THE WALL STREET JOURNAL / HAY GROUP 2014 CEO COMPENSATION STUDY

Cooking up a better pay mix:
Active shareholders as a new ingredient

Irv Becker – US Leader – Board Solutions
November 2015

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CEO PAY CONTINUES TO RISE AS SHAREHOLDERS SAW COMPANIES ACHIEVE SOLID PERFORMANCE GAINS

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AGENDA

PRESENTATION OVERVIEW

1 Overview of findings

- What did another year mean for CEO pay in 2014?

2 Examples of changing programs

- How did companies respond to Say-on-Pay votes and shareholder outreach?

3 What's next?

- What will be 2014's lasting impact on executive pay in the United States? What will we see in 2015 & 2016?

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01 OVERVIEW OF FINDINGS

OVERVIEW OF FINDINGS

ABOUT THIS STUDY

- Hay Group's eighth year partnering with *The Wall Street Journal* on the study
- 300 U.S. public companies:
  - Median FY 2014 revenues of $18.3 billion
- Proxy filings between May 1, 2014 – April 30, 2015
- CEO pay for FY 2014

FULLY ONLINE AND INTERACTIVE

Full database can be found at wsj.com / execpay

OVERVIEW OF FINDINGS

COMPONENTS OF COMPENSATION IN THE STUDY

COMPENSATION COMPONENTS

	Base Salary
+	Annual Incentives
=	**Total Cash Compensation**
+	Long-Term Incentives
=	**Total Direct Compensation**
+	All Other Compensation + Change in Pension Value + Non-Qualified Deferred Compensation Earnings
=	**Total Compensation**

OVERVIEW OF FINDINGS
US COMPANY PERFORMANCE IN 2014

MORE BALANCE BETWEEN SHAREHOLDER PERFORMANCE AND FINANCIAL PERFORMANCE WAS DISPLAYED IN 2014

Companies demonstrated solid year-over-year top- and bottom-line growth (median revenue growth of 4.5% / median net income growth of 6.6%) with the market responding to these levels of performance

Shareholders had another strong year, with companies in our sample achieving a **median TSR** of nearly

17%

That improved profitability resulted more from increased efficiency rather than from growth

GDP and wage growth in the US were fairly modest, with low inflation

Companies that had issued debt at historically-low interest rates and had made capital investments in their core businesses began to reap some of the benefits in improved operating efficiency, managing to 'do more with less'

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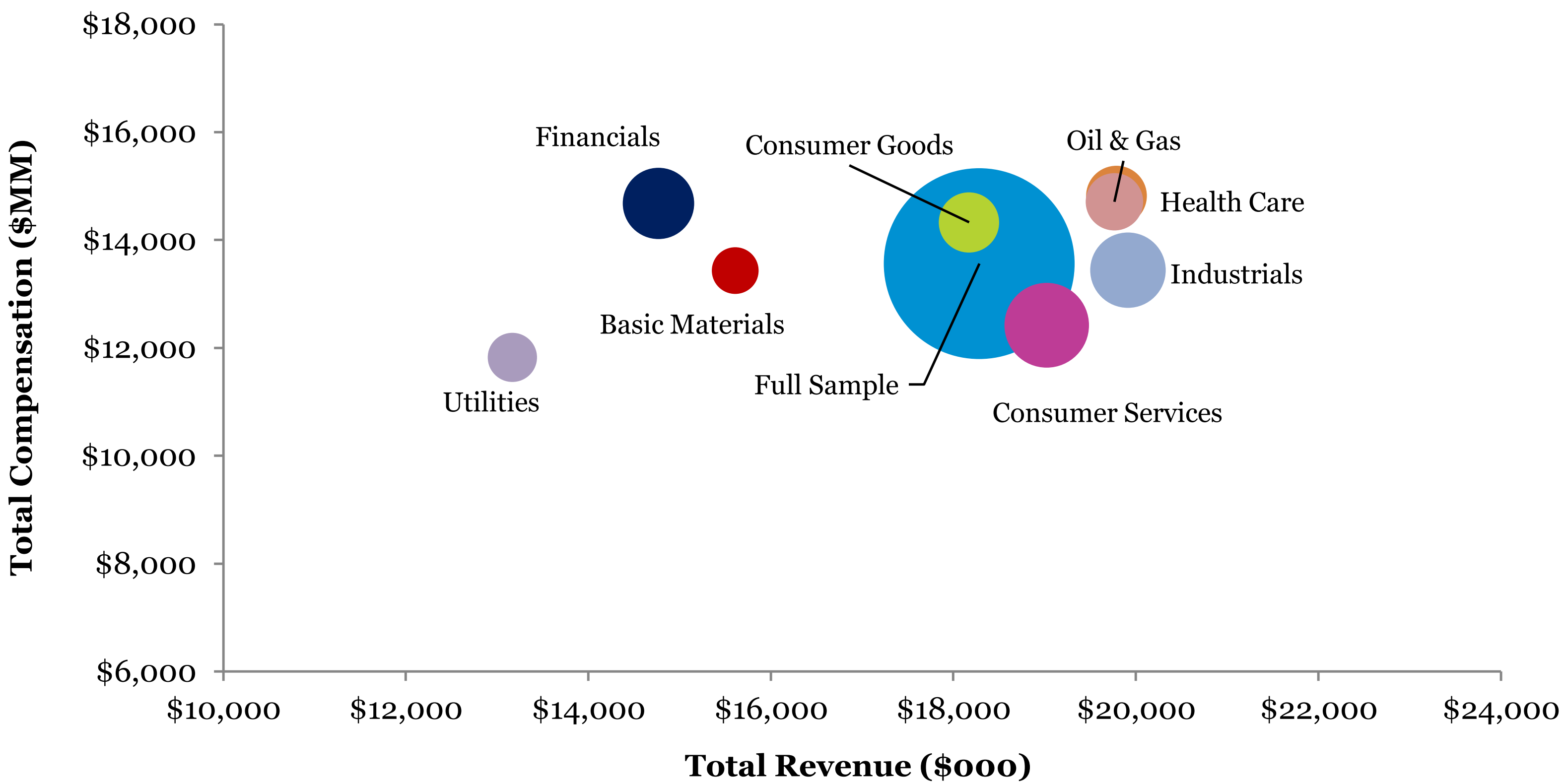
OVERVIEW OF FINDINGS

SNAPSHOT – CEO PAY AND REVENUE BY INDUSTRY

- Our sample shows that **larger company CEOs generally make more** than that of smaller companies

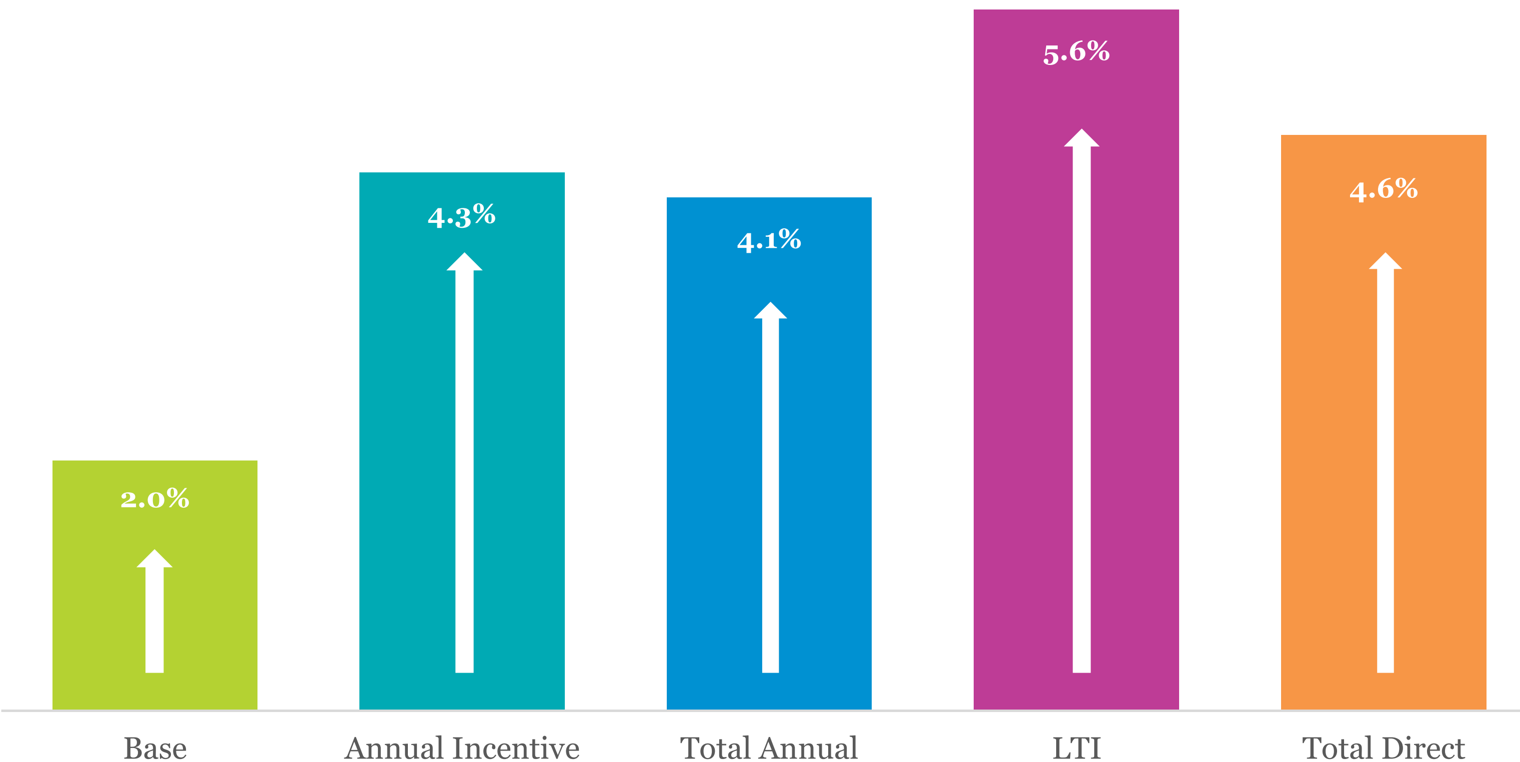


OVERVIEW OF FINDINGS

MEDIAN CEO COMPENSATION INCREASES AND VALUES

- As a result of performance, **bigger bonuses and LTI grants drove meaningful increases in total direct compensation**, which increased 4.6% over 2013 pay levels

