Pearl Meyer

ADVISOR BLOG

Preserving the Motivational Effect in 2020 Annual Incentive Programs

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For many companies, fiscal 2020 annual incentive goals that were set prior to the impact of COVID-19 are no longer attainable. While most companies and their boards have been prioritizing other issues, appropriately so, consideration should be given to preserving the incentive effect of 2020 annual incentive programs.

Compensation committees are faced with a choice. They could continue to maintain the current program and goals. Many incentive programs will fail to achieve necessary performance thresholds and thus will not fund. And, in many of the most adversely impacted sectors, zero funding may be fully appropriate. Particularly in instances where employees and shareholders have suffered. Some compensation committees may elect to exercise some degree of discretion at year-end based on a subjective assessment of performance.

Or, compensation committees could consider restructuring the 2020 annual incentive program, incorporating new metrics and goals for the balance of the fiscal year. In doing so, compensation committees have an opportunity to realign incentives with key imperatives for the balance of the year. It's likely those imperatives will not be the standard growth and profitability objectives but rather a set of key performance indicators that expand beyond traditional financial yardsticks to best focus management on pulling the right levers to protect the company during the pandemic and position it for eventual recovery.

For example, compensation committees could consider putting in place a key performance scorecard linked to a portfolio of key indicators as follows:

- **Financial discipline:** managing expenses and working capital
- **Operational execution:** prioritizing logistics and supply chain fluidity
- **Customer experience:** achieving satisfaction and net promoter scores
- **Strategic focus:** positioning for recovery and workforce optimization

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If companies are to consider putting in place such a program, the performance indicators used should be as objective and measurable as possible. In addition, there are a few other considerations to keep in mind.

- **Be sensitive to other stakeholder experiences.** Companies should consider reduced incentive opportunities by pro-rating bonus opportunities based on time elapsed during the fiscal year and/or capping bonus opportunities at target.
- **Consider disclosure and communication issues.** Companies may want (or need) to disclose program changes in an 8-K filing. Institutional Shareholder Services has recommended that companies publicly disclose such changes contemporaneous with the launch of the new program. To get the most mileage out of the new program, communication to employee participants will need to be robust.

Even with a performance scorecard, there is likely to be some degree of subjectivity in evaluating performance at year-end. Compensation committees will need to ensure the right balance is struck between the benefits delivered to management and the experience of other stakeholders.

About the Author

Steve Van Putten is a senior managing director with Pearl Meyer and leads the firm's Northeast region. His primary focus and expertise is on advising compensation committees and senior management on executive and director compensation matters. Steve has twenty years of board-level experience consulting to Fortune 1000 companies on executive pay.

About Pearl Meyer

Pearl Meyer is the leading advisor to boards and senior management on the alignment of executive compensation with business and leadership strategy, making pay programs a powerful catalyst for value creation and competitive advantage. Pearl Meyer's global clients stand at the forefront of their industries and range from emerging high-growth, not-for-profit, and private companies to the Fortune 500 and FTSE 350. The firm has offices in Atlanta, Boston, Charlotte, Chicago, Houston, London, Los Angeles, New York, Raleigh, and San Jose.

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