Pearl Meyer

WomenCorporateDirectors
A Foundation Inspiring Visionary Boards Worldwide

WCD Compensation & Human Capital Committee Peer Group

Virtual Peer Exchange

Avoiding Pandemic Payout Pandemonium: Compensation Tools & Techniques

December 3, 2020

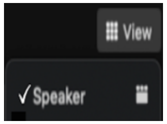
WCDirect
Virtual Programming

Peer Exchange Agenda

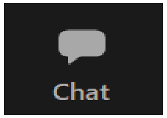
- **Welcome, Opening Remarks**
- **Opening Presentation: Compensation Tools & Techniques** (3:05 - 3:40 pm)
- **Peer Exchange: Small Group Breakout Discussions** (3:40 - 4:20 pm)
- **Large Group Reconvenes: Recaps Across Breakouts (**4:20 - 4:30 pm)

Helpful Participation Tips

Turn Your Camera On
Click the video icon in the bottom left corner of your screen.



Switch to “Speaker” View
Click “View” in the top right corner of the screen. Make sure that you select the “Speaker” option from the list.



Submit a Question or Comment
To ask a question or comment, click on the “chat” icon in the “access” bar at the bottom of your screen. Type your question or comment in the chat box for everyone to see.

Unmute/Mute in Small Group Breakouts
Click the microphone icon in the bottom left corner of your screen.

Opening Presentation is Recorded.
Small Group Breakouts are Chatham House Rules and <u>not</u> Recorded.
A replay email will be sent and available on the WCD Connect mobile app tomorrow

Tweet during the event today @WomenCorpDirs and @PearlMeyer

Peer Group Member Steering Committee

Chair: Martha Finn Brooks
Director, Bombardier Inc., Constellium SE, and Jabil Inc.

Vanessa Chang
Director, Edison International, Sykes Enterprises, Inc., and TransOcean Ltd.

Evelyn D'An
Director, Enochian Biosciences Inc., and Summer Infant, Inc.

Deborah Ellinger
Director, Covetrus, Inc., and iRobot Corporation

Susan C. Keating
Chief Executive Officer, WomenCorporateDirectors (WCD) Foundation

Wonya Lucas
Director, JC Penney Company, Inc., and The EW Scripps Company

Gretchen W. McClain
Director, AMETEK, Inc., Booz Allen Hamilton Holding Corporation, Hennessy Capital Acquisition Corp., and JM Huber Corporation

Eugenia Ulasewicz
Director, ASOS plc, Hudson Group, Signet Jewelers, and Vince Holding Corporation

Meet the Presenters

Susan C. Keating
Chief Executive Officer
WomenCorporateDirectors
(WCD) Foundation

Jan Koors
Senior Managing Director and
Western Region President

Jane Park
Principal, Pearl Meyer

A Lot Has Changed Since March

In our April webcast we noted that a company's approach to compensation would vary based on the degree of impact from the pandemic

Severely Negatively Impacted	Moderately Negatively Impacted	Positively Impacted

- Some negatively impacted companies had better-than-expected 2nd/3rd quarters
- Were some companies too quick to respond at the beginning of the pandemic?
- 2020 incentive plan payouts continue to be evaluated
- Consider a holistic assessment of 2020 and 2021 compensation actions
- We have more information:
  - Market practices from non-calendar year filers
  - Better sense for how the proxy advisory firms will react

Balance is Key: Constituents and Other Factors

Management Considerations		External Considerations	
Plan otherwise set to pay out before the pandemic	Fairness	Workforce Experience	Furloughs / Layoffs Comp for Essential Workers
How do we keep participants focused on the right metrics?	Engagement	Shareholder Experience	Absolute/Relative TSR Financials
Retention concerns from underwater equity. Are companies ready with succession plans (beyond CEO)?	Retention/ Succession	Proxy Advisory /Media/Other	**ISS/GL:** • Open to discretion on STI (but watch out for above target payouts) • Less open to discretion for PSUs

Philosophical Question: Should all participants be made whole? Should we differentiate by level (rank and file, managers, NEOs?)

