

BALANCING PURPOSEFUL COMPLEXITY & GREATER SIMPLICITY IN PAY DESIGN

"WHERE WE ARE, HOW WE GOT HERE"*

CHRO GUIDE



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Over the past few decades, there has been an explosion of criticism of CEO compensation, particularly in the wake of the 2008 financial crisis. The so-called “quantum” level of executive compensation, the apparent lack of a strong correlation between executive pay and performance (often expressed as returns to shareholders), and the correlation between rising pay and wealth disparity have been the main targets of criticism. Many legislative and regulatory measures put forth by critics (see Appendix for a thorough analysis) have significantly increased the complexity of pay and transparency.

Efforts to lower executive pay or strengthen the link between pay and performance have only increased complexity without actually addressing the issue.

To date, these initiatives do not appear to have lowered executive pay or altered the opinions of those who argue that pay and performance are too loosely linked. A new strategy dubbed “simplification” is emerging in response to the perceived inability to restrain executive pay. On the one hand, proponents of the current structure make a strong case that, given all the goals that businesses are required to accomplish, any complexity that does exist is needed and intentional. On the other hand, this may be an opportunity to challenge ourselves and explore alternative ways to structure executive pay.

In other words, the time may be ripe for new thinking and experimentation in the design of executive incentives.

There are three prevailing viewpoints when it comes to simplification:

- 1. “If it ain’t broke, don’t fix it.”***
- 2. “Radical simplification.”***
- 3. “Executive compensation isn’t broken, but aspects of it should change.”***

First, let’s delve quickly into the evolution of pay design: how we got here and why pay plans are so complicated. Then we will review the major voices calling for simplification, a company example of simplification in practice, and the questions management and the Compensation Committee should be asking to assess if simplification is right for their company.

* Kevin J. Murphy, University of Southern California - Marshall School of Business; USC Gould School of Law, *Executive Compensation: Where We are, and How We Got There*, last viewed at https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2041679.

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The evolution of executive compensation has been influenced by several factors, including:

- Market competition for executive talent
- Increased size and complexity of companies
- Legislative and regulatory changes
- Investor and proxy advisory firm policies
- Calls for including non-financial incentive metrics based on environmental, social and governance objectives.

Critics of executive pay have pushed through a number of initiatives designed to address perceived concerns with executive pay.



Why have these initiatives failed to produce the desired result? They do not consider the dynamics of supply and demand in the market for executive talent. Indeed, increased disclosure means increased transparency of pay for executive talent - which means boards are obligated to make pay as competitive as possible to attract, motivate and retain the requisite talent to lead large, complex, global companies.

Regulation and legislation have significantly increased the level of complexity around plan design and disclosure.

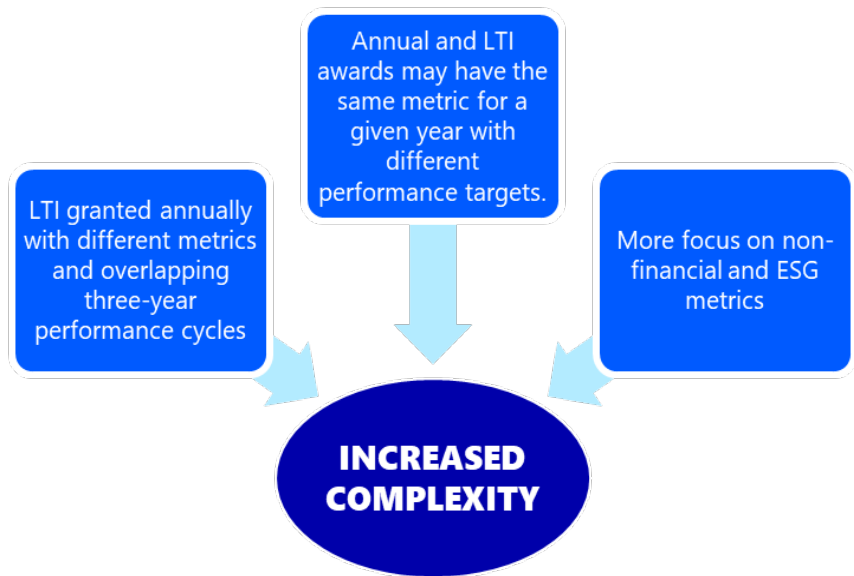
In fact, in the end, the plethora of regulation and legislation around executive compensation have only *increased* the level of complexity, both in plan design and disclosure.

