



European Centre for Employee Ownership  
9th Annual Global Equity Forum

Executive Remuneration  
Performance Targets – Latest Trends in Executive  
Reward  
1 February 2008

Steigenberger Belvedere Hotel  
Davos Platz, Switzerland

Alan Judes – Strategic Remuneration



# Agenda

- Performance Targets
  - Supporting corporate strategy and objectives
  - How demanding are they?
  - How demanding should they be?
- Latest trends in executive reward
  - The ratio of incentives to base salary
  - The impact of regulation and compliance
  - Executive pension provision
    - The move to DC and other variants
- Reactions to corporate governance
- Conclusion



# What are measures and goals?

## Measures

### Examples:

Revenue growth

Economic value

Customer satisfaction

New product development

## Goals

The level of performance for which an company or individual strives

Examples: 15%

£900MM

Complete by July 2008

Top quartile

# Selecting measures and goals: critical



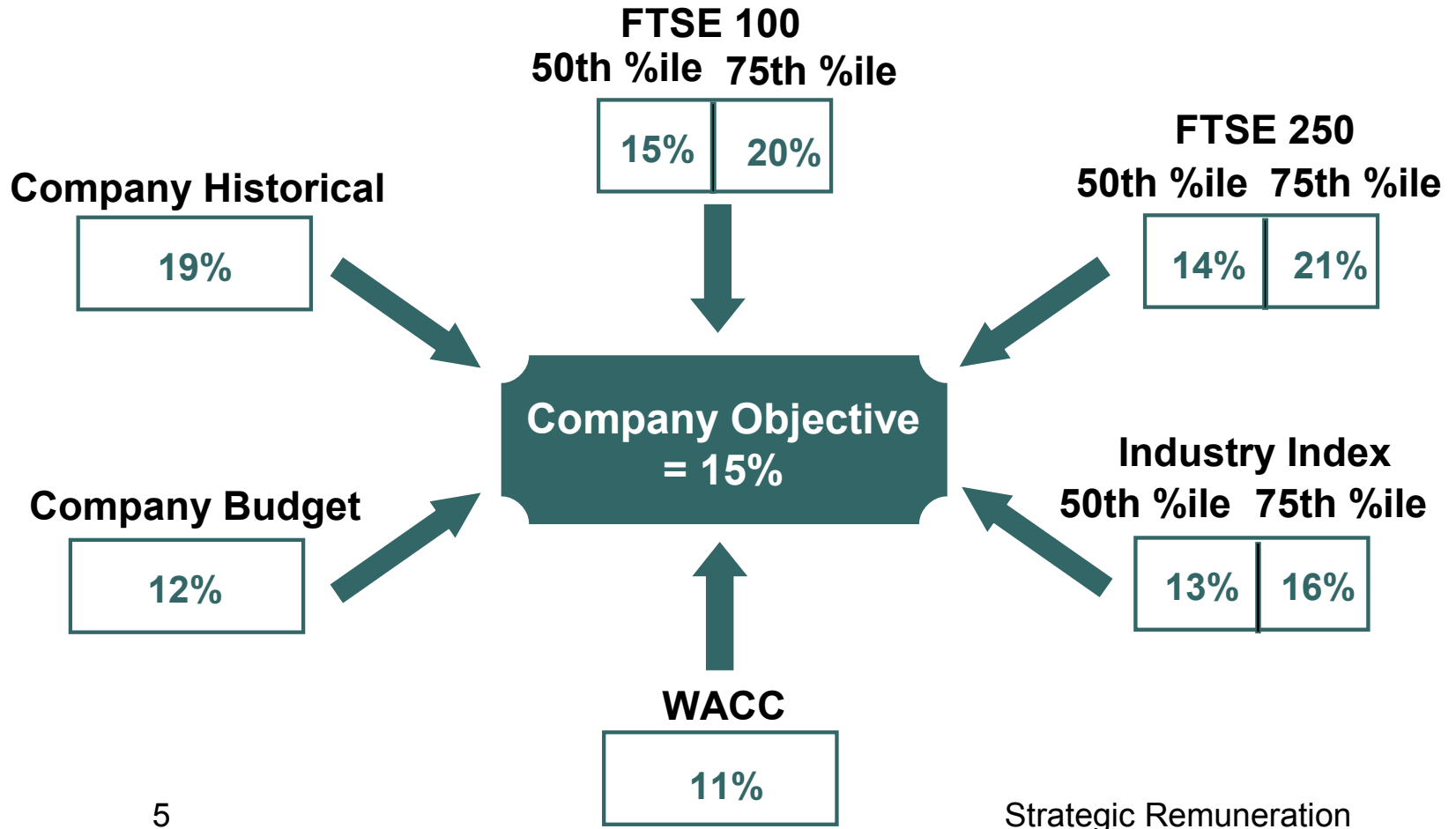
## Examples

- Exceed median peer TSR
- Double value in 5 years
- Penetrate markets
- Develop new products
- Revenue Growth
- Return on Invested Capital (ROIC)
- Economic Value
- Incentive determination process
- Working capital
- Customer Retention
- Revenue from New Products

