

# ON POINT

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## **PM&P On Compensation Planning: Looking Ahead to Executive Pay Practices in 2011**

Executive Summary –Technology Edition

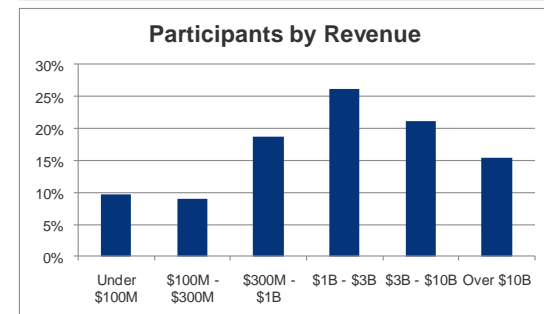
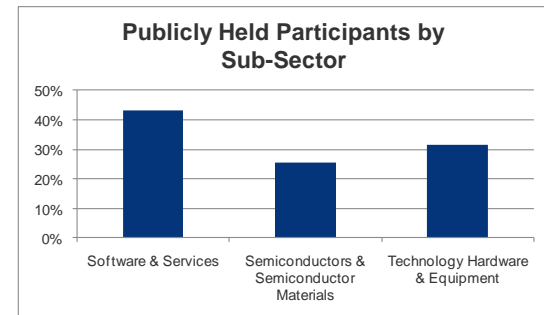
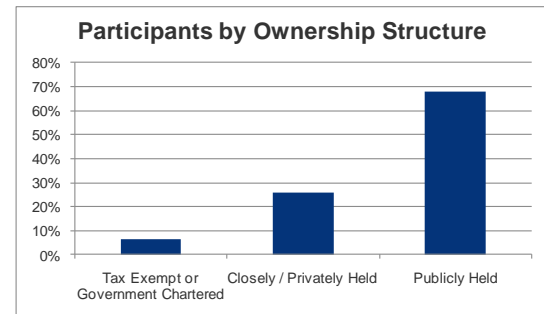
## Table of Contents

Introduction	3
Summary of Executive Pay Decision Making Environment	4
<u>Report Findings</u>	
Company Performance	5
Executive Base Salary Changes	6
Modifications to Annual Incentive Program Design and Payout Levels	7
Modifications to Long-Term Incentive Program Design and Award Levels	8
Perquisites	9
Severance and Change-In-Control Payments	10
Compensation Committee Agenda Items for 2011	11
Differences by Industry Sub-Sector	12
About PM&P	13

## Introduction

- This survey series was designed to arm executive pay decision makers with information on how others are responding to the latest changes in the environment in which executive pay decisions are made
- The 2011 survey was conducted online in August and September of 2010
- Of the 279 total participants, 51 represented the technology sector
- The complete results are available for purchase at [www.pearlmeier.com](http://www.pearlmeier.com)
- If you would like to discuss any aspect of these findings further, please contact Jim Heim at [jim.heim@pearlmeier.com](mailto:jim.heim@pearlmeier.com) or (508) 630-1502

### ***Among Technology participants...***



## Summary of Executive Pay Decision Making Environment

### *The latest developments influencing executive pay decision making include...*

#### Broader Market Trends

- Economic and market turmoil is dissipating, but not yet a “return to normal”
  - Perceived importance of goal setting and metric selection for incentive plans is increasing, resulting in a more rigorous review process
  - As various sectors recover, “winners” and “losers” have begun to emerge. As the “winners” more aggressively pursue proven executive talent, companies are again focusing on retention
- Expanding list of “poor pay practices” from various institutional shareholders and proxy advisory firms
  - Downward pressure on executive perquisite programs, severance arrangements
  - Pay “irritants” have greater consequence in a Say on Pay environment
- Executive pay decision making process continues to grow more transparent
  - Dodd-Frank is the latest in a series of events bolstering SEC disclosure requirements
  - Investors demand more information relating to links between pay and performance, as well as detailed explanation of how compensation program risk is managed