SOURCES OF INCREASED COMPLEXITY: DESIGN AND DISCLOSURE

Sources of Increased Complexity: Design and Disclosure

INCENTIVE DESIGN

The forms of annual and long-term incentives that comprise the typical mix of executive compensation are increasingly complex. They span different time periods, use a mix of internal and external performance metrics and may vary among named executive officers (e.g., mix of corporate-wide and single division metrics).



SOURCES OF INCREASED COMPLEXITY: DESIGN AND DISCLOSURE

DISCLOSURE

Mismatch in definitions of pay and performance. Most companies award long-term incentives on a forward-looking basis. That is, the final value of the incentive is contingent upon the accomplishment of forward-looking financial objectives and growth in stock price, and the company's assessment of the pay for performance linkage is conducted at the end of the performance period when results are known and the awards earned and vested.

By contrast, investors and proxy advisors typically assess the pay for performance linkage by comparing Summary Compensation Table reported total pay, which is in large part the current estimated expense of long-term incentives that may or may not be earned at some future date, with total shareholder return over the prior 3- to 5-year time frame. This mismatch of time frames for assessing performance and the use of the Summary Compensation Table measure of pay at date of grant, rather than the pay realized at the end of the performance period, adds to the complexity of assessing pay for performance.



Supplemental Pay Disclosures. Due to the failings of the Summary Compensation Table, companies have developed and disclosed supplemental measures of pay, primarily realizable and realized pay, to help investors understand the pay for performance linkage. As if this were not complex enough, the SEC has now required yet another version of pay to be disclosed, "Compensation Actually Paid," as part of its 2022 Pay Versus Performance rule.

Proxies Too Long. A 2015 study¹ by Equilar, RR Donnelley and the Stanford Graduate School of Business found that 55% of investors thought the typical proxy was too long, resulting in the average investor only reading 32% of the proxy. Since this study was conducted in 2015 the length and complexity of the proxy has increased significantly due primarily to additional mandated disclosures.

Company-Specific Names. The same form of award may have different names across companies (e.g., for short-term incentives, "Performance Incentive Plan," "Management Incentive Plan," "Key Incentive Compensation Plan," and for long-term incentives "Performance Shares," "Performance Units," "Restricted Performance Shares of Units," "Growth Shares," etc.) thereby making the comparison of pay programs difficult for investors to decipher.

¹ Stanford Graduate School of Business *et al.*, 2015 *Investor Survey: Deconstructing Proxy Statements*, last viewed at <https://www.gsb.stanford.edu/faculty-research/publications/2015-investor-survey-deconstructing-proxy-statements-what-matters>.

PURPOSE BEHIND EACH ELEMENT OF COMPLEXITY

Purpose Behind Each Element of Complexity

"If it ain't broke, don't fix it." The current structure of executive compensation does what it is supposed to do. The complexity is purposeful and designed to accomplish necessary objectives.

Complexity is purposeful and each element is necessary. The evolution of executive compensation design and disclosure represents an effort by compensation committees to bridge the expectations of external stakeholders and regulators with company objectives. The combination of these considerations has contributed to a degree of purposeful complexity in the design of executive pay programs.



OBJECTIVES

Long-term incentive programs are designed to accomplish the following objectives:

- **Encourage a long-term perspective;**
- **Combat short-term decision-making** that may undermine sustained value creation;
- **Address the agency problem** inherent in the separation of ownership and management of the modern corporation (long-term incentives are predominately equity-based awards which align the interests of management with those of shareholders);
- **Achieve favorable accounting expense treatment** (i.e., to favor awards that have "fixed accounting" based on grant date value rather than awards that require mark-to-market accounting); and
- **Ensure ongoing alignment with shareholders** beyond the performance period of the incentive award (often through use of share retention requirements and ownership guidelines).

