Pearl Meyer

On Point

TIMELY, ACCURATE, INSIGHTFUL

Looking Ahead to Executive Pay Practices in 2022

Executive Summary

Table of Contents

Introduction

Pearl Meyer's "Looking Ahead to Executive Pay Practices" is an annual, online survey and valuable compensation planning tool. This year's survey was conducted in late August and September of 2021, with total participation of 255 companies, including 140 publicly traded, 76 private-for-profit, and 39 not-for-profit (NFP) organizations. As with prior surveys, responses are broken out separately by respondent role (board member vs. employee), ownership type, industry, and company revenue size.

This year's survey addresses key topics associated with the current environment, including compensation actions taken or contemplated in response to working from home, the ongoing COVID-19 pandemic, and current labor environment, as well as anticipated use of discretion for incentive awards. It also covers subjects such as compensation philosophy, compensation committee oversight, expected pay outcomes for Fiscal 2021, projected pay opportunities and mix for 2022, recent or anticipated incentive plan design changes, and long-term incentive award prevalence and participation.

While the use of environmental, social, and governance (ESG)-related metrics within executive incentive plans continues to receive a lot of attention, this topic was recently addressed in a separate Pearl Meyer study entitled "Tracking and Reporting on Diversity, Equity, and Inclusion."

Introduction (cont.)

This year's survey includes the following eight industry groups:

- Business/Other Services
- Consumer
- Energy/Utilities
- Financial/Insurance
- Healthcare/Life Sciences
- Industrials/Materials/Transportation
- Real Estate
- Technology

Certain industry categories in the online questionnaire were combined to allow for more meaningful sample sizes. Statistics are based on the number of responses for each question, and sample sizes vary. We believe this information will serve as a useful tool as your organization prepares for year-end pay determinations and Fiscal 2022 compensation planning.

Please feel free to contact me with any questions.

Bill Reilly
Managing Director
bill.reilly@pearlmeyer.com
770-261-4082

Key Highlights

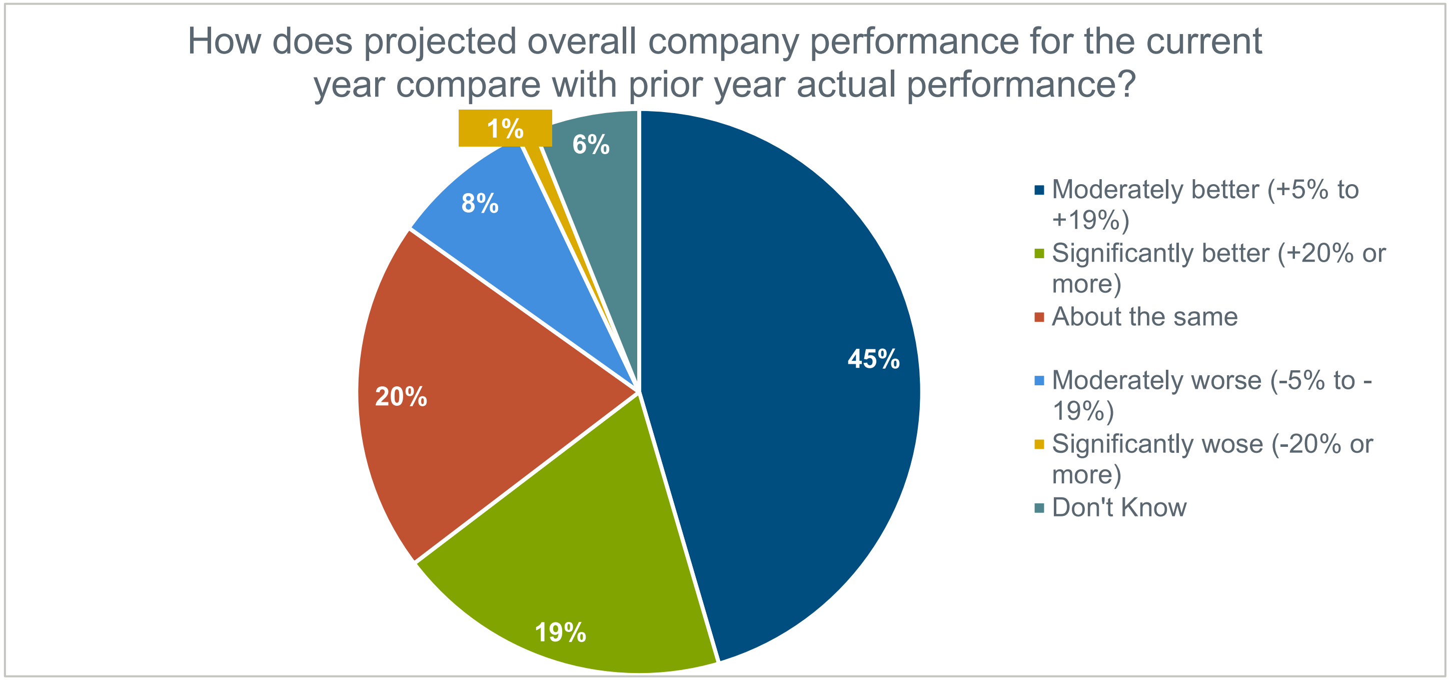
While the COVID-19 pandemic continues to significantly impact the way we live, work, and interact, approximately two-thirds of all respondents anticipate improved financial performance compared with the prior year, with most also expecting above-target payouts for incentive cycles ending in 2021. Nearly half of all respondents exercised discretion or modified performance goals or metrics for 2020 incentive awards (typically short-term) in response to the pandemic, while the large majority do not anticipate taking any action for incentive cycles ending in 2021.

Most respondents have not yet required employees to return to the office, with many maintaining flexible or “hybrid” working arrangements, and very few changing compensation practices to entice employees back to the office. Compensation committee responsibilities continue to increase, especially among public companies, where 17% of respondents report increased oversight responsibilities (often pertaining to diversity and inclusion or other ESG-related topics).

Base salary merit increase percentages are returning to, and in some cases exceeding, pre-pandemic levels, with the prevalence of salary freezes declining considerably on a year-over-year (YOY) basis. Nearly half of respondents are experiencing higher than normal turnover, especially at the broad-based level, with many making or considering off-cycle base salary adjustments. As a result, salary increase projections reported in the survey may ultimately wind up being somewhat conservative. More than half of respondents are also providing or considering sign-on bonuses, primarily at the broad-based level, to bolster recruiting efforts. These and other survey findings are addressed in more detail on the following pages.