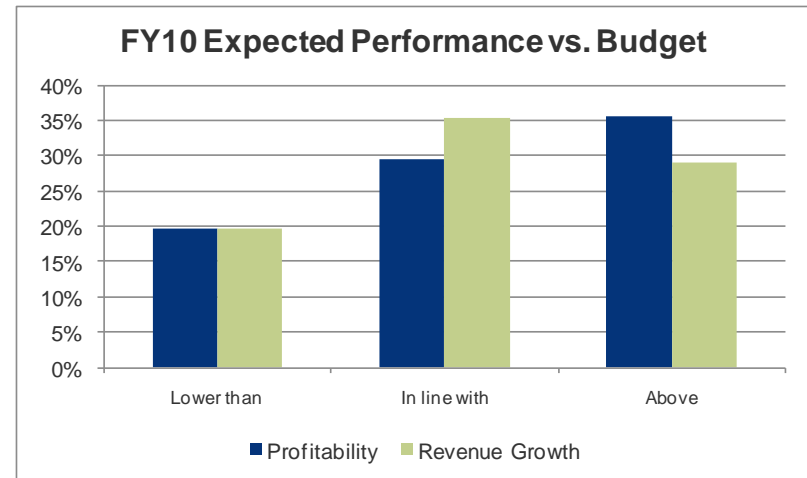
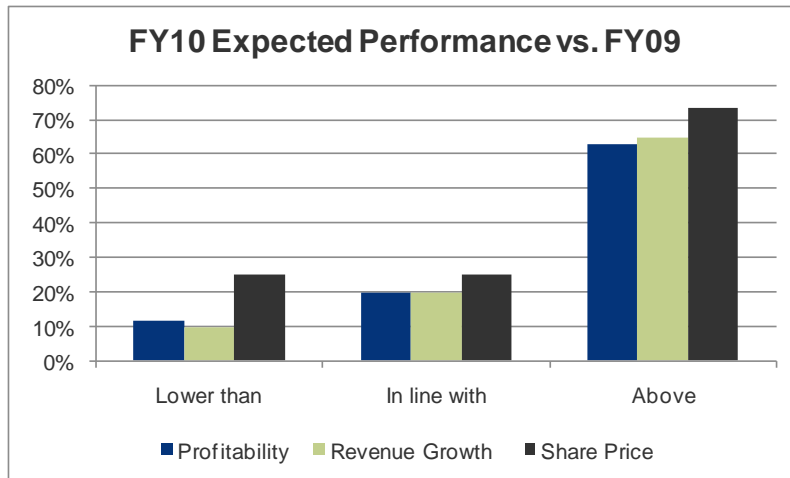
#### Factors Unique to Tech Industry

- Goal-setting and metric selection is especially challenging in cyclical sectors (such as semiconductors and semiconductor equipment) and for companies where new product launches represent a significant portion of each year’s revenue (as is the case for many software companies)
- Equity compensation is emphasized to a greater degree than in other industries, and absent new equity grants, companies with stagnant or depressed share prices have little retentive glue to hold their executive talent in place
- Technology companies traditionally offered fewer executive perquisites than other industries; the scrutiny of remaining perquisite programs is increasing (especially at larger, more mature companies where legacy programs represent a small percentage of total compensation)
- The acquisitive nature of many technology firms and the industry’s emphasis on equity compensation have caused executives to focus more on the treatment of equity awards and less on cash severance upon termination; as companies continue to migrate towards performance-based equity grants, treatment of equity upon a change-in-control is an increasingly important negotiation point
- It is difficult to identify performance metrics that function as true “value drivers” in cyclical / new product-dependent industries
- Given the competitive nature of many technology sub-sectors, performance “peers” are readily available, and companies are increasingly likely to measure performance relative to peers (e.g., based on total shareholder return) in determining long-term incentive payouts and demonstrate stronger pay-for-performance links

