

Goal-Setting: The Fundamentals Haven't Changed, But Judgment Matters

A Compensation Committee Series Webinar

Presented by NACD and Pearl Meyer

October 14, 2021

Presenters



Carol Stephenson is a director and chairs the compensation committee at General Motors. She served as dean of the Ivey Business School at the University of Western Ontario from 2003 until her retirement in 2013. Prior to joining the Ivey Business School, she was president and CEO of Lucent Technologies Canada from 1999 to 2003 and a member of the Advisory Board of General Motors of Canada, Limited, a GM subsidiary, from 2005 to 2009. Stephenson is an officer of the Order of Canada and also serves as a director of Maple Leaf Foods Inc.



Matt Turner is a managing director in Pearl Meyer's Chicago office. He specializes in advising company boards and senior management on executive compensation strategy, incentive plan design, tailoring of performance measures, and the setting of shareholder-focused performance objectives. With nearly 30 years of experience, Matt has worked with public and private companies in a range of industries including insurance, manufacturing, technology, real estate, transportation, and retail. In addition to ongoing advisory services, he has also worked extensively with companies undergoing changes in ownership structure, business transformation, and other strategic events.



Veronica Glowacki is a consultant in Pearl Meyer's Chicago office, where she works closely with the firm's managing directors on compensation and company performance data analysis and recommendations.

- Submit a question and receive your answer directly from the presenters, either during today's webinar or as a follow-up. You will also be opted-in to receive future executive compensation thought leadership from Pearl Meyer.
- Presentation slides are available today at www.pearlmeyer.com/goal-setting-fundamentals and within the webinar console.
- The replay will be available early next week at www.nacdonline.org/webinars and www.pearlmeyer.com/goal-setting-fundamentals.

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Setting performance goals for incentive compensation is always a challenge and never more so in the COVID economy, with workforce and supply chain disruptions, as well as the broadening definitions of performance that increasingly include environmental, social, and governance issues.

It is still important to understand the “orthodox” inputs to financial goal-setting (long-range plans, the cost of capital, historical and expected performance, peer performance, etc.). But they are no longer enough.

