

Pay vs. Performance: *The Questions You Need to Be Ready to Answer*

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Introducing Today's Speakers



Brooke Fernandez is the General Manager of Main Data Group (MDG), a provider of executive compensation benchmarking and corporate governance analytics. The MDG team continues to innovate upon a comprehensive proxy database and offers custom research services to top-tier companies and Executive Compensation firms worldwide. MDG's mission is to empower executive compensation professionals with meaningful, comprehensive total rewards and corporate governance information through the industry's most cost-effective and easy-to-use data platform. She holds a bachelor's degree from UCLA and a master's degree from the Stanford Graduate School of Business.



Adam Kahle is a principal at Pearl Meyer. He has more than 20 years of experience in both corporate compensation and consulting. His consulting experience covers a range of industries, including business services, consumer products, education, energy, financial services, healthcare, industrial manufacturing, life sciences, media and telecommunications, retail, transportation, and technology. He holds a B.A. from St. Olaf College and a M.A. in HRIR from the University of Minnesota.

In 2023, Adam lead Pearl Meyer's efforts in assisting a wide range of clients with PVP calculations and disclosures.



What is Pay-vs-Performance? Primer on the new disclosure rules



What are the trends? Common approaches and emerging trends in PvP disclosures



What questions should I be prepared for? FAQs from multiple constituents



How do I make sense of my company's PvP results? Analyses and insights vs. peers



Q&A



Who did you engage to help you develop the PvP calculations, analysis, and disclosure for your company?

SELECT ALL THAT APPLY:

- Law firm
- Valuation firm
- Compensation consulting firm
- Internal company employees / resources
- Other external partner
- Don't know / unsure

What is Pay vs. Performance?

Primer on the new SEC disclosure rules



What are the new Pay versus Performance (“PvP”) Disclosure Rules?

Context

- **More than a decade after** mandating the disclosure of pay versus performance (“PvP”) under **the Dodd-Frank Act**, the **SEC adopted** and released **the final PvP disclosure rules on August 25, 2022**
- **Companies must comply** with the new disclosure **rules in proxy statements for fiscal years ending after December 15, 2022** (generally, proxies filed in 2023)

What is Required to be Disclosed?

Companies must now include a new proxy table with 5 years of data (initially 3 years and then a 2-year phase-in to 5 years) disclosing executive “compensation actually paid” in relation to the company’s financial and Total Shareholder Return (TSR) performance

Compensation Disclosure

1. Summary Compensation Table (SCT) total compensation for CEO and average of Other NEOs
2. Compensation Actually Paid (CAP) to CEO and average of Other NEOs
 - Reflects SCT-disclosed compensation with adjustments for pension and equity values
 - Replaces SCT grant-date fair value of equity with equity compensation actually paid based on the fair value at end of fiscal year (similar to “realizable pay”)

Performance Disclosure

1. Total Shareholder Return (TSR) for the company and its peer group
2. Company Net Income
3. The most important financial metric used to determine compensation actually paid in the most recent fiscal year
4. New Tabular disclosure including 3-7 most important measures driving NEO compensation

Smaller Reporting Companies (“SRCs”) have reduced reporting requirements:

- *Only two years of data in initial year (with up to 3 years in subsequent years)*
- *Only company TSR and Net Income reported; peer TSR, CSM, and list of other measures not required*

Pay versus Performance Tabular Disclosure

- The new table includes the elements below with phase in starting at three years of data in 2023
- In addition to the table below, the company must also include a list of three to seven financial performance measures that it determines are its most important performance measures for linking executive compensation actually paid to company performance

Year	SCT Total for CEO	“Compensation Actually Paid” to CEO	Average SCT Total for Other NEOs	Average “Compensation Actually Paid” to Other NEOs	Value of \$100 Initial Fixed Investment Based on TSR	Value of \$100 Initial Fixed Investment Based on Peer Group TSR	Net Income	Company Selected Measure
Year 1								
Year 2								
Year 3								
[Year 4]								
[Year 5]								

Highlights

- Peer Group is either CD&A benchmarking peers or 10-K performance graph industry index
- CAP Takes SCT totals and adjusts so that equity includes fair value of awards in progress or that vest during the year, and pension includes only amounts attributable to service cost for the year
- Details required either in text or graphical format to explain relationships between CAP vs. Net Income, TSR and Company Selected Measure, as well as company TSR vs. peer group TSR



What is included in “Compensation Actually Paid”?