***...our survey results preview how companies will respond to these developments***

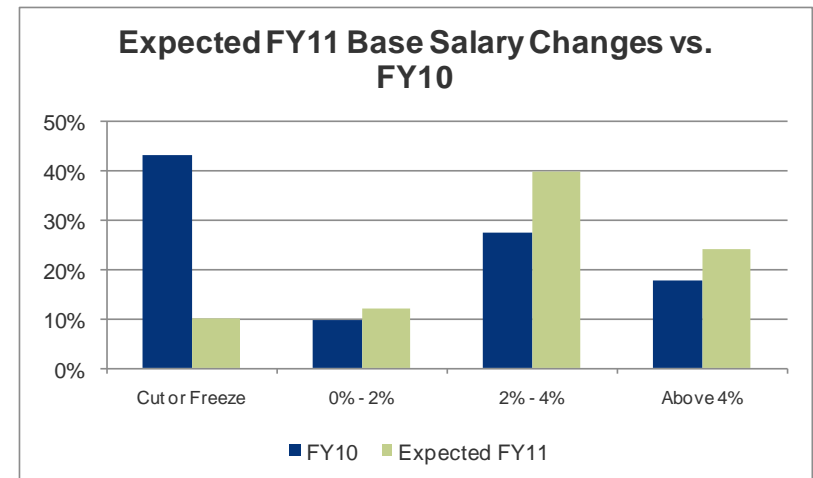
## Company Performance

- Company performance is up year-over-year across all sub-sector categories, and most participants indicate they are meeting or exceeding their own internal budget goals



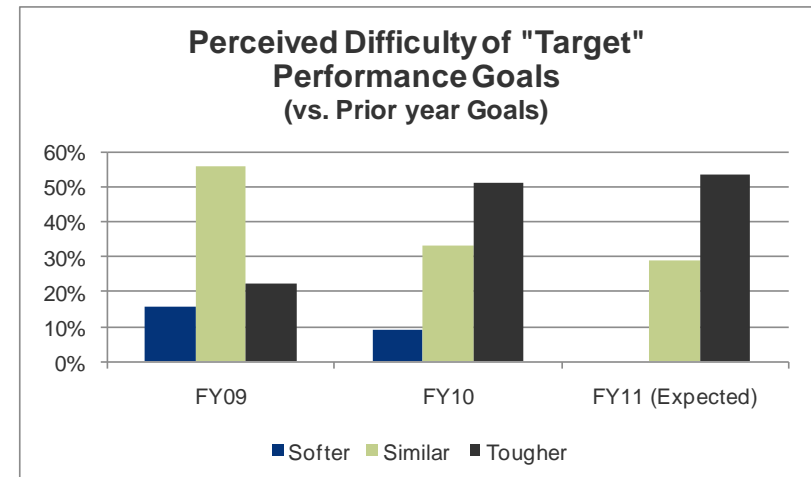
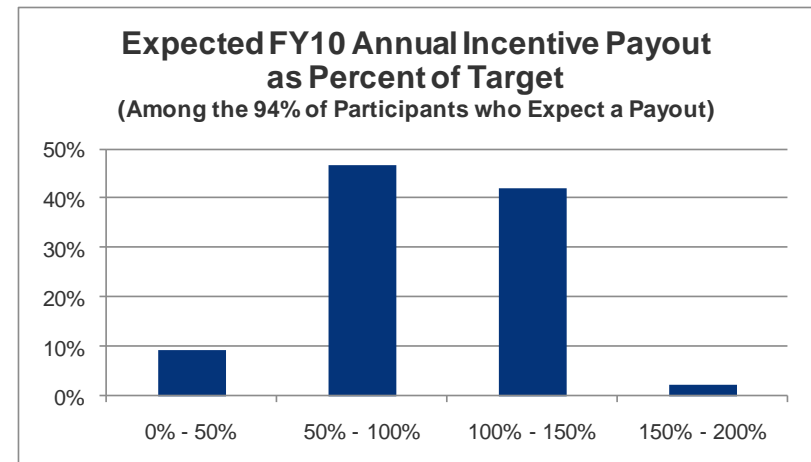
## Executive Base Salary Changes

- Participants are coming off of a year (FY10) in which 43% froze or decreased executive base salaries
- Anticipated FY11 increases are modest:
  - 10% anticipate a salary freeze or decrease
  - A plurality anticipates an increase in the 2% - 4% range, below the historic 4% average of the past two decades