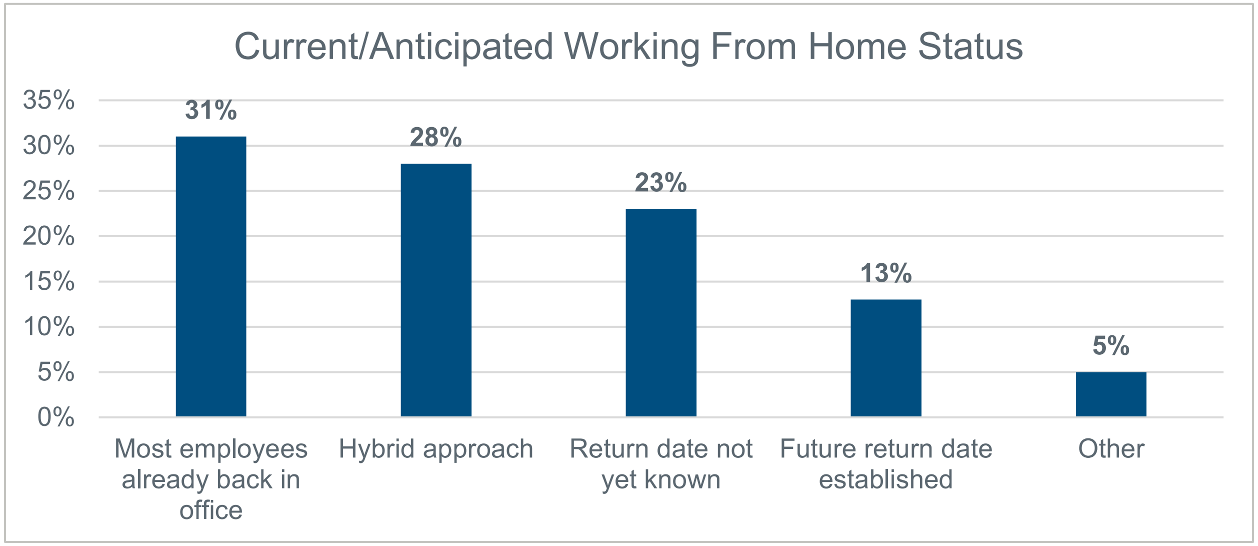
COVID-19 Financial Impact

- Most respondents anticipate YOY improvements in financial performance, with 45% projecting moderately better results (+5% to +19%) and 19% expecting significantly better outcomes (+20% or more); less than 10% expect YOY reductions.
  - Outside (or non-employee) directors were generally more optimistic than employee respondents (approximately 76% vs. 61% expect YOY improvements), as were public company respondents (72% vs. slightly more than half of private for profit and NFP organizations).
  - A majority of respondents in all industry sectors other than energy/utilities (39%) and business/other services (45%) expect YOY improvement in financial performance.



Working from Home

- Respondents are fairly evenly split in terms of status/approach to working from home.
- Nearly 25% of respondents have not yet established a return date, and among those in the "other" category, some originally set a date which was later deferred and others vary the approach by employee category.
  - Those that set a future return date typically are targeting the fourth quarter of 2021.
- The large majority of respondents have not taken (or expect to take) any compensation or benefits-related actions to entice employees back to work.
- Most respondents have not modified any existing or established new base salary geographic pay differentials to account for working from home, and virtually none have reduced salaries for a lower cost-of-living home office location.



Compensation Committee Oversight Roles

- The role of compensation committees continues to expand, with most responsible for executive succession planning across all ownership types and for non-employee director compensation at for-profit organizations.
  - Approximately 12% of all respondents and 17% of public companies increased compensation committee oversight responsibilities within the past year, typically pertaining to diversity and inclusion (D&I) or other ESG-related topics.

Oversight Category	Compensation Committee Oversight Prevalence		
	Publicly Traded	Private (For-Profit)	Private (NFP)
Board of Director Pay	80%	55%	45%
Executive Succession Planning	69%	78%	70%
Leadership/Talent Development	47%	26%	33%
Diversity & Inclusion (D&I)	49%	24%	24%
Culture	26%	17%	12%
Employee Engagement	23%	19%	9%

- More than half (~ 55%) of public company respondents review executive compensation for all CEO direct reports or corporate officers, as compared with 44% of private for-profit and 20% of NFP organizations.

Targeted Executive Pay Positioning

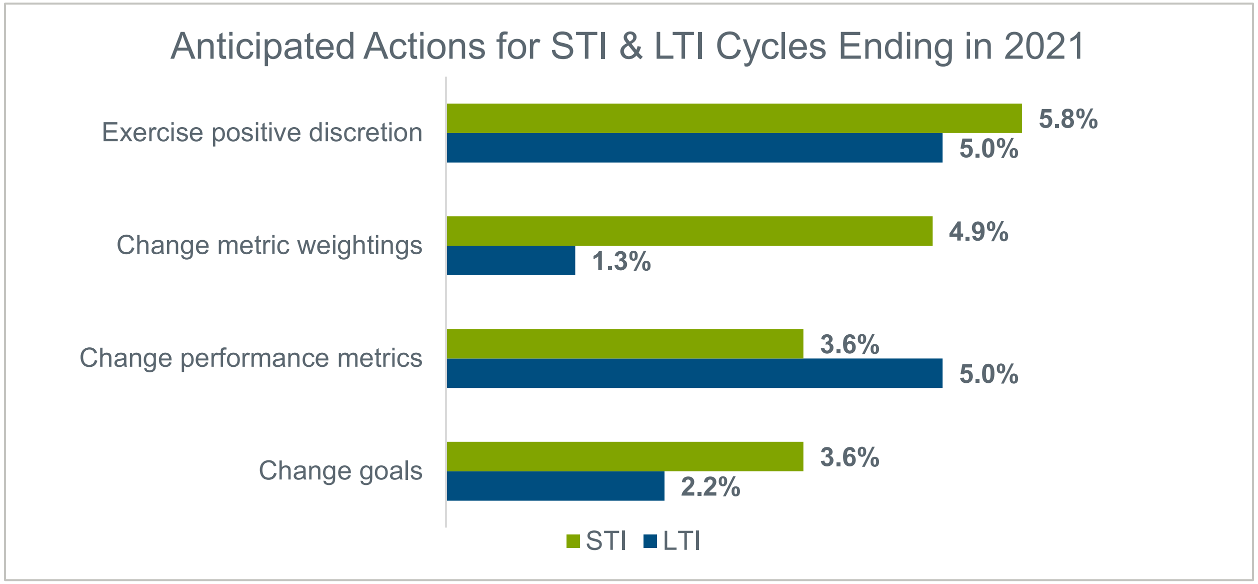
- Approximately half of all respondents target executive compensation at the market 50th percentile, with prevalence higher for base salary than variable pay (STI and LTI).
  - Public company respondents are much more likely to target executive pay at the 50th percentile (or median) compared with private organizations, reflecting the impact of greater external scrutiny.
  - Respondents in the largest size category (revenues at or above $10 billion) had the highest prevalence of above-median positioning for target total direct compensation (46%), while those in the smallest size category (revenues less than $100 million) had the lowest prevalence (23%).

