NACD New England Chapter
November Breakfast Forum
Compensation Strategies That Drive Value

November 10, 2015

Panel Members:
Ellen Zane
Alex Wittenberg
Duncan McFarland
Theo Sharp (Moderator)
Compensation Strategies that Drive Value

- Long-term value creation is what all companies seek

- According to the NACD’s Blue Ribbon Commission on Long-Term Value Creation, it is incumbent on the Board to support management as they seek to create value

- Several questions face Boards regarding long-term value creation:
  - How is long-term value created? (Full Board)
  - Are short- and long-term corporate strategies aligned with value creation? (Full Board)
  - How should value creation be measured? (Full Board and Compensation Committee)
  - How should value creation be supported or rewarded? (Compensation Committee)
The Commission report outlines actions and processes for the Board to address these questions.

In simple terms, the Board should:

• Be sure the corporate strategy is clearly developed and aligned with long-term value creation
• Assess how well executives are aligned with the strategy
• Measure progress against the strategy

An effective tool to drive strategic goals is an integrated short-and long-term incentive plan

• The Compensation Committee leads plan design
• The Committee is responsible for integrating corporate strategy in compensation
Compensation Committees help support value creation through pay program design by actively linking business strategy to compensation
  - Consider, but don’t be bullied by short-term pressure for short-term results

It’s not easy…
  - Directors should be actively involved with strategy development
  - 75% of Directors say that their involvement in metric selection has increased*
  - 75% of Directors also say that the Board’s involvement in goal setting has increased*

* Source: NACD Public Company Governance Survey
What’s important for the Committee to consider?

- About 70% say that the short-term operating plan is very important in determining metrics and goals*
- 50% say that long-term strategic plan is very important*

- Business cycles
- Corporate maturity
- Corporate culture
- Financial results

- Strategic goals should be making a comeback
  - It’s easy to fall back on financial goals
  - The Blue Ribbon Commission notes that strategic goals are sometimes better indicators of long-term value creation than any current financial measure

What about Total Shareholder Return?

- Our recent study with Cornell shows that including TSR in long-term incentive plans does not necessarily correlate with value creation.

- TSR is the ultimate indicator of long-term value creation, but it is also ultimately backward looking.

- This is a challenge with the new pay-for-performance disclosure regulations looming.

- If not, TSR then what?
Experience and Insights

Let’s discuss with our panelists their experiences and insights into how long-term value is created and how compensation plans are used to support that value creation.
Experience and Insights

- What is the definition of Long-Term Value?
  And...Do Boards explicitly discuss it or is it just a part of the strategy development?

- How does the Compensation Committee integrate the short- and long-term strategy into their discussion?
  And...Does it get muddled with the short-term pressures of the market or proxy advisory groups?

- How willing do you think Boards are to go against the short-term market pressures?
  And...ISS?
Experience and Insights

- Do you think it's better for short-term incentives to be linked to longer-term goals?

  Or…Should there be tension between the two?

- How about integrating strategy goals into incentives even though they are harder to measure?

- Should Committees conduct an exercise to map the annual plan goals to the long-term strategy?

- How about just using TSR as the long-term metric?
Additional Resources

NACD Blue Ribbon Commission Report
The Board and Long-Term Value Creation

www.nacdonline.org

Total Shareholder Return:
It’s Not the Magic Metric

Compensation as a Catalyst
Value Creation and Compensation

Pearl Meyer Research Report:
The Myth and Reality of TSR as an Incentive Metric

www.pearlmeyer.com
Panel Members

Ellen Zane
Director, Brooks Automation, Haemonetics Corporation, PAREXEL International, Lincare Holdings and Press Ganey
Vice Chair of the Board of Trustees, George Washington University
Chair of the Board, Wellforce
Phone: (617) 620-5123
Email: ezane@tuftsmedicalcenter.org

Alex Wittenberg
BRC Commissioner on the Value Creation Commission
Executive Director, Marsh and McLennan's Global Risk Center (GRC)
Partner, Oliver Wyman Group
Phone: (917) 374-3498
Email: alex.wittenberg@mmc.com

Duncan McFarland
Former Chairman and CEO, Wellington Management Company
Former Member Compensation Committee, Gannett Co. and NYSE
Trustee, The Bromley Charitable Trust and RARE, Inc.
Director, New Profit, Inc.
Phone: (617) 763-0956
Email: dmcfarland299@comcast.net

Theo Sharp
Managing Director, Pearl Meyer
Phone: (508) 630-1498
Email: theo.sharp@pearlmeyer.com