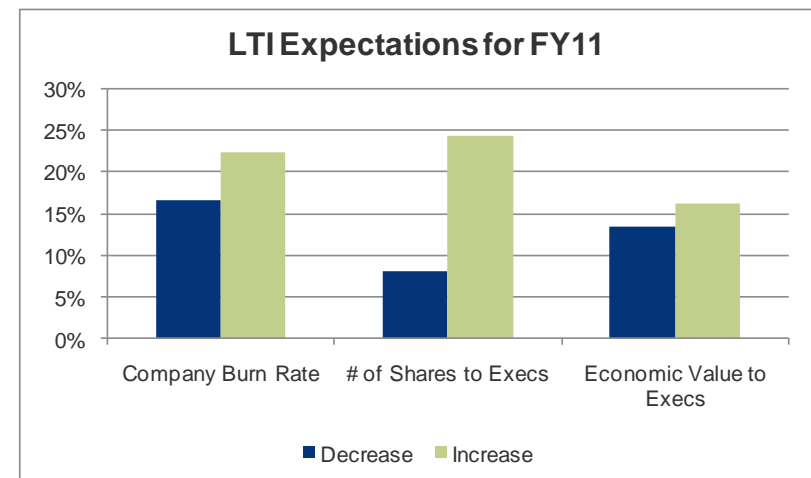
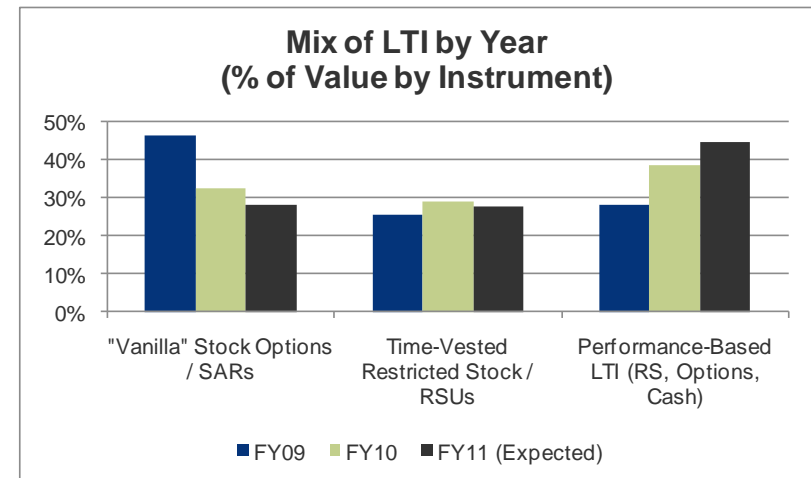
## Modifications to Annual Incentive Program Design and Payout Levels

- 35% of participants did not pay an annual incentive for FY09 performance, and the majority of those who do expect a payment for FY10 expect to pay within 25% of “target” payout levels
- The number of participants who indicate that “target” performance goals as compared to the prior year are lower (i.e., a softer performance hurdle) is trending down – in fact, none of the participants indicated that expected FY11 targets would be softer than FY10 – while the number of participants indicating that “target” performance goals are tougher trends up