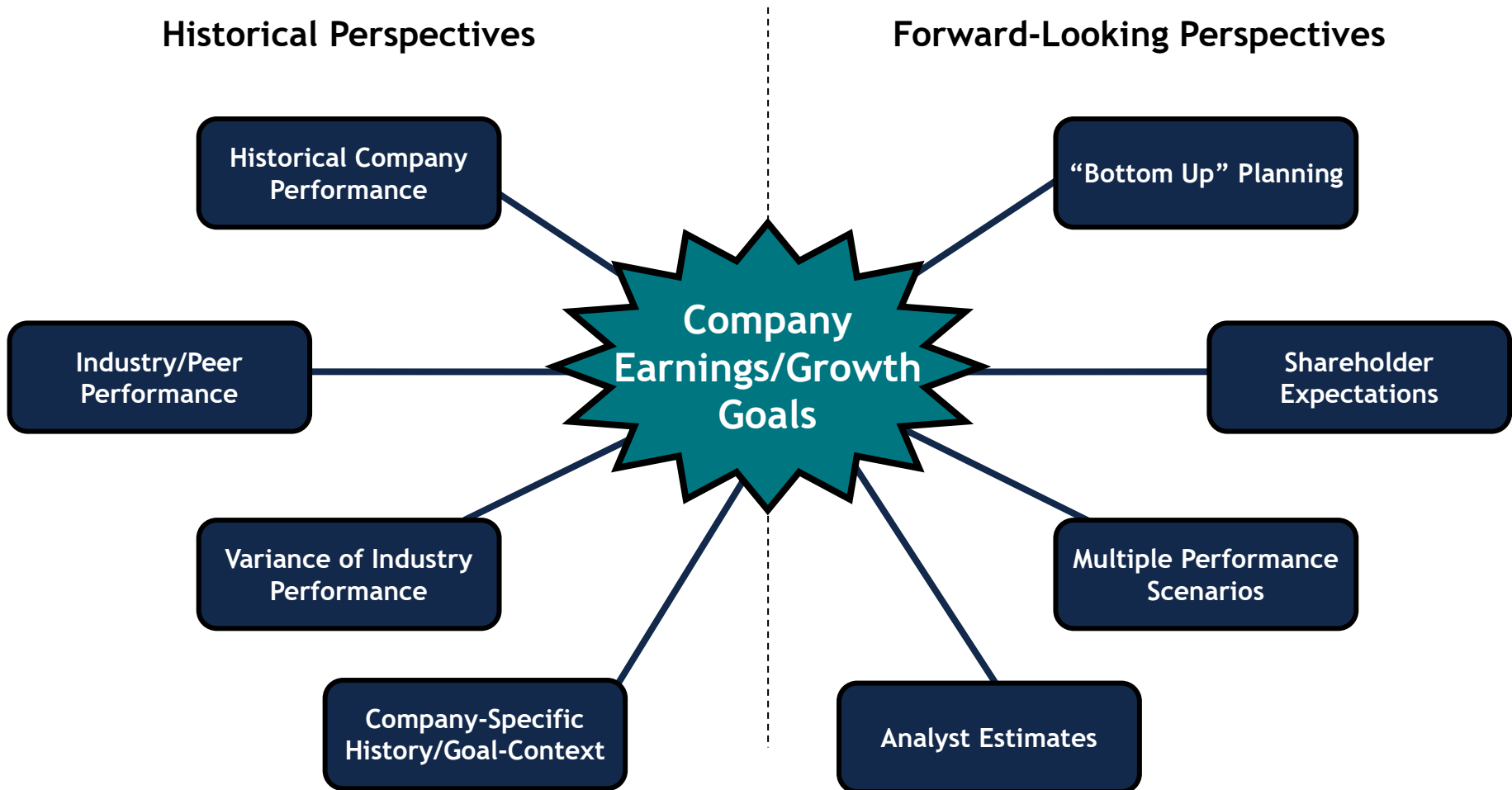
Our new business environment requires at least some qualitative evaluation and the exercise of judgment. It also prompts us to ensure plan design does not exacerbate goal-setting difficulties. In this webcast with Pearl Meyer and the NACD, we will discuss how to balance an ever-evolving goal-setting and performance assessment landscape and do so while remaining firmly rooted in the fundamentals of good business management.

- Multiple perspectives
 - Management budgeting and long-range forecasts, including various business cases
 - Shareholder expectations, as can be inferred from valuations and share price levels
 - Industry expected profit and growth performance
 - Relative performance comparisons within industry, against peers
- Pay-to-performance calibration
 - Meaningful targets
 - Robust performance ranges (threshold to maximum)
- Context; other factors known to management and the board