Consider a Holistic Approach to Assess Comp Plans

Decisions with respect to 2020 incentive plans may impact 2021 pay levels and design

	2020	2021
	Focus is on incentive plans and whether discretion will be used	Focus is on goal-setting and whether there is enough visibility to establish new 1- and 3-year targets and retention through new equity awards
Base	Restore, if reduced	Merit?

STI	<u>Assess Payouts for Fairness</u>
	• What is the projected payout? (including and excluding COVID)
	• Was a new 2nd half plan established?
	• Consider discretion or "let it lie"?
	  • If discretion, what criteria should be considered?
	  • Should use of discretion vary by participant level?
		<u>Visibility to Establish New Target/Increase Likelihood of Some Payout</u>
		• Performance period (annual, semi-annual, quarterly)
		• Revisit financial measures/weights
		• Increase non-financial measures / ESG
		• Leverage curve (threshold to max)
		• Delay goal-setting
		• Cancel STI in favor of more equity

LTI	<u>Assess Payouts for Fairness/Retention</u> • What is projected PSUs payout for all open cycles? • Consider discretion or "let it lie"? • What is current value of other (time-vesting) equity? • Retention Grants? • Check retirement vesting	<u>PSUs: Visibility to Establish New Target/ Increase Likelihood of Payout</u> • Performance period (1, 2 or 3 years?) • Revisit financial measures/weights • Consider relative measures • Leverage curve (threshold to max) • Delay goal-setting • Eliminate PSUs for 2021 only <u>Retention/Other</u> • Change LTI mix: More RSUs/options • Increase LTI value modestly • Use cash if burn rate is an issue • No grant if retention grant in 2020

Examples of Holistic Decision-Making

	2020	2021
Brinker	**Base Salary:** Temporary reduction **Bonus:** Exclude impact of COVID; negative discretion to reduce payouts to 91%	**Bonus and PSUs:** Quarterly performance measurement **LTI Mix:** 80% RSUs / 20% PSUs • 2020 Mix: 50% PSUs / 25% options / 25% RSUs • Expect to resume "normal" LTI mix in 2022
Darden	**Base Salary:** Temporary reduction **Bonus:** Exclude impact of COVID; 94% payout	**Merit:** None **Bonus:** Measure 2nd half financials (goals TBD); non-financial measures for 1st half will be a modifier on financials Same target bonus payout as 2020 **LTI:** Same value as 2020
Estee Lauder	**Base Salary:** Temporary reduction **Bonus:** No discretion (22-65% payouts) **PSUs:** No discretion (109.9% payout)	**Bonus:** Increased max payout (150% to 165%) and introduced a 50% floor payout; eliminated ROIC as a measure **LTI:** Higher grant value; incremental value based on what the 2020 bonus would have paid assuming a 40% BU floor and 90% corporate floor Increased max payout (150% to 175%) and eliminated ROIC
FedEx	**Base Salary:** Temporary reduction **Bonus/PSUs:** No discretion (no payout)	**Bonus:** No plan **Retention Grants:** FMV options for CEO; RSUs for others (4-year vest) **PSUs:** New measures emphasize capital efficiency and capital deployment – EPS and CapEx to Revenue

Early Disclosures

We found a precedent for nearly all actions but no prevalent market trend. Each company and industry will respond based on their own facts and circumstances

- Majority of the early disclosure companies are in the severely negatively impacted sectors (consumer discretionary and industrials)

2020 Compensation Actions

STI Plans

- **6%** Cancelled STI
- **6%** Created New Plan
- **17%** Exercised Discretion

LTI Plans

- **9%** Modified PSUs
- **17%** Special Grant (restore cash / retention)

2021 Compensation Actions

STI Plans

- **5%** Cancelled STI
- **8%** Delayed Goal-Setting
- **9%** Include Non-Fin'l Measure

LTI Plans

- **5%** >50% Mix in RSUs
- **2%** No Grant
- **2%** PSUs w/ <3 yr perf
- **8%** PSUs only measure rTSR
- **5%** Delayed PSUs Grant

Questions for Management and the Consultant

Data analysis (beyond benchmarking) can be used to support the decision-making process

How are the incentive plans tracking, to date?