CAP starts with SCT table total compensation and makes the following adjustments:

Category	Adjustment Type	Details
Pension	- Pension Benefits	Change in the actuarial present value of DB and pension plans from the SCT
	+ Service Cost	Service cost and prior service cost
Deferred Compensation	+ Deferred Compensation	Deferred comp above-market earnings that are not tax-qualified
Equity Compensation	- Grant Date Fair Value	Grant date fair values for all equity awards from SCT
	+ Change in Vested Value	Fair value of equity awards on vest date minus fair value of equity awards as of the prior FYE (full amount is included for new grants during FY)
	+ Change in Value of Outstanding and Unvested	Fair value of equity awards as of the end of the FY minus fair value of equity awards as of the prior FYE (full amount is included for new grants during FY)
	- Forfeitures	Fair value at prior FYE for awards forfeited/cancelled
	+ Dividends	Dividends or dividend equivalents not otherwise included in total compensation

Key takeaway:

- “Compensation Actually Paid” isn’t “Compensation Actually Paid” – because it contains a blend of realized and unrealized compensation values!



Examples of PvP Footnote Reconciliation: Horizontal or Vertical

VERTICAL

	2022		2021		2020	
	PEO	Average for Other NEOs	PEO	Average for Other NEOs	PEO	Average for Other NEOs
Summary Compensation Table	\$ 19,363,648	\$ 5,822,260	\$ 18,155,739	\$ 8,256,157	\$ 12,855,275	\$ 5,286,409
Adjustments						
Deduction for amounts reported under the "Stock Awards" and "Option Awards" columns of the Summary Compensation Table ^(a)	(14,389,009)	(4,285,485)	(15,000,000)	(6,600,000)	(9,000,000)	(4,220,000)
Increase/(decrease) for the Inclusion of Rule 402(v) Equity Values ^(a)	(311,194,269)	(10,504,254)	789,889,155	65,378,871	466,112,330	53,919,185
Year-End Fair Value of Equity Awards Granted During Year That Remained Unvested as of Last Day of Year	18,930,378	5,957,933	25,410,484	7,893,516	53,681,961	14,619,557
Change in Fair Value from Last Day of Prior Year to Last Day of Year of Unvested Equity Awards	(216,035,770)	(5,734,897)	577,920,879	29,752,324	347,020,376	30,590,579
Change in Fair Value of Prior Years' Equity Awards that Vested During the Year	(114,088,877)	(10,254,023)	186,557,792	27,733,031	65,409,993	10,481,461
Change in Value of Prior Years' Equity Awards that Forfeited During the Year	—	(473,267)	—	—	—	(1,772,412)
Compensation Actually Paid	(306,219,630)	(8,967,479)	793,044,894	67,035,028	469,967,605	54,985,594

(a) Compensation Actually Paid excludes the Stock Awards and Option Awards columns from the relevant fiscal year's Summary Compensation Table total. The Rule 402(v) Equity Values instead reflect the aggregate of the following components, as applicable: (i) the fair value as of the end of the listed fiscal year of unvested equity awards granted in that year; (ii) the change in fair value during the listed fiscal year of equity awards granted in prior years that remained outstanding and unvested at the end of the listed fiscal year; and (iii) the change in fair value during the listed fiscal year through the vesting date of equity awards granted in prior years that vested during the listed fiscal year, less the fair value at the end of the prior year of awards granted prior to the listed fiscal year that failed to meet applicable vesting conditions during the listed fiscal year. Equity values are calculated in accordance with FASB ASC Topic 718.

Source: Moderna 2023 Proxy

Reconciliation of SCT total compensation to CAP for CEO

All amounts in U.S. dollars

(a)	(b)	(c)	(d)	(e)	(f)	(g)	(h)	(i)	(j)	(k) = (b)-(c)+ (d)-(e)+(f)+ (g)+(h)+ (i)-(j)
Fiscal Year	SCT Total for CEO	Minus SCT Change in Pension Value for CEO	Plus Pension Service Cost ⁽¹⁾	Minus SCT Equity for CEO	Plus EOY Fair Value of Equity Awards Granted During Fiscal Year that are Outstanding and Unvested at EOY ⁽²⁾	Plus Change from BOY to EOY in Fair Value of Awards Granted in Any Prior Fiscal Year that are Outstanding and Unvested at EOY ⁽³⁾	Plus Fair Value at Vesting Date of Awards Granted and Vested During the Fiscal Year ⁽⁴⁾	Plus Change in Fair Value from BOY to Vesting Date of Awards Granted in Any Prior Fiscal Year that Vested During the Fiscal Year ⁽⁵⁾	Minus Fair Value at BOY of Awards Granted in Prior Year that were Forfeited During the Fiscal Year ⁽⁶⁾	CEO CAP
2022	14,031,387	—	742,142	11,000,949	5,780,110	(5,795,900)	—	(3,604,307)	—	152,482
2021	18,200,584	2,978,538	756,691	10,501,098	11,644,213	756,097	—	560,744	—	18,438,692
2020	20,700,347	7,709,350	512,179	10,001,635	13,484,523	(559,922)	—	(721,377)	—	15,704,765

"EOY" = End of Year, "BOY" = Beginning of Year

HORIZONTAL

Source: 3M 2023 Proxy



What details must I footnote?

