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Day 1
Pay for Performance – What Matters Now
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Liz Dunshee: Thanks for watching our celebration video. Now I want to introduce our first panel, Pay for Performance – What Matters Now. The speakers have an agenda that covers about 45 minutes and then they're living 15 minutes at the end for Q&A. So you can enter questions in the chat box to the right of the speaker view throughout the program and then they'll save those for the end and address them.

Our speakers today, thank you all for participating. We have Brian Breheny of Skadden Arp, Ning Chiu of Davis Polk & Wardwell, Dave Eaton of Aon, and Renata Ferrari of Ropes & Gray.

So thank you all again and I will turn it over to Ning to frame the discussion.

Ning Chiu: Thanks, Liz. Hi, everybody. Welcome to the conference. We're really excited to be here with you today. We're especially excited to be your first panel of the day of the conference.

So what we've prepared is a discussion on a very relevant topic for the moment, which is Pay for Performance. The way we've kind of structured it is we're going sort of past, present, and future. We're going to talk a little about what happened this proxy season, then we're going to go what's happening now, what people are thinking and all of the various controversies and decisions people are trying to determine that would make sense for their proxies for 2021, and then looking ahead to goal setting and future issues in light of the uncertainties that everyone is facing.

So with that, as Liz mentioned you can put questions in the chat. As you may expect, depending on the number of questions we get, we may consolidate some, we may not be able to get to them all, but we will try to do that at the end. It's a little bit of an experiment. We are hoping to make this a little more interactive as much as possible for a virtual setting, and so we'd love hear from you.

Also we know that you're seeing CLE credits. The four of us actually can't see that so we hope you pay attention to it and we hope you don't mind if we're not able to repeat them for you, although we will try if we can, as Liz is going to send those to us in our own chat.

So with that, I'm going to turn it over to Brian to kick off with background in the 2020 season. With the pandemic hitting us right around the 2020 season, what, and then you've got the 2019, proxy statements in 2020 that really reflect 2019 performance, how do companies handle that and discuss that, and then you've also got pay cuts and layoffs and furloughs. There was just a lot going on in the 2020, this past season, with the 2020 proxy.

Brian Breheny: Yes, indeed. Well, thanks, Ning. Good to be here with you all. As with most things in 2020, the proxy season was anything but normal. The potential impact of the COVID crisis is, I think we all may recall, kind of hit the northeast of the US hardest in late February and early March, and it was at that time when many of us and our clients were deep into proxy statement prep and 2020 compensation decisions based on the sort of normal compensation calendar.

In response to the crisis, as Ning just mentioned, many companies took immediate compensation actions. Those actions included a number of things like reduction of executives' pay, director pay, employee pay, furloughs, halts to 401k contributions, and the like. We've been sort of tracking what the Fortune 200 companies have done in response and based on our sort of back of the envelope averages, about 60 of the 200 companies announced some sort of COVID-19 related executive compensation decisions, or about 30%.

You know, as Ning pointed out, the CDA as well all know generally tells the story of compensation for the prior year, in this case 2019, and that left companies grappling with how best to explain the impact, or potential impact, of the COVID crisis on the company in 2020, and what impact, if any, that would have on compensation decisions, including how 2019 Pay for Performance metrics were impacted by the crisis, when looking back at 2019 and the story might have been very different than what it was when we were preparing the proxy, when the proxy was going to get filed, when the annual meeting was going to be held, and of course for the rest of the year.

And as I mentioned, at the same time many companies were in the midst of their annual compensation review and approval cycles, with compensation levels and performance targets being determined about the same time the proxy disclosures were being prepared. And of course in many of those cases, many companies previously granted awards which were severely impacted by the market conditions.

So compensation committees charged with implementing programs intended to incentivize and retain employees through alignment with company performance, strategic business objectives, found themselves with a very uncertain future and tasked with kind of knowing the unknowable at that point.

And so what do they do? Do they address the metrics now? Or later? Do they exercise discretion to adjust performance targets either based on pre-existing discretionary adjustment provisions in the contracts? Or perhaps triggered by an extraordinary non-recurring event? Which I think most people would agree COVID-19 is that. Do they do it now? Do they do it later? Or do they do nothing? Which, as Ning said, we're going to get into sort of where we are today so I won't answer that question.

But, you know, with all compensation decisions, factors considered, including what your investors are interested in and, of course, with the proxy advisory firms we're focused on, I think we're all interested in ISS among one of the key proxy adviser firms, came out with some suggestions, which pretty much was we're paying attention, we think disclosure is incredibly important so if you're going to do something you better be prepared to tell the story, and we're going to kind of look at it in some ways in hindsight.

And so that's kind of set up as kind of where we were. I'll mention one positive from this season, and that's we didn't get final SSE Pay for Performance rules. If you've been tracking the timing of the Dodd-Frank provision, you might have thought 2020 was the year we would get something, because it seems to happen in every fifth year. In 2010 we got the actual Dodd-Frank, in 2015 we got SSE proposal rules, so naturally 2020 we all thought… I'm kidding, we didn't think we were going to get anything, but we didn't, so I guess I'll say, with a caveat, that was a positive for the season and I'll let the group maybe later speculate whether we'll see anything ever on those Pay for Performance rules.