PURPOSE BEHIND EACH ELEMENT OF COMPLEXITY

FORMS OF EQUITY

Companies often grant two or three forms of equity (generally stock options, performance shares and time-vested restricted stock) to reinforce different aspects of performance.



Stock Options provide alignment with shareholders' interests in that the executive only realizes gains if shareholders benefit through share price appreciation. Stock options generally have a ten-year term and multi-year vesting requirement, which emphasizes longer-term performance.



Performance-Based Awards in the form of shares, units or cash, motivate the accomplishment of medium-term performance, generally three years, based on strategic and operational goals linked to sustained value creation and relative returns to shareholders versus peers.



Time-Vested Restricted Stock provides immediate alignment with shareholders through share ownership and is a powerful tool to support the company's talent strategy and retention of key individuals deemed critical to the longer-term success of the company.



PERFORMANCE METRICS

Metrics generally vary between annual awards and long-term incentives to reinforce differing aspects of operational and strategic goals and investor expectations. Further, given the prevailing practice of annually granting long-term awards that have overlapping performance periods with prior awards, there may be differing performance objectives for overlapping performance periods in recognition of a changing competitive or economic context prevailing at the time of each annual award.

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COMPANY GOALS

Metrics are expected to reinforce both the level of performance, such as revenue growth, and the quality of performance, such as return on investment. To reward competitively superior performance, some metrics may be measured relative to peers or industry index, while other metrics may be measured based on an absolute target to reinforce achievement of budget or strategic objectives.

Metrics may be:

- Purely financial in nature
- Non-financial but strategically important (this may also include ESG goals)
- Relative or absolute returns to shareholders

INVESTOR EXPECTATIONS

Companies are challenged by differing investor and proxy advisor requirements for performance metric selection. For example, ISS focuses primarily on relative TSR to an ISS-defined peer group, while Glass-Lewis assesses performance based on both TSR and four standard financial metrics. Investors also differ - some favor profit measures while others prefer growth measures, measures of the product pipeline, or return measures in their evaluation models.

In view of these differences in focus, it is not surprising that while companies have invested significant resources in communicating the purposes behind the complexity of incentive arrangements, investors continue to express frustration with the perceived lack of clarity of the pay for performance linkage of executive pay.



CALLS FOR SIMPLIFICATION

Calls for Simplification

“Radical simplification.” The current approach to designing executive compensation is outdated and not serving the interests of stakeholders. Alternative approaches such as eliminating performance shares or equity incentives altogether should be considered.

Critics assert that the current structure of long-term incentives is unnecessarily complex and that the multiple forms of incentives and performance metrics have contributed to the rise in executive pay, thereby prompting calls for simplification of program design. The challenge for companies is to determine if there are ways in which compensation programs may be simplified without jeopardizing the objectives underlying the purposeful complexity of current executive compensation design.

The current structure of long-term incentives is unnecessarily complex.

Further, it is important that companies engage with investors to understand the extent to which complexity is truly the driver of concerns over the current structure of long-term incentives, if the underlying motivation for simplification is an effort to rein in pay rather than reduce complexity, or whether investors have multiple objections to current executive compensation designs.

Vocal examples of this viewpoint include Norges Bank Investment Management (largest sovereign wealth fund in the world, owning 1.5% of 9,000 companies globally), the Council of Institutional Investors, and the UK Executive Remuneration Working Group.



Norges Bank argues that equity-based compensation has not aligned CEO pay with shareholder interests, overall levels of CEO pay do not correlate with company performance and “increasingly complex remuneration takes up considerable time and focus in the relationship between companies and investors” thereby diverting attention from important other company issues.² The Norges position is that long-term incentive plans are ineffective and expensive and put pressure on corporate governance.³

² Norges Bank Investment Management, 01/2017 Remuneration of the CEO: Asset Manager Perspective, at 5, last viewed at <https://www.nbim.no/contentassets/bc85c448e6b24ff5a31088883695a344/ceo-remuneration---amp-1-17---norges-bank-investment-management.pdf>.