Base Salary	Annual Incentive	Total Annual	LTI	Total Direct
$1,235,693	**$2,510,988**	**$3,674,628**	**$8,103,758**	**$11,798,322**

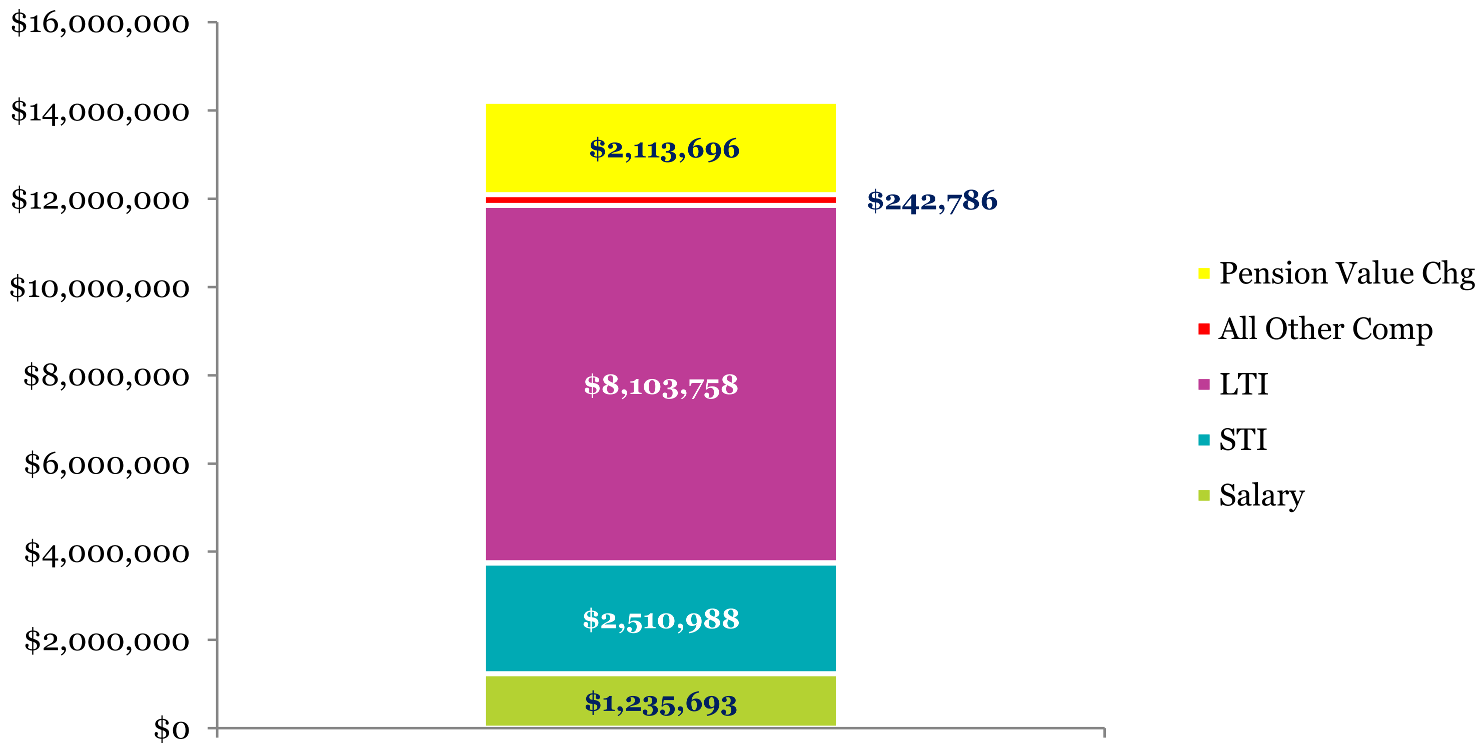


Note: Individual values represent medians that should not be added.

OVERVIEW OF FINDINGS

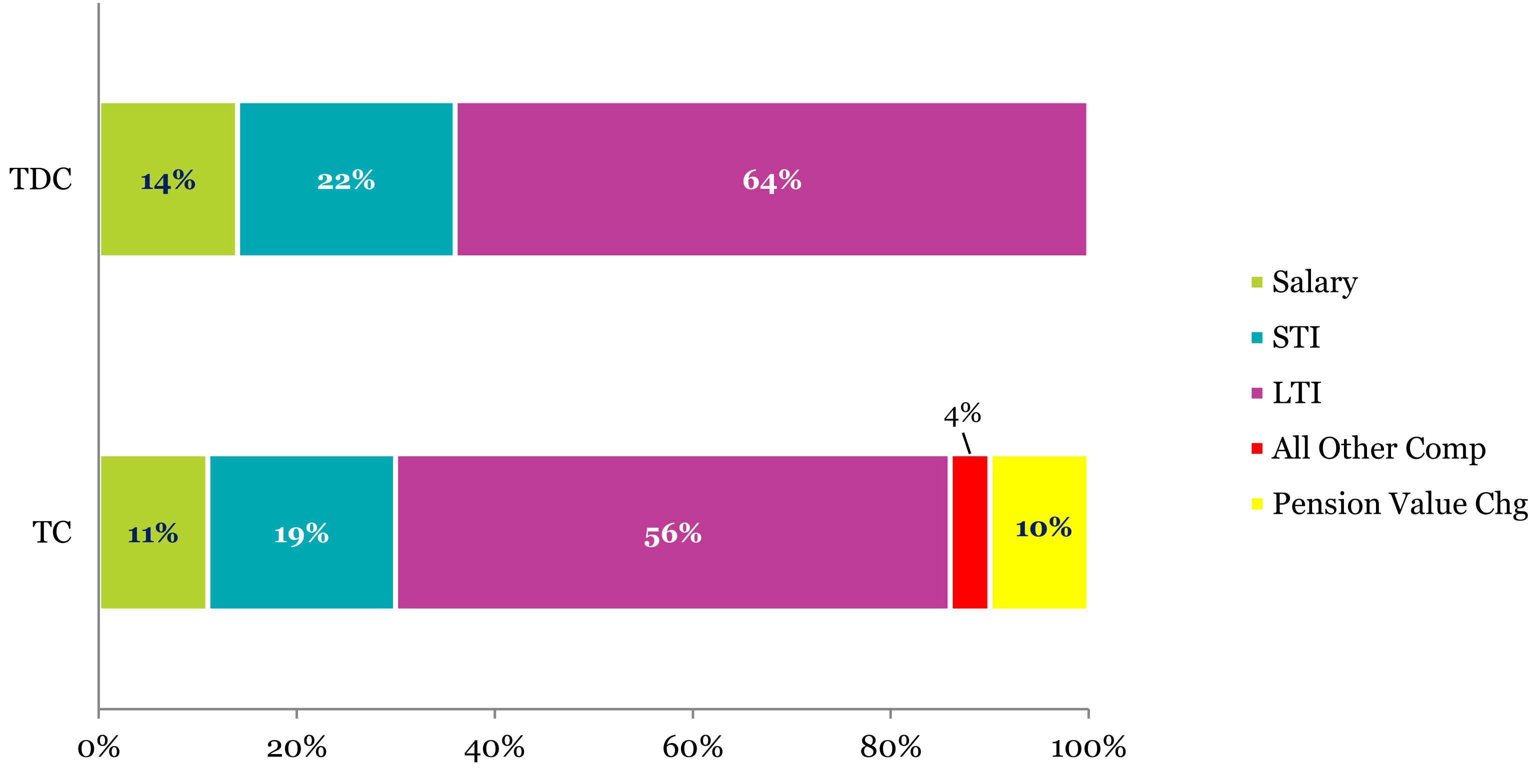
SNAPSHOT – MEDIAN CEO TOTAL COMPENSATION

