

**FARIENT**  
**ADVISORS**

AN RAFCAPITAL COMPANY



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**WorldatWork**

# “What the Compensation Committee Wants”

May 22, 2008

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**Chief Executive Officer, RAF Capital LLC**  
**Executive Chair, Fariant Advisors LLC**

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**Law Student, Michigan State**  
**Compensation Committee Chair,**  
**Public company boards**



We are discussing this subject from a number of perspectives



- **Line Executive:** RAF Capital LLC
- **Board Member:** Private cos., Higher Ed
- **Compensation Consultant:** Farient Advisors LLC
- **Compensation Committee Chair:** Private cos., Higher Education



- **Compensation Committee Chair:** Public cos.
- **Law Student:** Michigan State
- Former **SVP, HR:** Public co.
- Former **Head of Executive Compensation:** Private and public cos.



## Our agenda

- **What does the Compensation Committee want?**
- **Why do they want this?**
- **Are we there yet?**
- **What can you do?**



# What Does the Compensation Committee Want?



# The Compensation Committee wants:

## Positive Outcomes

- The **company is performing** well, in both absolute and relative terms
- The **executives are happy** and motivated by their compensation arrangements
- **Shareholders vote “yes”** on director proposals; there are no shareholder proposals
- The **media** considers this company to be a **non-event** (or at least we are in a defensible position)

## High Confidence/ Low Exposure

- The Committee is **confident** that:
  - They are **protected** - there are no hidden legal, accounting, HR, or other issues
  - Shareholders and executives (pay and performance) are **aligned**
  - They have untainted information, analysis, and process to make **good decisions**
- The compensation consultant and internal staff **work well** together, but both push back if warranted



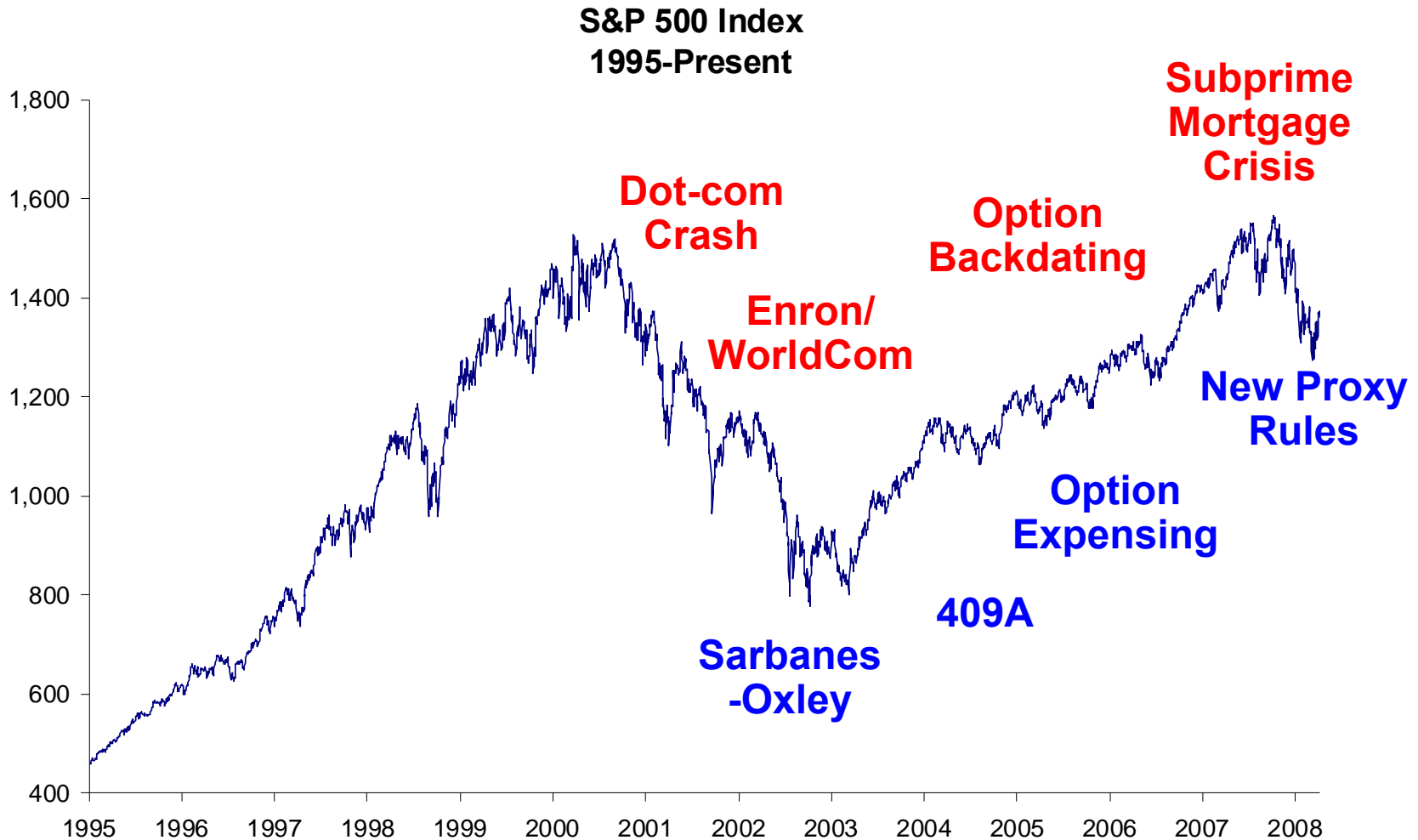
The Compensation Committee does NOT want:

- **To be “gamed”**
- **To be surprised**
- **To be a rubber stamp**
- **To be in a “general contractor” role**
- **To be embarrassed**
- **To give up decision rights**



Why Do They Want This?

# Shareholders, the government, and the media continue to be on "red alert"





## Pressure on Board governance will continue

- **Pressure from external forces**
  - **SEC**
  - **Shareholder groups (ISS)**
  - **Political agenda**
  - **Media**
- **Desire by boards to influence big issues that move the needle**
  - **Business strategy (managing the upside, not just the downside)**
  - **CEO selection**
- **More work pushed down into Committees**
- **Technical capabilities required in Committees, particularly Audit and Compensation**
- **Prodigious time commitments that aren't always predictable**

Pay and performance misalignment = exposure

### Shareholder Alignment

Executive Pay	Hi	<b>Misalignment:</b> shareholders not happy; executives happy	<b>Alignment:</b> shareholders happy; executives happy
	Lo	<b>Alignment:</b> shareholders not happy; executives not happy	<b>Misalignment:</b> shareholders happy; executives not happy
		Lo	Hi
		<b>Company Performance</b>	

### Hidden Causes

- Program design
- Program administration
- Fine print
- Timing

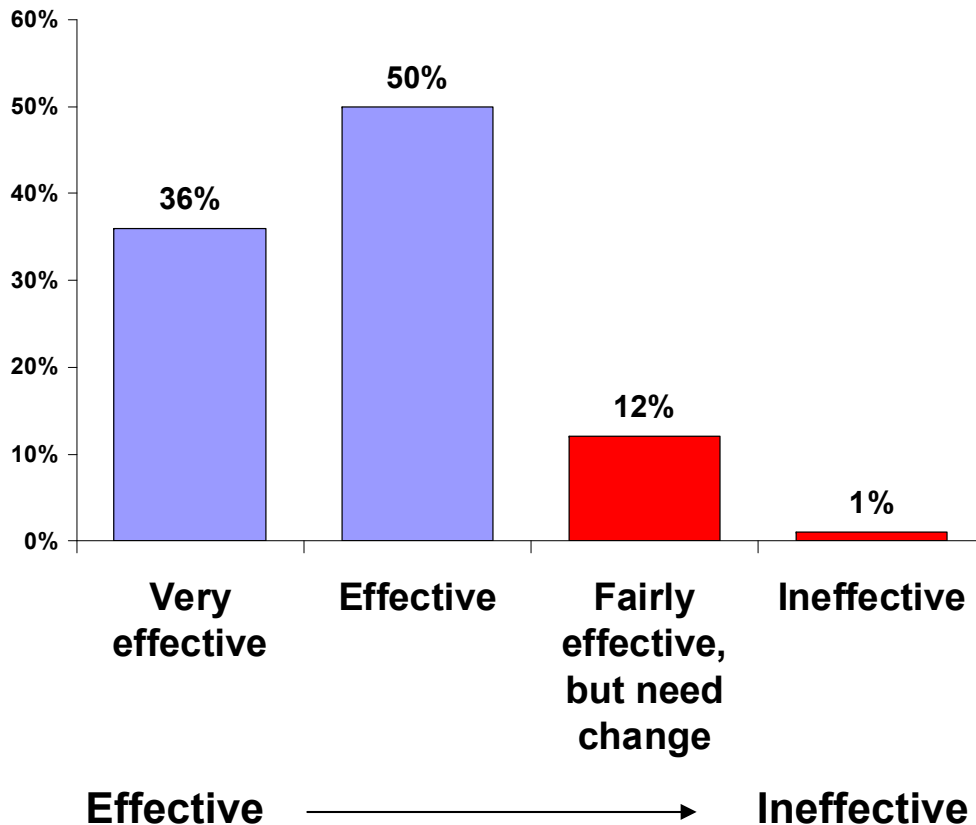


Are We There Yet?

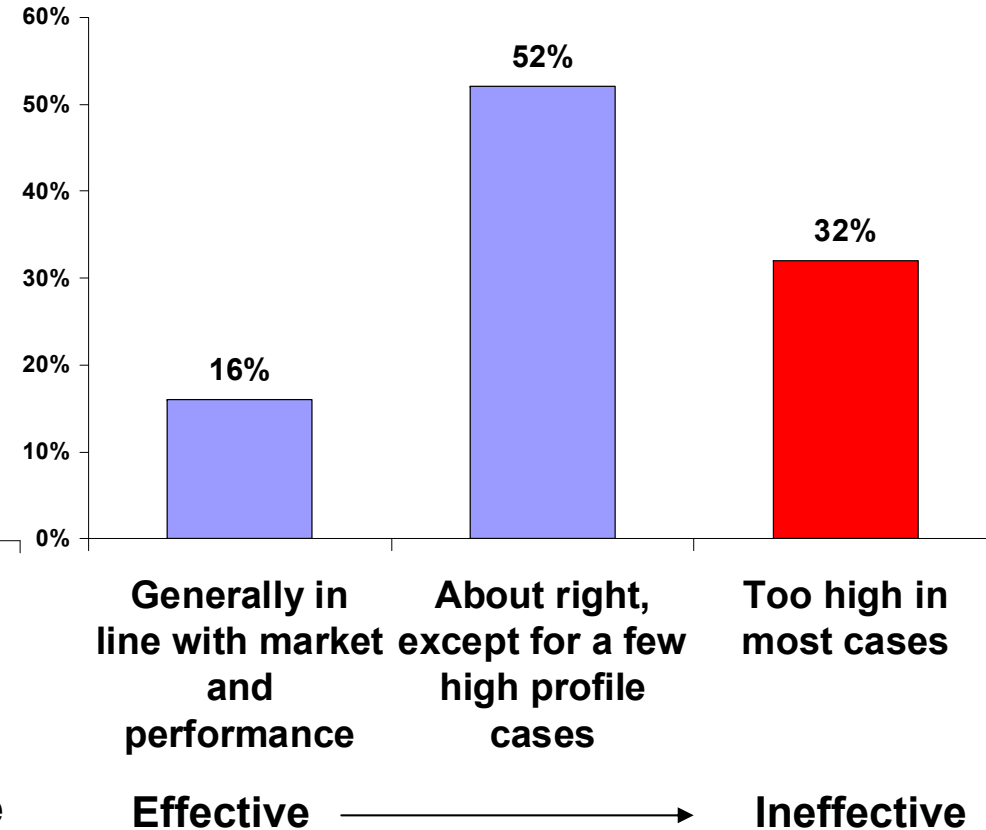
Board Directors generally feel that CEO compensation is effective at their companies, but often too high at others

## Survey of Board Directors

How do you feel about your company's CEO compensation program?

