



Adapting Compensation Strategy to New Demands

Compensation Series

March 17, 2011

Pearl Meyer & Partners
Comprehensive Compensation[®]



ADVANCING EXEMPLARY BOARD LEADERSHIP



Meet the Presenters



Richard Goeglein (moderator), Chairman, Pinnacle Entertainment; Member, Advisory Board of The Board of Veteran CEOs; Trustee, Board of Volunteers in Medicine of Southern Nevada



Rich King, a Managing Director in the New York office of Pearl Meyer & Partners, has more than 17 years experience advising Boards and senior management of publicly-traded and privately-held companies on executive compensation matters.



Peter Miterko, a Managing Director in the New York office of Pearl Meyer & Partners, has practiced in the area of executive compensation for 25 years, assisting clients in the design of programs that drive long-term value creation and in matters of corporate governance.





Why We're Here



Directors and Compensation Committee members are having a tougher time making pay decisions for their particular businesses:

- Pay is one of the best tools available to boards to build share value
- Each company is different, and compensation should be tailored to each individual company's circumstances
- Significant environmental changes are now hampering Boards' ability to set executive pay:
 - Legislation and regulation, including Say on Pay
 - Shareholder advisory & watchdog groups (ISS, The Corporate Library, etc.)
 - Uneven economic recovery
 - Pressure to “conform” to peer pay practices
- A well thought-out compensation strategy can help directors stay focused on tailoring pay programs to their business needs and to enhancing long-term shareholder value





Q1



What is a Compensation Strategy?

The fundamental tenets on which your compensation programs and practices are built: essentially, the “why” “how” and “how much” of programs that will:

- Align employee behaviors with business strategy to drive performance and shareholder value
- Tailor employee behaviors to targeted company priorities and circumstances
- Be the cornerstone of a successful Say on Pay strategy

A comprehensive compensation strategy is more than what’s disclosed in the CD&A





CD&A Summaries



General Electric (March 2010)

“The goal of our executive compensation program is to retain and reward leaders who create long-term value for our shareowners. This goal affects the compensation elements we use and our compensation decisions. Our compensation program rewards sustained financial and operating performance and leadership excellence, aligns the executives’ long-term interests with those of our shareowners and motivates executives to remain with the company for long and productive careers built on expertise.”

Key Considerations in Setting Pay Include:

- Emphasis on Consistent and Relative Performance
- Emphasis on Future Pay Opportunity Versus Current Pay
- Discretion and Judgment
- Significance of Company Results
- Consideration of Risk





CD&A Summaries (continued)

Pfizer (March 2010)

“Pfizer’s compensation philosophy, which is set by the Committee and approved by the Board, is designed to align each executive’s compensation with Pfizer’s short-term and long-term performance and to provide the compensation and incentives needed to attract, motivate and retain key executives who are crucial to Pfizer’s long-term success.”

“Our executive compensation program is structured to support the ongoing transformation of Pfizer’s business and is designed to ensure that total direct compensation is competitive and tied to performance. . . and has three key principles:

1. Positioning total direct compensation (the sum of salary, annual incentive awards and long-term incentive awards), as well as each individual compensation element, at approximately the median of our peer companies, with emphasis on pharmaceutical companies with large market capitalization.
2. Placing greater emphasis on aligning short-term incentive awards with our annual operating financial objectives.
3. Rewarding both absolute and relative performance in total shareholder return through long-term equity incentive awards.”





CD&A Summaries (continued)



JP Morgan Chase (March 2010)

“Our compensation philosophy, practices and principles are an important part of our business strategy in helping to attract and retain the employees we need and to provide a control framework for the elements of compensation we use and the processes to implement and maintain a reasonable and appropriately balanced approach to compensation.”

“The Firm’s Compensation practices and principles, which articulates how we operate . . . help build the following foundation for our approach:

- Independent Board oversight.
- Compensation should not be overly rigid, formulaic or short-term oriented.
- Teamwork and a shared success environment should be encouraged and rewarded.
- A meaningful ownership stake in the Firm should be used to reinforce alignment with shareholders.
- Risk management and compensation recovery should be robust to deter excessive risk taking and improper risk management.
- Attracting, retaining and developing talent is critical to sustaining success.
- Strict limits or prohibition on executive perquisites and special benefits.”





Why is a Compensation Strategy Important?