But anyway, with that background, I'll turn it back to Ning and others if they want to weigh in on what they saw this season.

Ning Chiu: Sure, great, Brian. So we're going to move a little forward into the present, while Renata and Dave can also weigh in on what you saw that was of particular interest in the season. While it seems like March's, we're still living March every day, at the same time March seems like a very long time ago. So it's a very odd time.

I will make a plug that on Wednesday I'm going to be doing the ISS Glass Lewis panel that's always a favorite of this conference, and we are definitely also going to talk about their perspective on Pay for Performance, so I'll make that plug now so everybody should tune in.

So Renata is going to lead us into the current situation right now that companies are grappling with about whether or not, frankly, to just put a really fine point on it, should people be thinking about making adjustments to goals and metrics in light of COVID, and to the extent that the goals and metrics that were set previously perhaps no longer make sense.

So Renata…

Renata Ferrari: Sure. And one point on the actions that were taken at the beginning of proxy season, and there was a note on this in our outline, but some of them, I think companies were, they were trying to react and do something that they thought worked for their employees generally, and then of course when you look at most of them who'd just done, a lot of them who'd done base salary reductions, which is a small percentage of total compensation.

And so then there was a number of articles about, you know, sort of don't make such a big deal about this because really what you've done at the end of the day has done a very small reduction. And I think, the reason I bring that up, is I think that it will play into what companies are thinking about now when they're looking at 2020 as a whole, and just to say it, it's going to be, different companies are going to do different things, and what a company does will be highly dependent on their industry, how hard they were impacted by COVID, you know, whether they were impacted by COVID at all.

And I know it seems like we've all been impacted by COVID, but there are some businesses that are actually doing quite well, although they're, you know, probably a small minority of the businesses.

So it will depend, but if a company is considering making adjustments, and I think a number of them are, now is the time the companies, I mean, companies have been, a lot of the companies I work with, they've been reporting only to their compensation committees in terms of how they are tracking against goals. They've done it in the last couple of meetings and really they're trying to set up their committee for the best discussion that they can have, the most informed discussion, when the committee ultimately makes judgments as it relates to 2020 compensation decisions.

First thing you should be doing, look at your plan, look at the terms of the awards. This is really more important, I think, for long-term rewards. Brian mentioned it, there may be, you may be lucky in a sense if you have these automatic adjustments. For a lot of plans, we've moved away from automatic adjustments because we, you know, they were really more of a thing in the 162(m) world, but if you have, especially for the 2018 to 2020 grants, some, when those grants were being made in 2020, it wasn't quite clear where we were going to be with 162(m) and you may luck out in some way in having some good adjustment language that the committee can then look at and it could actually impact if you have to take a charge or not with respect to any adjustments that you make to equity awards.

You know, right now, as I said, I think a lot of companies are thinking about what they think that they can do, what they think their committee is sort of willing to do, and what the potential range of alternatives are. I think that basically conventional wisdom is that right now people are thinking discretion will be used. If discretion is going to be used, and it's really more, I think, on the annual plans, but if discretion will be used, having a framework for how that discretion will be exercised, thinking about, you know, especially in the case of pure financial goals, thinking about other things that became important to companies during COVID, whether it may be some nonfinancial goals, health and safety, or even some financial goals different from the ones that were in place at the beginning of the year when the metrics for an annual bonus plan were established.

You know, for annual plans there are a number of plans out there that especially after 162(m) was no longer a factor that have individual goals as a performance metrics under those plans. For those plans, committees may choose to focus more, much more on the individual goals on the level of achievement of those goals and generally on how management of a company, or tried to shore up that company, in light of COVID, and really to get to a place where there can be some payout under those bonus plans.

I will say, it's a much better fact if all employees are being treated in the same way, then management is sort of getting an extra bit and the employees are getting treated in the same way. Now most companies have different plans, larger companies for different levels of employees, but it will be, I think, even for the disclosure, a much better story to tell if you take, if a company takes the consistent approach with its plans. For companies with purely financial goals for their annual bonus plans, then it's really a question of do you sort of live by those goals, do you exercise some discretion. My sense is that companies will exercise some discretion and they'll probably be doing it on all levels, not just for executives, but for other employees.

Obviously depending on the company. If a company isn't doing well at all and is cash poor, they're most likely not paying bonuses, so it will really depend on the company.

I think where it gets trickier, oh, sorry, Ning.

Ning Chiu: Go ahead. It was, yeah, I was going to ask you a question that you were just about to get to.