- Total compensation comes in at **$13.6 million**



OVERVIEW OF FINDINGS
MIX OF ELEMENTS – MEDIAN CEO

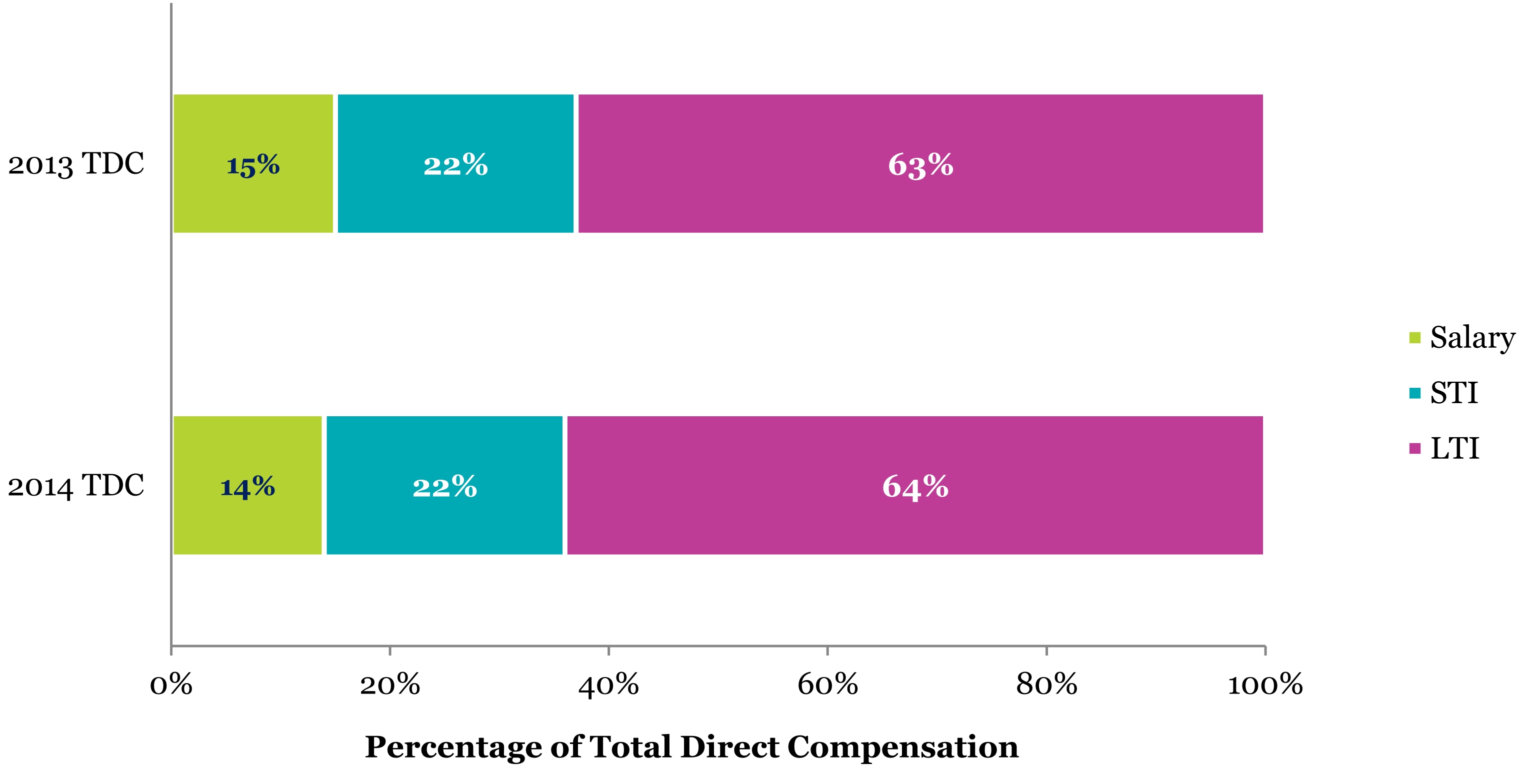
- In the US, **long-term incentives always maintain the heaviest emphasis within CEO pay** – which is very different from the practices in other parts of the world



