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By Richard Milne

DRIVE TO LINK PAY TO SUSTAINABILITY BEGINS

The idea is gaining ground even in the absence of any agreed index, writes Richard Milne.

Sustainability has been a trendy, if sometimes derided, concept for some time in business circles. Now it appears to be becoming a buzz word in executive remuneration.

DSM and TNT, the Dutch life sciences group and postal operator respectively, this week join a multiplying band of companies- predominantly from the Netherlands- that link part of the bonuses senior managers received to sustainability, an all-encompassing term that refers not only to the environment but to issues such as employee satisfaction and safety.

The decision raises question such as how to measure sustainability as distinct from something more tangible such as rise or fall in a share price, and whether it make sense to do it.

Akzo Nobel, the Dutch paint company that bought ICI of the UK three years ago, was among the pioneers. It based half of its long-term incentive scheme on its position in the Dow Jones sustainability index for chemicals companies.

"There is a risk that if rewarding for performance is your value, you put all your eggs in one basket", Hans Wijers, chief executive says.

It is an idea Mr Wijers has introduced at Royal Dutch Shell, the oil group at which he is head of the remuneration committee.

In addition to safety, which fellow oil company BP also uses to calculate bonuses, its ranking in the Dow Jones index wil count in the future.

Mr Wijers says the idea has been positively received by shareholders – Akzo`s proposal was passed by 97 per cent of investors – as well as by workers.

"The sceptical parts of the company [i.e. in regard to the idea of sustainability] now think. 'Hmm, this is interesting.'"

Carola van Lamoen, a pay expert at Robeco, the Dutch investor, says it has been asking companies to include sustainability in remuneration for several years.

"We are convinced that strong corporate values, including care for the interest of employees, customers and the environment, are a precondition for stable, long- term, above-average results for a company"

But not everyone is convinced.

The VEB, the powerful Dutch retail shareholder`s association is against using sustainability in regard to pay.

Jan Maarten Slagter, its director, argues performance is sufficient. Good companies, he says, know sustainability components and still do poorly in [forming] shareholder value.

"You would still get some of your variable pay. We would like to see pay policies directed to [forming] shareholder value in the long term"

One important challenge concerns how to measure sustainability in a concrete manner.

Akzo Nobel managers receive a full bonus when the company is in the top three, out of about 90 companies, in the sustainability index. They would receive some shares if the company were to be placed fourth or fifth.

Both DSM and postal operator TNT rejected using the sustainability index. They have instead opted to adopt a mixture of ideas to measure things such as employee and customer satisfaction, greenhouse gas reduction and energy use.

A glance at DSM`s greenhouse gas reduction target demonstrates the ways in which they have tried to make the targets measurable.

DSM last year reduced greenhouse gases by about 2 per cent once revenue growth was stripped out. Feike Sijbesma , the company`s chief executive, says the proposals are still being finalised but would see an annual reduction of 1-1.5 per cent go unrewarded ; if 5-6 per cent were to be achieved, the full bonus would be paid and there would be a sliding scale in between.

Mr Sijbesma pitches the proposal as being about more than merely business: "It is very good to pay attention to this because we need a next generation that is going to live here."

"Our grandchildren will be less interested in what our returns were on the stock market in 2009 or 2010 but [they] will be [interested] in what impact we had on the planet"