Renata Ferrari: I think where it gets a little, gets trickier is the long-term awards, but of course the long-term awards are where there's the most significant amount of value. And so for most companies, if they're thinking about their long-term awards, there's probably three cycles in play for those companies that set their, basically had their meetings before everything shut down at the beginning of March or middle of March. You have 18 to 20, 19 to 21, and then you have 2020 to 2022. The considerations for each cycle are likely going to be different, you know. For 19 to 21 and 20 to 22, one of the things companies may be thinking about, although at least we've had some guidance from ISS that they don’t like in-flight changes to performance goals, is thinking about adjustments to those goals.

I think the problem with that, or the difficulty with that, is that a lot of, right now a lot of companies couldn't actually say with certainty what they think the right goals are for 2020 to 2022, and no company wants to be in a position where they make a change now and then in a year they're going and making the change again, partly because the change itself will, it will need to be disclosed, but there may be accounting consequences to it. If it's a modification, then it's going to show up in the summary compensation table, and then potentially skew compensation.

So at least what I'm hearing now is for 19 and 20 is at least, right now, and we'll what happens at the beginning of the year for these calendar year companies, is wait and see. And then you have 18 to 20, and for a lot of these companies they were doing quite well, in 18 and 19 and 20 until say March, and so there's, you can look at it and say, "Well, executives shouldn’t be paid," but you could also look at it and say, "The company was doing really well."

And like a lot of other things that have happened where we've had dips in the economy, this one isn't really anyone's fault, right? So what should we be doing? And for the 2018 to 2020, I mean, one option is do nothing. I think if companies do nothing and those awards pay out at zero or a very low percentage and they were tracking before COVID at a high percentage, companies may feel like they should maybe increase the size of the 2021 LTI award or perhaps to a special 2021 PSU award that maybe focuses on metrics different from the typical metrics that a company would use, maybe stock price performance or relative TSR is being thrown out for those companies that have more of the operational financial goals.

Then maybe think about a time-based award or something to encourage retention, because for a lot of these companies, these are the things that really, especially the equity awards, are what motivate executives, employees, it's not just the executives who have these awards. So thinking of doing something that will keep the sort of, the team focused on the mission at hand.

I have, so that's sort of do nothing. I've heard at least thrown out there as a possibility looking at each year in the performance period as a separate performance period. So there, it's not a separate performance period, these are three years. But if you can look at 2018 and let's just say you were at 160%, in 19 you were 180, in 20 you're at zero, you take the three and you average, and that's just a way of using, exercising discretion, which likely may not even be part of that award.

And then I've also heard of companies thinking, if they can, to try to remove the COVID period, which of course is really hard because we're still living in it, but for a lot of companies it really impacted them, let's just say March when a lot of us shut down, April, maybe May, and things are coming out of maybe June, is there a way that you could take three months. Now for some metrics, it's not going to be possible, but take some portion of it out.

For all of these, if companies are exercising discretion, I think what we all expect is that the awards would be capped. So if you're thinking about taking a performance period out, you wouldn't give the credit of a three year award, so you'd sort of have to do some type of _____ award. So for all, so it doesn’t look like a windfall, so it doesn’t look like the executives are getting these significant awards when the employees are suffering, all to say that any decision that will be made needs to be made in the context of the company's own financial circumstances and looking at all stakeholders, all right, so it's not just the executives who will have a view, it's the employees generally, it's stockholders, it's institutional investors, and thinking about sort of what works the best. None of this is going to be perfect. Most compensation committees don’t, haven't exercised significant discretion, so it's going to be a new world a little bit the beginning of next year for these committees and thinking about the best possible alternative, the best possible outcome given the different alternatives.

And then disclosure is going to be key, then getting out the disclosure and saying, "These are the principles we used, this is what we did, this is why we think it's appropriate," and then hoping that it's received at least well enough that it doesn’t cause the company a problem.

Ning Chiu: So before I unpack some of things you said, you gave us a lot of really good advice. First of all I want to mention that the CLE code is "blue," not case sensitive.

A couple of questions, and this is to all of you, one is, I'd like to start with the first one which is, "Is it better to do a little bit of, for example, a little annual, a little bit of adjustment to annual, a little bit of adjustment, like one of the options Renata mentioned to the 2018 to 2020 period, and just take haircuts on each, or is it better just to do one thing? And explain that one thing? Is it better because right now we're living with a very unusual year, unfortunately, it looks like we might be living with it for longer than just a year, but is it better just do one thing for this one year and leave everything else alone? Or is it better to make a few changes all along so that you don’t have to make future changes?"

Do you have a sense of that? To any of you.

Renata Ferrari: I can start. I mean, I don't know, honestly. I go back and forth. There's sometimes what I think, sometimes I think it's figure out the bonus, because I think the bonus, the bonus will impact all employees. I mean, they're not maybe all using the same metrics, but take an approach on bonus as to how you're paying your employees generally. Obviously the quantum will be different for the executive officers.