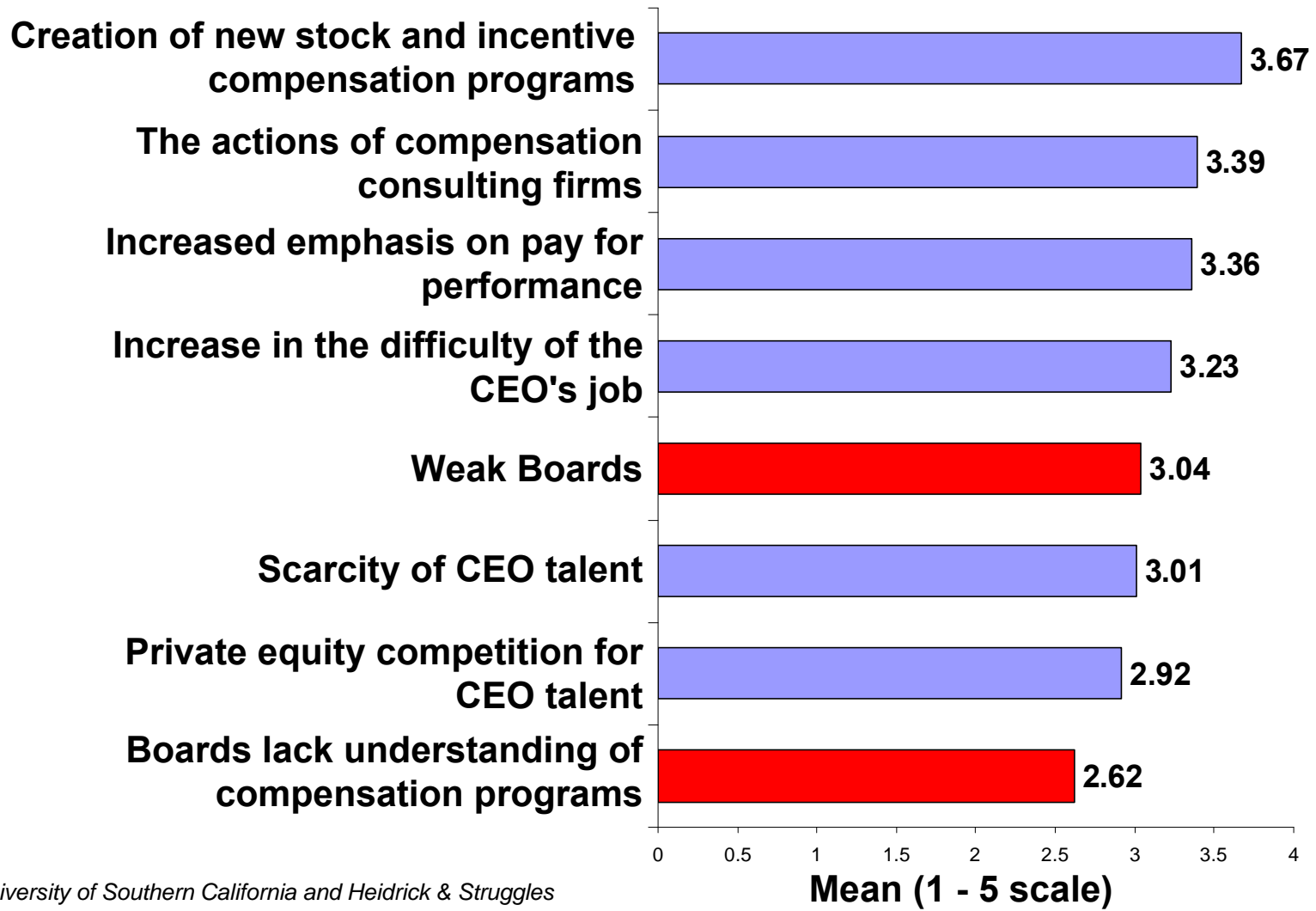


How do you feel about CEO compensation in general?