OVERVIEW OF FINDINGS

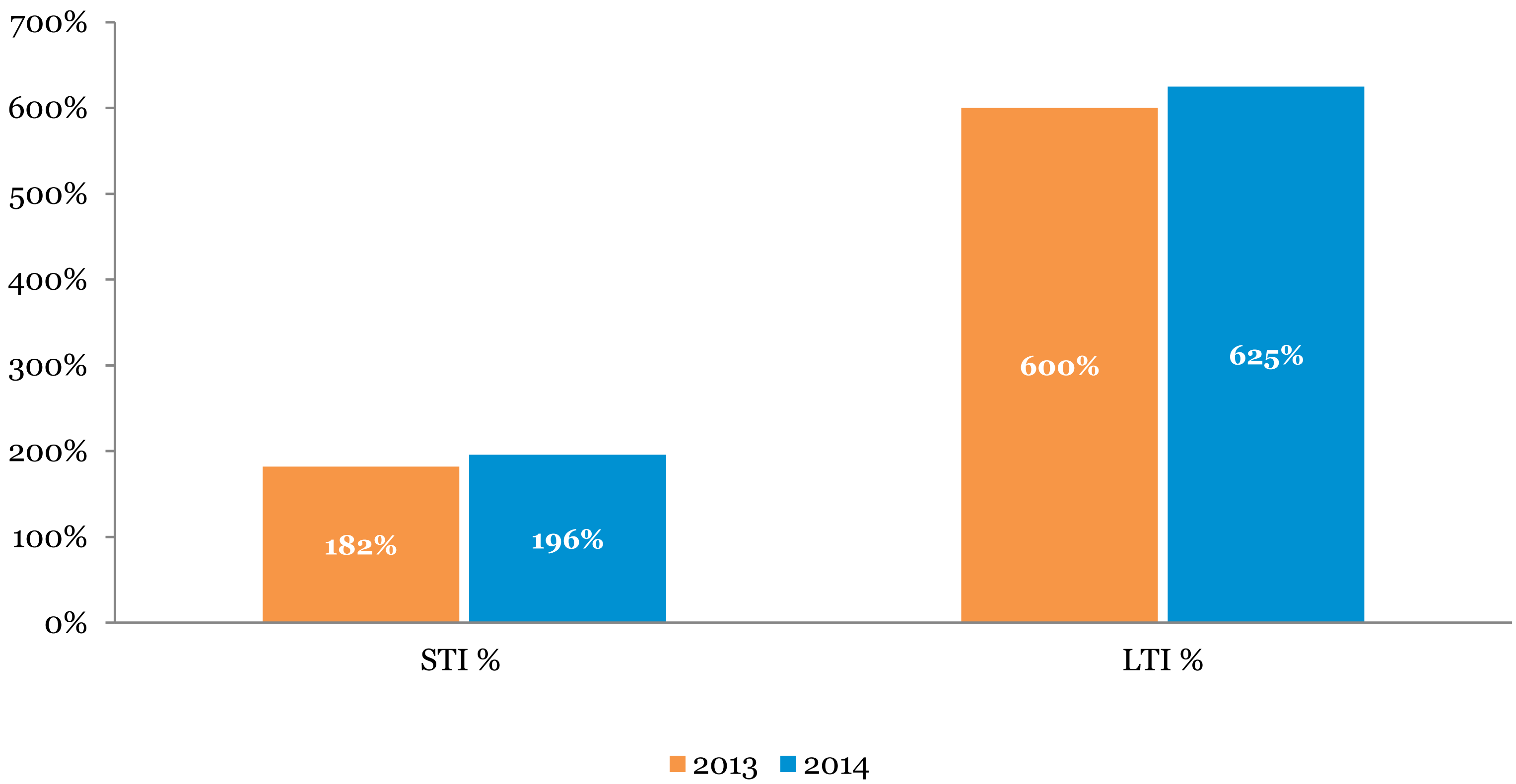
CHANGE IN CEO PAY MIX – 2013 VS. 2014

- **Pay mix has remained steady** year-over-year



OVERVIEW OF FINDINGS
INCENTIVES AS A % OF BASE

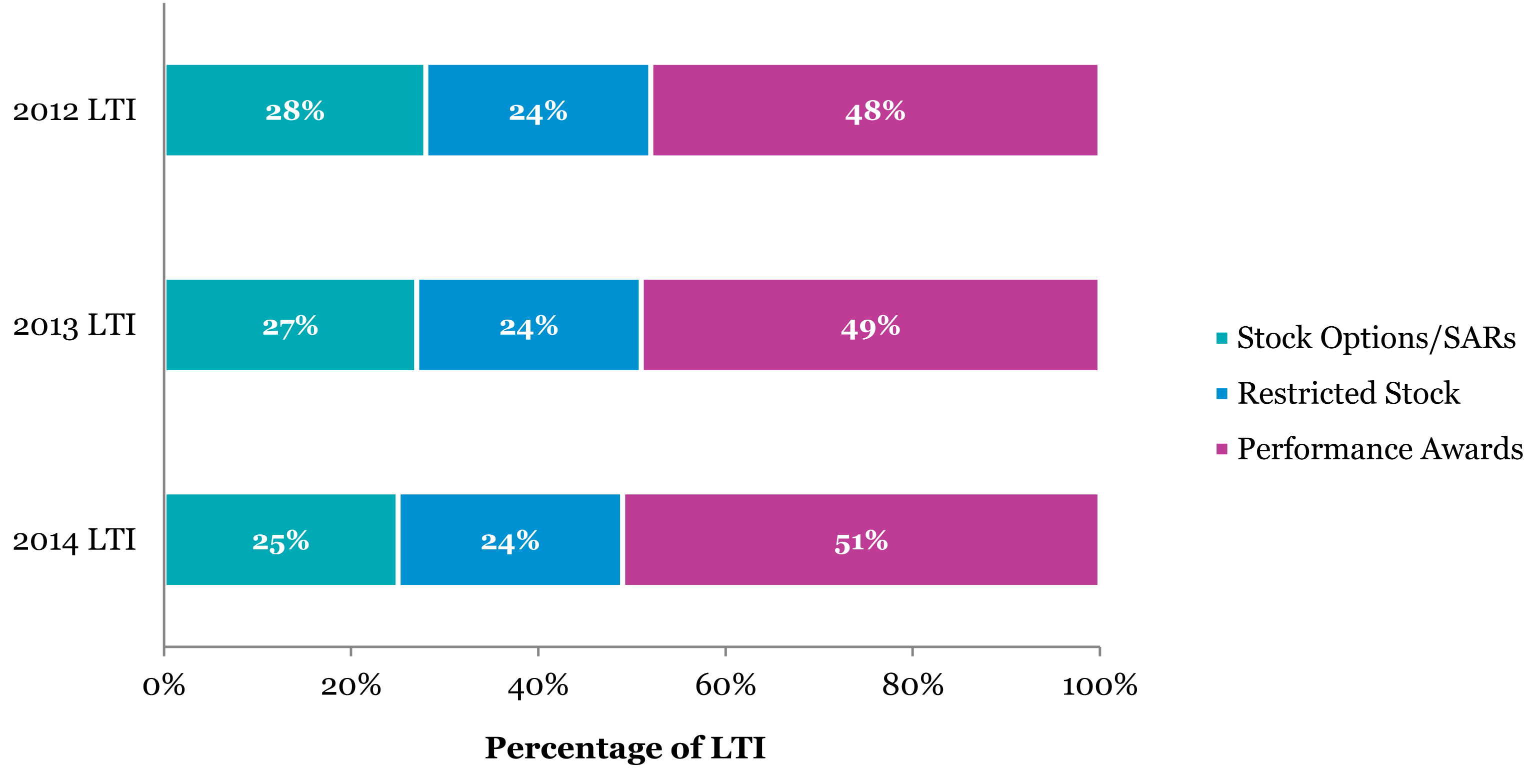
- Annual and long-term incentive **payout percentages exhibited meaningful increases**



OVERVIEW OF FINDINGS

CHANGE IN CEO LONG-TERM INCENTIVE MIX – 2013 VS. 2014

- The **emphasis on performance awards increased to their highest levels ever**, as emphasis on stock options continues to decline over time



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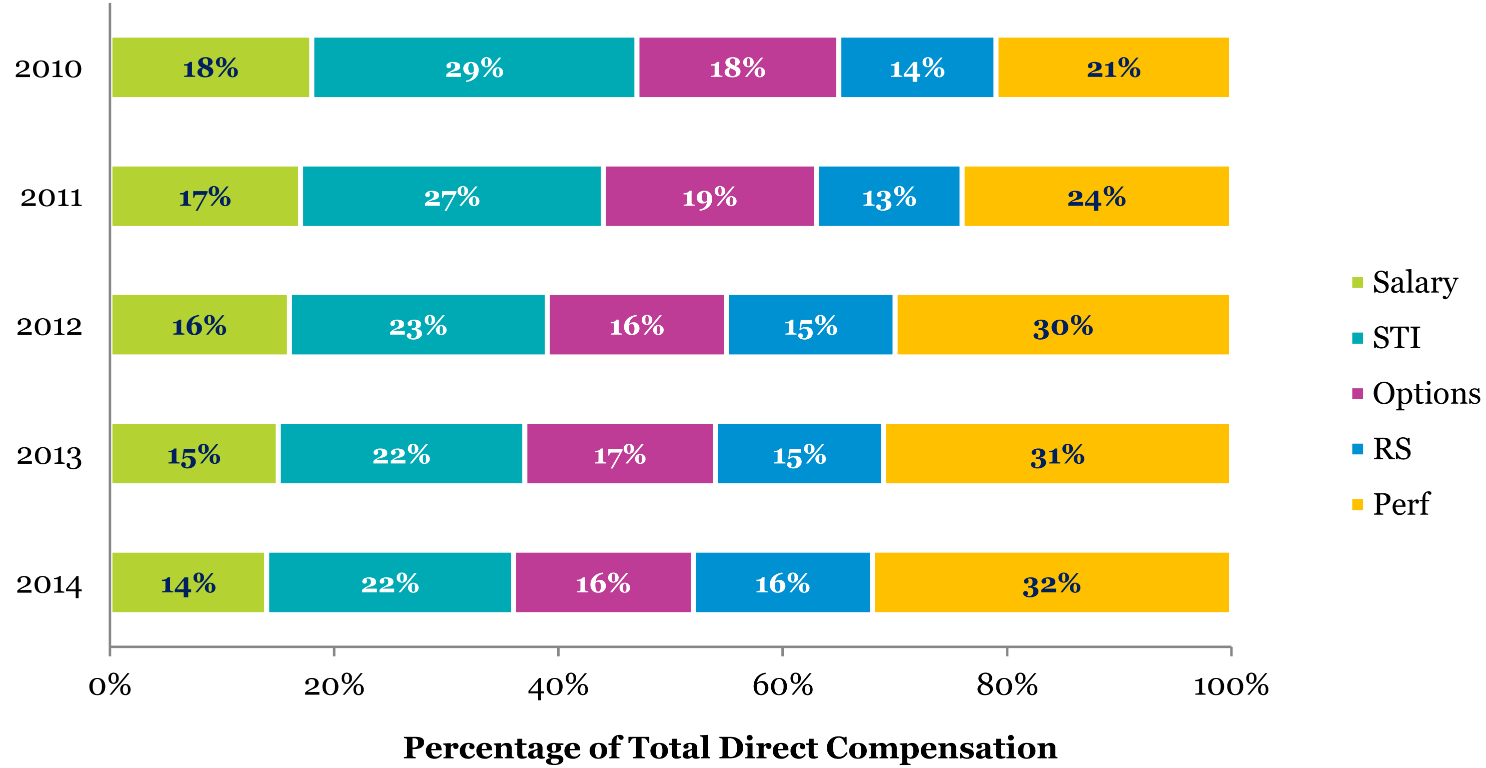
OVERVIEW OF FINDINGS

HISTORICAL VIEW: TOTAL DIRECT COMPENSATION MIX

- Over the last five years, **emphasis on performance awards has gradually increased** (and appears to have begun to steady), while **emphasis on base salary has declined**



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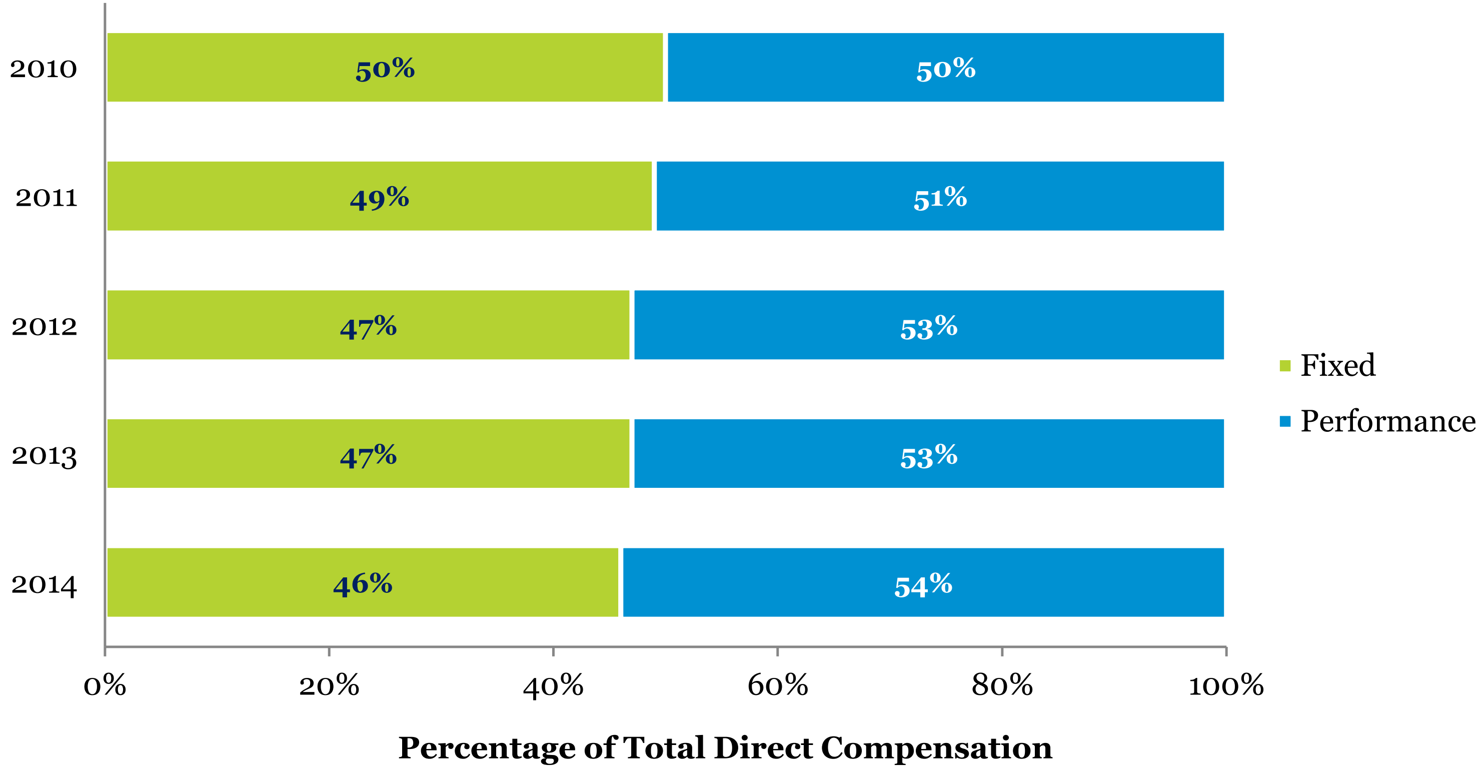
HISTORICAL VIEW: 'FIXED' VS. PERFORMANCE PAY