And then there's, sometimes I think, you know, and I know easy for me to say because I don't have the PSU award, but leave the award as they are and try to right size it in 2021, because now 2021, and I think Dave's going to talk about that, 2021 is going to be a tricky time, too. We're sort of living, I think between now and basically March of next year, we're all going to be really busy and trying to figure out what the best thing is, but it really will depend on the comp committee, but if the comp committee is really allergic to exercising discretion, then I think you can try to sort of, I don't want, not make it up because I think there's not going, no one really wants to be like, "Well, you lost this, so therefore you got the next thing," right?

But really in 2021 trying to figure out what is the right program going forward. Like we sort of have to just count the ability of our executive officers to meet or in our employees who have PSUs to meet those goals. How do we at least fix this now so we can provide the right retention incentives as well as the right goals to try to motivate our employee workforce?

So sometimes I'm on there, sometimes I'm on do something with the bonus, do something with 18 to 20, and leave 19 and 20 alone, because there's no good way to fix those right now other than saying the 20 to 22 may just be a wash and it may be too soon to tell that.

Brian Breheny: You know, as Renata was talking, I was thinking among two things, that was some really good update. Number one is timing. You know, we're almost at the end of the third quarter. If we're really thinking about tweaking 2020 comp and it's intended to, I don't know, incentivize, motivate, maybe reward, you know, we're almost, we're three-quarters of the way through the year, so if you're going to make a decision, we have lots of clients that, Renata, as you mentioned, are withholding the decision as to whether they'll exercise discretion they have or by the way maybe perhaps amend agreements to add it, because I think you can do that without shareholder approval and If you don't have it, you might be able to get it. But if you're going to do that, when are you going to do it?

And then, probably the most important thing is, what's the message you're sending to your investors and your employees? Because I've had some clients who took executive, senior executive reductions in salary. They've increased them, but that's because they've also furloughed employees that brought them back in. I think the message there was we're kind of, the executives are kind of sharing the pain, and then now that the, and in this particular case, it was a business that while it was off for a while has now kind of come roaring back, because there are definitely clients that are having really good, or more than likely, a really good 2020.

But if you are in a case where you furloughed employees, reduced compensation and then you're somehow thinking, "Well, it's important to incentivize some of those executives," what message is it going to send? So I'm not sure I know the best answer. If they do decide to fix, whether it's take it now or spread it to things that initial question, but those are at least two of the factors I'm thinking about, or I know clients are thinking about before they make any of these decisions.

Renata Ferrari: And just one other point and then, sorry, I'll stop talking, but on the decision to take, to make the decision now or later for the equity awards can have significant consequences because if you are making and adjustment to the equity awards in 2020, you're going to have a, excuse me, chances are you'll have some adjustment, some value associated with the modification that's going to be included in your 2020 proxy statement. There are a lot of companies that are really sensitive to having their 2020 comp not be higher than 2019 because here there's a story, I mean, all those companies went out and they reduced fees and they did all of these things, and employees were furloughed, I mean, obviously not every company, but at least the ones that maybe are having a really, where this is going to be a sensitive decision for them.

If they do it in 2020, there's sort of something about like take your lumps and move on, but your 2020 comp may look outsized for a year where you were supposed to be this idea of sharing the pain…

Brian Breheny: Yeah.

Renata Ferrari: And so that may lead companies to say we're going to try to, we're going to do all of this in 2021 and then try to manage a little bit the numbers, if you can. Of course, we have no idea with this, this all sort of assumes and with the hope that by the time we're doing this next fall and then in the 2020 proxy statement, life will look, 2022 proxy statement life will look quite different and we'll hopefully be back. But, you know, of course none of us know that.

Brian Breheny: Sure.

Ning Chiu: Dave? Did you want to go ahead and, if you had a response to the question that I posed? And also go ahead and take us to the future, which is, as Nata teed it up already so nicely, goal setting for the future based on all this uncertainty. Is it even possible? Does it even make sense to do it? Should we punt that? Can it be punted? I mean, can we get out of this? One radical idea is can we get out of this notion that we need to goal set that far in advance. Is that even radical? Or is that even, is that possibly on the table? Because how do we know at this point what 2022 is supposed to look like? Or even, you know, keep going forward beyond that.

Dave Eaton: Yeah, no, thanks. I think, you know, this has really teed up the discussion of the going forward, right? There's more questions than answers that we've kind of posed so far, because we've been talking about adjusting goals mid-year, adjusting performance periods for 2020, or thinking about how that affects bonus or incentive plans, but when you look at going forward, the question that has come up, certainly with some of my clients and I think it came up in our prep sessions among us, was do you go back to normal? Do companies think, can we reset to normal? Even if we have made adjustments in 2020, for 2021 do we kind of go back to our bonus structure? Back to our incentive plan? To Renata's point about which performance cycles do we touch or not touch.