- List of Principal Executive Officers and Other NEOs
- Any materially new equity valuation assumptions
- Peer group composition (if using anything other than a published index)
- Changes to peer group composition in each year
- Detail reconciliations from SCT to CAP (typically provided in a supplemental table)
- If using a non-GAAP measure as a CSM, provide reconciliation from GAAP (either in footnote or via reference)



What are the biggest challenges with preparing a PVP?

Equity Valuation

- Detailed grant and vesting history data required for multiple years
- Complex vesting schedules (e.g., monthly vesting)
- Stock Option Black-Scholes valuations required for every tranche
- Dividends not otherwise included in grant date fair value
- Award modifications
- Forfeitures

Performance-Based Equity

- Monte Carlo valuations required for PSUs with market-based metrics
- Probable award outcomes in each fiscal year
- Unique performance measurement periods
- PSUs with milestone-based goals

Special Situations

- IPOs / de-SPACs
- Transactions (e.g., mergers, spin-offs)
- Multiple CEOs
- Changing NEOs
- NEO terminations / severance payments / equity acceleration
- Volatile stock price
- Pre-commercial companies not using financial goals in their incentive plans



How many hours would you estimate the PvP disclosure took your company and external resources to put together?

SELECT ONE

- <10 hours
- 10 hours < 20 hours
- 20 hours < 40 hours
- > 40 hours
- Don't know, don't want to know...

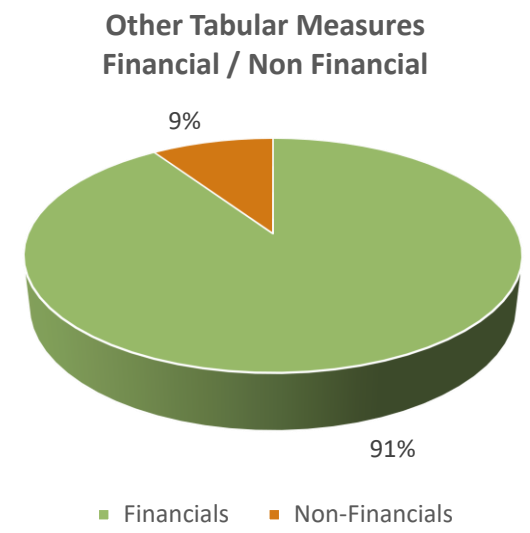
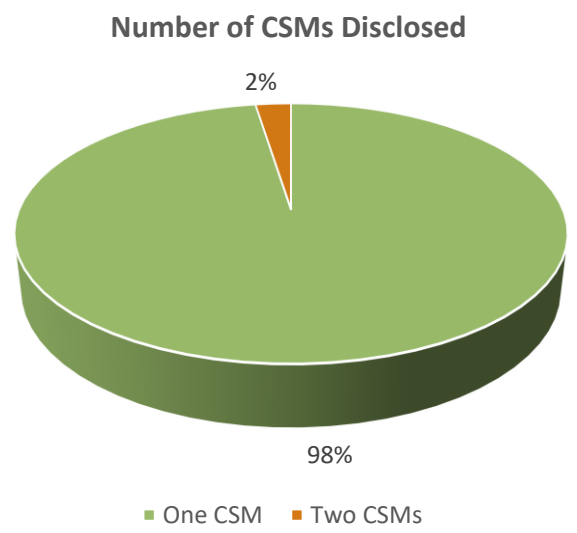
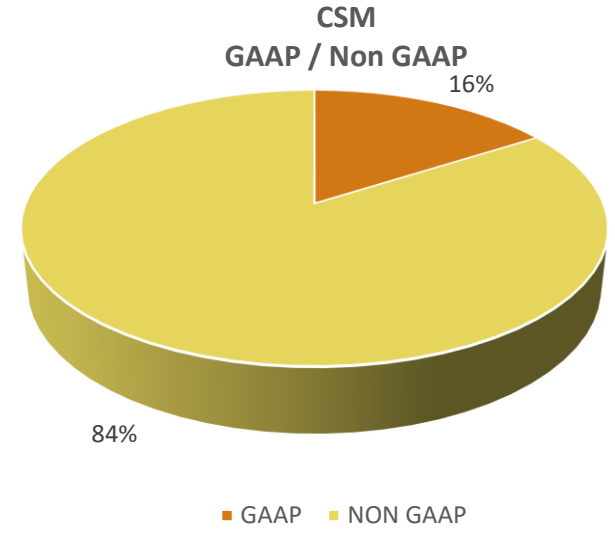
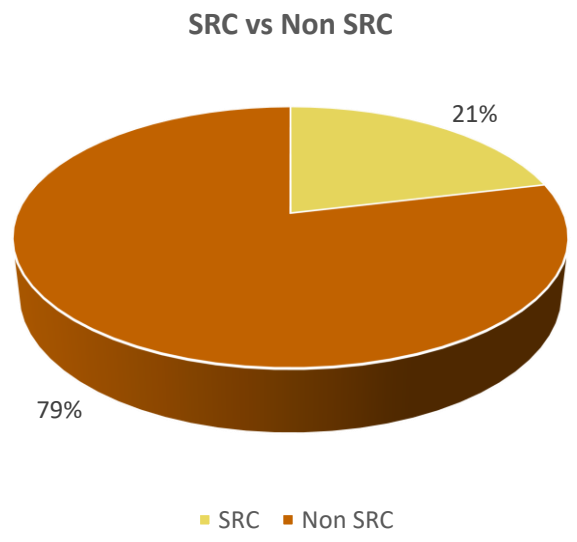
What are the Trends?