Multiple Inputs Provide Grounding

Historical Perspectives

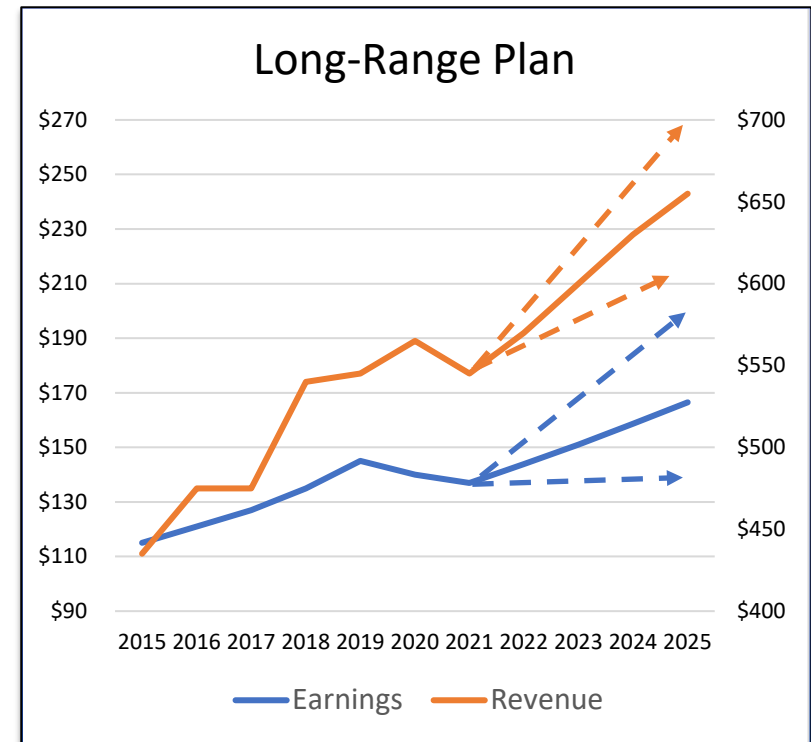
Forward-Looking Perspectives



Budgeting and Long-Range Planning

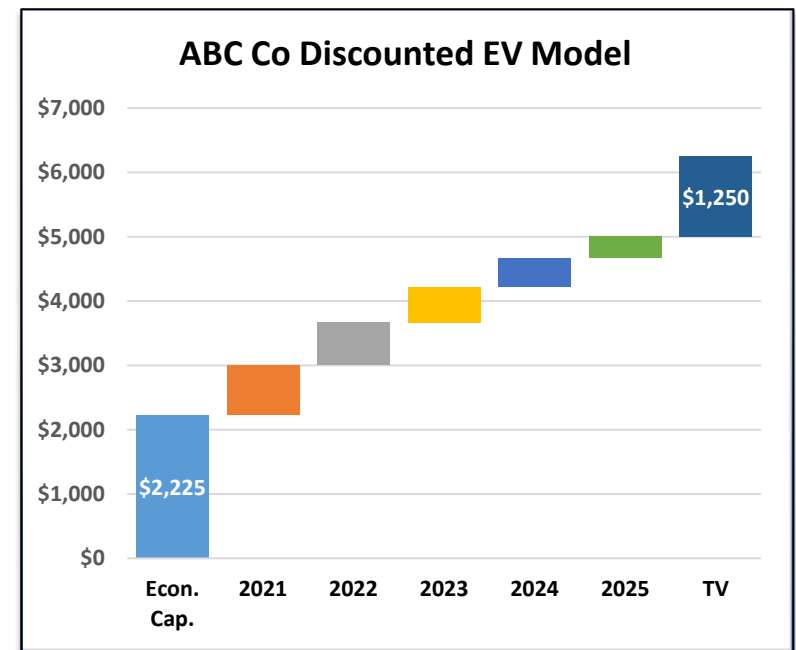


- “Bottom up” planning provides company-specific context
- Multiple business cases help us understand expected variance (and can inform threshold and maximum levels of performance)
- Best plans are grounded in market and industry external data/analysis



Shareholder Expectations

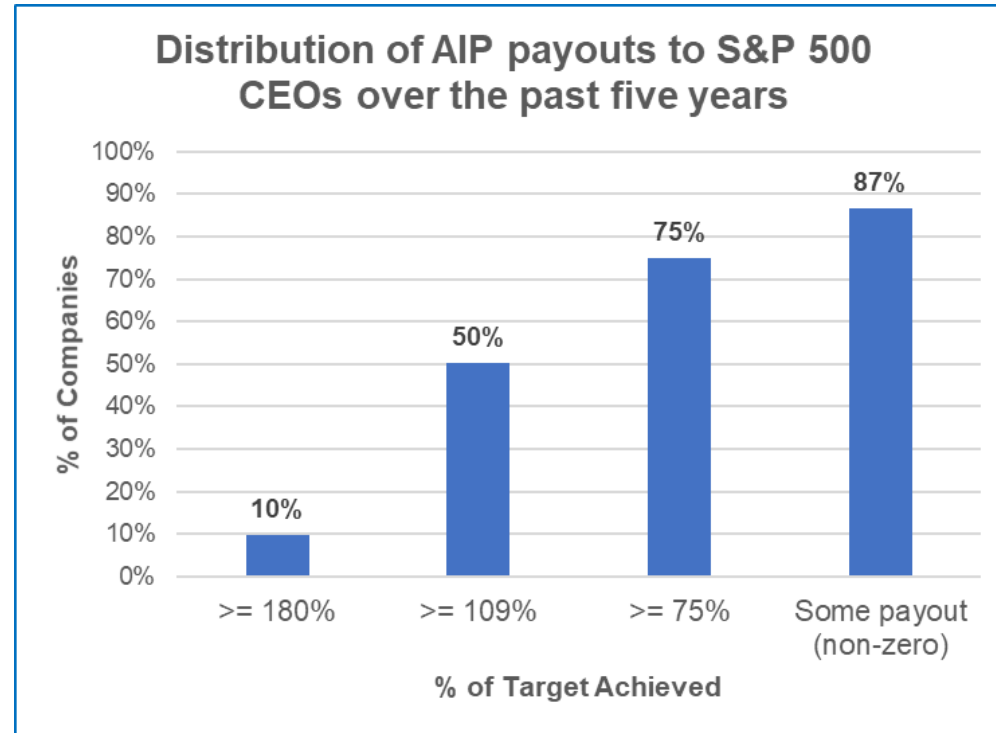
- Management plans should be viewed in light of external performance expectations (“top down”)
- Share price performance and value ratios can be tied back to profit and growth expectations