Pay Component	Targeted Pay Positioning (% of All Respondents)		
	Below 50th Percentile	At 50th Percentile	Above 50th Percentile
Base Salary	11%	59%	24%
Short-Term Incentives (STI)	8%	51%	26%
Long-Term Incentives (LTI)	7%	44%	28%
Total Direct Compensation	8%	48%	34%

- Approximately two-thirds of all respondents have not changed (or plan to change) targeted executive pay positioning, with 14% increasing pay positioning vs. market and 12% increasing the emphasis on variable pay (STI and/or LTI).
  - By industry, prevalence of increased targeted pay positioning was highest for the technology sector (32% of respondents) and lowest for energy/utilities (5%).

Changes to Outstanding Incentives & Use of Discretion

- Most respondents have not made or plan to make changes to outstanding incentive award cycles ending in 2021, especially among publicly-traded companies.
  - Slightly more than half of respondents took some type of action for incentive cycles ending in 2021, typically via use of positive discretion in response to COVID-19 and primarily for STI rather than LTI awards.
- The most commonly cited actions taken or considered for incentive cycles ending in 2021 include:



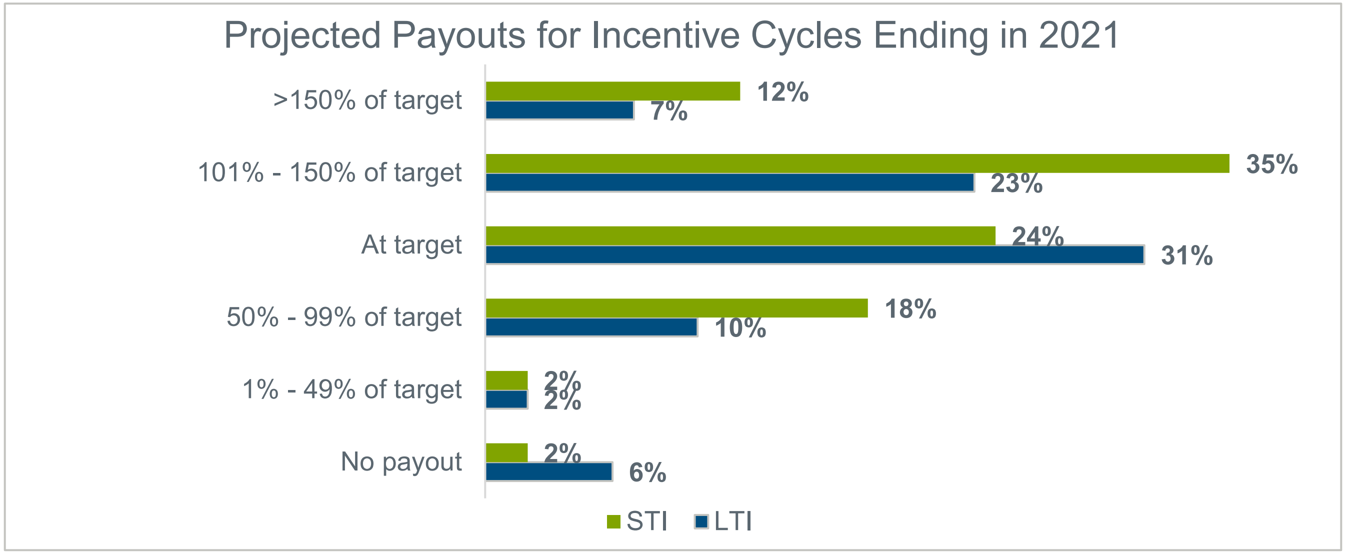
- Publicly-traded companies are far less likely (only 20% to 30% of respondents, varying by employee category and award type) to consider use of any discretion for incentive cycles ending in 2021 as compared with private for-profit organizations (40% to 60% of respondents).
  - When applied, most respondents expect similar levels of discretion vs. the prior year.

Pay Projections

- Salary increase projections for 2022 are returning to, and in some cases exceeding, pre-pandemic-levels, with median values equal to 3.0% across all employee categories with slightly higher averages.
  - Nearly 90% of all respondents expect increases for senior executives and 99% for other employees.
  - Average projections are lower for publicly-traded respondents than for privately-held organizations.

Employee Category	Average %	Median %
CEO	3.6%	**3.0%**
CEO Direct Reports	3.5%	**3.0%**
Other Employees	3.4%	**3.0%**

- Most respondents with incentive cycles ending in 2021 expect payouts to be at or above target, with only 2% forecasting no payouts for STI and 6% for LTI.



  - By industry, projections are most favorable for the industrials/materials/transportation sector (66% expect above-target for STI and 50% for LTI) and least favorable for energy/utilities (55% below target for STI and 50% for LTI).

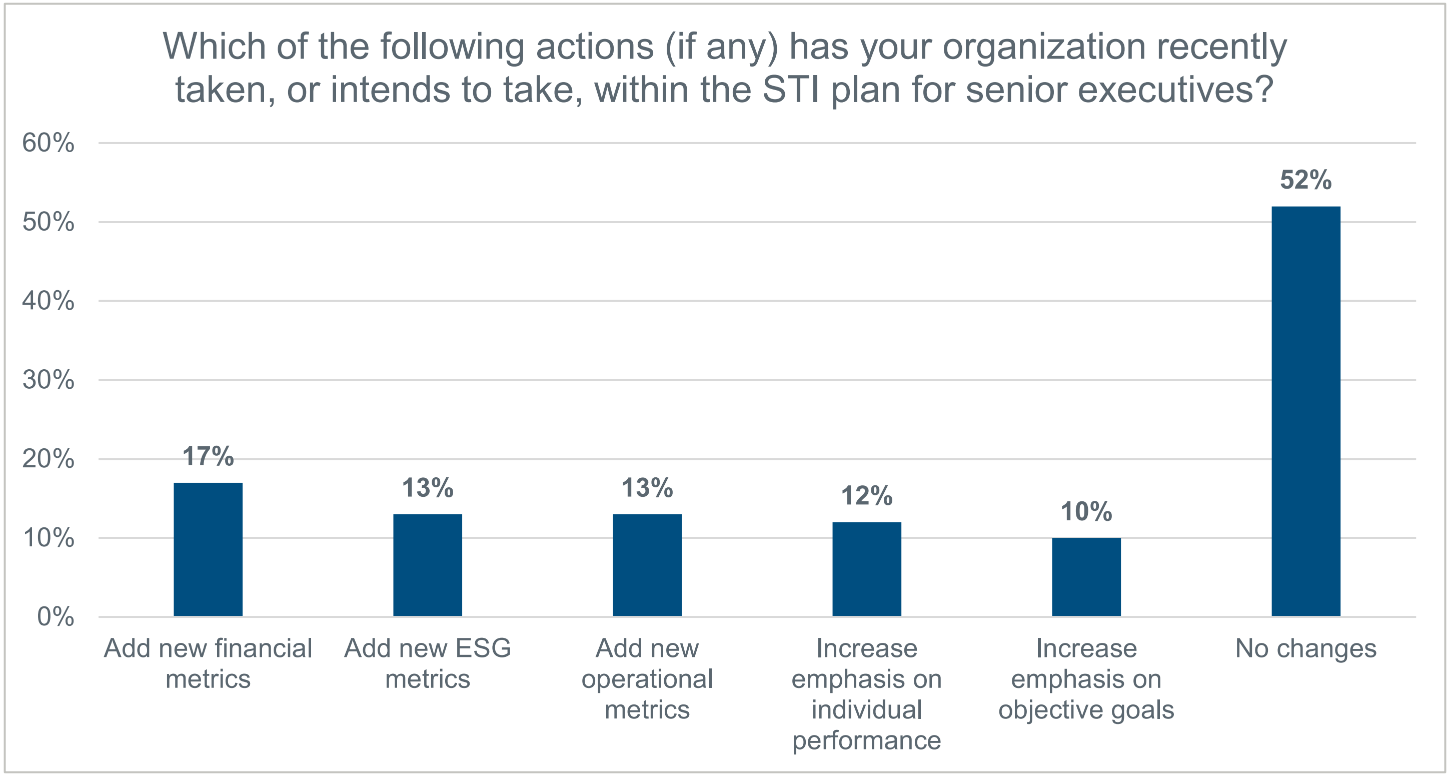
STI Performance Mix Projections for 2022