- Governance experts agree that developing and communicating a thoughtful, comprehensive compensation strategy is one of the Compensation Committee's most important tasks
- An effective compensation strategy:
 - Provides a framework for consistent decision-making and overall efficiency
 - Supports the company's business strategy in a clear, recognizable manner
 - Guides the development of pay programs consistent with the company's missions and values
 - Communicates to shareholders, advisers and, increasingly, regulators a persuasive rationale for how and why the company's compensation programs were developed
 - Increases the likelihood of a positive Say on Pay vote
 - Demonstrates how the company's incentive programs avoid the promotion of excessive risk

The Upshot: Companies need to take a step back and re-evaluate their compensation strategy, which serves as the foundation for their pay programs



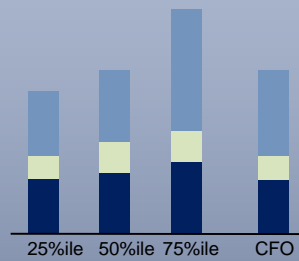


Compensation Strategy Framework



Primary Considerations

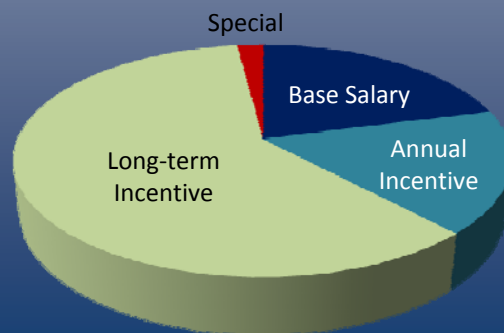
Competitive Positioning



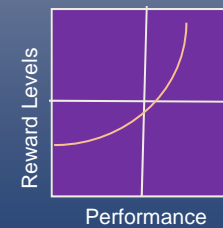
Performance Measures

EBITDA EPS
ROE EVA
ROIC Individual
 Performance

Pay Mix



Risk/Reward Relationship





High Performing Organizations Approach Compensation Differently...

Q4



Base Salary

- Are no more likely than other companies to position above-market average
- Base pay is less important in competing for labor
- Allocate more merit dollars to high-performing employees

Variable Pay

- More likely to use a performance rating to determine variable pay eligibility and payouts
- Committed to sharing results of strong financial performance with those that have an impact on business results

Long-Term Incentives

- More likely to award other forms of long-term incentives to top performers and determine eligibility based on performance
- Use stock and variable pay, rather than benefits, to promote retention





...and Manage the Pay Process Differently



Performance Management

- More differentiation of high performers
- More likely to promote high-performing employees
- Greater connection in the timing of pay delivery and performance reviews
- More “Full Circle” feedback, including from external customers and subordinates
- Employee performance linked to key business drivers

Communication

- More open to sharing pay information and communicating the value of the total rewards package
- More clear about communicating the link between pay and performance
- Much more likely to measure managers’ ability to communicate and the success of rewards communication