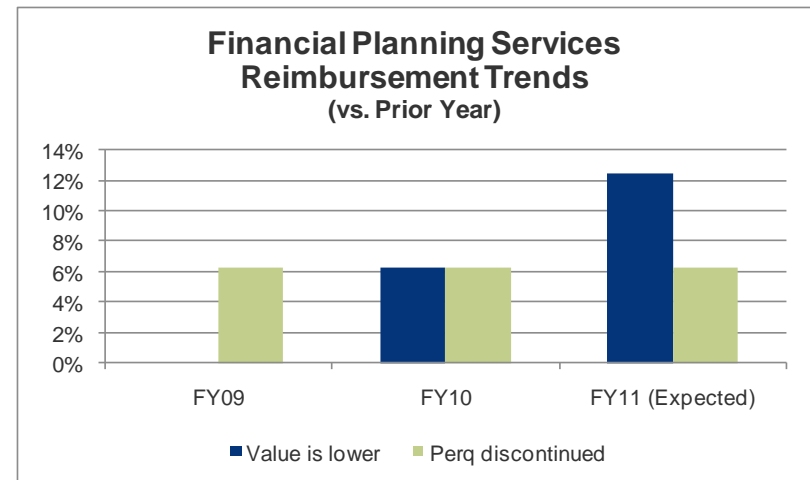
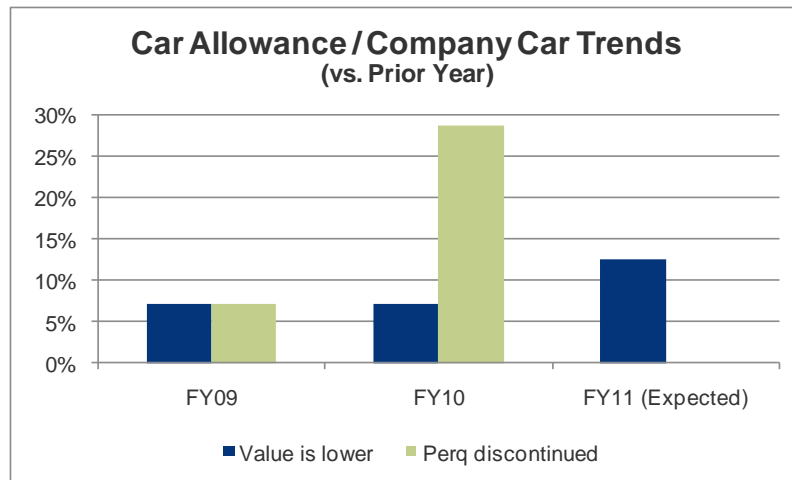
## Modifications to Long-Term Incentive Program Design and Award Levels

- There has been a trend away from plain vanilla stock options and SARs and towards awards that feature some form of performance measurement
- In the aggregate, participants indicated that LTI award levels will be up modestly in 2011



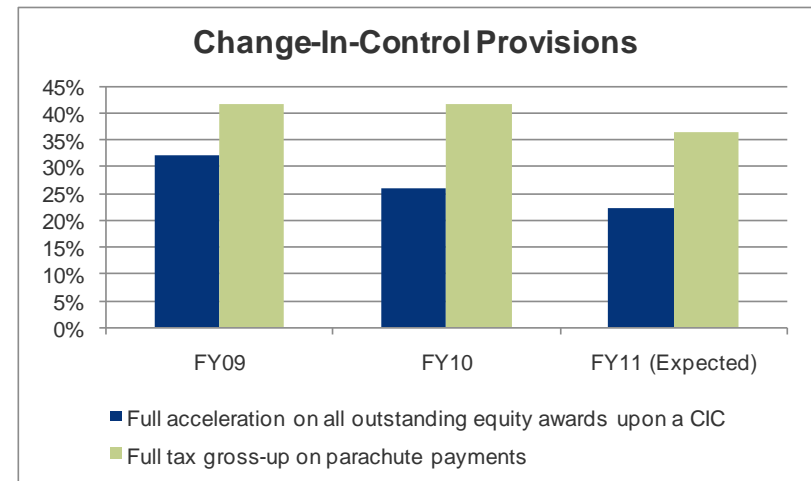
## Perquisites

- The prevalence of traditional executive perquisites continues to wane
  - Executive perquisites are a small percentage of total compensation value, but a significant driver of shareholder and employee dissatisfaction
  - Commentators have suggested elimination of perquisites that generally lack a legitimate business purpose and that other employees must cover on their own, such as a car allowance and/or company car, personal use of a corporate aircraft and tax preparation services