Best practices in PvP disclosures, data findings from MDG



What CSMs and Other Tabular Measures are Co's Using?

MDG compiled data on PVPs disclosed by 2,372 companies as of May 31st and has summarized the following practices:

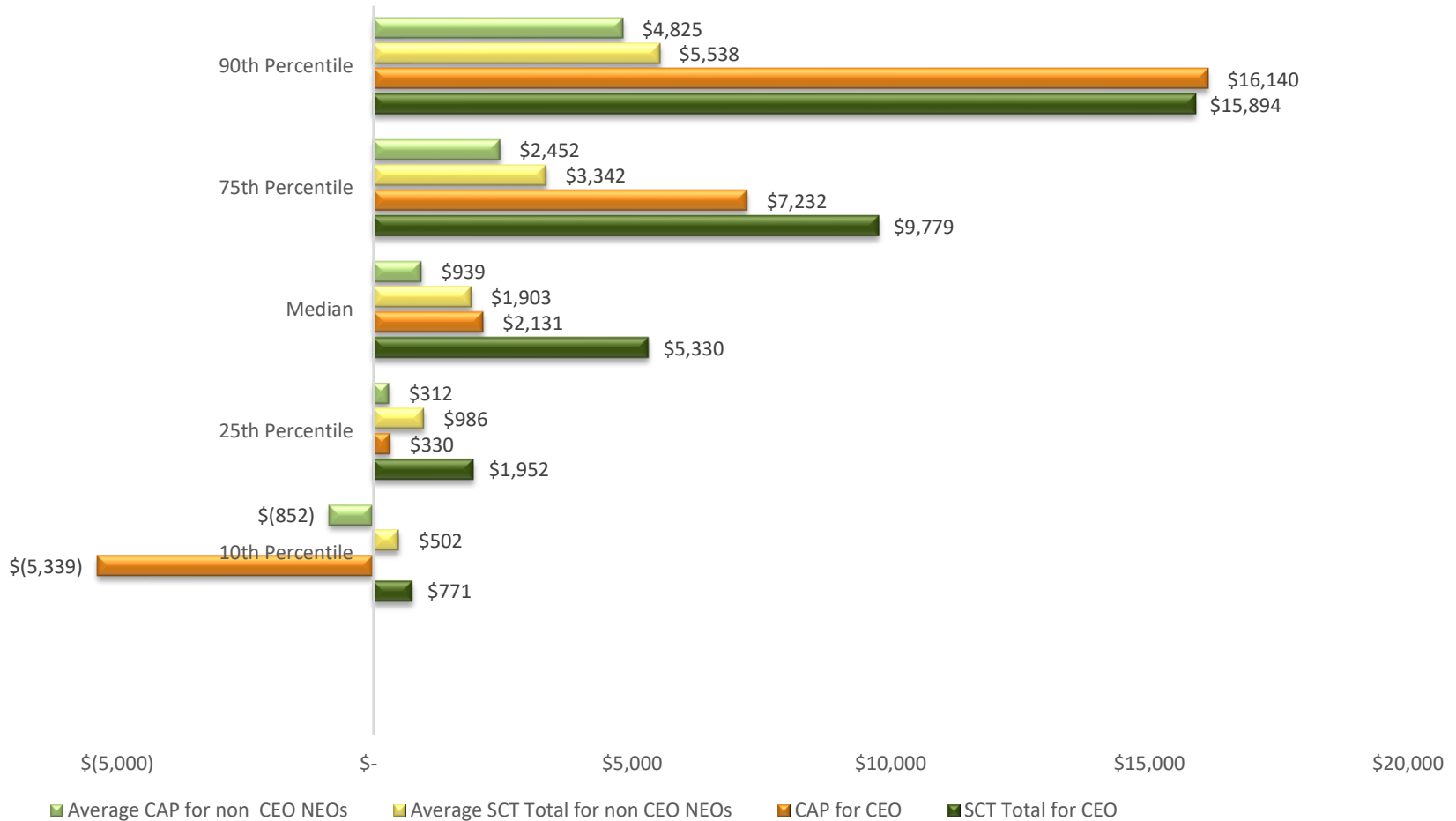




What Levels of SCT and CAP are we seeing?