³ *Id.* at 9.

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The approach Norges recommends is simple: traditional long-term incentives should be eliminated. Rather, a substantial portion of annual pay should be delivered in restricted stock that vests over the long-term, beyond the typical three-year performance period that some may argue is short term in the business cycle. Norges argues that this simplified approach is more transparent and provides an ongoing alignment of management interests with those of shareholders. While the stated objective is simplification and transparency, the objective may actually be to limit the size of CEO pay by limiting “the prospect of unanticipated and outsized awards that challenge legitimacy” since Norges calls on boards to set a cap on the amount of CEO pay.⁴

Meanwhile, the Council of Institutional Investors, which provides corporate governance insights to a membership of asset owners including pension and retirement funds, has stated it believes performance plans are a “major source of today’s complexity and confusion” and are “susceptible to manipulation.” Therefore, CII argues, the Compensation Committee should consider whether performance shares should simply be replaced with “long-vesting restricted shares” over a period of at least 5 years and preferably as long as ten years, or even into retirement.⁵

Finally, the UK Department of Business, Energy and Industrial Strategy published a “Green Paper” on corporate governance⁶ criticizing the complexity of executive pay which “has contributed to poor alignment between executives, shareholders and the company, sometimes leading to levels of remuneration which are very difficult to justify.”⁷ To remedy this perceived problematic structure, the Green Paper questions whether companies should eliminate LTI programs and merely grant restricted shares that vest over a minimum of 5 years.⁸ Given that time-vesting restricted shares are assumed to have a greater certainty of value when compared to performance-based long-term incentives, the Green Paper solicited comments on whether the grant date value of restricted share awards need only be set at discount of 50% or more of the targeted value of performance-based long-term awards.

⁴ Norges Bank Investment Management, CEO Remuneration Position Paper, at 1, last viewed at <https://www.nbim.no/en/responsible-investment/position-papers/ceo-remuneration/>.

⁵ Council of Institutional Investors, 3/6/2023 Policies on Corporate Governance, last viewed at https://www.cii.org/corp_gov_policies.

⁶ The Executive Remuneration Working Group was created by the Investment Association of the UK and issued a report encompassing 10 recommendations arguing that companies should “be given the flexibility to select the right pay structure that works for them and their shareholders, rather than focusing solely on the currently dominant ‘one-size-fits-all’ Long-Term Incentive Plan (LTIP) pay structure.” See “Investment Remuneration Working Group Issues Ten Recommendations to Rebuild Trust in Pay,” July 26, 2016, last viewed at <https://www.theia.org/news/press-releases/executive-remuneration-working-group-issues-ten-recommendations-rebuild-trust>.

⁷ UK Department of Business, Energy and Industrial Strategy, Corporate Governance Reform Green Paper, p. 17 (quoting the Final Report of the Executive Remuneration Working Group).

⁸ See *id.* at 32-33.

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CORPORATE PERSPECTIVE

This viewpoint is not without corporate support. A study conducted by PricewaterhouseCoopers which surveyed over 1,000 executives across 43 countries, including the US, found that fewer than half of the participants believed long-term incentives are an effective incentive, although two-thirds valued the opportunity to participate.⁹ Participants preferred current pay, based on internal financial measures they felt they could more directly influence, as opposed to deferred compensation that has a more ambiguous value, even though the potential for gain may be higher.¹⁰ The study recommended “[W]henever possible go for the simpler option – requiring executives to hold shares may be a better approach than plans with complex performance conditions.”¹¹

Unilever, a UK-headquartered company, in 2016 eliminated long-term incentives for its top 500 managers (other than “Executive Directors” such as the CEO and CFO) and instead implemented a co-investment model to drive an “owner’s mindset.”¹² Under the revised approach to incentives, executives were encouraged to invest up to 100% of their annual incentive payouts in Unilever shares. The company matched the participants’ investment based on the performance of the company. The amount of the company match ranged from 0% to 200% of the participants’ share investment and vested over a 4-year period.¹³

Why do that? The stated rationale for this change was to simplify rewards; increase shareholding levels throughout Unilever’s management population; ensure consistent alignment of performance measures with strategy; and increase the timeframe over which incentives are delivered.¹⁴ Since the time period over which the incentive is earned matched the time period of the reported performance results, it was easier to communicate to executives.

