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Hot Topics in Executive Compensation

By Brad Smith

I recently attended an annual symposium on Executive Compensation with a wide spectrum of information covered. Below are a few observations:

There is increased involvement/governance by compensation committees. Government regulations and the overall investor climate have triggered and in some ways required increased compensation committee scrutiny of executive compensation plans.

Observations:

a. A growing trend is for compensation committees to meet with major shareholders to ensure they understand the executive compensation plan and assist in improving the likelihood of passing the Say on Pay vote.
b. Most corporations are incorporated under Delaware law. Delaware law does not require business decisions to be good; however, it does require governance to be good and free from conflicts of interest.
c. Over the last few years, there have been many cases involving executives receiving severance or other compensation that have provided negative publicity for corporations.

For now, the CEO Pay Ratio, which came out as a result of the Dodd-Frank Act, is here to stay. The final ruling was approved by the SEC during 2016 – see Findley's Legislative Update for more details.

Observations:

a. The determination of the median employee is a significant investment of time by corporations.
b. Different corporations will calculate the ratio in different ways, thus not allowing for comparability between entities.
c. There may be a need to increase communication with nonexecutive employees on compensation philosophy.

Several organizations, ISS/Glass-Lewis/SEC/Activist, are closely tracking several topics:

Areas of Interest:

a. Evergreen renewals of executive compensation agreements
b. Golden parachute excise tax gross ups
c. Guaranteed bonuses/equity grants
d. "Excessive" severance or perquisites
e. "Liberal" change of control definitions and/or payouts
f. Single trigger vesting of equity grants
g. Reconciliation of non-GAAP performance measures to GAAP

Trends in executive compensation design

Observations:

a. Mandatory holding periods after vesting are growing in popularity for accounting purposes.
b. A portfolio approach (more than one vehicle) is becoming the norm for delivery of long term incentive compensation.
c. Total Shareholder Return is becoming a more popular performance metric.
d. Clawbacks are becoming more of a standard practice in executive compensation in light of upcoming Dodd-Frank regulations.
e. Use of stock options is becoming less common because of accounting issues and advisory firms' stance that they are not pay for performance.

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