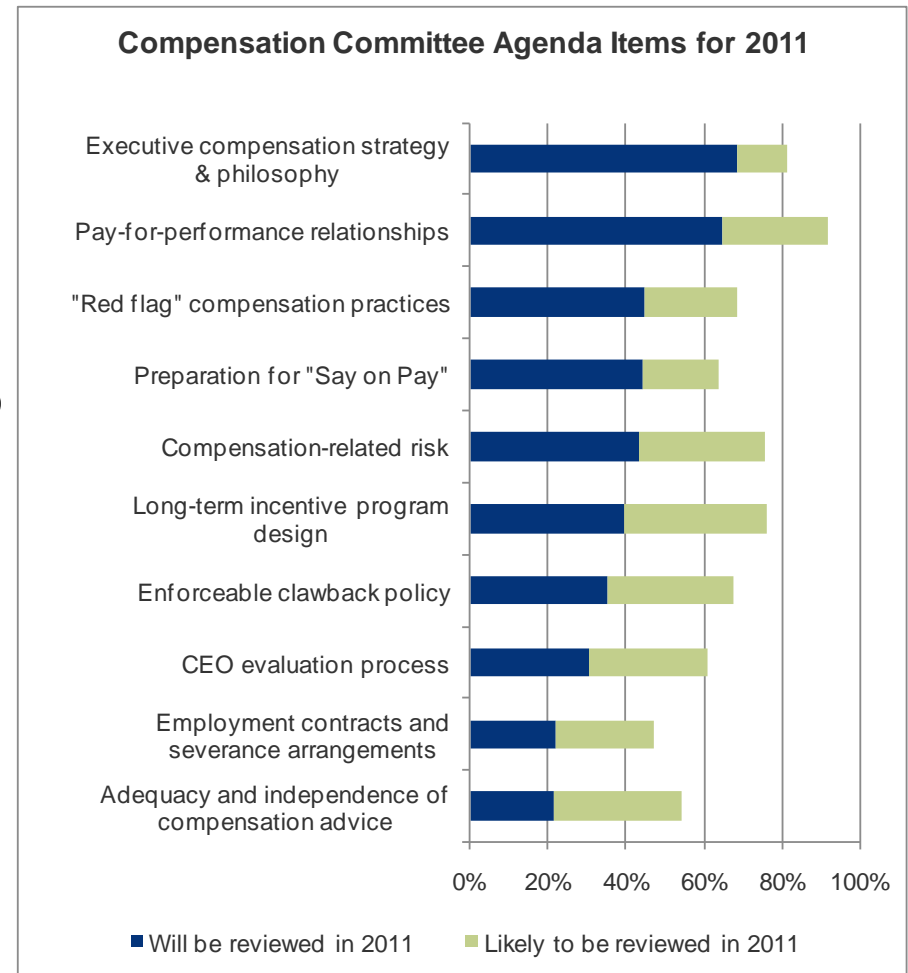
## Severance and Change-In-Control Payments

- The three-year trend is clearly toward decreasing benefits
  - For cash severance upon terminations that do not follow a change-in-control, 17% curtailed provisions in FY09, an additional 17% curtailed in FY10, and 13% anticipate doing so in FY11
  - The percentage of participants providing full acceleration of all outstanding equity awards upon a change-in-control (single-trigger) has fallen slowly but steadily, as has the percentage who provide a full gross-up (for excise tax attributable to parachute payments)