Goals Should be Relevant and Robust



- Target should be “stretch but achievable”
- Range from threshold to maximum should reflect a broad spectrum of potential performance outcomes
- Calibrate to ensure desired pay-to-performance



Source: Main Data Group

But the Orthodoxy is no Longer Sufficient



- **Adjusting expectations** - an embarrassment of riches for some, continued rough waters for others. How to set 2022 growth and earnings goals?
- **Discretionary use of discretion** - 2021 saw increased tolerance due to Covid, but what about 2022?
- **Continued uncertainty** - the continuing threat of Covid, tremors from China, Federal government budget troubles, etc. all point to historic difficulties in forecasting performance. How can incentive compensation plans cope?
- **The expanding performance scorecard** - ESG is not a fad. Many such areas of “performance” cannot be easily reduced to a few quantitative metrics

“Embarrassment of Riches”

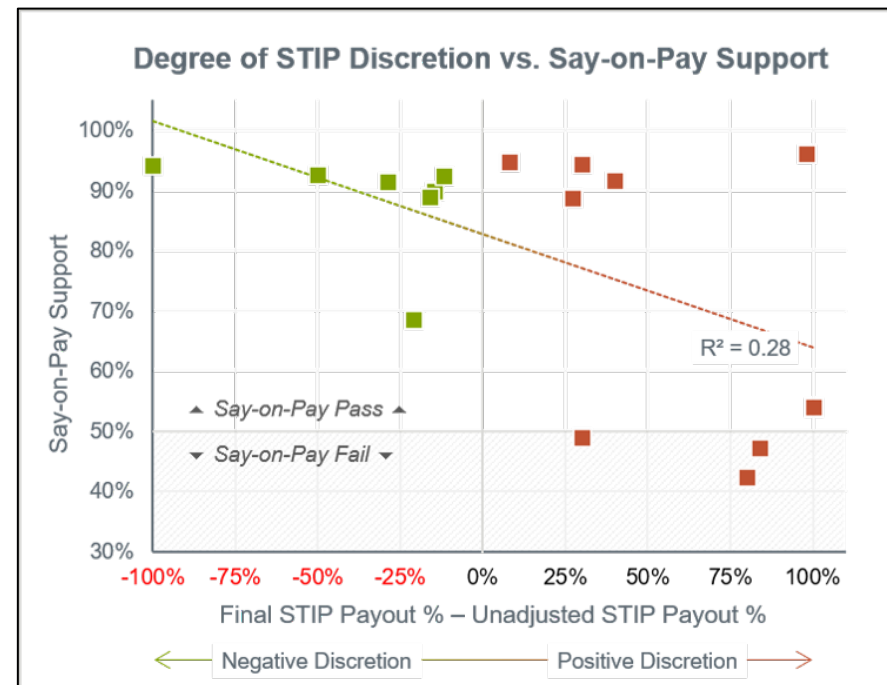
- Construction trades, energy, financials...
- 2021 results shaping up to pay at max or better
- Are results repeatable? Is year over year growth even possible?
- Do management and the Board have the same view for 2022?