There was a wide range in CAP, with some companies reporting negative CAP values

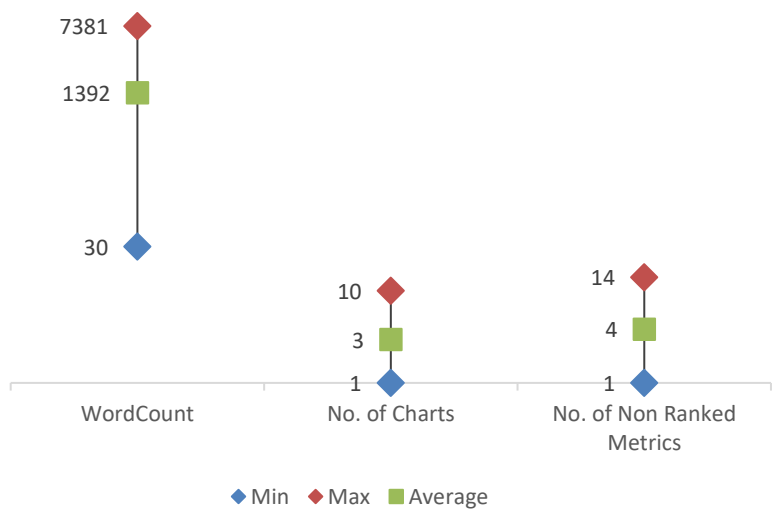
Percentiles of Executive Compensation



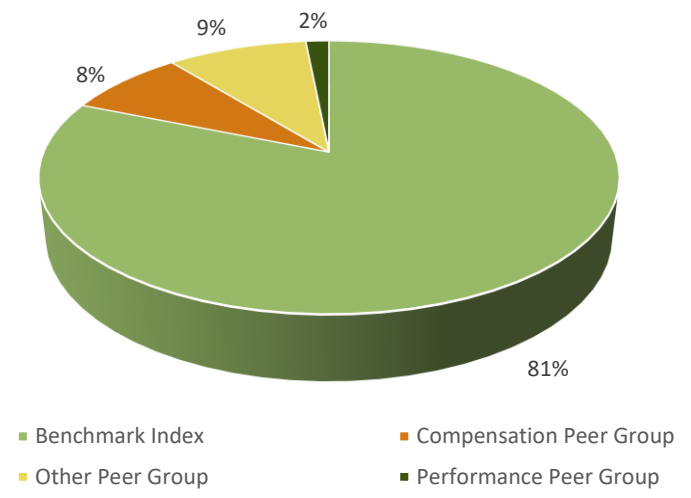


What did disclosures look like?

Word Count, Charts, Tabular Metrics



TSR Peer Group / Index





What are common Company Selected Measures?

Most Common CSMs among the S&P 500*

Category	CSM	Rank	Prevalence	Top CSM in Each Industry Sector
Revenue	Revenues / Sales	2	18.1%	Consumer Staples, Health Care, Info Tech
Profit	EPS	1	22.2%	Materials, Utilities
	EBITDA	3	10.6%	Industrials, Materials
	Op. Income / EBIT	4	10.3%	Communication Svcs., Consumer Discretionary
	Funds From Ops. Per Share	6	5.5%	Real Estate
	Net Income	9	3.3%	
	Pretax Income / EBT	10	2.5%	
	Operating / Profit Margin	11	2.3%	
	Gross Profit	15	0.3%	
	Op. Income Before Dep. & Am.	15	0.3%	
Cash Flow	Free Cash Flow	9	3.3%	
	Operating Cash Flow	12	1.8%	
Return / Ratios	Return on Equity	5	6.8%	Financials
	Return on Capital	10	2.5%	
	Return on Capital Employed	13	1.5%	Energy
	Return on Income	15	0.3%	
	Combined Ratio	14	0.5%	
TSR / SP	TSR / Stock Price	8	3.8%	
Other	Other Financial**	7	4.3%	

*Source: MDG database as of June 1, 2023 (represents 397 S&P 500 companies that filed as of this date).

**Reflects measures that were not categorizable as above and/or represented combinations of several categories of metrics.



What are some “Best Practices” for PVP disclosures?

- **Less is more** – view this simply as a compliance exercise
- Encapsulate adjustments into as **few tables** as possible
- **Clearly footnote** all assumptions
- Display the relationship between the following **graphically**:
 - CAP vs. Company Net Income
 - CAP vs. CSM
 - CAP vs. Company and Peer Group TSR
- **Minimize narrative on PVP alignment** – let the graphs speak for themselves
- CSM is typically the **most heavily weighted financial measure** in the annual incentive plan (most often Non-GAAP)
- **Industry index** as opposed to a compensation or performance peer group for TSR comparison
- To the extent your Compensation Committee uses **other tools/methodologies to evaluate pay-for-performance, clearly describe or illustrate the process in the CD&A**

What questions should I prepare for?

FAQs from multiple constituents



Did you receive any negative feedback / reactions to your PvP disclosure?

If so, from whom/from which groups did the feedback come?