- Can we exclude the impact of the pandemic?
- If 3rd and 4th quarters are stronger than expected, what if we only exclude 1st and 2nd quarters of 2020?
- No need for “one-size-fits-all” approach. Consider tailoring adjustments by level (rank and file vs. NEOs).

Track other performance factors

- Financial and non-financial

Tally sheets: What is the actual impact on retention?

- One-page document, by individual, summarizing last 3-5 years of target compensation, realized compensation and current value of equity awards (YTD performance for PSUs, in-the-money value of options, current value of RSUs)
- Check retirement/other termination vesting provisions. Are individuals better off retiring because PSUs are tracking at zero and retirement provides target vesting?

Pay vs. performance analysis: Would compensation actions/payouts be aligned with performance?

- Model/test proposed incentive plan payouts

Other External Considerations

ISS/GL have indicated they will be more favorably disposed to STI adjustments and less so toward adjustments to multi-year long-term incentives, but will review on a case-by-case basis

- Recently, ISS published COVID-19 FAQs to address how they may view various pay actions related to COVID-19; key takeaways for incentive adjustments include:

Key Annual and Long-Term (LTI) Incentive Themes
Disclose rationale for changes/awards and why the approach was chosen instead of other choices • Boilerplate language on "retention concerns" or "strong leadership during challenging times" is not sufficient
Explain how actions taken will further investors' interests • Discuss what the original payout would have been and how final payouts align with performance, especially if goals were lowered without lowering payout opportunities • Above-target payouts under changed programs will be closely scrutinized
Changes to LTI performance cycles will generally be viewed negatively • Includes changes to in-progress 2018-20 and 2019-21 cycles; and • More drastic changes to the 2020-22 cycle, e.g., shift to time-vesting or shorter periods
One-time, discretionary awards should be performance-based, with guardrails to avoid windfalls

Likely "Third Rail" Actions

- Modify all outstanding PSUs now
- Positive discretion on STI resulting in max payout (or above target payout) without sufficient explanation
- Lowering performance goals, without decreasing payout opportunities
- Other unexplained discretionary bonuses
- Stock option repricing
- Reducing PSUs in the 2021 CEO LTI mix to <50%

Breakout Session Questions

1. **What is your point of view on discretion?**
   - What types of analyses have you considered to help determine whether to exercise discretion?
   - Are you taking a holistic approach and considering both 2020 and 2021 compensation design? Or are you taking a more siloed approach?
   - Do you expect to treat rank and file incentive plan participants differently from senior executives/NEOs?

2. **What is your perspective on 2021 goal-setting?**
   - What is your line-of-sight in establishing new 1- and 3-year performance goals for 2021?
   - Is there a different mix of long-term incentives vehicles being contemplated for 2021?

3. **Does your compensation committee and management agree on the definition of "fair" (e.g. efforts, results, impact of business-line type)?**

Case Studies

VF CORP – Case Study (1 of 8)

VF CORP.

Fiscal Year	STI Discretion	LTI Discretion	ISS Vote	Glass Lewis Vote	SOP Vote Outcome
March 31	Yes	Yes	For	Against	90%

Annual Incentive Program

The committee used discretion to set the 2020 STI funding at 90% of target, reflecting on (1) above-target performance in the first 9 months of the year and (2) the estimated financial impact of COVID-19 on the last 3 months of the year

Long-term Incentive Program

The committee again used discretion for the 2018-20 LTI cycle to establish fiscal 2020 performance at 90% of target (same as with annual incentive) and then averaged 2020 with actual results for 2019 (200%) and 2018 (142%), resulting in a 144% of target attainment for the fiscal 2018-2020 LTI cycle

ISS Recommendation

Recommendation: FOR. ISS did not comment on use of discretion on the STI or LTI programs. ISS looked favorably at the positive alignment of pay and performance. Quantitative tests yielded "Low Concern."

Glass Lewis Recommendation

Recommendation: AGAINST. Unlike ISS, Glass Lewis identified concerns with the company's weak disclosure of incentive goals and use of discretion. GL criticized the fact that the company did not disclose what results would have been if not for the use of discretion.