“Rough Waters”

- Travel, entertainment, automotive...
- Supply chain shocks; raw materials and component costs; Covid employee shortages, etc.
- Was positive discretion used for 2020? How will ISS and investors view another year of “exception?”

Discretionary Use of Discretion: Caution

- ISS and Glass Lewis signaled openness to positive discretion for 2020. Actual experience for companies exercising it was a mixed bag (*see graphic*)
- Is discretion part of the new normal, or will shareholders shut it down?
- What are the rules for discretion?
 - Preparedness
 - Consistency
 - Fairness
 - Modesty
 - Integrity (of incentive plans)



Source: [Pearl Meyer](#)

Polling Question #1



- Is your company anticipating using discretion to adjust STI payouts for 2021 results?
 - Yes, definitely
 - Likely
 - Unsure
 - Probably not
 - Definitely not

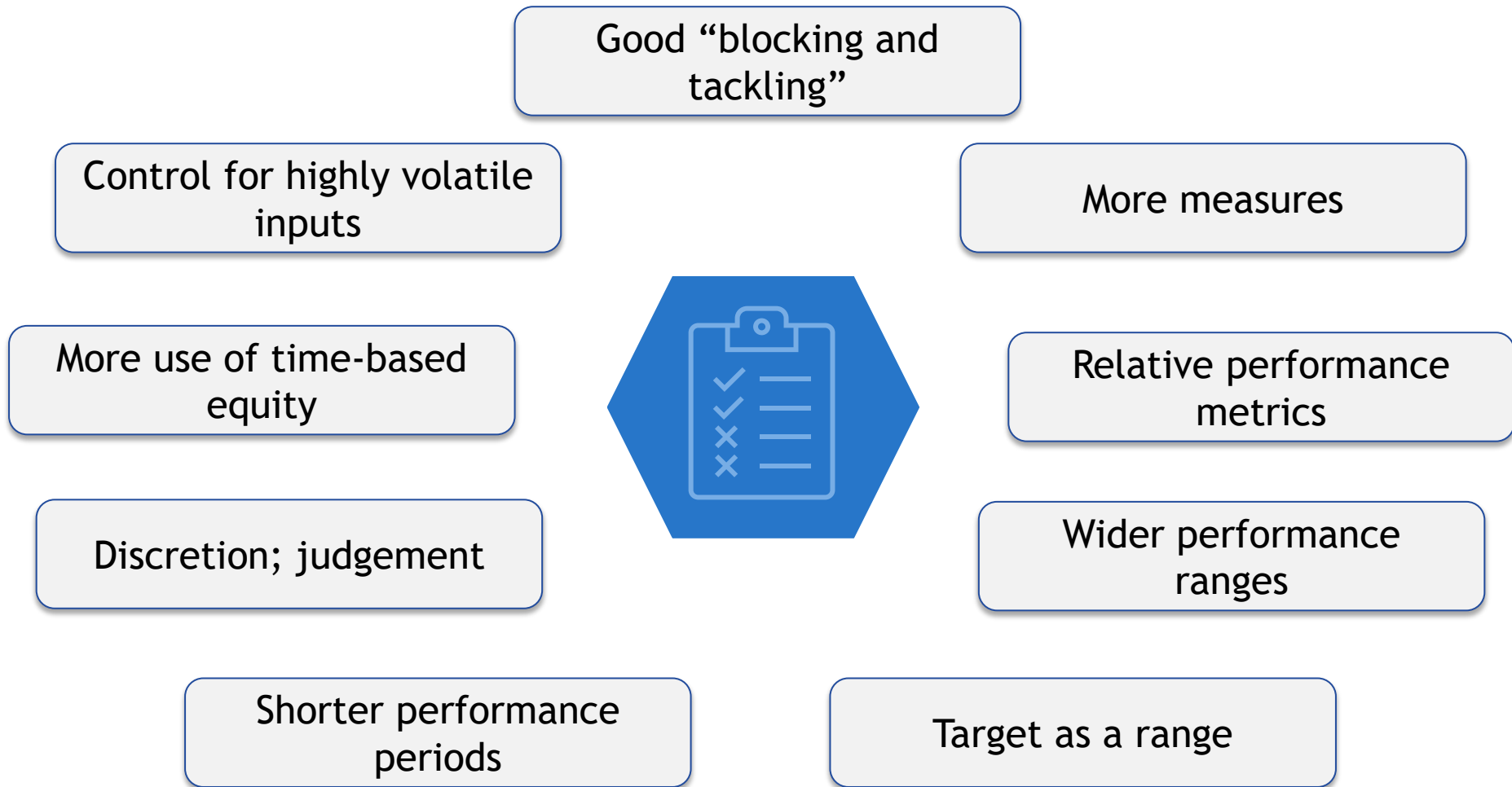
Uncertainty Reigns

Elevated uncertainty increases...

- Likelihood of goals becoming irrelevant during the year
- Chances that ex post pay and performance appear out of line
