Pearl Meyer

ADVISOR BLOG

Board of Directors Stepping Up In Troubled Times

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Delta's dramatic pay actions reflect the severe and immediate challenges the company and airline industry face. First, Delta's CEO, Ed Bastian, already gave up his salary for the next six months. Then it was announced that its officers will take a 50% pay cut through June 30. Board members will also participate in the cuts by forgoing pay for the next six months.

While I was reading the Delta article, I was overcome with déjà vu to 2008/2009 and the executive compensation pay actions taken by public companies in the wake of the liquidity crisis that threatened the solvency of the global banking system. Everyone was uncertain and frightened of the potential outcomes, even those who would never admit to feeling insecure. Admittedly, today's crisis is different. We are facing an economic enemy we can't see and don't understand—a virus.

Yet, parallels exist with potential compensation actions that are appropriate given the challenges, particularly with respect to director pay. And although not all industries are as negatively impacted to the extent that travel and leisure has been impacted, nearly all companies have seen significant recent erosion in shareholder value. That significant erosion should be taken into consideration when determining equity grants over the next several months.

For example, we are right around the corner from annual shareholder meetings during which companies will approve board of director equity grants. Boards will need to consider whether they should award full target equity grants. Depressed stock prices will require companies to use significantly more shares to deliver target grant values. As boards begin to discuss their 2020 equity grants, they may want to dust off the 2008/2009 executive compensation playbook and consider a few alternative equity granting approaches:

- Switch from granting equity based on a target value to a target share approach:
  - Establish a target share approach by determining the number of shares to award using a 30-day (45, 60, etc.) stock price average

    - Award the same number of shares as awarded in the prior year
    - Adjust the number of shares granted based on a capped burn rate; for example, if it takes 30% more shares than last year to provide the target equity value, adjust the grant value using 15% more shares
- Grant restricted stock units that settle in cash
- Set a minimum conversion rate collar for establishing a grant price, for example, if at any time the current 30-day average price is below $20, the company will use $20 to determine the number of shares to grant
- Consider switching to quarterly grants if the company typically grants equity annually; this approach mimics the dollar-cost-averaging concept
- Delay making any grants below a set stock price

As the board discusses potential changes to its equity practices, consider drafting proxy language to ensure you can clearly describe the change, the reason for the modification, and how the action aligns with any executive compensation changes taken during the year.

Remember that any board director grant changes may require resolutions and documentation in meeting minutes. Also, check to ensure you don't need to amend any legal plan documents to allow for changes to the board equity grant values or grant frequency.

A final thought: shareholders will enjoy a modest economic benefit when boards approve reduced board equity grant values to reflect a difficult operating environment. Yet, the financial gain realized by shareholders will pale in comparison to the goodwill generated when stakeholders realize boards have stepped up and reduced their own pay to help companies navigate through this challenging period.

About the Author

Pete Lupo is a senior managing director and head of the Atlantic Region. Pete has worked extensively with compensation committees and management covering a variety of needs including the development of total compensation programs covering the senior leadership team, aligning pay to performance, designing annual and long-term incentive plans, developing board of director pay programs, advising on change-in-control, executive benefits, perquisites, and governance-related matters.

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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