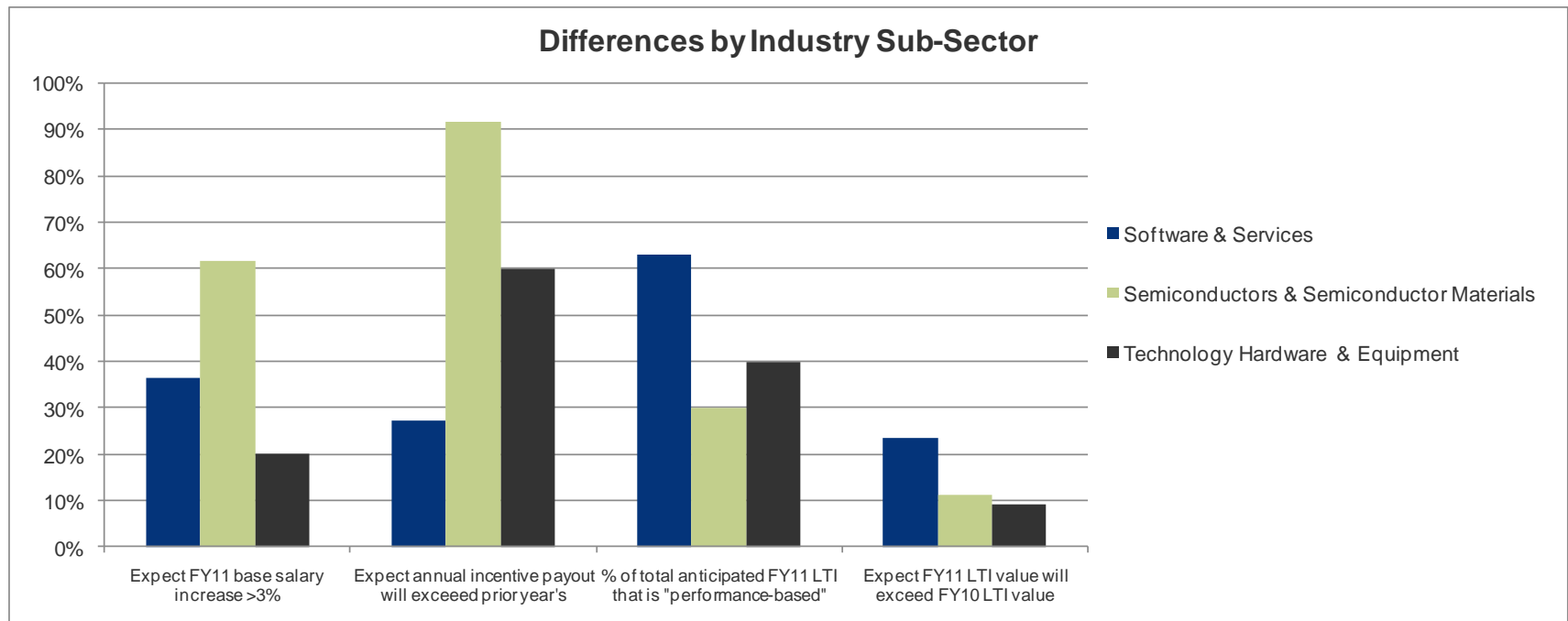
## Compensation Committee Agenda Items for 2011

- We asked participants to indicate whether various items from our 2010 “Top 10 Compensation Committee Agenda Items” Trends & Issues report will be reviewed in 2011
- For our detailed commentary relating to each of these agenda items , please visit [www.pearlmeier.com/2010top10](http://www.pearlmeier.com/2010top10)



## Differences by Industry Sub-Sector

- Semiconductor & Semiconductor Materials companies were the most optimistic in their expectations for FY11 base salary increases and annual incentive payout levels (for performance in FY10)
  - Note that the majority of Semiconductor & Semiconductor Materials participating in this survey did not pay an annual incentive to executives for performance in FY09
  - These results speak to the volatility in Semiconductor & Semiconductor Materials year-to-year pay levels
- Software & Services firms are allocating larger percentages of their FY11 LTI grants to “performance-based” awards and had the most optimistic expectations for FY11 LTI values



## About Pearl Meyer & Partners

*For more than 20 years, PM&P has served as a trusted independent advisor to Boards and their senior management in the areas of compensation governance, strategy and program design. The firm provides comprehensive solutions to complex compensation challenges through the development of programs that align rewards with business goals to create long-term value for all stakeholders: shareholders, executives and employees. The firm maintains offices in New York, Atlanta, Boston, Charlotte, Chicago, Houston, Los Angeles and San Jose.*

## About our Technology Industry Expertise

*PM&P specializes in working with technology firms from venture-backed start-ups to the largest multi-nationals. We handle hundreds of assignments each year in software, semiconductors and semiconductor equipment, computers and peripherals, technology services, research & development, consumer electronics, new media, medical devices, pharmaceuticals, and bioscience. We know your market.*

*To learn more about PM&P's technology compensation services and to review additional content go to [www.pearlmeyer.com/technology](http://www.pearlmeyer.com/technology) or email us at [technology@pearlmeyer.com](mailto:technology@pearlmeyer.com)*

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