You know, it's a really good question and I like that Brian brought up the word "normal" several times in his opening remarks because there's nothing normal anymore, and certain companies want to, and are perhaps better situated to keep calm and carry on, but really I see the going forward aspects of and ramifications of COVID as being an opportunity for a lot of companies. It's an opportunity to reexamine their entire incentive structures, and that means all aspects of it. Your goal-setting process, what goals you're using, the appropriateness of those, the rigor of those, even things such as your grant timing, or your performance cycles. Renata alluded to that. You know, do you switch to one year performance in your long-term incentive plans? Things like that.

So that opportunity for companies right now, this fall compensation committee planning time, is critical. And I think 2021 will be somewhat defined by how do companies set their incentives going forward, both annual and long-term, and also the disclosure that companies provide in the 2021 proxies.

The first thing I want to kind of touch on would be that goal-setting, or really the metric setting, and companies reexamining that, because like I said, I think it's an opportunity to examine all aspects of it. For example, grant timing. Is, should companies delay their grants? You know, there's maybe some advantages to that. Certain clients have asked us that. The uncertainty of the market. It's hard to set goals if you're looking at PSUs. Can you wait? Can you delay? On the time vesting side, if a business has been strongly impacted by the pandemic and their TSR is quite depressed, there's concerns that keeping your normal granting cycle, you're granting at depressed, perhaps artificially depressed in some people's eyes, stock price and you're setting up your executives for a large, huge windfall that will not go unnoticed by a lot of your key investors and the proxy advisors. So there's definitely some thoughts there.

One of the things that some of our clients are thinking about is do you switch to a semi-annual grant cycle for 2021. And that could possibly help reduce the effects of market volatility. Grant pricing is another option, another consideration beyond just what your metrics are. Most companies use a closing price on the grant date, a spot price, but do you want to switch to using a trailing average price? 30 days for an option? Maybe more for a full value award. And the benefits, again, avoiding the effect of the volatility of the marked and really you have to do that within the parameters of your plans, not all plans allow you to switch like that, but it's something to consider.

And then, of course, maybe the biggie is reconsidering your metrics, what do you want to do there? There's been a push for, I've certainly heard, I think we all have, for reconsidering at least relative metrics and incorporating those into plans, and then also which we'll touch on a little later is some of the newer goals, or the newer metrics, that people might want to incorporate around ESG and other more hot topics of the recent past.

But with relative metrics, I think it makes a lot of sense. I think about two-thirds of the S&P right now uses a relative TSR metric. That percentage decreases as you get outside of the S&P, but we advise companies to use a relative metric when basically two things are happening. You're unable to set absolute goals for some reason, and then if you have concerns about how your incentive plan payouts are either aligning currently or will align with stock price performance and really how investors are being affected in their wallets.

So I think COVID and the pandemic kind of checks both boxes there and the consideration for a relative metric makes a lot of sense. Relative TSR rewards stock price, it aligns with shareholders, easy to set, easy for participants to understand really. There's a slight disadvantage sometimes to it, which I shouldn't leave that unsaid, is that TSR is an output metric, it's a market view on your performance. There can be a lag to that. And also participants sometimes don't feel like they have control over TSR. That's the big argument against it, I guess, but…

Ning Chiu: When you're talking about relative TSR, Dave, what is relative to? You know…

Dave Eaton: Mm-hmm. That's a great question. I think the two kind of obvious choices that companies use are either their self-selected peer group that they're using to benchmark their pay and use as a competitor group, or an index, and that could be something broad, like the S&P 500 or it could be a subsector of that, more defined by your industry.

And I think they both have advantages and disadvantages, really. I think it's, in a lot of cases, it's easier to understand that you're going to compare all of your pay components and decisions to one peer group, here's the 20 companies we think is our peer group, we compare our base to that, we compare our annual incentive levels, we compare our equity as well and that carries through to your PSU. However, comparing it to the S&P 500, for example, does make sense in certain situations as well where perhaps your industry isn't robust enough or size wise you don't have enough companies that are comparable within that industry, so it's, there's definitely backtesting on that and thinking that through is really critical.

I think it's also a question of how you use, if you're going to go this route, use the relative TSR, so about, I think it's about 80-85% of the companies that do use relative TSR, use it as a discrete metric within their plan. So there's a certain weighting to it. You hit different threshold target max performance and you get a payout. There's a wider range of potential payouts from that metric. Euro dollars up to a couple X percent, X times your target.

But then the other 15-20% of the companies use it as a modifier, where they have operational metrics that are determining the bulk of the payout, but the TSR is being used as a modifier to bring the payout up or down, typically it's about, you know, up or down 25%. And it's a smaller effect of the TSR, but the can be effective as well. I think in the current environment and looking forward to the market volatility and the continued effects of the pandemic, I think the first option, discrete metric, is perhaps being considered more but either way, it can be an effective way of kind of dealing with the environment going forward.