Further, a co-investment approach ensures the executive risks his or her own money in company shares, creating real alignment with shareholders. In the Unilever Annual Report and Accounts for 2022, the performance metrics for the co-investment plan included not only measures of financial performance but had evolved to include broader stakeholder objectives.¹⁵ Drawing on research from behavioral economics, one might expect the incentive effect of investing an executive’s own money to be increased effort to create shareholder value and avoid loss. This research suggests that individuals are more highly motivated to avoid losses than to seek gains, suggesting the co-investment model may help create sustained shareholder value while avoiding excessive risk.¹⁶

⁹ PwC, Making Executive Pay Work: The Psychology of Incentives, at 6, <https://www.pwc.com/gx/en/hr-management-services/publications/assets/making-executive-pay-work.pdf>.

¹⁰ *Id.*

¹¹ See *id.* at 7.

¹² *Unilever Annual Report and Accounts 2016*, p. 50.

¹³ See *id.* at 49.

¹⁴ *Id.*

¹⁵ *Unilever Annual Report and Accounts 2022*, p.118

¹⁶ Richard H. Thaler, *Quasi Rational Economics*, p. 7 (1991).

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“Executive compensation isn’t broken, but aspects of it should change.” We should assess the extent to which complexity is helping or inhibiting the intended motivational impact of incentives and simplify where possible.

ONE SIZE DOESN’T FIT ALL

Although the call for simplification tends to emphasize the use of restricted shares as the preferred approach to long-term incentives, even Norges Bank points out that one formulation of incentives may not be appropriate for all companies. “Boards must be able to tailor remuneration plans to the challenges of the company and encourage the CEO to take appropriate risk. Boards should be able to reward strategic moves by the CEO, even if the market does not immediately appreciate their significance.”¹⁷

The desirability of tailoring long-term incentives to best meet the company’s objectives would suggest that compensation committees assess the extent to which the current complexity in the company’s long-term incentive design is helping or inhibiting the intended motivational impact of long-term incentive awards. If there is a better approach to incentives that clarifies the pay for performance linkage while maintaining flexibility to accommodate potential changes in strategy and the competitive environment, compensation committees should know about it.



¹⁷ Norges Bank Investment Management, CEO Remuneration Position Paper, p. 2.

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Key questions the committee should ask:

- Do participants understand the incentive program and exhibit the behaviors that lead to the accomplishment of performance objectives (i.e., are the compensation programs effective)?
- Do participants believe the relationship between pay and performance to be fair?
- Is the relationship between absolute pay and performance proportionate?
- Relative to peer companies, are the compensation programs competitive? Are the payouts and performance proportional to that of competitors?
- Do shareholders understand the pay for performance linkage and assess the proportionality of pay and performance to be appropriate?
- Does management have the appropriate analytical tools to demonstrate the appropriateness of the pay for performance relationship?
- Is the accounting expense of the compensation programs efficient?
- Can the company deduct the expense of the compensation programs (i.e., are they tax efficient)?
- Is the company getting the highest return, as measured by performance outcomes, in comparison to participants' perceived value of the form and level of compensation received?
- Are there simpler approaches to executive incentive design that accomplish the performance objectives and desired alignment with the interests of shareholders and other stakeholders?
- How often does the Compensation Committee need to apply discretion when determining the appropriate award because of the inherent challenges of formulaic plans (e.g., setting goals, making assumptions, uncontrollable events)?

One formulation of incentives may not be appropriate for all companies. If there is a better approach, compensation committees should know about it.

SIMPLIFICATION OPPORTUNITIES

Simplification Opportunities

Should a compensation committee determine that current approaches to executive compensation are overly complex and want to explore alternatives to simplify their designs, here are some examples.