# Board Directors do not feel accountable for CEO pay escalation over time

How important do you think the following have been in increasing CEO compensation since 1980



Source: University of Southern California and Heidrick & Struggles

The performance side of the equation and forward projections are still blind spots

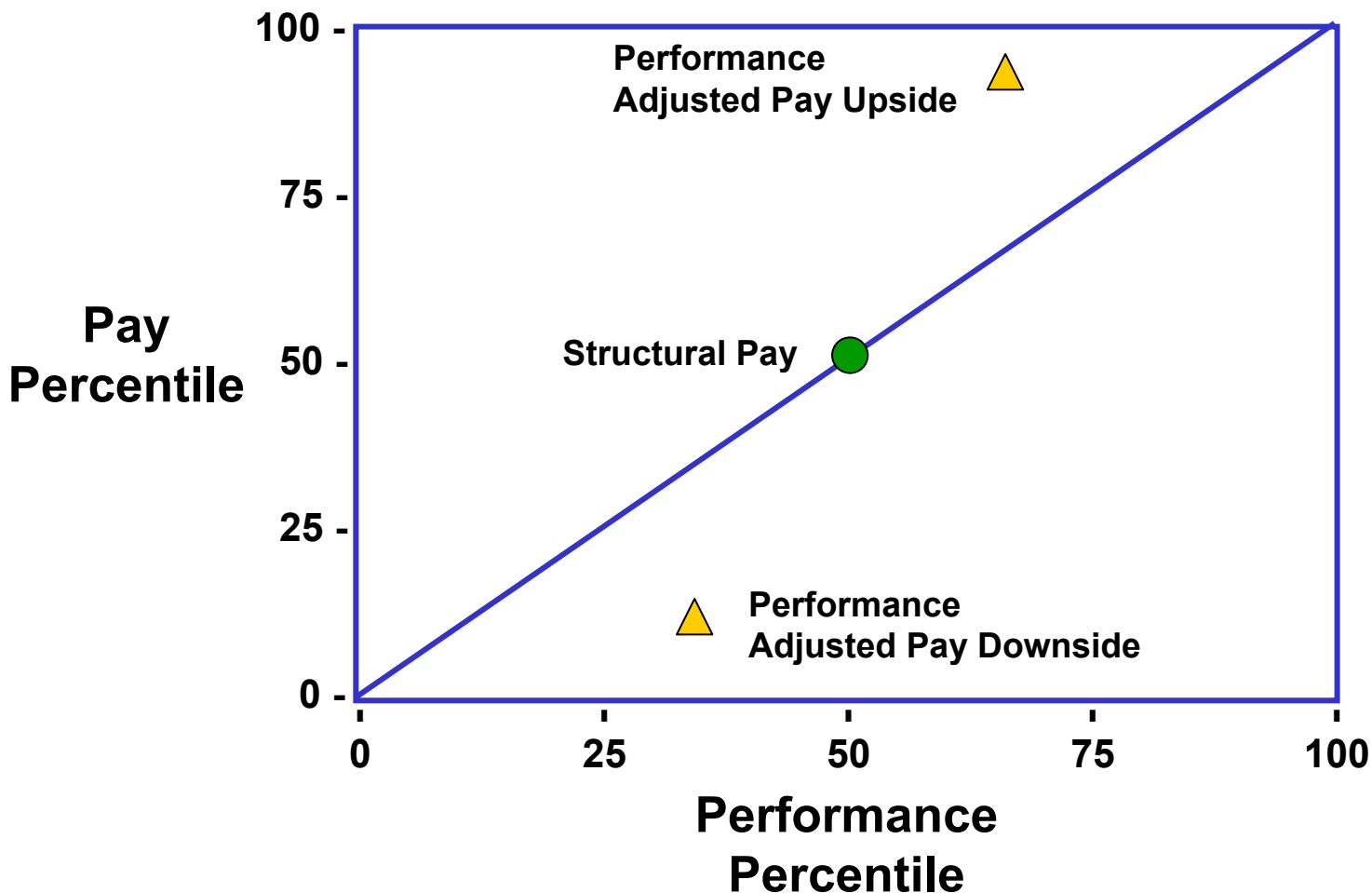
**Quality of Typical Executive Pay Assessment**