- Most respondents (79% of full sample and 90% of public companies) have formulaic STI plan designs, with pre-defined weightings for metrics and award opportunities.
- The anticipated performance mix for 2022 is very similar to 2021, with a primary emphasis on objective corporate/business unit financial goals; approximately one-third of respondents plan to also use operational, strategic, and/or individual goals, with average weightings ranging from 22% to 38% when used.
  - Nearly three-fourths of respondents use multiple performance metric categories.
  - When provided, average weightings for non-financial metrics increased vs. last year's survey, suggesting that respondents are looking to incorporate more award funding flexibility within STI plans, reducing the need for additional discretion outside of normal plan parameters.

Performance Metric Category	2022 STI Performance Mix: CEO		2022 STI Performance Mix: Direct Reports	
	Prevalence	Average Weighting (when provided)	Prevalence	Average Weighting (when provided)
Financial	94%	75%	96%	69%
Operational	28%	38%	36%	37%
Strategic	30%	23%	28%	22%
Individual	24%	34%	35%	33%
Discretionary	11%	34%	11%	24%

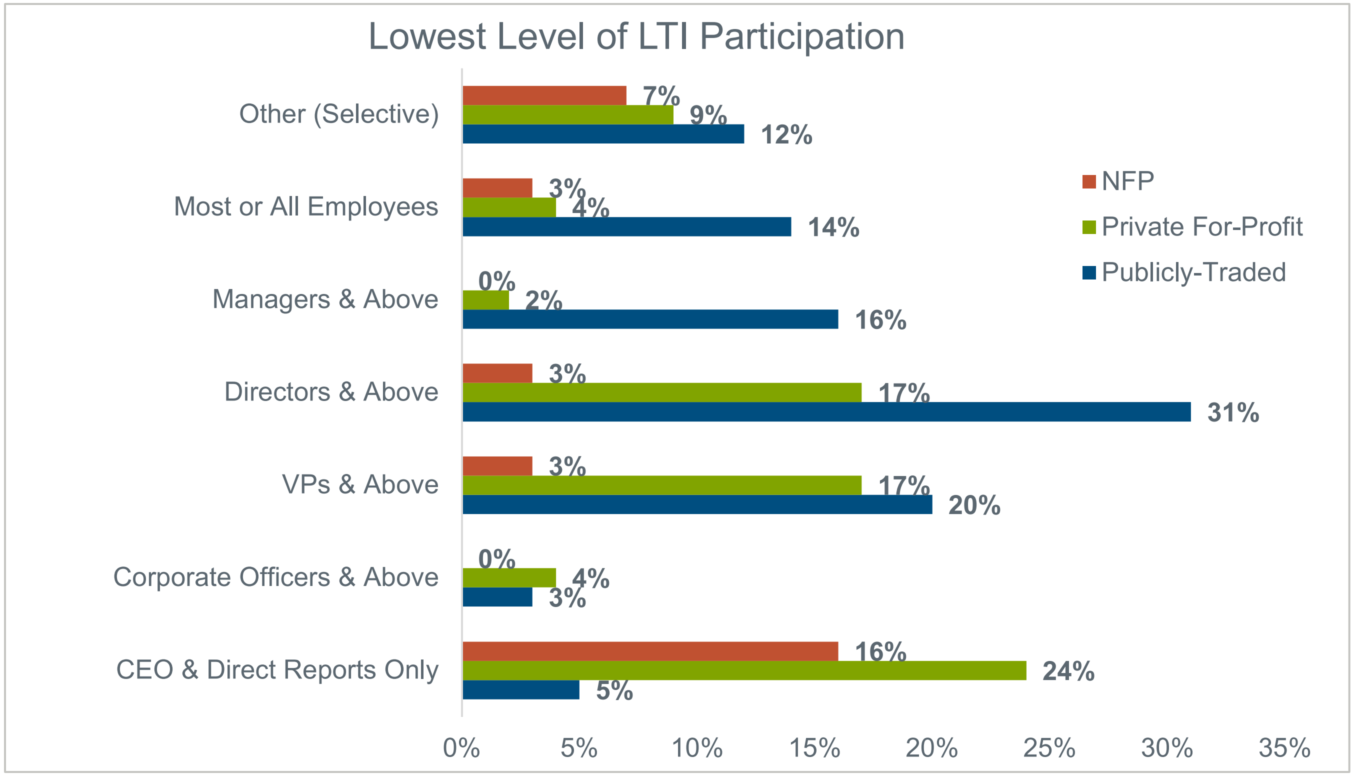
STI Plan Design Changes for 2022

- Nearly half of all respondents recently made or are considering making changes to STI designs for 2022, with the most common actions (expressed as a percentage of all responses, not just for those making changes) shown below.
  - 13% of all respondents, and 19% of public company respondents, plan to add new ESG metrics, with prevalence highest for the largest-sized companies (21% for those with revenues of $10B or more).
  - Prevalence of actual or anticipated changes was higher for publicly-traded respondents than for other ownership types, and highest by industry for the industrials/materials/transportation sector (62% of respondents) and lowest for the financial/insurance sector (35% of respondents).