SELECT ALL THAT APPLY:

- None (no negative feedback)
- Yes – investors
- Yes – media
- Yes – employees
- Yes – from other groups (put in chat)



What Questions from Investors/Media/EEs might I receive?

Although PvP has garnered less attention than initially anticipated, be prepared to answer the following questions:

- 1) Why is ABC Co. making this new Pay vs. Performance disclosure in the proxy statement?
- 2) What is included in “Compensation Actually Paid”?
- 3) What is the additional supplemental table under the main PvP table with the detailed reconciliation?
- 4) Did the CEO really receive \$20M in [Fiscal Year X]?
- 5) Why are the CAP numbers so high in [Fiscal Year X]?
- 6) Why are there negative CAP numbers?
- 7) Does the Compensation Committee consider the results of the SEC Pay vs. Performance disclosure in making its annual compensation determinations for the Named Executive Officers (“NEOs”)?
- 8) What other pay-for-performance related analyses does the Compensation Committee consider in making compensation decisions for the CEO and other NEOs?
- 9) Do the results indicate a positive correlation between ABC performance and executive pay?
- 10) How do the company’s PvP results compare to peers?

How do I make sense of my company's PvP results?

Analyses and insights vs. peers



Let's use a real example to illustrate how we'd approach these questions and get started:

- An NYSE-traded chemicals firm – American Vanguard Corp [NYSE: AVD]
- Market Cap <\$1B
- Revenue <\$500M

- >> First Question to start with is – How does my company compare to my peers?
- Where do I go to find this information – World @ Work has a solution for you to get you started...



SALARY DATA CENTER

Use of the Salary Data Center is available exclusively to WorldatWork members. Click below to instantly access data from over 4,500 public companies, 11 countries, 225 industry breakouts, and over 15,000 job titles.



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Sample Dashboard – what yours should look like

Pay vs Performance | Insights & Trends

Insights & Trends

PVP Data

Select Focal Company

Select Fiscal Year

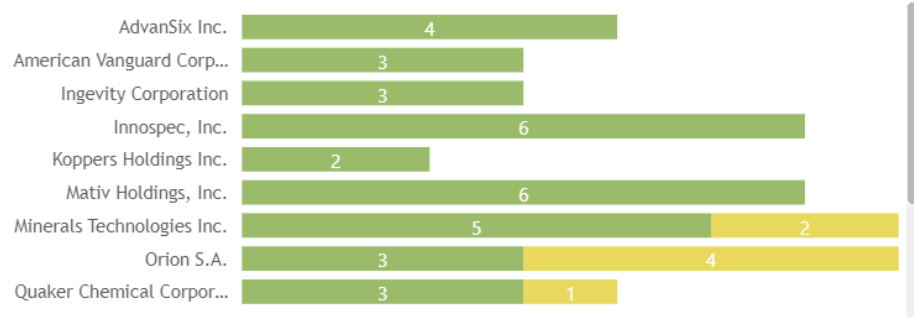
Select Field for Statistics

American Vanguard Corporation

2022

SCT Total for CEO

Non Ranked Measures Financial / Non Financial

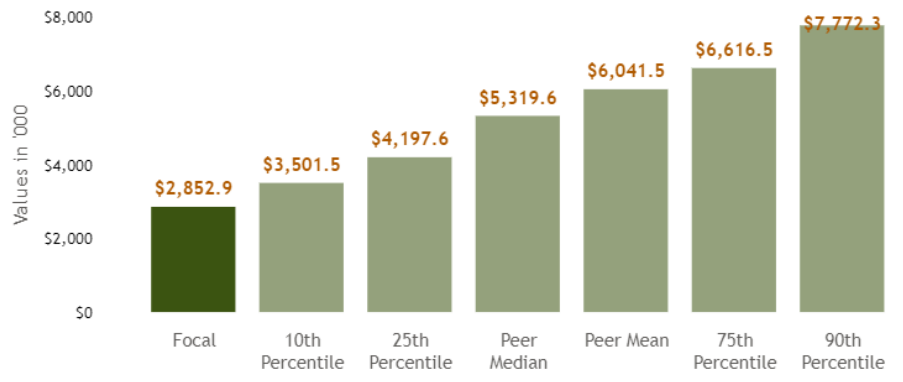


● No. of Financial Metrics ● No. of Non Financial Metrics

American Vanguard Corporation

\$2,852,874.0	\$3,432,747.0	\$729,905.0	\$817,432.0
SCT Total for CEO	CAP for CEO	Average SCT Total ...	Average CAP for non-...
\$27,404,000.0			
Net Income			