Which actually kind of slides into the other thing that I mentioned earlier, disclosure. I want to make sure, you know, 2021 the most essential thing really, to me, the big word is disclosure. I think companies have two opportunities throughout the year really, two main opportunities to message their shareholders, and one is direct shareholder outreach and the other is their filings, and particularly their proxy. And this is the year, I mean, 2021's going to be the year that if any company that's kind of considered their proxy summary or considered an executive summary to the CD&A and not really paid much attention to doing that, this is the year to do it. You need to tie together COVID and business impact and what impact that's had on certain strategies, but what impact has it had on human capital management, you know, going back to some of those things we talked about earlier, furloughs or pay cuts.

But then also tie that together with executive compensation decisions with pay cuts there or executive compensation outputs, such as missed bonuses, things like that. And that story has to be cohesive and it really needs to come through for investors and proxy advisors. Already I've seen articles, I've seen the AFL-CIO pointing out companies with high pay ratios that furloughed employees due to COVID and questioning whether, how these decisions and numbers work together. So nobody wants to be on that list, nobody wants to be called out for stuff like that, so really I think part of this metric setting or metric reconsideration is being able to tell that story at the end of that.

So we've been recommending companies do some P for P modeling, understand their ISS classes' modeling, understand their investors' modeling, and then engage with shareholders if and when possible, and then really consider how your story's going to get told. It's just a critical step to, I hate to use the term like get credit, but to get credit from your investors and from the proxy advisors.

Ning Chiu: So I'm going to follow up with some things you said. First, Dave, I want everyone in the audience to know that we believe that you're only seeing Brian while you're hearing the rest of us speak…

[cross-talk]

Ning Chiu: There's a technical glitch that they're working on fixing. Apparently somehow Brian got control of this panel. We don’t exactly know how…

[Laughter]

Ning Chiu: But that's why you're seeing him only. We're all still here, we're all still engaged, and we're all still talking, in fact. But we know you can only see Brian, they're going to fix that, hopefully for the rest of your sessions. Including the one Brian's not on.

Brian Breheny: You thought I could…

Dave Eaton: Well, that's a good transition, though, because I was going to try to transition over to Brian, so…

[Laughter]

Ning Chiu: Well, I want to get to a few things that you said, Dave, before we transition to our next topic. So one of the things is relative TSR, which is a thing that we hear about all the time. Some investors really like it. Some major investors really like it and they push for it. And you said S&P 500, for example, or whatever your index is. As we know, the S&P 500 has been moving a lot because of a few very large tech companies. Does that actually make sense? Does it make sense to take out those, if you're not one of those companies that are in those fortunate spots, does it make sense to take out some people in the S&P 500. Not form a new peer group, but take out a few people in the S&P 500 that's having a disproportionate impact on the market.

You know, if you take out Microsoft, Apple, Amazon, Facebook, Google, what does the S&P 500 then look like? And that's what's they think, well, what does that look like? What does that market look like? Has anyone done that? Does that make sense?

And then in terms of peer group, what are you all seeing on adjustments to the peer group, because some companies have a lot of peers, but they might be impacted by COVID in a unique way that's different for their business than some of the others.

So I know, for example, a lot of companies have, 3M I think is the most popular company in a peer group, and I haven't actually checked to see how they're doing, but they make a lot of stuff that's actually related to COVID, masks and protective equipment and things like that. Maybe you don’t have anything even remotely similar to that, and so they may be doing, their business may be operating a little bit differently.

So peer group and then generally relative TSR, but peer group, S&P 500, if you all have a reaction to that, and then we'll move on to the next topic.

Dave Eaton: Yeah, I'll start off and happy to have other people jump in. I'd say the first question, S&P 500 and whether you want to think about excluding the effect of the high performers, some of those tech companies you mentioned, generally speaking I wouldn't really recommend that. It gets a little into the picking and choosing of peers and a little, you know, the criticism of peer group selection has always been you're really cherry picking who to compare yourself against and at least would give of the appearance that you're doing that. Even though you're actually eliminating some of the high performers and maybe that's, you're comparing a little more favorably to the rest of the S&P 500, I think it's more effective probably to choose a different peer group at that point, choose an industry index or to use your peer group, but…

The second point about the volatility and how it's affecting peer groups is actually a really interesting one and we've been working with a lot of clients on that. It's, certainly I've seen some dramatic changes among several peers within a peer group where they really just have to be eliminated and it's usually for the other direction, that they're severely underperforming and they're just no longer a good comparable company.

Ning Chiu: Renata or Brian? Did you have a reaction to any of that?

Renata Ferrari: Yeah. On the peer group question, I have a couple of clients I work with that are thinking about peer groups. They're not, when they have the self-selected peer groups, because they realize that the pandemic has, because of just little differences in the business model, that the pandemic has had a significantly different impact on different businesses because of small parts of their models. So is it whatever, you know, they're not going to change it for in-flight for existing awards, but thinking about now, like anything else and as we see things that we hadn’t seen before when the circumstances change, and thinking about really are these the right companies to be comparing ourselves to because within their business model there are certain things that can really, can lead to very disparate results when you normally wouldn’t have thought so, and so there's going, I think for the going forward peer groups, thinking about is there, are we really as similar as we seem to be, or are there things that our model, that make those companies although on their face they look like us, but they're really different from us.