Strategic Remuneration

# Shareholder expectations should drive long-term goals

**Equity Value**  
**Compound Annual Growth Rate – (assumed figures for illustration only)**





# Performance measures

Source NBSC The 2007 FTSE

100 Directors' Remuneration Survey

## ○ Annual Bonus Plans

- Personal performance
- Profit
- Non-financial measure
- Specific financial measure
- EPS
- Cashflow
- Turnover
- Return on a measure
- Strategic
- TSR
- NAV
- EBITDA
- EVA

## ○ LTIPs

- EPS
- TSR
- EPS & TSR
- Profit
- Other combination
- Share price
- ROCE
- NAV

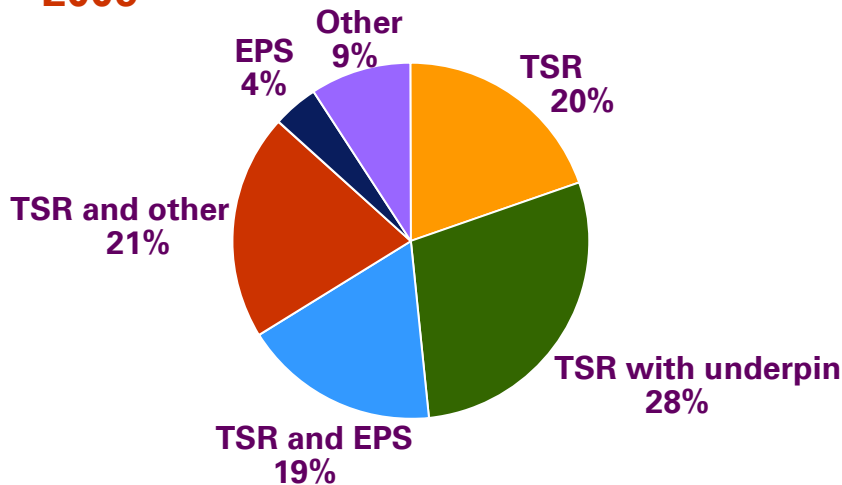
# Performance measures

changing...slowly Source KPMG's Survey of Directors' Compensation 2007

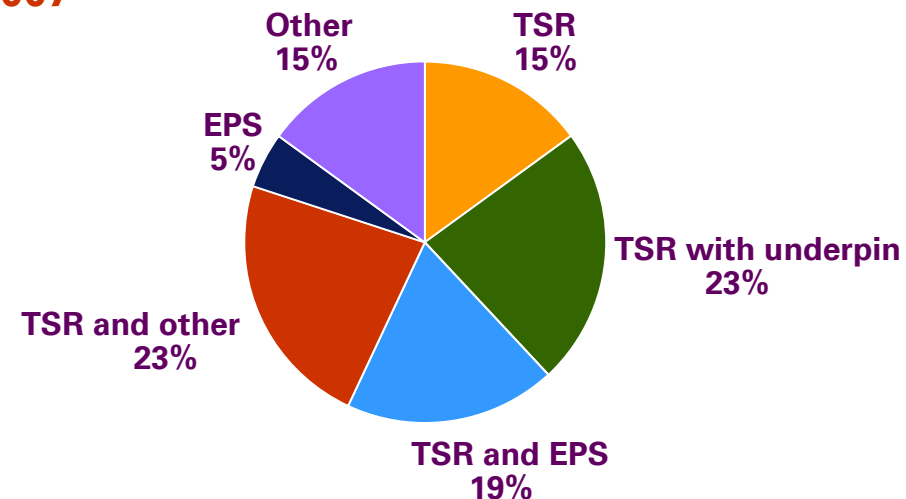
- Annual bonuses increasingly using non-financial measures...otherwise profit and EPS dominate
- Relative TSR is still the most common measure in long-term PSPs
- EPS is most common in option plans
- Trend away from using single measures
- Increased willingness to consider other metrics (e.g. ROCE, Economic Value Added)