THE CONTAINER STORE GROUP

Fiscal Year	STI Discretion	LTI Discretion	ISS Vote	Glass Lewis Vote	SOP Vote Outcome
March 31	Yes	Yes	For	For	97%

Annual Incentive Program

Additional discretionary bonuses were paid to impacted NEOs in the amount equal to the difference between 1) 50% of the projected bonus achievement prior to COVID-19 and 2) the bonus earned. All bonus payments were deferred until such time the committee or board determines.

Long-term Incentive Program

The number of performance shares vesting on June 1, 2020 were increased by the excess of the projected vested percentage over the actual vested percentage.

ISS Recommendation

Recommendation: FOR, *with caution*. ISS cited concerns on the limited disclosure around performance metric targets and actual performance for the STI and LTIP programs. However, the discretionary adjustments were modest and overall payouts in both programs were well-below target. Quantitative tests yielded “High Concern.”

Glass Lewis Recommendation

Recommendation: FOR. Glass Lewis noted that increases to STI and LTIP due to COVID-19 warranted scrutiny but acknowledge a reasonable level of disclosure and the extraordinary circumstances at the time of its FYE. No concerns were raised given the pay and performance alignment which resulted in a “C” grade.

Nike – Case Study (3 of 8)

NIKE

Fiscal Year	STI Discretion	LTI Discretion	ISS Vote	Glass Lewis Vote	SOP Vote Outcome
May 31	Yes	Yes	Against	Against	54%

Annual Incentive Program

Annual bonus payout increased from 0% to 100% to approximate Adjusted EBIT performance during the first three quarters of fiscal 2020 (June 1, 2019 – February 29, 2020).

Long-term Incentive Program

LTIP payout was increased from 0% to 75% to approximate Adjusted Revenue and Adjusted EPS performance during the first eleven quarters of the period spanning fiscal 2018-2020. The 2020 – 2022 LTIP cycle is based solely on rTSR (previously based on revenues and EPS).

ISS Recommendation

Recommendation: AGAINST. ISS criticized that large discretionary bonuses were awarded when payouts were not earned under the 2020 STI and 2018-2020 LTI program without sufficient explanation. Quantitative tests yielded “Low Concern.”

Glass Lewis Recommendation

Recommendation: AGAINST. Glass Lewis cited the quantum of awards granted during the year and the continued use of one-off discretionary awards as areas of concern. Pay and performance test resulted in a “F” grade.

Brinker International – Case Study (4 of 8)

BRINKER INTERNATIONAL

Fiscal Year	STI Discretion	LTI Discretion	ISS Vote	Glass Lewis Vote	SOP Vote Outcome
June 30	Yes	No	For	For	96%

Annual Incentive Program

Impact of COVID-19 was excluded from fiscal 2020 payout calculations; however, payouts were not to exceed 100% of target despite superior performance before and during the pandemic. Negative discretion applied.

Long-term Incentive Program

No action for fiscal 2020.

- Performance periods under the fiscal 2021 STI and LTIP are to be set and measured on a quarterly basis
- LTI mix of 50% performance shares, 25% options, and 25% RSUs for the fiscal 2020 grant was adjusted to 80% RSUs and 20% performance shares for the fiscal 2021 grant
  - Committee noted expectation to return to a higher percentage of performance shares and options in fiscal 2022

ISS Recommendation

Recommendation: FOR. ISS did not comment on the fiscal 2020 STI payouts or fiscal 2021 program adjustments. ISS looked favorably at the positive alignment of pay and performance. Quantitative tests yielded “Low Concern.”

Glass Lewis Recommendation

Recommendation: FOR. Glass Lewis noted the temporary reduction in performance-based awards under the LTIP for fiscal 2021. However, given the moderate NEO pay levels and absence of above-target payouts in the STI and LTIP programs for fiscal 2020, no concerns were raised at this time. Pay and performance test resulted in a “D” grade.