LTI Prevalence and Participation Levels

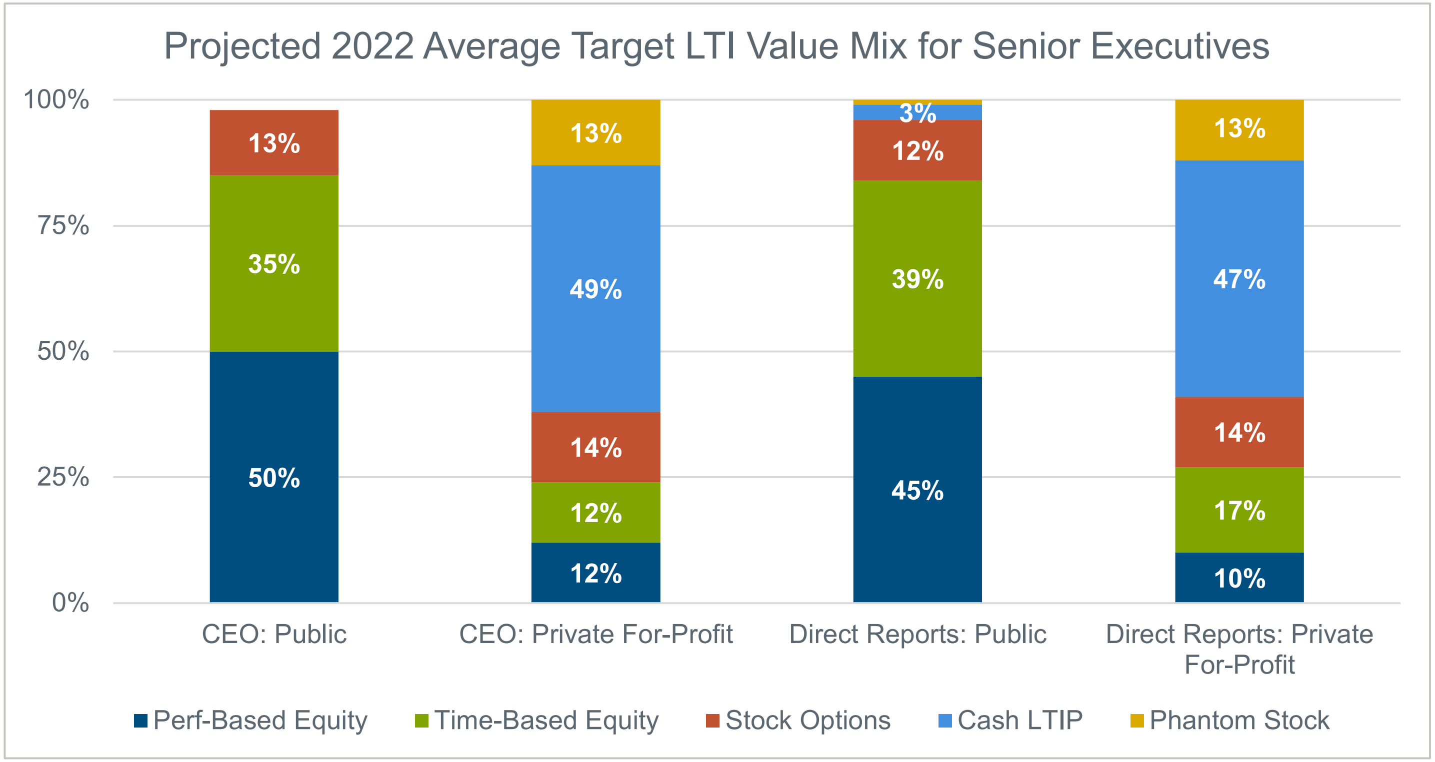
- All publicly-traded and 76% of private for-profit respondents grant LTI awards to senior executives; 42% of NFP respondents grant LTI (prevalence may be impacted by relatively low sample size).
- Most respondents do not grant LTI below the employee director level, with publicly-traded companies having broader participation than privately-held organizations.
  - Approximately 60% of public company respondents make at least some grants below the Vice President (VP) level vs. 23% of private for-profit and 6% of NFP organizations.
  - Approximately 20% of all respondents (and 30% of private for-profit companies) recently extended or plan to extend LTI participation due to employee attraction/retention concerns.



Note: "Other" refers to other non-specified categories (e.g., SVPs & above, senior managers & above, or some other combination of roles)

Target LTI Value Mix Projections for 2022

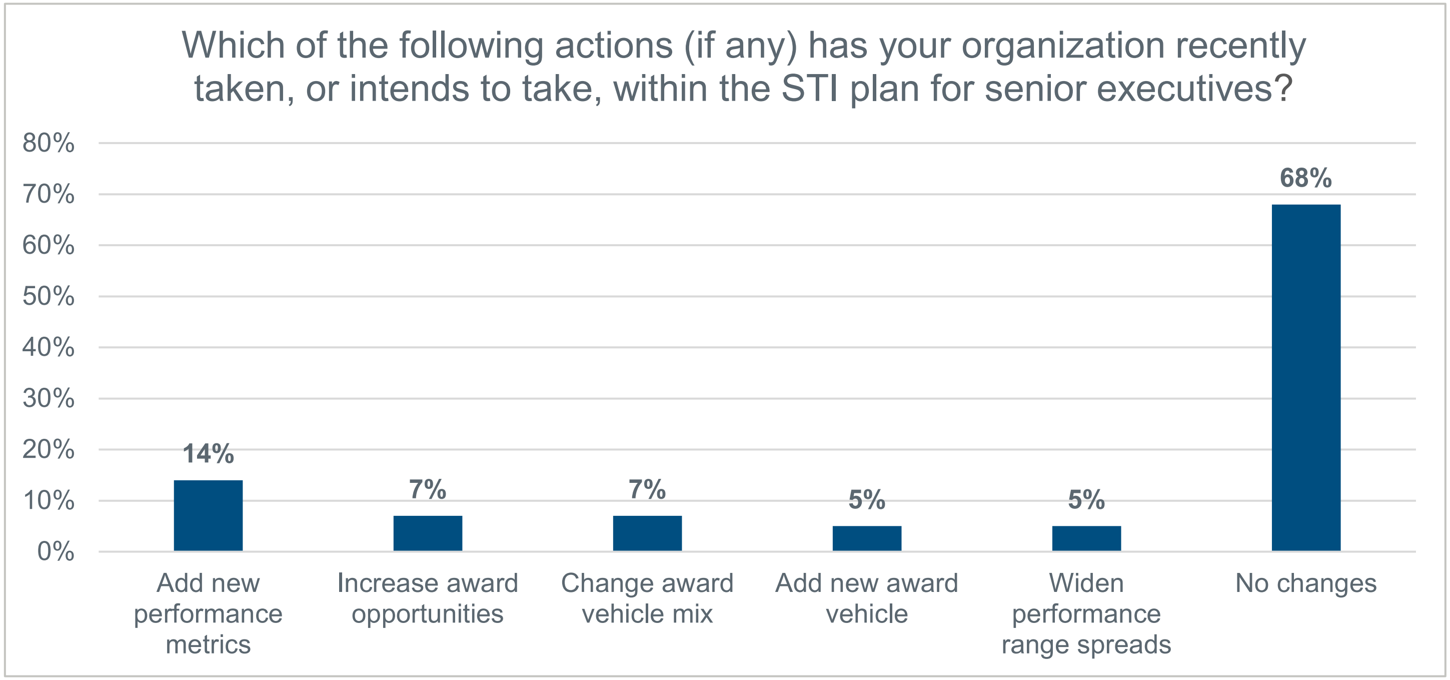
- Most publicly traded respondents grant time-based and performance-based equity to senior executives, while private companies rely more heavily on performance-based cash (cash LTIP); average overall target value mix projections for 2022 are shown below.
  - Most publicly traded (85%) and private for-profit (45%) respondents express LTI award opportunities as percentages of salary or fixed target values.
  - Use of performance-based equity for executives increases with company size (~ 20% for respondents with revenues < $300 million and 71% for those with revenues of $10 billion or more).
  - The average mix for NFP respondents (not shown below) is 100% cash LTIP.
  - For non-executives, public companies rely on time-based restricted stock (88% prevalence, 68% average weighting).