- Possibility of significant underpayment, risking retention
- Possibility of significant overpayment, risking Say-on-Pay vote; firm reputation



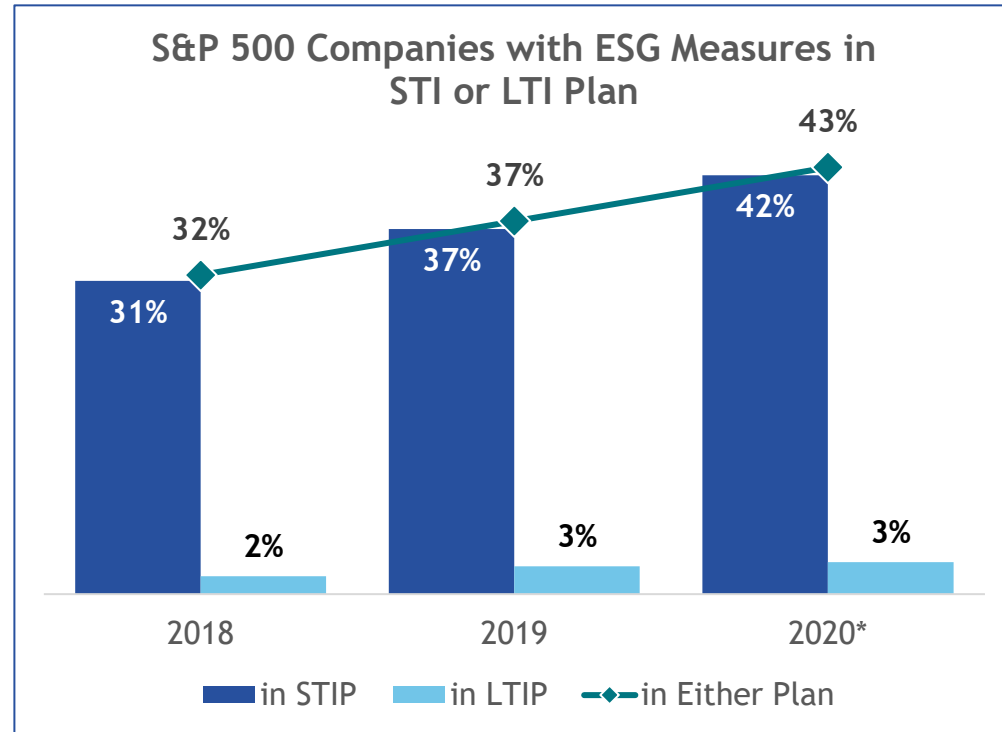
Tools for Dealing with Uncertainty



The Expanding Performance Scorecard



- ESG is here to stay
- Some of this is familiar, some is very new
- Doing it right...
 - Multi-year implementation
 - Build a common understanding
 - Recognize complexity
 - Beware unintended consequences
 - Ensure integrity of goals



Source: Main Data Group

Polling Question #2



- Will ESG measures be a part of your 2022 incentive plans?
 - Yes, they already are
 - Yes, first year of meaningful ESG inclusion
 - Unsure
 - Not likely, but considering for the future
 - No, and not likely for the foreseeable future

- Get the fundamentals right
- Review plan design and pay mix
- Prepare for increased qualitative assessment and discretion
- Stay engaged; invest the time needed to do it right

Q&A

Submit your question using the “Ask the Experts” box on the right side of your screen.

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