Estee Lauder – Case Study (5 of 8)

ESTEE LAUDER

Fiscal Year	STI Discretion	LTI Discretion	ISS Vote	Glass Lewis Vote	SOP Vote Outcome
June 30	No	No	For	Against	98%

Annual Incentive Program

No action for fiscal 2020.

Long-term Incentive Program

No action for fiscal 2020.

- Given the outstanding performance for fiscal 2020, additional value was provided to the NEOs and other executive officers in the form of additional amounts to the fiscal 2021 annual equity grants.
- EL also adjusted the STI and LTIP plan designs for 2021. Adjustments include increased maximum payout levels and goal changes for STI and LTIP and introduction of an STI floor payout of 50%

ISS Recommendation

Recommendation: FOR. ISS noted the plan to enhance the 2021 equity grants but did not comment further. ISS looked favorably at the positive alignment of pay and performance. Quantitative tests yielded “Low Concern.”

Glass Lewis Recommendation

Recommendation: AGAINST. Glass Lewis cited concerning pay practices for fiscal 2021 (STI and LTIP adjustments) and pay and performance disconnect. Pay and performance test resulted in a “D” grade.

Aramark – Case Study (6 of 8)

ARAMARK

Fiscal Year	STI Discretion	LTI Discretion	ISS Vote	Glass Lewis Vote	SOP Vote Outcome
Sept. 30	**No**	**Yes**	*TBD**	*TBD**	*TBD**

Annual Incentive Program

No action disclosed to date for the fiscal 2020 program.

Long-term Incentive Program

Payout for the 2018 – 2020 PSUs was determined by measuring the performance for the first 2.5 years of the 3-year period, removing the results and portion of the targets attributable to the period hardest hit by COVID.

- Fiscal 2021 equity awards were accelerated to September (typically granted in Nov.) and consisted of 50% options and 50% RSUs
  - Board expects to return to a program that is at least 50% PSUs in fiscal 2022
- Special performance awards of premium exercise price stock options that vest 33% on each of the 3rd, 4th, and 5th anniversaries of the grant date, consisting of 6 performance tranches were also granted for Fiscal 2021

ISS Recommendation

Recommendation: *TBD*

Glass Lewis Recommendation

Recommendation: *TBD*

**Given Aramark's fiscal year just ended, we expect the proxy to be filed in December like last year*

8-K Filed 9/3/20

Macy's – Case Study (7 of 8)

MACY'S

Fiscal Year	STI Discretion	LTI Discretion	ISS Vote	Glass Lewis Vote	SOP Vote Outcome
January 31	Yes	No	*TBD*	*TBD*	*TBD*

Annual Incentive Program

Reduced annual payout opportunity range from threshold of 25% of target and maximum of 200% of target for each metric to 50% and 150%, respectively; reduced overall annual maximum payout from 200% to 125% of target.

Long-term Incentive Program

Delayed approving LTI awards. When granting awards in July, Committee reduced payout opportunity variability from threshold of 25% of target and maximum of 200% of target to 50% and 150%, respectively; additionally, the Company utilized rTSR as sole performance metric and reduced the portion of LTI delivered in PRSUs; granted RSUS for the first time instead of stock options.

ISS Recommendation

Recommendation: *TBD*

Glass Lewis Recommendation

Recommendation: *TBD*

Macy's also published a presentation in October that is a good example of shareholder engagement with respect to COVID-19 issues.

Nordstrom – Case Study (8 of 8)

NORDSTROM

Fiscal Year	STI Discretion	LTI Discretion	ISS Vote	Glass Lewis Vote	SOP Vote Outcome
January 31	No	Yes	*TBD*	*TBD*	*TBD*

Annual Incentive Program

No action disclosed to date for current program.

Long-term Incentive Program

Cancelled PSUs granted to officers in February 2020 and granted stock options in August 2020 as replacement awards.

ISS Recommendation

Recommendation: *TBD*

Glass Lewis Recommendation

Recommendation: *TBD*

Thank you for joining the Peer Group!

WCD Compensation & Human Capital Committee Peer Group

Brought to you by WCD *and* **Pearl Meyer**

Watch for email invitations for 2021 quarterly peer exchanges!