- **Eliminate LTI awards and provide only salary and annual incentives**, but require a significant portion of the annual incentive to be deferred into restricted stock to negate the potential for short-termism and align with long-term shareholder interests.
- **Eliminate LTI and provide only salary and restricted stock**, with shares vesting over a multi-year period.
- **Grant only one form of performance-based long-term incentive** to reduce complexity.
- **Grant only stock options that provide a clear pay for performance relationship** with shareholder returns,
- **Simplify the number of performance measures used** in both annual and LTI awards.



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Change	Intent	Impact
SEC Disclosure Rules of 1983	Narrative disclosure of executive compensation in the proxy	Increased the length and complexity of compensation disclosure.
Tax Reform Act of 1984	Created IRS Code §280G, tax treatment of golden parachutes	Companies reacted by instituting gross-ups for the excise tax on excess parachute payments.
Revised SEC Disclosure Rules of 1991	Tabular disclosure of executive compensation in the proxy	Turned attention away from the narrative section of the pay disclosure and increased attention to the “numbers” as opposed to design.
Omnibus Reconciliation Act of 1993	Created IRC §162M, limiting the deduction of non-performance-based compensation	Increased the use of stock options given that §162M deemed options to be per se performance-based and deductible and increased the tendency of companies to increase salaries of CEOs to \$1 million, the amount deductible for non-performance-based pay.
Introduction of 10b5-1 plans, 2000	To provide an affirmative defense for executives against claims of insider trading	Facilitated the trading of company equity by directors and officers by providing a way to trade without the appearance of timing trades based on material non-public information
Sarbanes-Oxley Act of 2002	Mandated SEC-executed clawbacks for CEOs and CFOs and prohibition of loans to executive officers.	SOX requires CEO and CFO certification of filed financial reports. The Act prohibits loans to executives and introduced an SEC-enforced clawback applied to CEO and CFO in the case of willful misconduct in financial filings and created demand for a broader clawback mandate.
FAS 123R (now ASC 718) 2004	Mandated financial expensing of stock options	Reduced the prevalence of stock options below the senior-most executives thereby denying a broad group of employees from benefiting as the stock market increased, generating gains from equity-based compensation.

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American Jobs Creation Act of 2004	Established IRC §409A, limitations on the design of deferred compensation arrangements	Reduced the attractiveness of deferred compensation and potentially negated the risk-mitigation aspect of executives having significant amounts of their earnings at risk as general creditors of the company.
SEC Disclosure Rules of 2006	Mandated the Compensation, Discussion & Analysis section of the proxy	Added the total pay column to the Summary Compensation Table, even though the total is a mix of actual pay and the accounting expense of contingent pay and the actuarial change in the expense associated with interest changes in defined benefit pension plans. The total pay column has resulted in pay for performance analysis being conducted based on this erroneous concept of total pay.
Troubled Asset Relief Program (TARP)	Mandated clawbacks, Say on Pay and reduced deductibility of executive compensation under §162(m) for TARP firms	For companies receiving TARP financial relief, TARP mandated say on pay, and reduced deductibility limits under 162(m). These compensation provisions paved the way for the compensation provisions of the Dodd-Frank Act that apply to corporations beyond TARP recipients.
SEC Disclosure Rules of 2009	Mandated reporting of risk and incentives. Established new compensation standards for banks	Compensation Committees undertook a review of incentive plans to ensure pay arrangements do not motivate excessive risk. While not required, companies disclose in their CD&As that the committee has conducted a review of compensation programs and they do not believe the pay arrangements "are reasonably likely to have an adverse material impact on the company" and many companies disclose the mitigating factors that help guard against the potential for excessive risk. In the financial sector, stock option use has declined dramatically due to the view that stock options may motivate excessively risky behavior.
Dodd-Frank Act of 2010	In reaction to the financial crisis of 2008/2009 and the belief that excessively risky executive incentives were a contributing factor to the financial crisis	Created say on pay and say on parachutes, clawbacks, pay ratio disclosure, pay-for-performance disclosure, limitations on incentive-based compensation for banks, compensation committee independence, disclosure of hedging policy