Note: Average overall target mix includes 0% values for award vehicle types that are not provided. Performance-based equity represents half of average overall target value for public companies, with private for-profit companies providing nearly half in cash LTIP

LTI Plan Design Changes for 2022

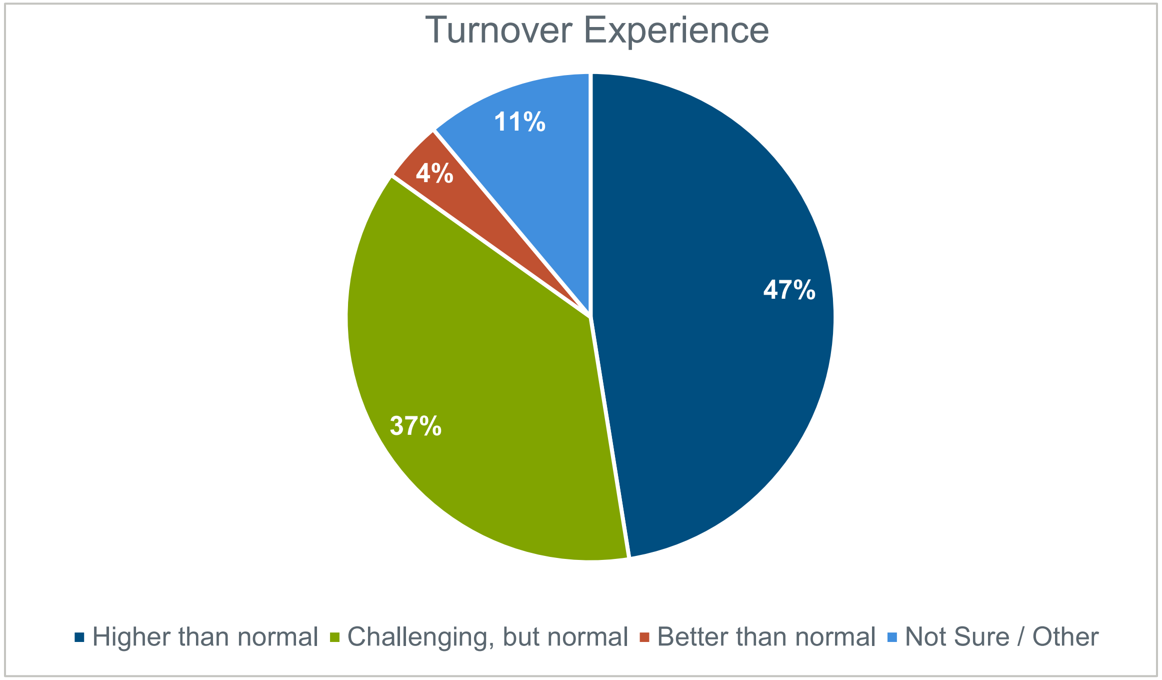
- Approximately one-third of respondents with LTI plans recently made or are considering making design changes for 2022, with the most common actions (expressed as a percentage of all responses other than "N/A", not just for those making changes) shown below.
  - While not a majority practice, smaller companies (revenues < $300 million) were relatively more likely to increase LTI award opportunities, while larger-sized companies (revenues of $1 billion or more) were generally more likely to add new performance metrics.
  - Prevalence of actual or anticipated changes was highest for respondents in the industrials/materials/transportation and consumer sectors (approximately half of respondents).



- Most respondents do not anticipate any change in LTI grant practices for 2022.