<b>Executive Pay</b>	<b>Performance Adjusted</b>	Poor	Non-Existent
	<b>Structural</b>	Good	Poor
		<b>Rear View</b>	<b>Forward Looking</b>

**Time Perspective**

A performance adjusted pay analysis yields high quality insight and discussion

### Pay for Performance Alignment





What Can You Do?

Compensation Committees need to effectively address the three Ps: Performance, Pay, and Processes

## THE THREE “PS”

Corporate and  
Executive  
Performance

The  
Organization

Executive  
Pay

Compensation  
Committee  
Processes

Each of the players in the process broadly tracks each "P"

## STAKEHOLDERS

**Corporate and Executive  
Performance:  
Shareholders**

**The  
Organization**

**Executive Pay:  
Executives**

**Executive Staff:  
HR, Finance, Legal**

**Compensation  
Committee Processes:  
Compensation  
Committee**

**Compensation  
Consultant**

Everyone wants the same things... but they don't always agree on how to get there

## STAKEHOLDER MODEL

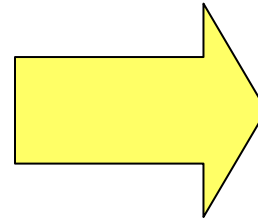
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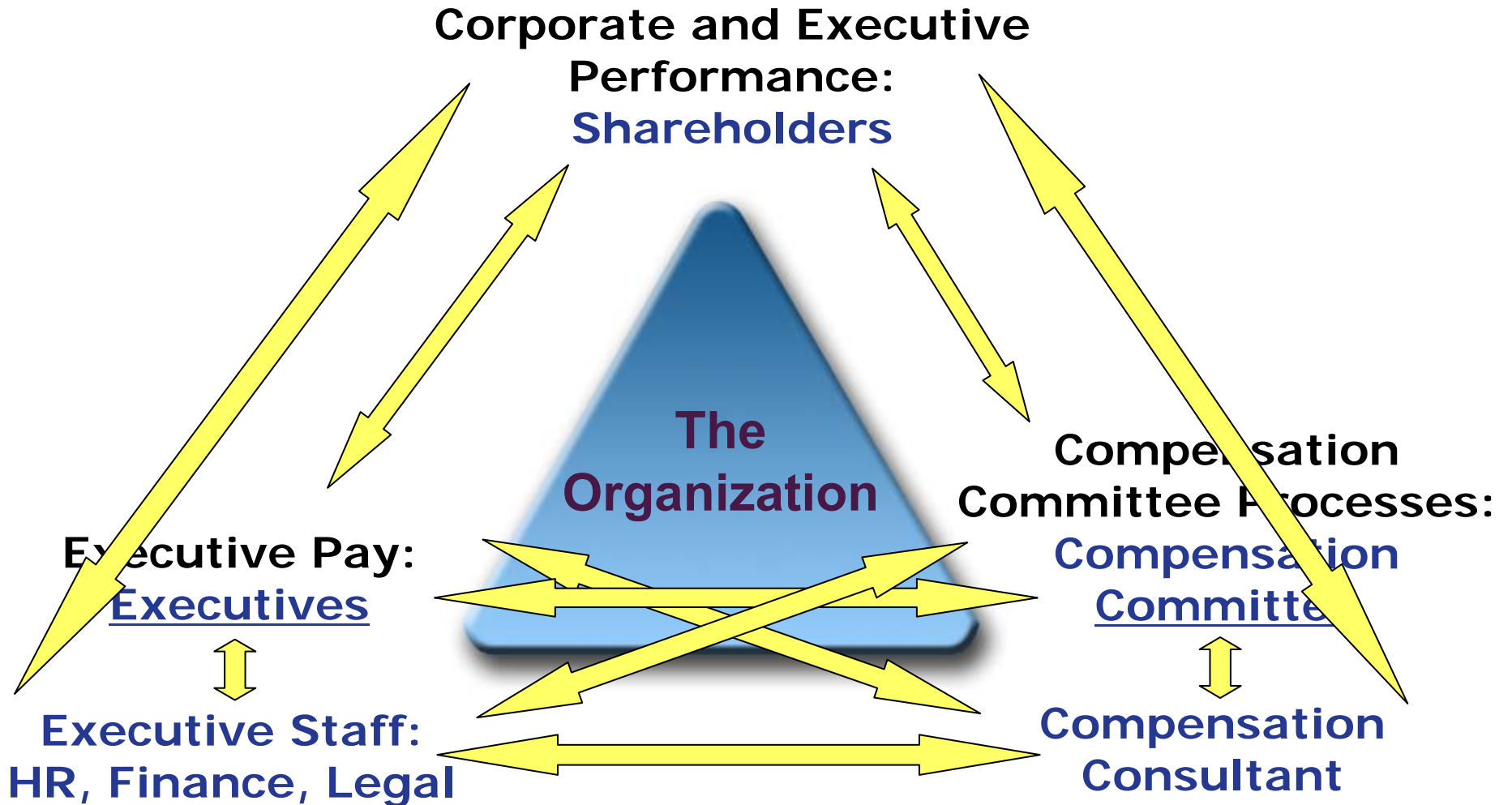