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Effective Date of Dodd-Frank Act Say on Pay, 2011	Following the financial crisis, the SEC implemented rules that require companies to allow shareholders to vote on the frequency with which they are provided the opportunity to vote on the company's compensation disclosure (say on pay). Shareholders can elect to have a say on pay vote every 1, 2 or 3 years. The vote is non-binding.	Shareholders have almost universally adopted annual say on pay votes. The desire by companies to receive strong shareholder support, and a "for recommendation" from proxy advisory firms has led to greater engagement with institutional investors, phasing out problematic pay practices, homogenization of long-term incentive plans with 50% or more of long-term incentives in the form of performance-based equity with relative shareholder-return as the most prevalent performance metric.
Tax Cut and Jobs Act of 2017	Eliminated the performance exception under §162(m) and provided that if an executive officer is a Named Executive Officer the executive will forever be subject to §162(m) even if not a Named Executive Officer in subsequent years	The elimination of the performance-based exception to §162(m) may have contributed to the continued decline in prevalence of stock options for NEOs and the increase in the use of restricted stock.
Effective Date of Dodd-Frank Act Pay Ratio Disclosure, 2018	Companies must disclose the ratio of CEO pay to that of the median employee. Additionally, the pay of the median employee must be disclosed	Aside from the cost and effort required to collect employee pay information globally, there has not been a discernable impact on CEO pay or the pay of employees in general.
American Rescue Plan Act of 2021	The ARPA provides that beginning after Dec 31, 2026, in addition to the CEO, CFO and next highest paid "executive officers," the next five highest paid "employees" will be subjected to the limitations of §162(m) in the year they are among the five highest paid employees	Greater limitations on the ability of companies to deduct compensation for employees below the executive officer level.

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<p>Effective Date of Dodd-Frank Act Pay for Performance Disclosures, 2023</p>	<p>To provide a standardized disclosure of the relationship between NEO compensation and the financial and stock performance of the company.</p>	<p>The Pay for Performance rules are highly prescriptive and require complex annual valuation and disclosure of outstanding and vested equity-based incentives. Companies will also be required to disclose financial metrics required by the rule (TSR and Net Income) and metrics selected by the company as being the most important metrics for compensation decisions and provide a description as to the relationship of pay to these metrics (either graphically and/or as narrative) and the TSR return of peer companies (either companies used for compensation benchmarking as disclosed in the proxy or an industry index as disclosed in the 10-K).</p>
<p>Effective Date of Dodd-Frank Act Clawbacks, 2023</p>	<p>To ensure that executive officers do not benefit from incentive awards based on performance outcomes that are impacted by a material restatement due to non-compliance with financial reporting requirements (big R) or restated financials that do not rise to the level of requiring a material restatement of previously issued financial statements if left uncorrected (little R)</p>	<p>Most large companies have adopted clawbacks but there may need to be adjustments to comply with the Dodd-Frank clawback rules (e.g., remove the requirement of fault and limit board discretion to situations where a clawback would be impractical). Companies must formally adopt and disclose in the 10-K their compliant clawback policy. In the event of a restatement, companies must disclose in the proxy the date of the restatement, the amount of the clawback and how it was calculated, and the aggregate amount of uncollected amounts to be clawed back.</p>
<p>Effective Date of Changes to 10b5-1 Plans, 2023</p>	<p>Based on the belief that executives are using 10b5-1 plans as a shield to benefit from the timing of trades in company stock-based on the possession of material non-public information (MNPI) and that board may be timing the granting of options to avoid the granting of awards prior to the release of unfavorable information (“bullet dodging”) or in advance of the release of favorable information (“spring-loading”)</p>	<p>The 10b5-1 rules will reduce the attractiveness of such plans due to the 90-day cooling-off period, required certification that the director of officer is not aware of MNPI, and they acted in good faith. Additional restrictions on single-trade plans and disclosure requirements of 10b5-1 plans adopted or terminated in the year and the company policy on insider trading or why the company has not adopted and such a policy. There is also a requirement for stock options granted to NEOs in the four business days preceding the release of MNPI (including earnings) or one business day afterward.</p>