- Over time, the **balance continues to shift from 'fixed' or 'time-vested' (base + options + restricted stock) to the performance-oriented (annual incentive plans + performance-vested LTI)**



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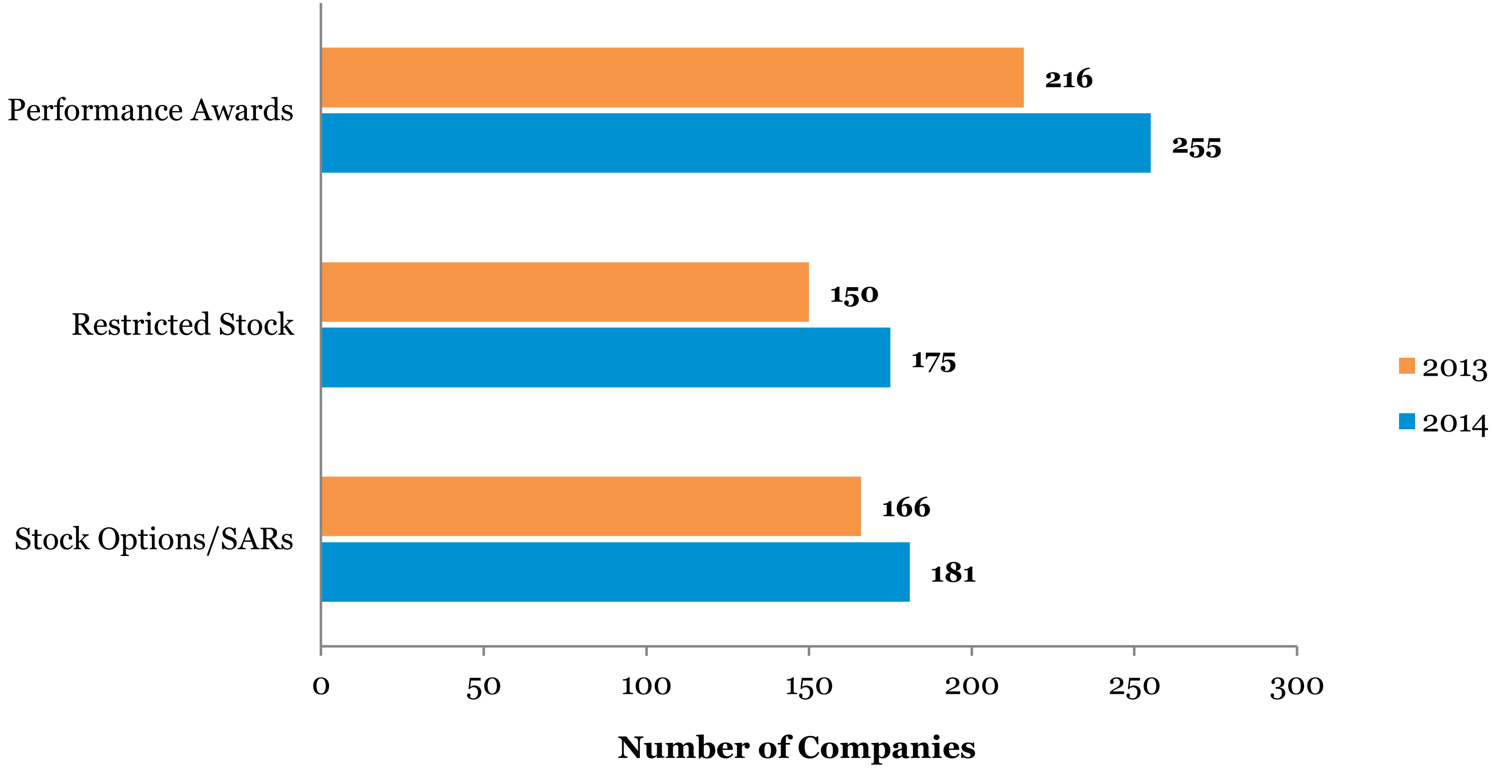
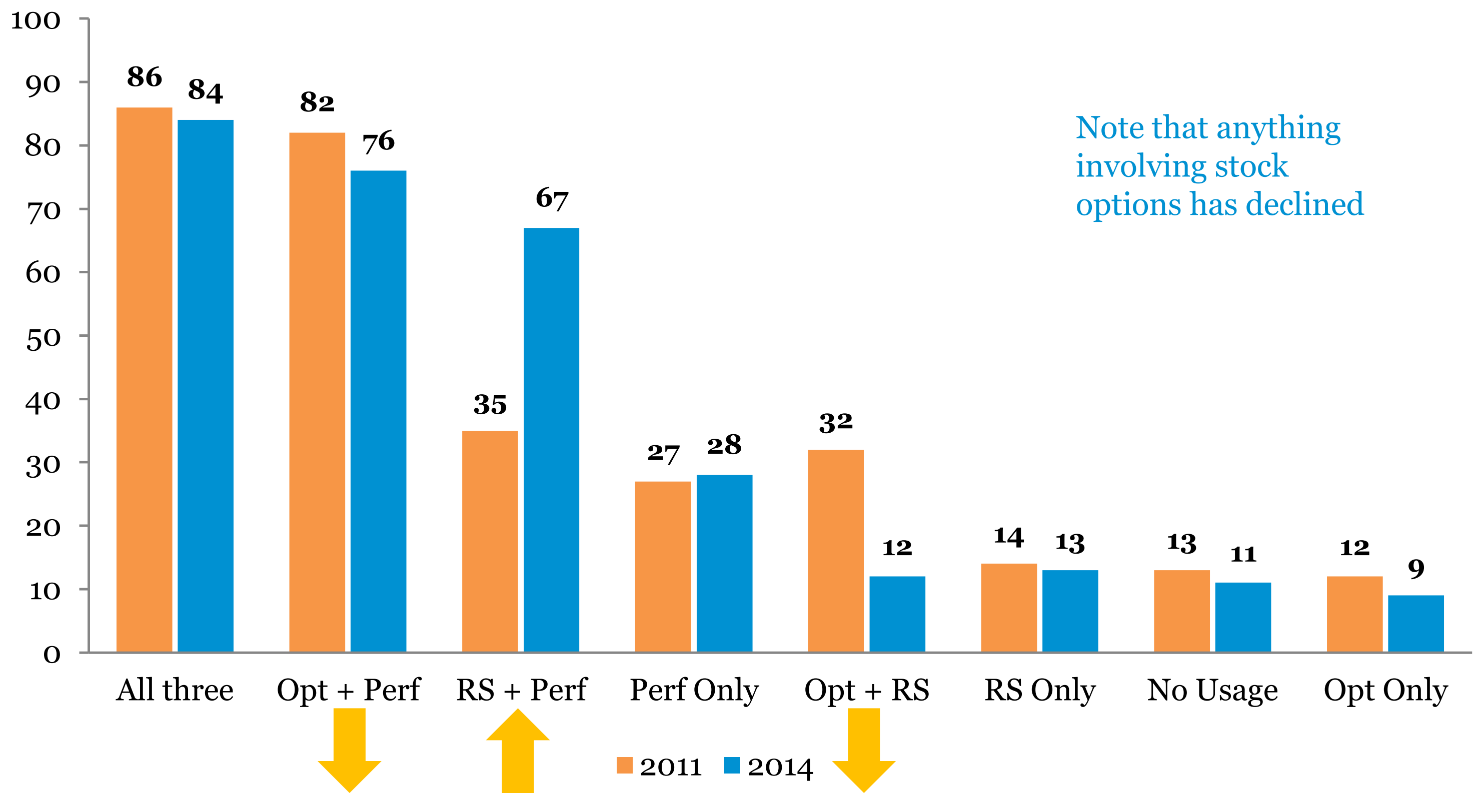
CHANGE IN CEO LONG-TERM INCENTIVE PREVALENCE – ALL INCUMBENTS

- **Performance awards continue to reign as the most widely-used vehicle**, with the biggest jump in usage. However, every equity vehicle increased in prevalence



OVERVIEW OF FINDINGS
USE OF LTI PORTFOLIOS

- The most widely-used 'portfolio' includes use of all three LTI vehicles, with over 80% using more than one vehicle. Over a three-year period, the biggest increase has been seen in RS + performance awards, while the biggest drop has been in options + RS