What Everyone  
Wants

- Positive outcomes
- High confidence/low exposure

Ideally, all players need to interrelate well in the process, although different motivations can create natural tensions


## STAKEHOLDER CONNECTIONS



# Stakeholder roles and behaviors still need to evolve in some organizations

## STAKEHOLDER ROLES

Stakeholders	Roles we like to see	Roles we sometimes see
<b>CEOs</b>	<ul style="list-style-type: none"> <li>▪ <b>Shareholder advocate</b></li> <li>▪ <b>Involved</b> in pay strategy and design</li> <li>▪ <b>Recommends</b> pay for executives other than him/herself</li> </ul>	<ul style="list-style-type: none"> <li>▪ Personal advocate</li> <li>▪ Executive advocate</li> </ul>
<b>Compensation Committee Chair</b>	<ul style="list-style-type: none"> <li>▪ <b>Shareholder advocate</b></li> <li>▪ Owns <b>governance</b> and <b>decision-making</b></li> <li>▪ Owns <b>pay</b> and <b>performance</b></li> </ul>	<ul style="list-style-type: none"> <li>▪ Peacekeeper</li> <li>▪ Copycat</li> <li>▪ Scared-y cat</li> </ul>
<b>Compensation Consultant</b>	<ul style="list-style-type: none"> <li>▪ <b>Shareholder advocate</b></li> <li>▪ <b>Trusted</b> advisor</li> <li>▪ <b>Fact-based opinions</b> and <b>advice</b> on pay, performance, and process</li> </ul>	<ul style="list-style-type: none"> <li>▪ Egomaniac</li> <li>▪ Management skill</li> <li>▪ Paint by numbers</li> </ul>
<b>Executive Staff</b>	<ul style="list-style-type: none"> <li>▪ <b>Shareholder advocate</b></li> <li>▪ <b>Assist</b> with process</li> <li>▪ <b>Trusted advisor</b></li> </ul>	<ul style="list-style-type: none"> <li>▪ CEO advocate</li> <li>▪ Control freak</li> <li>▪ Peacekeeper</li> <li>▪ Gatekeeper</li> <li>▪ Order taker</li> </ul>