Ning Chiu: So we have an audience question and it kind of goes, is consistent with what we've been talking about, which is addressing the companies that have been severely impacted by the pandemic, airlines, retail, travel industry. Is there any insight into addressing that and do we have a view on how we believe ISS and Glass Lewis may react, although I can also, that is on the agenda for Wednesday, so another plug for Wednesday, talking to ISS and Glass Lewis about that.

In some ways, this is just my own view, in some ways I think those might be the most sympathetic industries. It's the most understandable that with the airlines there was just nothing they could do no matter what. Even though I still get an e-mail from every single airline I've ever flown, every single day, that's not really making me want to fly, so those might be the most sympathetic industries, but just spending a moment on, obviously people at those companies are working extremely hard, in fact maybe harder, than they've ever worked before. So how, do we have a sense of whether there'd be more sympathy for those companies in terms of what Pay for Performance means this year? All around. Investors, you know, disclosure, everything.

Brian Breheny: Ning, you don't want to get on a plane. When they waive your baggage fee, that's not ____, drive you to the airport, I'm…

Ning Chiu: Not yet, not yet. Maybe, maybe someday soon. And by the way, just so the rest of us don't get too relaxed, I understand everyone can now see all of us.

[cross-talk]

Brian Breheny: By the way, when we were talking earlier I saw one of the comments, "We can only see Brian. Not that we don't mind seeing Brian," and I was like, "oh, thank you…."

[Laughter]

I was going to say if you are in an industry and your peer group is one that's being similarly impacted, I think you probably have less of a problem than you are perhaps if you're a company that's an outlier within a particular industry and you're comparing. I mean, I think in the travel industry, the airlines, the hotels, are all being impacted. I think if you think of something like the cruise industry, while they're in the travel space, they are particularly impacted, right? Airlines are still flying, hotels are opening, they were closed some of them, but they're opening. Cruise ships are sitting idle and I think the last notice I saw was they probably won't sail at least until the spring of 2021 at the earliest, so I think there's an industry that if they are comparing themselves, and I'm sure that they do compare themselves to each other, but if they add in to expand the group to include some other travel or leisure, I would think there's a situation where you might want to, you should, and I would hope and we'll hear it on Wednesday because Ning's going to ask the question, that the ISS and Glass Lewis and investors would have to understand there's a bit of an outlier in that industry.

And I can't think of another at the moment off the top of my head, but I would think if you're in that, I think you should be able to make a tweak. And as Dave mentioned in his remarks, which I think we talked a lot about, like disclosure is so important now, will the ISS and others focus on that disclosure? I hope so, because they say they do, but here

I think there will be nuance as to who's impacted and why. And if they make decisions that they feel they need to, I hope you'll go listen.

Ning Chiu: With that, Brian, maybe you can lead us off on what is our last topic, which is a little bit different in terms of we were talking and we thought this would be a good idea to share with the audience. We were talking about an interesting, in light of everything else that's happening this year, beyond the pandemic in terms of having additional goals. So it's related, but different kinds of goals. Nonfinancial goals, such as ESG goals, diversity goals, there's been a little bit of push for that. There's been some interest for that. Is that something that is growing in terms of interest by both companies and investors? What's the best way to do it? And I'm posing these questions for everyone, with Brian to lead off, but what's the best way to do it? Because if you make them qualitative goals, which is a way they most of the time are right now, then there's a ton of discretion.

And Renata's already mentioned the reluctance for investors and others to live with too much discretion, we're already going to have a lot of it. At the same time, if you make it quantitative goals, that shows a level of commitment that's understood but it's always the same issue with any kind of quantitative goal. If you meet them and exceed them by a lot, did you make them too easy? Was that a real commitment? If you make them really hard, are you not motivating people to reach them?

So what are, and what's the right timeframe, too? So we have the same goal setting issue we always do in comp, but now we're talking about something very different.

So Brian, your perspective on ESG goal setting and then Dave and Renata, as well. As our last topic.

Brian Breheny: Yeah, great. I'm happy to do that. I noticed that our internal agenda had the word "new," new goals in quotes, so I thought that was an interesting editorial on this point. I think the reason, I didn't prepare it, but I suspect the reason is because this has been around for a while. I remember when I was at _____ Shapiro, I came in as the first chairman under President Obama, we put together an investor advisory group, and this is going, now what? 12,13 years ago, and that group was very focused on ESG.

And at a time when there was talk but not nearly as much as some of the people around that group, who at that point said the SEC needs to mandate ESG disclosure. They have to come up with a new scheme and I thought, "Well, that's not going to happen." And it hasn’t happened, as it turned out, but hey, are we getting closer to potentially seeing that? So I guess the point is that they're new in some ways because people have been more interested in it.

And look, we have ESG waivers now and of course there's a ton of money being invested into ESG focused funds, and so naturally I think we need to pay attention to that.