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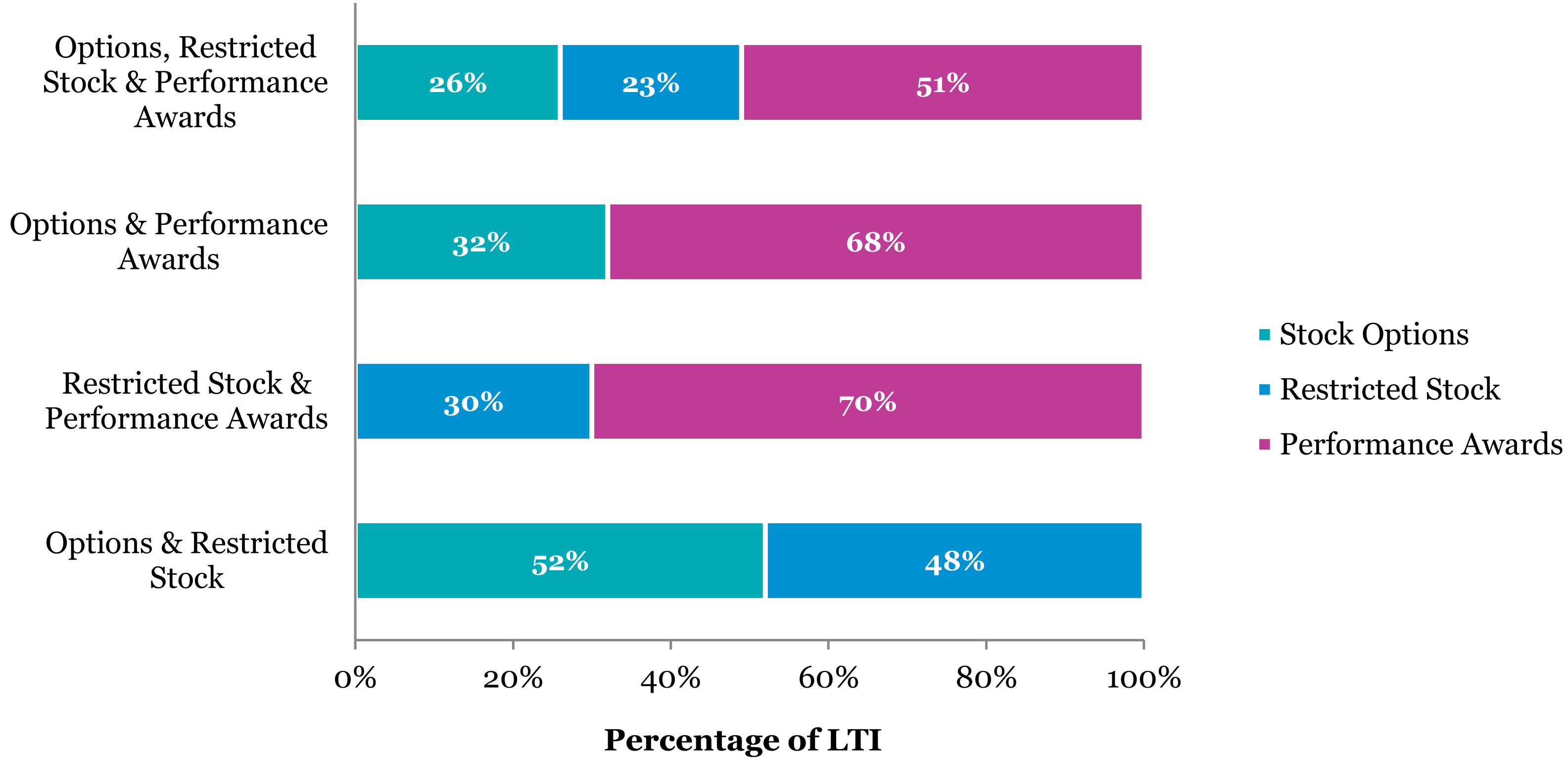
CEO LTI PORTFOLIO MIX

- Companies taking a **'portfolio' approach emphasize performance plans** over the other vehicles, while **restricted stock has the least emphasis** within the portfolio



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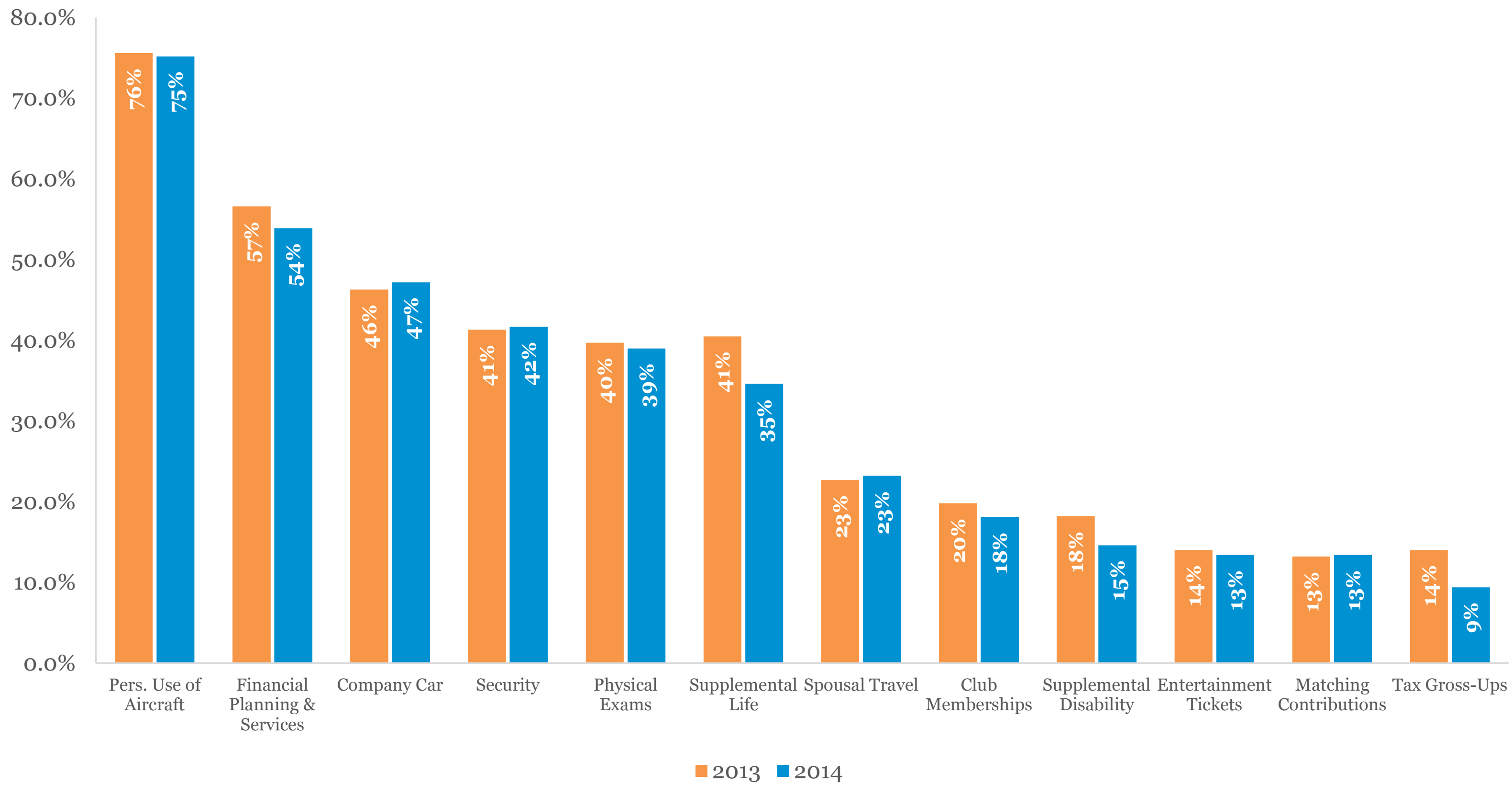
PERQUISITES – 2013-2014

- **Nearly every perk in our study declined year over year.** The biggest drops were seen in supplemental life insurance and tax gross-ups, while only personal aircraft use and financial planning remained in over half of companies