# The good news is that you can make a real difference

<b>Steps</b>	<b>Queries</b>
<b>1. Assess</b> how well your organization is doing	<ul style="list-style-type: none"><li>▪ Do we have <b>positive outcomes</b>?<ul style="list-style-type: none"><li>- Good performance</li><li>- Happy and motivated executives</li><li>- Shareholders voting “yes”</li><li>- Media non-event</li></ul></li></ul>
<b>2. Diagnose</b> the issues	<ul style="list-style-type: none"><li>▪ Do we have the <b>right information</b>?<ul style="list-style-type: none"><li>- Pay and performance?</li><li>- Internal and external?</li><li>- Strategic and technical?</li></ul></li><li>▪ Do we have the <b>right actors</b> and <b>resources</b>?</li><li>▪ Are our <b>processes sound</b>?</li></ul>
<b>3. Solve</b> the problems	<ul style="list-style-type: none"><li>▪ Get explicit agreement from all the stakeholders that <b>we’re all working for the shareholders</b></li><li>▪ Help <b>manage</b> the <b>process</b>, <b>not</b> the <b>outcomes</b> (ultimately, the committee has decision rights)</li><li>▪ Play a <b>strong trusted advisor</b> role</li></ul>



# Discussion



About. . .

**FARIENT**  
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**PARTNERING  
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# Farient Advisors provides superior advice, information, and service on the three P's: Pay, Performance, and Processes

## Corporate and Executive Performance

- *Insights into business, talent, and industry, and implications for compensation design*
- *Analysis of shareholder value drivers, measures, and goal-setting*
- *Appropriate design of pay for performance outcomes*

## Executive Pay

- *Sound methodologies, applied with integrity, transparency, and consistency*
- *Fact-based analysis; opinion-based advice*
- *Clarity on appropriate executive value relative to shareholder value*



**Our Clients**

## Compensation Committee Processes

- *Complete independence, working for the Compensation Committee*
- *Processes geared to multi-year needs*
- *Stability and availability of seasoned and trusted resources*
- *Sensitivity to external developments*

### OUR PEOPLE

- *Experienced, trusted resources*
- *Driven toward optimal results for our Clients and their shareholders*
- *Long-term, relationship-oriented service*

### OUR PLATFORMS

- *Consistent methodologies and templates used for “baseline” work*
- *Standardized, thorough data collection platforms for clients that serve as reliable data repositories*
- *Web-based resources for clients*



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Executive Chair, Farient Advisors LLC



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*Phone:* (626) 799-2700

**Over the last 25 years, Ms. Robin A. Ferracone has dedicated herself to building businesses that align organizational systems with business strategy. She is founder and CEO of RAF Capital, a firm that makes strategic investments in HR-related businesses, one of which is Farient Advisors. Farient Advisors, of which she is Executive Chair, helps Compensation Committees make performance-enhancing, defensible, and timely executive compensation decisions that are in the best interests of the Company's shareholders. Ms. Ferracone provides executive advisory services to public and private companies.**

**Prior to her roles at RAF Capital and Farient Advisors, Ms. Ferracone was President of Mercer's global Human Capital division. Prior to Mercer, Ms. Ferracone was President/Chairman of SCA Consulting, an executive compensation consulting firm she co-founded and was sold to Mercer in 2001. Ms. Ferracone serves on the Duke University and Harvey Mudd College Boards. She has an MBA from the Harvard Business School and a BA from Duke University.**



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**John Borneman is a Senior Vice President with Farient Advisors. Mr. Borneman has over 10 years of experience advising Compensation Committees regarding executive compensation and rewards issues. Mr. Borneman's areas of expertise include developing pay strategies, identifying performance metrics, and calibrating performance goals to align pay with business needs and shareholder interests. He is a thought leader in the area pay for performance, and he is a regular speaker on the topic of selecting the right measures for rewards programs and aligning rewards with performance.**

**Mr. Borneman's previous experience includes Mercer Human Resource Consulting, where he was a Principal in the Executive Compensation practice area and developed many of the firm's standards for performance measurement. Prior to Mercer, he was with SCA Consulting, which was acquired by Mercer in 2001.**

**Mr. Borneman holds an MBA from the University of Chicago and an undergraduate degree from the University of Michigan.**