Peer Group Statistics of SCT Total for CEO

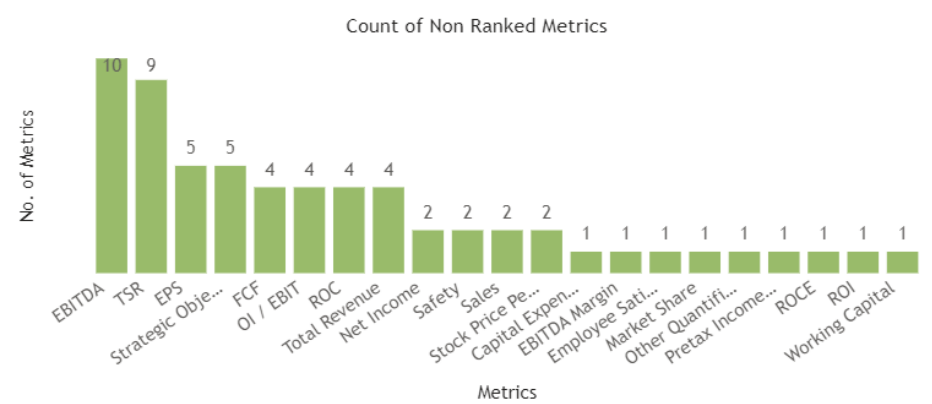
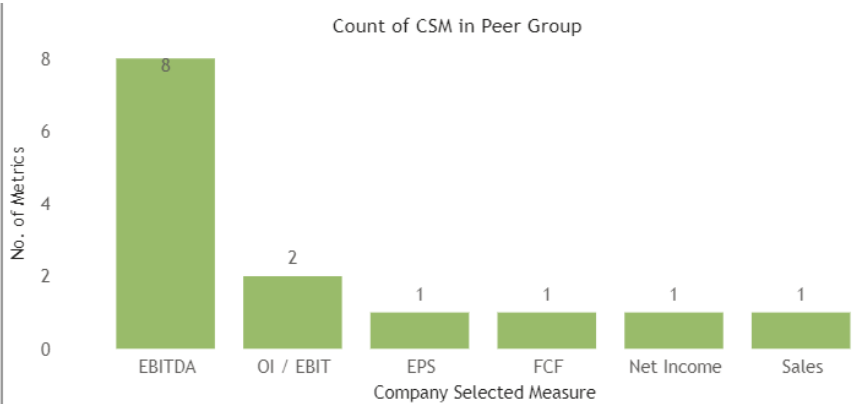


PvP Data Available for 16 out of 20 Companies

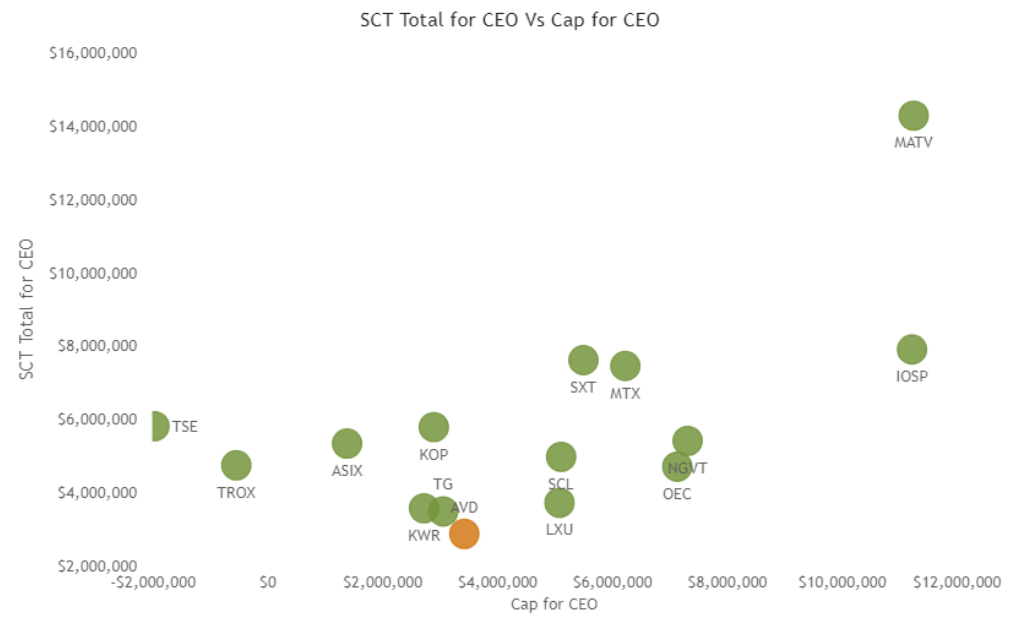
\$3,501,471.6	\$4,197,555.0	5,319,589.00	\$6,041,472.9
10th Percentile	25th Percentile	Peer Median	Peer Mean
\$6,616,529.5	\$7,772,253.0		
75th Percentile	90th Percentile		