Current Labor Market: Turnover Experience

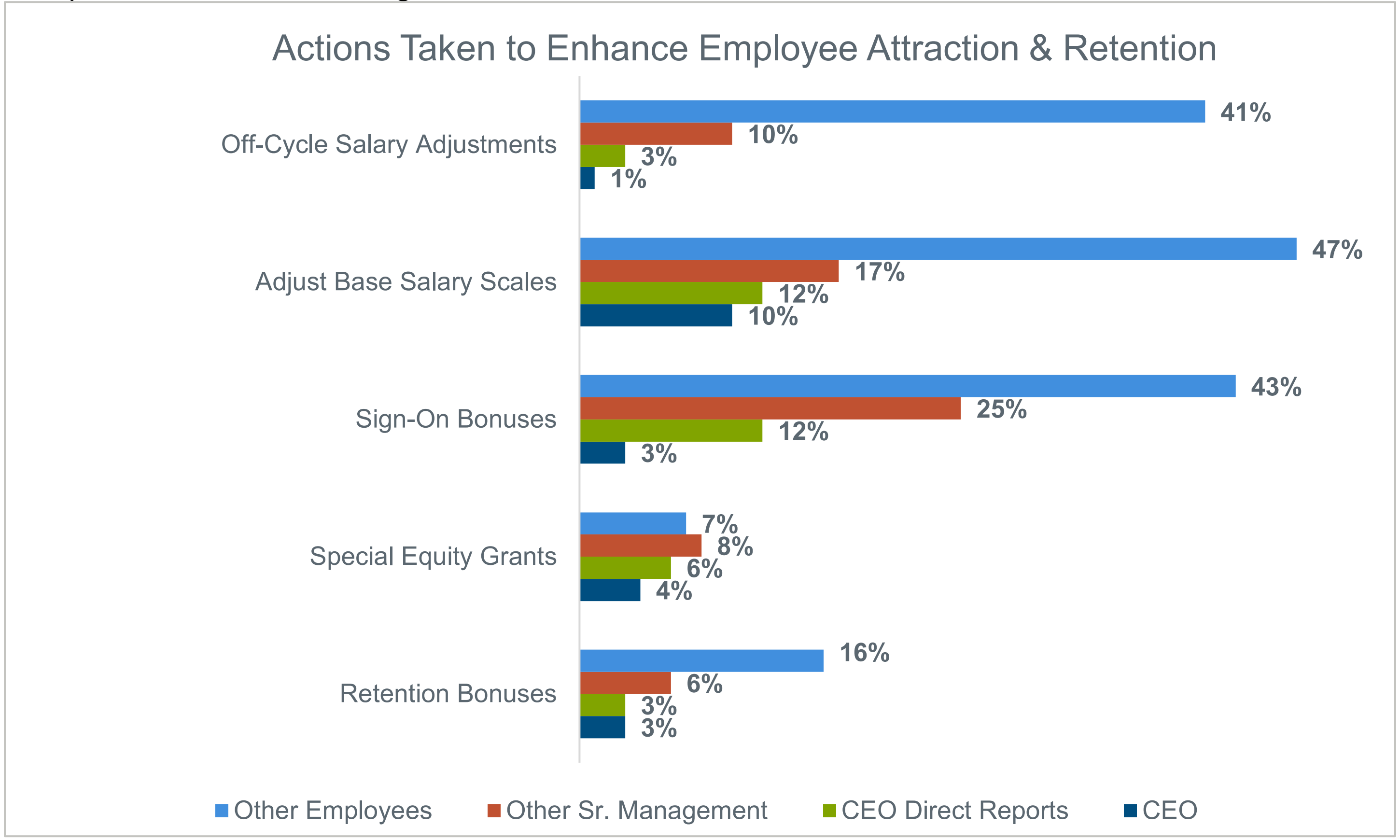
- Nearly half of all respondents are experiencing higher than normal turnover, especially at the broad-based level.
  - Only 5% cite higher than normal turnover at the senior management level (and 1% at the c-suite level).
  - Higher than normal broad-based employee turnover was reported by a majority of respondents within the healthcare/life sciences (67%), technology (56%), and financial/insurance (55%) sectors, with the lowest prevalence reported within the business/other services sector (27% of respondents).



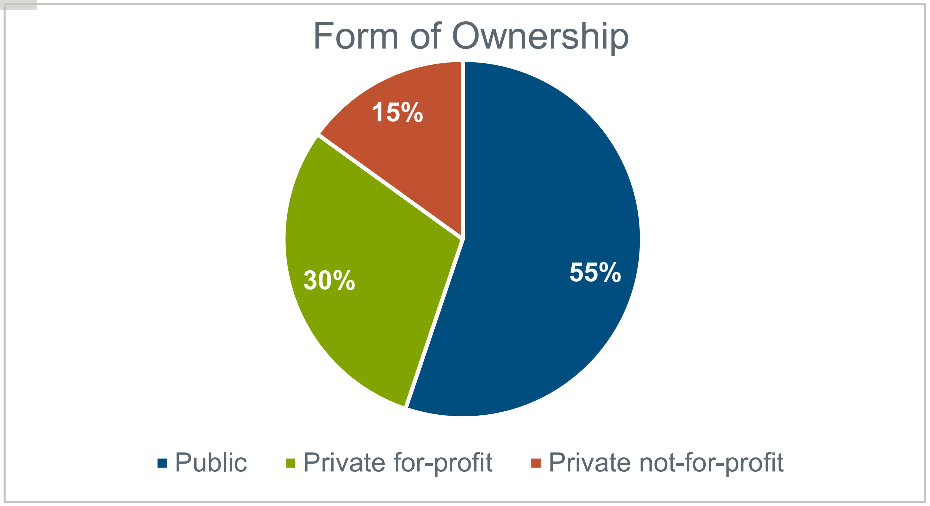
- Most respondents are receiving direct requests to enhance base salaries (56%) and provide more flexible working arrangements (53%) at the broad-based level, with lower prevalence for senior executives (12% to 15%) and other senior management (27% of respondents).

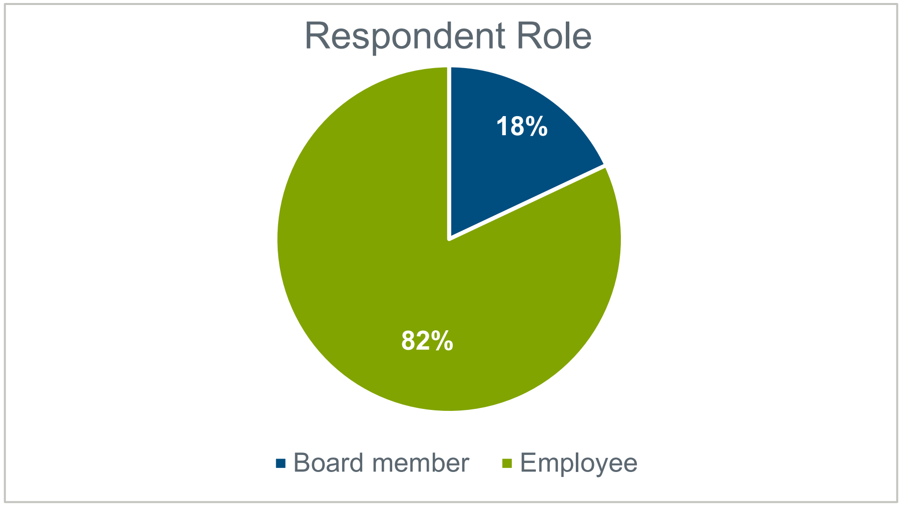
Current Labor Market: Actions to Enhance Attraction & Retention