Sources: Murphy, Kevin J., *Executive Compensation: Where We Are, and How We Got There* (August 12, 2012). George Constantinides, Milton Harris, and René Stulz (eds.), *Handbook of the Economics of Finance*. Elsevier Science North Holland (Forthcoming), Marshall School of Business Working Paper No. FBE 07.12, Available at SSRN: <https://ssrn.com/abstract=2041679> or <http://dx.doi.org/10.2139/ssrn.2041679>, and Center On Executive Compensation, *Long-Term Incentive Design: Where We Are, How We Got Here and An Assessment of Calls for Change* (2017)

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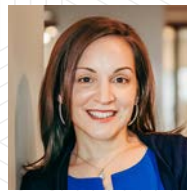
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About the Center On Executive Compensation

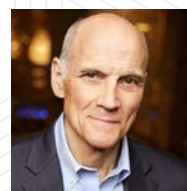
With deep experience and an unbiased perspective, [HR Policy Association's Center On Executive Compensation](#) serves as an extension of *your* executive compensation team. With timely information and resources, the Center empowers its members to rise to the challenge with their Compensation Committees and a growing number of interested stakeholder groups. Led by President and CEO Ani Huang, the Center is guided by an Advisory Board of 14 currently-serving CHROs or Heads of Total Rewards.

With over 165 members, the Center On Executive Compensation provides deep expertise and advocacy on the top executive compensation and corporate governance public policy and practice issues facing Chief Human Resource Officers and their teams. Full access to the Center's advocacy and educational resources is provided through this premium membership available exclusively to HR Policy Association members.

About the Authors



Ani Huang is President and CEO of the Center On Executive Compensation and Senior Vice President of the HR Policy Association. Ani joined the Association in January 2012 from Global Payments, Inc, where she was Vice President of Global Compensation and Benefits. She has almost two decades of experience in compensation and human resources. In her current role, Ani is responsible for overseeing the Center's practice on a wide variety of executive compensation and governance issues as well as Subscriber engagement and Center research and writing. She is a frequent speaker and writer on the topics of executive compensation and governance. Prior to serving as Vice President of Global Compensation and Benefits at Global Payments, Ani held various positions at Deutsche Bank A.G. in New York and Tokyo, Japan. She is a graduate of Stanford University.



Dr. Charles G. Tharp is Senior Advisor, Research and Practice at the Center On Executive Compensation. In that role, he is responsible for setting overall policy positions and research initiatives undertaken by the Center and representing the Center in public forums. He is also Professor of the Practice in the Management and Organizations Department, Boston University Questrom School of Business.

Tharp has over 25 years of corporate experience, including key human resource positions with General Electric, PepsiCo, Pillsbury, CIGNA and Bristol-Myers Squibb, where he served as Senior Vice President of Human Resources. Tharp also served as the interim Executive Vice President of Human Resources for Saks, Incorporated. Earlier in his career he served as an executive compensation consultant for the global consulting firm of Towers Perrin. Tharp holds a Ph.D. in Labor and Industrial Relations from Michigan State University, an LLM in Human Rights and Social Justice from the University of Connecticut School of Law, a J.D. from the Quinnipiac School of Law, a Masters in Economics from Wayne State University and a BA from Hope College where he was Phi Beta Kappa and a Baker Scholar. In 1998 Tharp was elected a Fellow of the National Academy of Human Resources and in 2010 was elected a Distinguished Fellow of the Academy, the highest honor in the HR profession. He previously served as President of the Academy.

Executive Summary

Evolution of Executive Pay Design

Sources of Increased Complexity: Design and Disclosure

Purpose Behind Each Element of Complexity

Calls for Simplification

Revisiting LTI Design

Simplification Opportunities

Appendix: Major Regulatory and Legislative Changes Involving Executive Compensation

About the Center On Executive Compensation

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