Sample Dashboard – what yours should look like



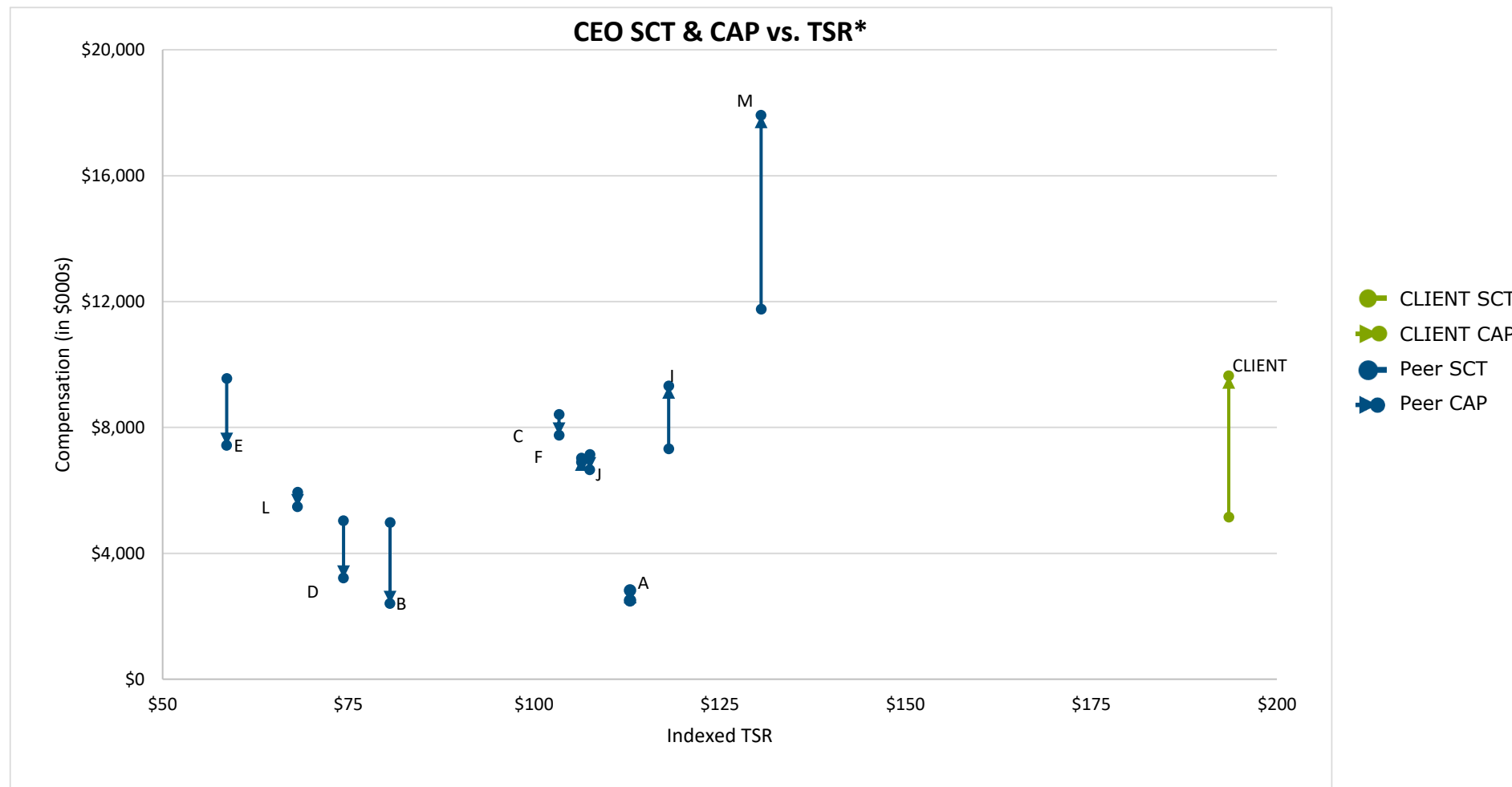
Governance & Disclosure Practice Prevalence	Focal	Peer Group
Is CSM 1 GAAP or NON-GAAP?		
No. of GAAP Metrics		1
No. of Non GAAP Metrics		10
Not Disclosed	✓	2
Is CSM 2 GAAP or NON-GAAP?		
No. of GAAP Metrics		
No. of Non GAAP Metrics		
Not Disclosed		
Supplementary Disclosure for CAP Inclusions & Exclusions		
No. of Companies (Disclosed)	✓	14
Not Disclosed		1
Comparator Groups used to Benchmark TSR Calculation		
Benchmark Index	✓	12
Compensation Peer Group		1
Not Disclosed		1
Other Peer Group		





How does my company's PVP compare to peers?

In this example, our client had the highest 3-year TSR vs. its peers, but its SCT and CAP was among the middle (median) of the peer group



* Analysis excludes peers with no available PVP disclosures and companies with less than 3 years of PVP data

Source: Main Data Group, AdvanSix, Inc. 2023 Proxy Statement



What other leading-edge PvP analyses are out there?

- CAP in excess of SCT compensation
- Relationship of CAP in Excess of SCT to TSR, relative to peer group TSR
- “Sharing Ratio” showing the CAP in excess of SCT relative to key financial metrics (e.g., market cap, revenues, net income, etc.)

Q&A



HOW TO CONTACT US



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