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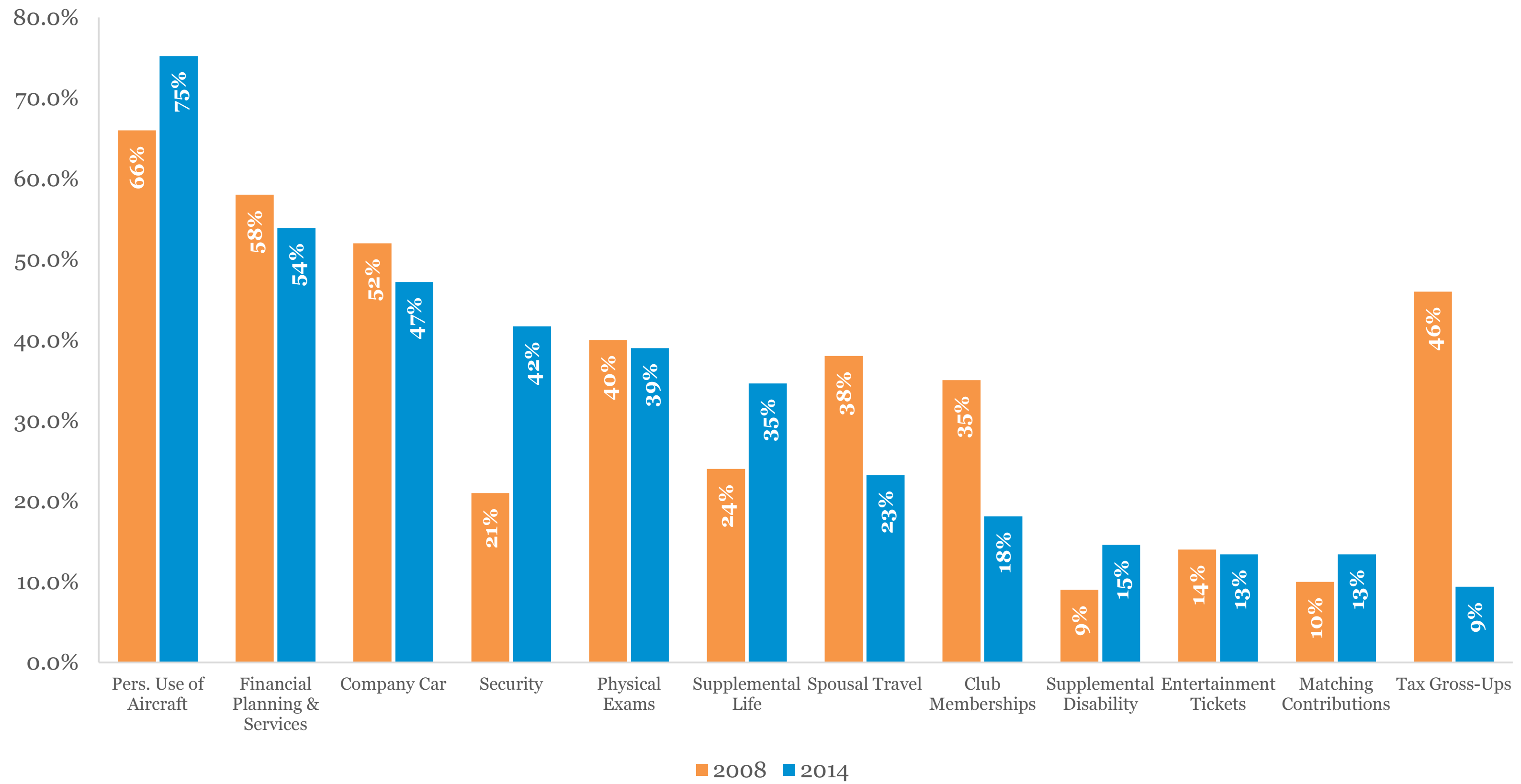
OVERVIEW OF FINDINGS

PERQUISITES – 2008-2014

- Looking over a 6-year period shows just how far perquisites have fallen. **Tax gross-ups, clubs, and spousal travel have declined the most substantially**, while personal aircraft use, personal security, supplemental life, and supplemental disability have actually increased



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TOP 10 – 2013 VS. 2014

- **Six CEOs appeared in the top 10 in both 2013 and 2014 – nearly all of whom run media companies** that now routinely sit a the top of the list in pay levels. Their pay positioning is in large part due to their size, scale, operating complexity, talent profile, and pay volatility in the sector

2013		
Company	**Executive**	**TDC**
Oracle	Lawrence J. Ellison	$78,060,229
CBS	Leslie Moonves	$64,358,386
Liberty Global	Michael T. Fries	$45,530,779
Viacom	Philippe P. Dauman	$36,778,696
Disney	Robert A. Iger	$33,352,517
Time Warner	Jeffrey L. Bewkes	$32,374,826
Estee Lauder	Fabrizio Freda	$30,941,918
Aetna	Mark T. Bertolini	$30,429,180
ExxonMobil	Rex W. Tillerson	$27,641,625
McKesson	John W. Hammergren	$27,164,283
	Median	$32,863,672
	Average	$40,663,244

2014		
Company	**Executive**	**TDC**
Liberty Global	Michael T. Fries	$110,607,895
Microsoft	Satya Nadella	$84,296,026
Oracle	Lawrence J. Ellison	$65,720,985
Qualcomm	Steven M. Mollenkopf	$60,619,442
CBS	Leslie Moonves	$53,013,427
Viacom	Philippe P. Dauman	$43,788,679
Disney	Robert A. Iger	$42,592,600
Actavis	Brenton L. Sauders	$36,558,642
Time Warner	Jeffrey L. Bewkes	$32,469,657
Liberty Interactive	Gregory B. Maffei	$32,149,260
	Median	$48,401,053
	Average	$56,181,661

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02 EXAMPLES OF CHANGING PROGRAMS

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EXAMPLES OF CHANGING PROGRAMS

COMPANIES RESPOND TO SAY-ON-PAY VOTES AND SHAREHOLDER OUTREACH

In 2014, **shareholder outreach intensified** as companies engaged investors throughout the year to identify and discuss pay issues that mattered most to them

- Following those meetings, companies often listened to the expressed concerns and recommendations of shareholders, with **many adopting substantial changes to their pay programs**
- In particular, companies have made **pay mix changes** that will be reflected immediately in 2014 and going forward

The most common types of changes seen in 2014 involved the following four areas:

- Adopted performance-based equity vehicles
- Enhanced emphasis on performance-based equity vehicles at the expense of time vested equity vehicles
- Redesigned STI and LTI programs with new performance metrics
- Enhanced disclosure and presentation in CD&A

We have seen pay mix evolve over the past 5+ years, but more so in 2014 as **shareholders stepped up their involvement in the pay process**

EXAMPLES OF CHANGING PROGRAMS

COMPANIES RESPOND TO SAY-ON-PAY VOTES AND SHAREHOLDER OUTREACH CONT'D

Company	New LTI Vehicle	Increased Emphasis on Perf-Based LTI	New Perf Metrics	New Incentive Caps	Perf Period / Goal-Setting Adjustment	STI Redesign	Enhanced Proxy Disclosure
Target	✓	✓	✓			✓	
Merck			✓		✓	✓	
Hess	✓	✓					
Republic Services	✓	✓	✓				✓
Huntsman	✓			✓		✓	✓
Manpower Group		✓	✓		✓		
Corning		✓	✓	✓		✓	
Aetna	✓				✓		
Avon Products			✓	✓	✓	✓	

- Most pay program changes in response to shareholders observed within our sample included **increased emphasis on performance-based LTI** and **new performance metrics**

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EXAMPLES OF CHANGING PROGRAMS

COMPANIES RESPOND TO SAY-ON-PAY VOTES AND SHAREHOLDER OUTREACH CONT'D

Company	Historical SOP Support	Pay Program Change	Shareholder Engagement?
Target	2014: 77.9% 2013: 52.1%	• **Introduced PBRSUs** – 100% of LTI mix tied to performance • **Added ROIC** to PSU plan • **Redesigned STI program** by adding new performance metrics	✓
Merck	2014: 96.6% 2013: 88.8%	• **Introduced a new PSU program** with rTSR and OCF, measured over a cumulative 3-year period (rather than three distinct 1-year periods) • **Streamlined company scorecard** to focus on critical performance metrics – revenue, EPS, and pipeline	✓
Hess	2014: 97.2% 2013: 71.4%	• **Decreased weighting on time-based RS** • **Increased weighting on PSUs**, raising the performance-based component from 50% to 80% • **Re-introduced stock options**	✓
Manpower Group	2014: 96.2% 2013: 80.6%	• **Return to 3-year performance period** for PSUs • **Replaced Economic Profit with ROIC** • **Increased emphasis on PSUs** to represent over 60% of long-term equity grants to NEOs	✓

03 WHAT'S NEXT?

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WHAT'S NEXT?

LOOKING BACK AT 2014/2015

Most companies continue to receive strong shareholder support for their pay programs

- Shareholders spoke and companies listened
- Pay mix continues to evolve as companies enhance their pay for performance reinforcement
- Performance share plans continue to be the enabler for the new, more shareholder friendly, compensation mix. Some companies are going farther than the 50% standard design

Shareholder outreach continues to pick up steam with no slow-down in sight

- Outreach activity continues to intensify and should carry into 2015

Companies are working hard at **improving pay program disclosures**

- More explanation and rationale on pay decisions and structure are becoming the norm within the CD&A
- More depth can be found today with respect to annual incentive and performance-based LTI disclosures

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WHAT'S NEXT?

ISS

ISS continues to be the dominant proxy advisory firm

- While the majority of large institutional shareholders continue to follow them, some have developed their own pay 'playbooks'

ISS has become more flexible and continues to improve its approach

- ISS has refined its approach to evaluating pay programs in each of the last three years and so far changes have generally been viewed favorably by corporate issuers and compensation consultants

Biggest pay related change for 2015 was a **change to how ISS evaluates equity plans**

- ISS adopted a 'scorecard' model that considers a range of positive and negative factors rather than a series of 'pass' or 'fail' tests to evaluate equity plan proposals

ISS has made strategic acquisitions to enhance its rigor in evaluating pay programs

- ISS acquired Incentive Lab in the Fall of 2014 to bolster its ability to benchmark performance-based compensation and assess the rigor of performance targets

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WHAT'S NEXT?

