Update on Executive Compensation

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BENEFITS
Symposium

Chester Mosteller, CEBS
President
Mosteller & Associates
Reading, Pennsylvania

International Society
of Certified Employee Benefit Specialists

Executive Compensation Overview

- Economy
- Demographics
- Legislation/Regulatory

Change in Total Executive Compensation S&P 500—Top Five

2007	+1.3
2008	-6.8
2009	-10.3
2010	+28.2
2011	+6.2

Economic Impact

- Worldwide Economy
- Net Income
- Stock Price
- Shareholder Return
- Growth
- Shareholder Expectations

Demographics

- Baby Boomer Bubble
- Skill Sets of Next Generations
- Technology
- Multi-Cultural

Regulatory

- Historical
  - ERISA
  - IRC 162(m)
  - 280(G)
  - 409A
  - FAS123(R) (ASC Topic 718)
  - SEC Proxy Disclosures—CD&A

Regulatory—Continued

- Emergency Stabilization Act of 2008
  - Established “Troubled Asset Relief Program” (TARP)
  - 766 companies (mostly banks) received loans
  - Loans @ 5% interest/dividend (Great deal for Uncle Sam!!!)
  - Over 50% have now paid loans back—represents vast majority of money
  - Primarily small banks which haven’t paid back loans – difficult capital market

TARP—Executive Compensation Restrictions

- No variable compensation for up to top 25 highest paid
- No severance for top 5 plus next 5 highest paid
- No tax gross up for top 5 and next 20 highest paid
- Mandatory risk assessment of all employees variable pay plans

TARP Restrictions—Continued

- Mandatory Clawback
- Only variable allowed is restricted stock grants to maximum of ⅓ annual compensation
- IRC 162(m)(5) decreased to $500,000 from $1,000,000

TARP—Consequences

- Higher CEO turnover—one study showed 33% for TARP versus 10% for non-TARP
- Difficulty recruiting talent
- Base pay increasing for TARP at 12% (2010 over 2009) versus non-TARP at 2%
- General reduction in alignment of pay and company performance

Dodd Frank

- Passed in July 2010
- Impacts publicly held companies
- Continued reaction to economy and Wall Street
- Primary impact on executive compensation process and disclosure versus pure limits

Dodd Frank—Main Executive Compensation Provisions

- Risk assessment of pay plans
- Clawbacks
- Say on Pay voting, frequency of Say on Pay
- Consultant disclosure
- Board Compensation Committee Independence
- CEO/Employee pay ratio disclosure
- Say on Golden Parachute

Employers/Boards Reactions To-Date

- More emphasis on performance based compensation
- Establishing internal CEO/employee pay ratio
- Contracts
  - Cutting back on 280(G) gross-ups
  - Lower severance awards
  - Fewer executives have contracts
  - Multiple triggers in change in control contracts

Employers/Boards Restrictions—Continued

- Compensation Committees re-examining compensation strategy – particular mix of fixed versus performance based compensation

Case Study
Sample Summary Compensation Table

Company A

5 Year Average Total Shareholder Return (TSR) (-3.8%)

5 Year Average Return on Equity (ROE) 2.5%

	Year	Salary	Bonus	Stock Awards	Option Awards	Non-Equity Incentive	Non-Qual. Deferral	All Other	Total
CEO	2011	$690,000	0	-	$3,100,000	$1,700,000	$198,000	$49,000	$5,737,000
	2010	$690,000	0	-	$832,000	$430,000	$741,000	$56,000	$2,749,000
	2009	$670,000	0	-	$2,300,000	0	$187,000	$45,000	$3,202,000

Company B

5 Year Average Total Shareholder Return (TSR) 7.6%

5 Year Average Return on Equity (ROE) 10.1%

	Year	Salary	Bonus	Stock Awards	Option Awards	Non-Equity Incentive	Non-Qual. Deferral	All Other	Total
CEO	2011	$785,000	0	$285,000	$1,700,000	$535,000	$123,000	$62,000	$3,490,000
	2010	$700,000	0	$300,000	$1,400,000	$0	$106,000	$59,000	$2,565,000
	2009	$800,000	0	$236,000	$1,500,000	$419,000	$119,000	$51,000	$3,125,000

Case Study Review

- Congruity of Summary Compensation Table and CD&A
- Footnotes and other Charts/Exhibits
- Short versus Long Term Performance
- Pay for Performance
- Internal Equity among Executives

Ideas/Concepts for Implementation

- Show Board Compensation Committee scenarios for linkage between strategy, performance, fixed/variable, actual versus target
- Use 5 and 10-year look backs and forward projections
- Understand industry and competitive performance
- Understand what “drives” executives

Questions?

Thank you!