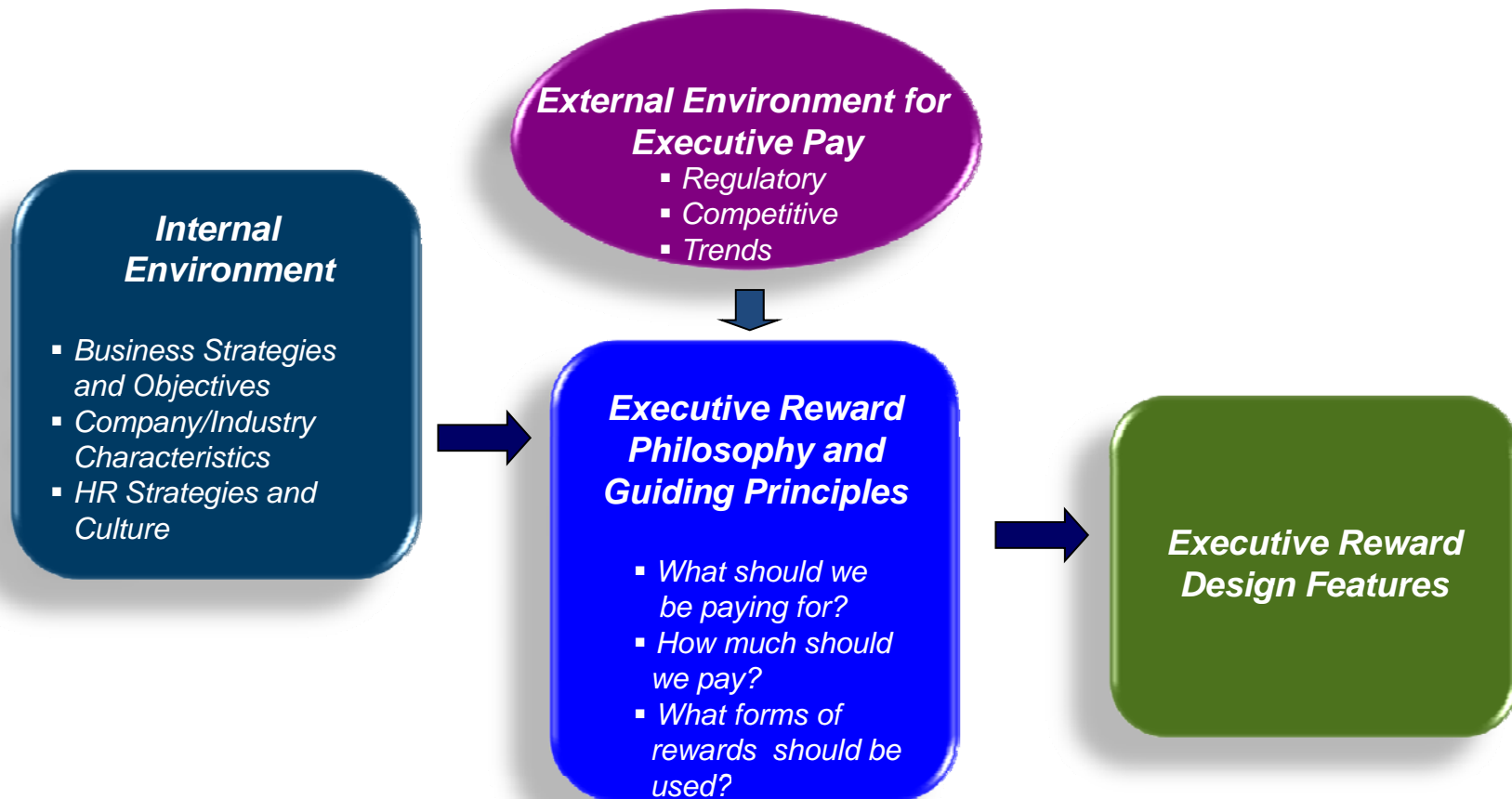




Compensation Philosophy Framework

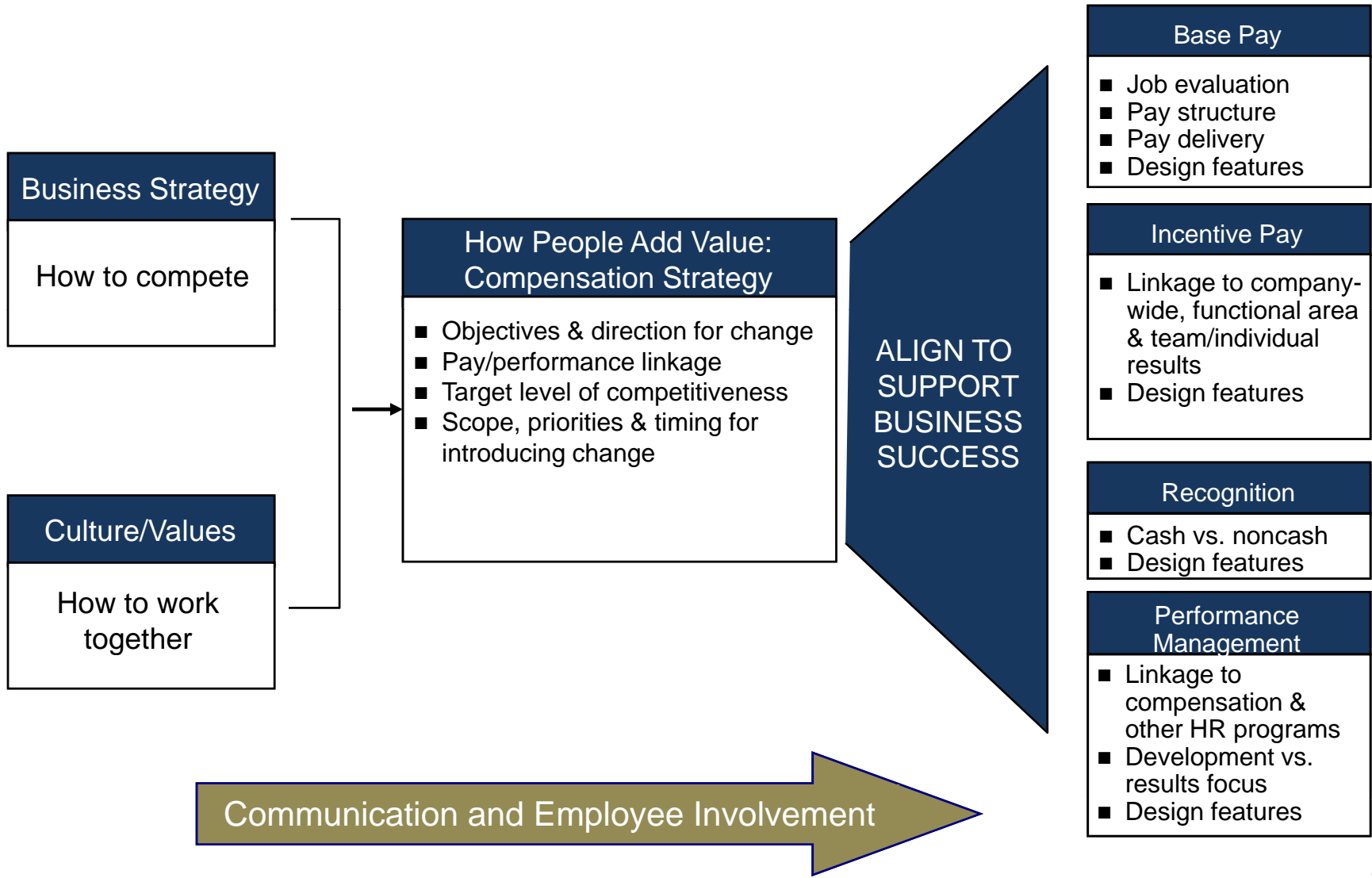


Both the internal and external business environment are critical considerations





Successful compensation programs are aligned with business strategies





Approach



Plan and mobilize

Set strategy and reward principles

Design programs and guidelines

Implement

Description			
<ul style="list-style-type: none"> Finalize detailed project plan and initiate effort 	<ul style="list-style-type: none"> Determine appropriate philosophy and guiding reward principles for program development 	<ul style="list-style-type: none"> Develop detailed plan designs and administrative guidelines 	<ul style="list-style-type: none"> Develop implementation strategy, process, and tools; roll-out
Detail Tasks			
<ul style="list-style-type: none"> Project planning/scheduling Data gathering Document review 	<ul style="list-style-type: none"> Leadership interviews Field organization interviews Best practices research Overall strategy and guiding compensation principles International integration implications 	<ul style="list-style-type: none"> Detailed program designs Cost and funding assessments Administrative guidelines Communications requirements 	<ul style="list-style-type: none"> Communications/Implementation strategy, process and tools Continuous improvement process Administration Roll-out/delivery





Guiding Principles for Compensation Programs



- **Align** compensation with company objectives to drive appropriate behaviors and provide a clear line of sight
- Structure compensation programs to **engage** employees and enable them to take greater accountability for their performance and compensation
- Evaluate company, business unit and individual performance using quantifiable goals/objectives and management's **informed judgment**
- Promote a **high performance culture** by significantly differentiating pay for high performers through all components of compensation
- Maintain compensation programs which reflect marketplace trends and best practices and instill a culture that embraces rational **innovation**
- Manage the **cost** of the compensation programs in a manner that balances Company's responsibilities to its shareholders, clients, and employees
- Target compensation at an appropriate **competitive position** relative to appropriate labor market(s) such that Company maximizes the value of its compensation programs
- Strive for internal **equity** and **consistency** in program design and application to facilitate flexible **management of workforce** across the businesses
 - However, differentiate pay for critical jobs/people to support the recruitment and retention of a critical talent
- Maintain **simplicity** by making the compensation programs easy to administer and communicate
 - **Communicate** pay programs in a timely manner and as part of an integrated total rewards program





NACD Credit and Fellowship Information



If you have any questions regarding NACD credit or the Fellowship programs, please contact:

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To learn more about the National Association of Corporate Directors, visit <http://www.NACDonline.org/>





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