You know, there's no doubt that ESG and diversity metrics in compensation programs is a hot topic, is the hot topic these days for comp committees. More and more companies are exploring adding ESG and diversity and human capital management metrics to performance based compensation. I think a recent study done, or a survey done, said about 60% of the companies are at least thinking about it. And a number of surveys that were conducted over the last year or so by different groups, I think, sort of again the way I would sum it up that due to the increase of pressure from shareholders and state and local governments and other stakeholders, ESG compensation plans are certainly on the rise. About 20% of respondents now already include ESG performance metrics. That number gets a little bit higher depending like if you're in the oil and gas or other natural resource companies seem to have those a little bit higher, closer to the 30%.

But I think that the takeaway, which I think the question is being posed to us, is there really isn't a consensus on the best way to do so, including how best to identify, set the appropriate goals, as Ning mentioned how long, how far off. I think everybody would like to see, or in some situations would like to see, hard steps that can be measured, what are you going to do in that regard?

And so maybe I'll stop there and say I don't know that there's a consensus yet, there's certainly, I think there's going to have to start to be a consensus. For instance, just focusing on diversity, which has always been, I think, something companies and others have been thinking about. This year, in particular with everything that's going on in the world, I think more and more people are being called to task on that. I know, for instance, law firms have many of them signed onto this Mansfield Rule which in there there's a metric, you need to be Mansfield certified, you need to have at least 30% of the pool of candidates that you're considering for partnership promotion or leadership positions and other situations, pitches to clients have to include a group of at least 30% that's diverse. That doesn't mean that they actually have to ultimately be promoted to 30%, although that's of course the hope at least, but the group needs to include.

So that's a hard metric. And we signed on to it recently. And it's something that we spent a lot of time thinking about, like a compensation committee is like, "Well, okay, if we're going to do this, how are we going to measure it? How are we going to be comfortable that we have the right measures? And how are we going to meet or exceed it?" Because obviously you put yourself up to that goal and you want to be able to do that. And there are other firms that have done similar exercises as well.

So it might be helpful for us to talk specifically about I haven't seen specific, for instance, diversity or ESG metrics as others have, like what that looks like. I've heard conversations about what it might look like, but I haven't seen companies specifically adopt it yet.

Ning Chiu: Renata and Dave?

Renata Ferrari: Yeah, on diversity. I mean, I've seen there may be alike a catch-all of workplace or something like that where that's one of the metrics, but it's soft. It's not an increase X by Y percent by Z, or something like that. I think for the ESG type goals, the ones that are the sort of hardest goals, and by hard meaning the most pre-established objective or really the, or at least what we've seen for health and safety. Now that may change, too, because health and safety has become a much bigger issue with COVID, right? So retailers, restaurants, all of that. One of the things that they're spending a lot of, airlines, health and safety, they're customers and employees, so that means we may see a health and safety goal sort of morph into something more in terms of general, I don't want to say well-being, but something different from what we've tended to see for health and safety goals which are more in manufacturing companies, where they actually will measure number of deaths…

Ning Chiu: Right.

Renata Ferrari: And they actually have goals related to real, it's like, real safety measures.

Ning Chiu: OSHA. OSHA issues. Yes.

Renata Ferrari: Yeah, all of that. Well, we already see that and that's important for the industry, so I think, I think so far the health and safety, the sort of the strongest goals have really been the industries where they're manufacturers or things like that. My sense is that, especially in 2021 where there's a little bit less of, there's going to be more uncertainty around how to set some of the financial goals and COVID's still going to be front and center, depending on the business we may see some goals related to health and safety of employees and customers based on industry.

And diversity, I don't, I haven't see any company right now that I can point to, and there may be ones out there, where you say they actually have a strict goal. It's really, it's been, at least in my experience, more general and then in one of the things that companies are talking about, even in their executive summaries when they're talking about human capital and management, they will talk about their workforce and the strides that they made this year, or the last year, and increasing diversity in their workforce, but it's not clear, there's not a direct tie to bonus.

Dave Eaton: Yeah, and I would just kind of echo the same thoughts. I think the ability of companies to tie it to a hard metric can be difficult, but that's okay. A soft metric for a certain percentage of annual incentive plan is perfectly acceptable in the eyes of most investors. And I think it's good because really I think one of the most important responsibilities of a compensation committee is setting performance goals for both the annual incentive and long-term incentives, and it's not just that you're incentivizing your executives in a certain direction to achieve certain goals, it's that you're also messaging, you're saying these are the times that we think are important, and that are important to the company and important to our strategy and if the executives focus on these, the company will be moving forward and creating value and growing in the way that you as shareholders want it to.

Ning Chiu: Great. Well, with that I think that Liz is here to pull the plug on us, but I will mention that the CLE code, the second one, is "red," not case sensitive. And remember, I will be talking to ISS and Glass Lewis on Wednesday about some of these very same issues, so you'll get their perspective as well, so please tune in to that.