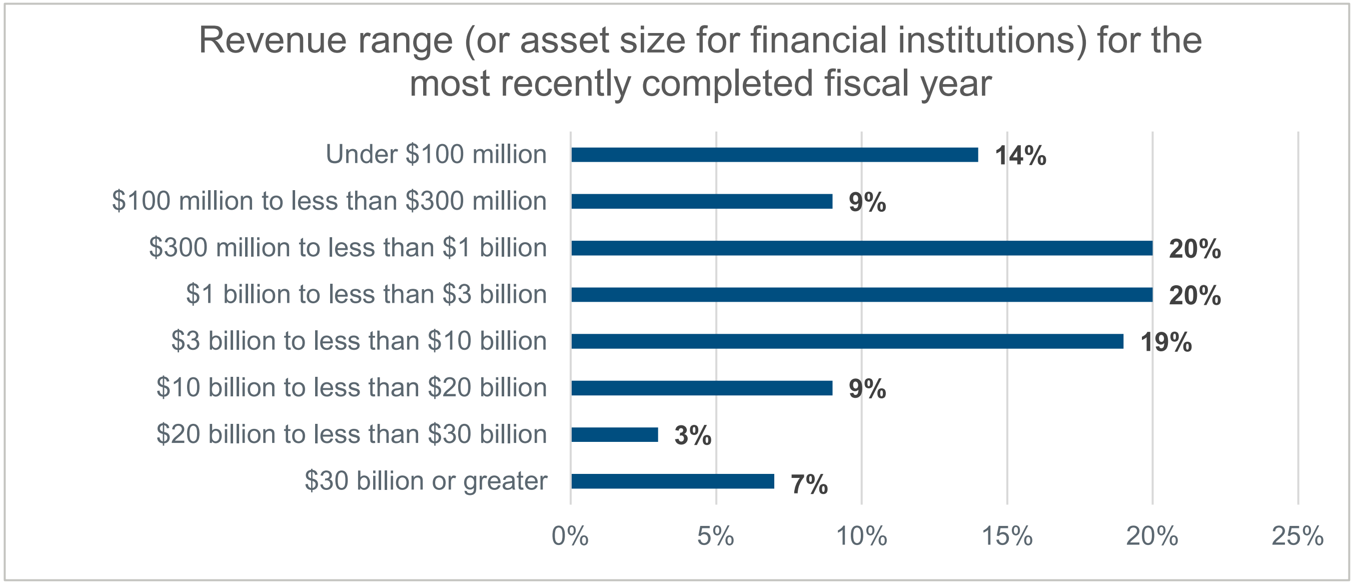
- Many respondents are providing sign-on bonuses to new hires and are more likely to provide off-cycle base salary adjustments rather than retention bonuses or special equity grants to existing staff, primarily at the broad-based employee level.
  - By industry, cash retention bonus prevalence was highest in the technology sector (39% of respondents) and lowest for business/other services (0%).
  - Another 17% of all respondents are considering adjustments to broad-based employee base salary scales for anticipated inflation and the tight labor market.



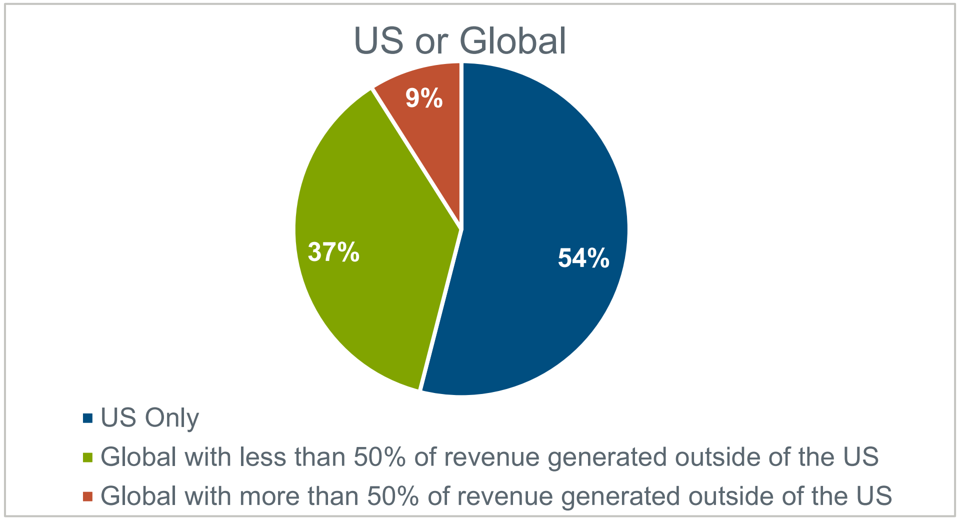
Demographics

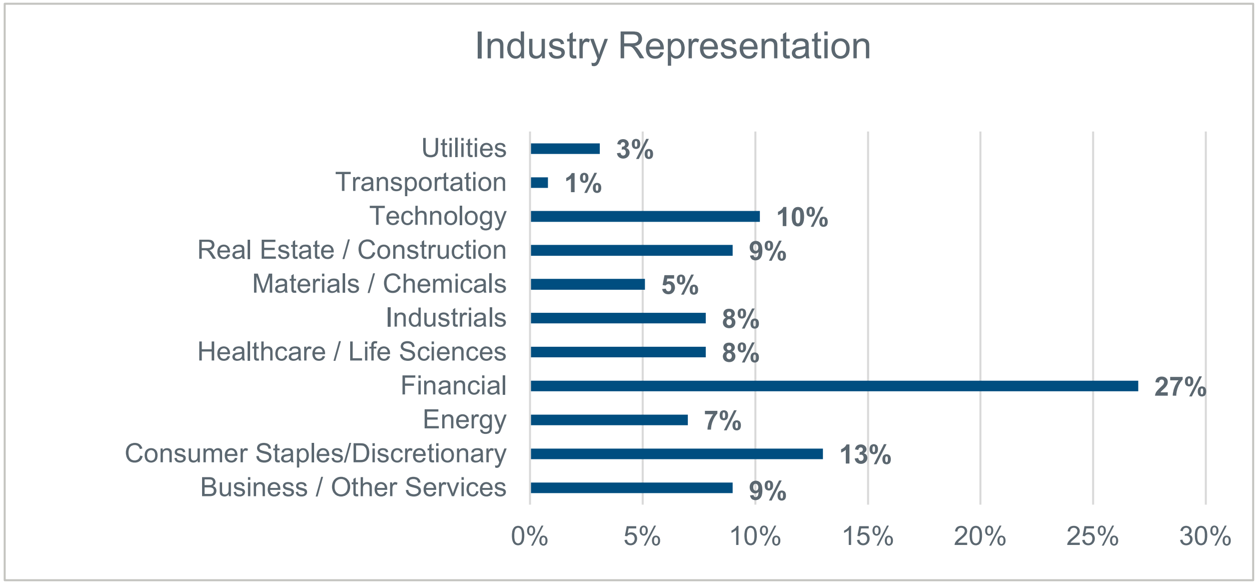






Demographics





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, Rochester, and San Jose.

Pearl Meyer

ATLANTA
(770) 261-4080
atlanta@pearlmeyer.com

BOSTON
(508) 460-9600
boston@pearlmeyer.com

CHARLOTTE
(704) 844-6626
charlotte@pearlmeyer.com

CHICAGO
(312) 242-3050
chicago@pearlmeyer.com

HOUSTON
(713) 568-2200
houston@pearlmeyer.com

LONDON
+44 (0)20 3384 6711
london@pearlmeyer.com

LOS ANGELES
(213) 438-6500
losangeles@pearlmeyer.com

NEW YORK
(212) 644-2300
newyork@pearlmeyer.com

ROCHESTER
(585) 713-1349
rochester@pearlmeyer.com

SAN JOSE
(669) 800-5074
sanjose@pearlmeyer.com

For more information on Pearl Meyer, visit us at www.pearlmeyer.com or contact us at (212) 644-2300.