NACD New Jersey Compensation Peer-to-Peer – October 31, 2017

In a lively and candid session moderated by Mike Marino of Fred Cook & Co., eleven experienced compensation committee members from a variety of industries, both public and private, global and emerging growth companies, exchanged ideas and discussed developments in executive compensation. Topics ranged from pay ratio disclosure, risk in compensation plans, metrics, use of equity vehicles, succession planning and director compensation. Here are a few of the highlights:

The CEO pay ratio disclosure raises more issues than the reactions of investors. Employees may be more interested in how their pay compares with that of the median employee than with that of the CEO, which is already visible. Boards may want to understand engagement scores for employees, how employees view the CEO, how fair pay is determined and whether HR systems need to be updated to be able to make the necessary calculations. Query whether this effort can be a spur to replacing outdated HR information systems, especially if data must be collected globally.

Compensation Committees are on point to understand how people in highly risky areas are incentivized and do these metrics present an exposure to aggressive risk-taking. Not all risk-inducing incentive programs are in the purview of the Compensation Committee, e.g., the Wells Fargo Committee would not necessarily have had a view of regional sales incentives. However, the full Board should understand how the strategy might induce risk-taking in order to achieve metrics. And at least one Compensation Committee member should also sit on the Audit Committee.

Options have experienced a reduction in prevalence, especially as the exclusive equity vehicle. There is a shift toward granting options in combination with other vehicles such as performance shares. Options remain in the equity overhang for a long period of time due to their typical 10-year life and hurt equity plan scoring by proxy advisory services. A full value equity grant that is relatively stable as a percentage of pay or dollar value may be more acceptable and produces less of an overhang as it has a shorter vesting schedule and is either issued or cancelled within a few years.

Total Shareholder Return rarely appears as the sole metric. Many industries still do not embrace TSR although some companies have adopted TSR as a modifier to other metrics. There has been some discussion of Return on Invested Capital in more capital intensive industries but it still is not widely used.

There should not be a complete overlap between short and long-term incentive metrics as ISS and Glass-Lewis disapprove of duplicative metrics, although a repetition of one metric in the long-term plan that also appears in the short-term plan is not necessarily fatal. One approach is to put the “steps” into the short-term plan and the “outcome” in the long-term plan.

Although much has been written lately regarding shareholder engagement, very few shareholders are actually interested in engagement unless there is an issue. It’s important to insure that a Board member who is asked to meet with a shareholder regarding compensation is prepared and accompanied by the relevant company expert and also that he/she is speaking to the right representative, for example the person controlling voting policy versus the portfolio manager where those duties are separated.

Succession planning has no magic formula. Matters such as handling multiple internal candidates, competitive employment offers and founder transition are all highly sensitive and individualized.

Meeting fees are largely supplanted by increased retainers, which avoids issues such as what constitutes a meeting and what happens when a director cannot attend a special meeting, as well as providing administrative simplicity. If the Board or a Committee must meet for an excessive number of times due to a particular matter, a supplement may be appropriate.