STAYING AHEAD OF SAY-ON-PAY

Shareholder outreach seems to be working in optimizing pay program support

- This is much easier to do with shareholders during consecutive strong TSR years

The **poor TSR year has not yet happened** in the era of mandatory SOP

- Building a close relationship now with your largest shareholders can help make the conversation easier when the market takes a downward turn
- The effectiveness of shareholder outreach efforts will really be tested in a poor TSR year

Aligning pay and performance will be a 'two-way street' between companies and their shareholders

- Companies have listened to shareholders and gave them a nod with respect to making pay programs more about performance in 2014
- However, aligning the pay program with the intended business strategy will require some trust on the part of shareholders as not all pay program changes should be about 'checking the box'

QUESTIONS?

Irv Becker
US Leader – Board Solutions
T: (215) 861-2495
E: Irv.Becker@haygroup.com

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ABOUT HAY GROUP

We believe that it's people who make change happen. So, while we operate on a global scale, we keep the individual at the very centre of our thinking.

We're world-sized: 4,000 employees, 87 offices, 49 countries. We draw on management data from over 125 national centres. We work alongside more than 8,000 organizations in the private, public and not-for-profit sectors, across every major industry, in virtually every corner of the earth.

We're focused: on people – who they are, why they do what they do, and how they can be inspired and enabled to perform better at every level. Confident of the knowledge and methods we've originated over 71 years in business, we remain enthusiastic about new ideas that prove their worth. We transform: we help managers to become leaders, and leaders to perfect their skills. Because when people are at their best, your strategic vision is ready to grow into business reality.

e services@haygroup.com
w www.haygroup.com
b blog.haygroup.com

linkedin.com/company/hay-group

@HayGroup

Facebook.com/HayGroup

Morgan Lewis

MARC J. SONNENFELD
PARTNER

msonnenfeld@morganlewis.com

Philadelphia Phone **+1.215.963.5572** Fax **+1.215.963.5001**

1701 Market St. \\ Philadelphia, PA 19103-2921 \\ United States

Noted by *Chambers USA* in 2014 as "an established figure for both his commercial and securities litigation practices," Marc J. Sonnenfeld defends public and private companies, officers, directors, controlling shareholders, and underwriters against securities and shareholder litigation (including derivative cases, claims arising from mergers and acquisitions, and appraisal actions) and related regulatory and enforcement proceedings. He is frequently sought after to counsel directors on corporate governance issues and has served as counsel to board committees.

Marc leads the defense of putative securities class actions around the United States. In many cases, he secures motions to dismiss. At both the federal and state level, he defends shareholder class actions, having challenged merger transactions collectively valued in excess of $10 billion. Among his appellate cases are two seminal cases deciding corporate governance issues under Pennsylvania law, *Cuker v. Mikalauskas* (1997) (amicus curiae), and *LeMenestrel v. Warden* (2008) (appellee). He was selected as a 2013 "Client Service All-Star" by BTI Consulting Group, and as one of five attorneys named "Securities MVP" by *Law360* in 2012.

A fellow of the American College of Trial Lawyers, Marc's trial and appellate experience includes cases outside securities and shareholder claims, and he obtained two defense verdicts in the last five years. One of Marc's trials was featured in a trial practice book, *Trying Cases to Win: Anatomy of a Trial by Herbert J. Stern and Stephen A. Saltzburg. Marc has been named one of Philadelphia's top business litigators in The Best Lawyers in America since 1997, most recently being selected as a "Securities Lawyer of the Year" (2013). He has been named by Philadelphia Magazine as one of the 100 "Pennsylvania Super Lawyers."*

Marc is active in bar activities, and was awarded the 2010 Wells Fargo Fidelity Award from the Philadelphia Bar Association for his work developing and maintaining the Commerce Court Program in the Philadelphia Court of Common Pleas. He served as chair of the Philadelphia bar's board of governors and co-chair of its Business Court Task Force.

After graduation from law school, Marc served as a law clerk to Judge Joseph S. Lord III, then Chief Judge of the US District Court for the Eastern District of Pennsylvania.

SELECTED REPRESENTATIONS

- In *Doshi and City of Livonia Emps. Ret. Sys. v. General Cable Corp.* (E.D. Ky. 2015), the Court granted a motion to dismiss with prejudice the first amended complaint alleging federal securities claims based on two restatements, finding that plaintiff had not adequately pled scienter.
- In *Hays v. Dvorak*, (Del. Ch. 2014), the Delaware Court of Chancery granted a motion to stay filed by Zimmer Holdings, Inc. and stayed a derivative case filed against Zimmer's directors, naming Zimmer as a nominal defendant. Zimmer's motion to stay was based on the fact that the derivative suit relied on an adverse ruling against Zimmer in a patent trial, which ruling was on appeal. After the Chancery Court granted the motion to stay, the Federal Circuit ruled on the patent lawsuit appeal, vacating the bulk of the damages awarded against Zimmer upon which the Plaintiff's claims were based, including the treble damages and attorney fees. On February 6, 2015, the Court approved the parties' stipulation dismissing the case without prejudice.
- In Cement & Concrete Workers District Council Pension Fund (N.D. Cal. 2013 & 2014), the district court twice granted motions to dismiss the putative securities fraud class action finding that publication of HP's Standards of Business Conduct (SBC) did not violate the securities laws based on claims that conduct by HP's former CEO, Mark Hurd, violated the SBC. This case is on appeal to the Ninth Circuit.
- In *Cockle v. Coustas* (Marshall Islands 2013), the High Court of the Republic of the Marshall Islands granted the motion to dismiss the derivative suit against a Greek shipping company based on claims relating to payment of management fees and terms of a private financing.
- In *Zucker v. Andreessen* (Del. Ch. 2012), the Delaware Court of Chancery granted the motion to dismiss derivative claims based on the severance package awarded to Hewlett-Packard Company's former CEO.
- In Saginaw Police & Fire Pension Fund v. Hewlett-Packard Company (N.D. Cal. 2012), the district court granted the motion to dismiss derivative claims, based on the board's alleged failure to prevent FCA and FCPA violations. Plaintiff appealed but dismissed its appeal days before oral argument was scheduled.
- In *Gammel v. Hewlett-Packard Company* (C.D. Cal. 2012), the district court granted the motion to dismiss the putative securities fraud class action based on HP's announcement that it was discontinuing webOS development. In 2013, the district court granted in part the motion to dismiss a further amended complaint, cutting the putative class period to a few weeks running from June to August 2011. The case later settled.
- In *Plumbers and Pipefitters Local Union 719 Pension Fund v. Zimmer Holdings, Inc.* (S.D. Ind. 2009), the district court granted the motion to dismiss in this putative class action case alleging claims based on a purported product flaw and FDA form 483 observations. This decision was affirmed by the Seventh Circuit in 2012.
- *Scheiner v. Midas, Inc. et al* (N.D. IL. 2013), the district court granted the motion to dismiss a Section 14 action, challenging the Form 14d-9 for the acquisition of Midas by TBC.
- In *Solomon-Shrawder v. CardioNet, Inc.* (E.D. Pa. 2010), the district court granted the motion to dismiss a putative securities fraud class action based on the company's alleged response to an analyst report.
- In In re GPC Biotech AG Sec. Litig. (S.D.N.Y. 2009), the district court granted a motion to dismiss a putative securities fraud class action based on the FDA's decision not to approve a NDA.
- In In re NutriSystem, Inc. Sec. Litig. (E.D. Pa. 2009), the district court dismissed the putative securities fraud class action based on alleged false and misleading statements about the company's financial health in the face of competition from an anti-obesity drug.
- In *LeMenstrel v. Warden* (Pa. Super. 2008), the Court of Common Pleas addressed issues of first impression under Pennsylvania law and dismissed derivative claims. This dismissal was affirmed by the Pennsylvania Superior Court in December 2008 in an opinion defining the proper scope for attorney involvement in an investigation by a special litigation committee and adopting the definition of "disinterested" and "independent" under Pennsylvania law.

AWARDS AND AFFILIATIONS

Listed, *Chambers USA: America's Leading Lawyers for Business* (2003–2014)

Noted in *The US Legal 500* for Securities: Shareholder Litigation (2014)

Listed, *The Best Lawyers in America* (1995–2011)

Listed, *Best Lawyers* Philadelphia Litigation-Securities "Lawyer of the Year" (2013)

Listed as a Client Service All-Star by BTI Consulting Group (2013)

Fellow, American College of Trial Lawyers

Listed, *Law360* Securities MVP (2012)

Listed, *The Legal 500 US: Volume III: Litigation* (2007)

Listed, *Top 100 Philadelphia Lawyers*

Listed, *Philadelphia SuperLawyer*

Former President, Harvard Law School Association of Philadelphia

Recipient, Joseph B. Shane Award by Swarthmore College

Listed as Recognized, Dispute Resolution, *PLC Which Lawyer? Yearbook 2008*

Recommended as a local litigation star for Pennsylvania for Commercial Litigation and Securities in *Benchmark Litigation* (2008–2014)

Recipient, 2010 Wells Fargo Fidelity Award

ADMISSIONS

- District of Columbia
- Florida
- Massachusetts
- Pennsylvania
- U.S. Supreme Court

CLERKSHIPS

- Clerkship to the US Supreme Court (1976)

EDUCATION

- Harvard Law School, 1971, J.D.
- Swarthmore College, 1968, B.A.

SECTORS

- Financial Services
- Technology

SERVICES

- Securities and Corporate Governance
- Investment Management
- Securities Enforcement, Regulation & Litigation
- Class Actions
- Commercial Litigation

REGIONS

- North America