader Human Resources discipline, Performance Management & Compensation (HRPC) reflects the process of planning, monitoring and evaluating an employee’s work objectives and overall contribution to the organization, as well as managing the monetary reward system in the forms of pay, bonuses, stock options and other benefits as linked to the achievement of organizational goals.

2 VALUE PROPOSITION

The inclusion of sustainability-related performance management and compensation criteria is often thought to signal a true integration of organizational sustainability. HRPC professionals play a critical role in the practical embedding of sustainability by clearly defining unacceptable behavior, encouraging desired behavior, reinforcing the priority of sustainability relative to other company goals, and providing feedback and financial incentives for employees who positively contribute to the achievement of sustainability goals. More symbolically, yet equally important, a clear message is sent that these measures are considered essential to the company by including sustainability metrics in the performance and compensation decision-making process.

As organizations continually look for new ways to keep their employees engaged, providing “work that matters” represents a potential non-financial perk that resonates with especially with a generation of socially and environmentally-conscious young talents. Many recent human capital reports indicate that a “company with purpose” tops the list for attracting and retaining top talent. By measuring and rewarding sustainability performance, a company can clearly demonstrate its commitment to sustainability and hopefully create healthy internal competition that further embeds sustainability into the organizational fabric.

3 STRATEGIC INTEGRATION

The heavy weighting of traditional performance metrics must give way for emerging sustainability considerations that are proving to be increasingly material to organizational performance. The purpose of the HRPC function needs to be re-defined so that it plays an integral part in defining and delivering superior performance on the organization’s sustainability objectives. Many organizations view corporate sustainability as a matter of good governance, while others view it as a driver of long-term business success. Regardless of the driver, organizations should work to bring sustainability performance measures on par with other performance criteria, and strategically integrate remuneration criteria to incentivize progress on priority sustainability issues.

4 OPERATIONAL INTEGRATION

Ideally, organizations should have fully developed competency models that are used to automatically generate the requirements for any position, as well as the necessary proficiency levels. These same job requirements, preferably including sustainability considerations, would then be used as the basis for the performance review process.

However, more likely, HRPC professionals must work with business leaders to adopt a clear process for manually identifying appropriate environmental, social, and governance (ESG) metrics for different functions and position that relate to sustainable shareholder returns and company strategy. Companies would then link the appropriate ESG metrics to reward systems in a way that forms a meaningful component to the overall remuneration framework.

The associated goals/targets should be integrated into an appropriate time horizon that is in line with the business strategy and the goals/targets should be challenging enough to encourage aggressive, yet attainable, top performance.

5 CULTURAL INTEGRATION

Performance management and compensation professionals play an incredibly powerful role in shaping the organization’s sustainability agenda. By incorporating and measuring sustainability criteria, these professionals make the sustainability agenda real for their organization and help to shape a culture where these topics are at the forefront and not an afterthought.
While the HRPc function represents a more quantitative dimension of HR, the reality is that relative to many other functions, their work is much more relational and story-driven. These qualitative strengths must also be leveraged with a view to translate the impact performance management and compensation decisions on sustainability into evaluation criteria that both motivates and inspires employee behavior. In turn, sustainability can for the HR functions more generally be framed most importantly as an opportunity to increase employee recruitment, retention, and engagement.

EMERGING TRENDS AND INNOVATIONS

Sustainability integration into executive pay
As part of the trend of designing more sophisticated pay packages, Boards have started exploring different ways for very substantially integrating sustainability factors in incentive mechanisms for directors and managers. Variable remuneration in many cases provide a substantially larger portion than the fixed salary component of executive pay, and it thus represents a useful tool for aligning executive interests with the company’s sustainability goals. While this, as described above, should apply to everyone in the organization, linking sustainability to executive pay sends the strongest of signals of its importance to the organization.

Metrics going beyond environmental performance
While the early incorporation of sustainability in the performance and compensation processes focused mostly on environmental factors, companies are increasingly expanding these metrics to include broader environmental, social and governance considerations. Many organizations have adopted a balanced scorecard approach, which considers additional metrics that are material to the company, such as human rights, anti-corruption, gender equality, local job creation and/or diversity.