## Performance measures in FTSE 100 Performance Share Plans

2006



2007





# Performance measures – how stretching?

Remuneration Survey

Source NBSC The 2007 FTSE 100 Directors' Remuneration Survey

## ○ Option Plans

- EPS median level for minimum vesting – real growth of 3% a year
- EPS median level for maximum vesting – real growth of 5% a year
- TSR median performance required for awards to begin to vest
- TSR UQ for 45% of plans to vest in full, >UQ for 55% of plans to vest in full
- Threshold vesting 33%

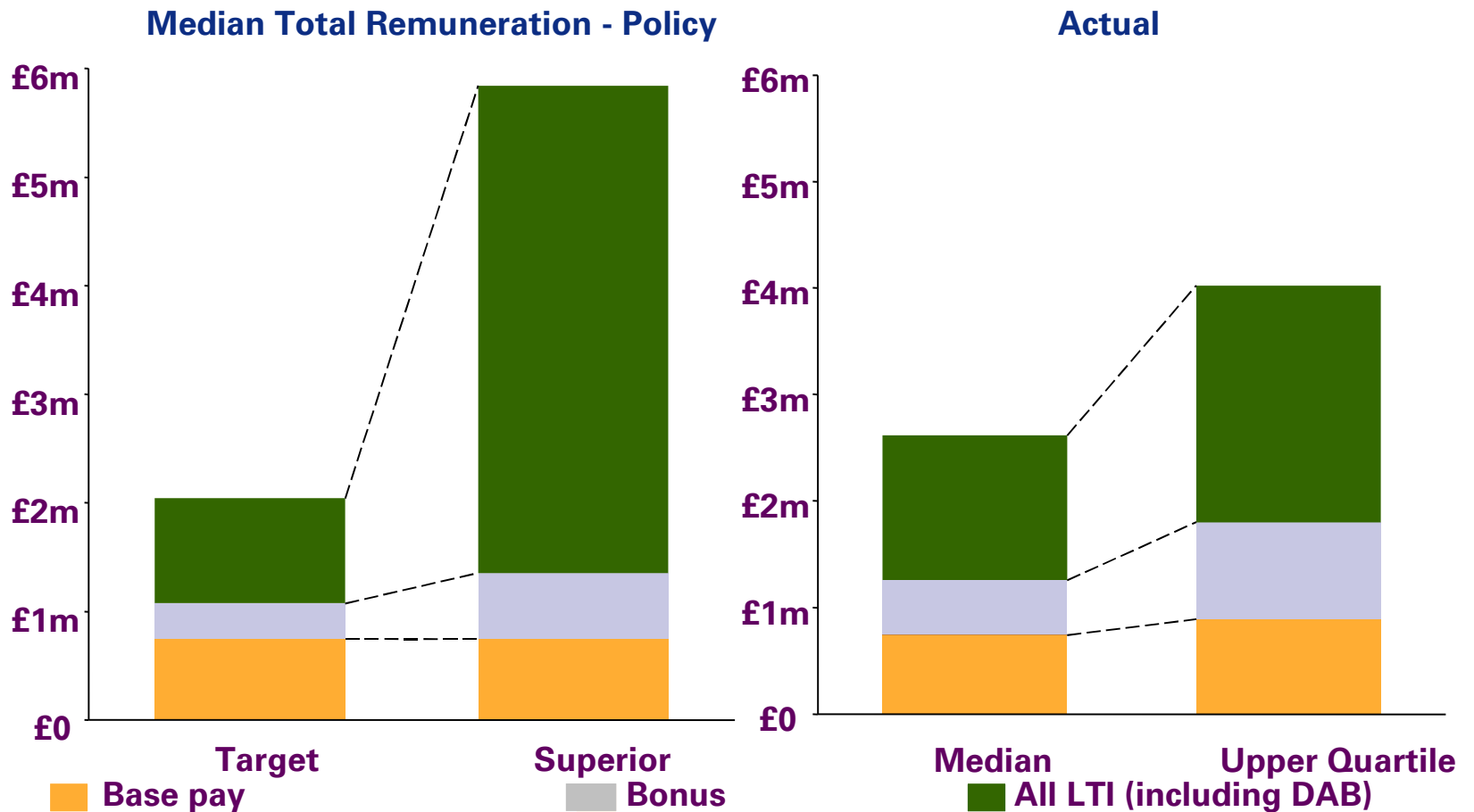
## ○ LTIPs

- EPS median level for minimum vesting – real growth of 3% a year
- EPS median level for maximum vesting – real growth of 8% a year
- TSR all plans require median ranking for awards to begin to vest
- TSR UQ for 48% of plans to vest in full but 52% require >UQ for full vesting
- Threshold vesting 25%

# Total compensation

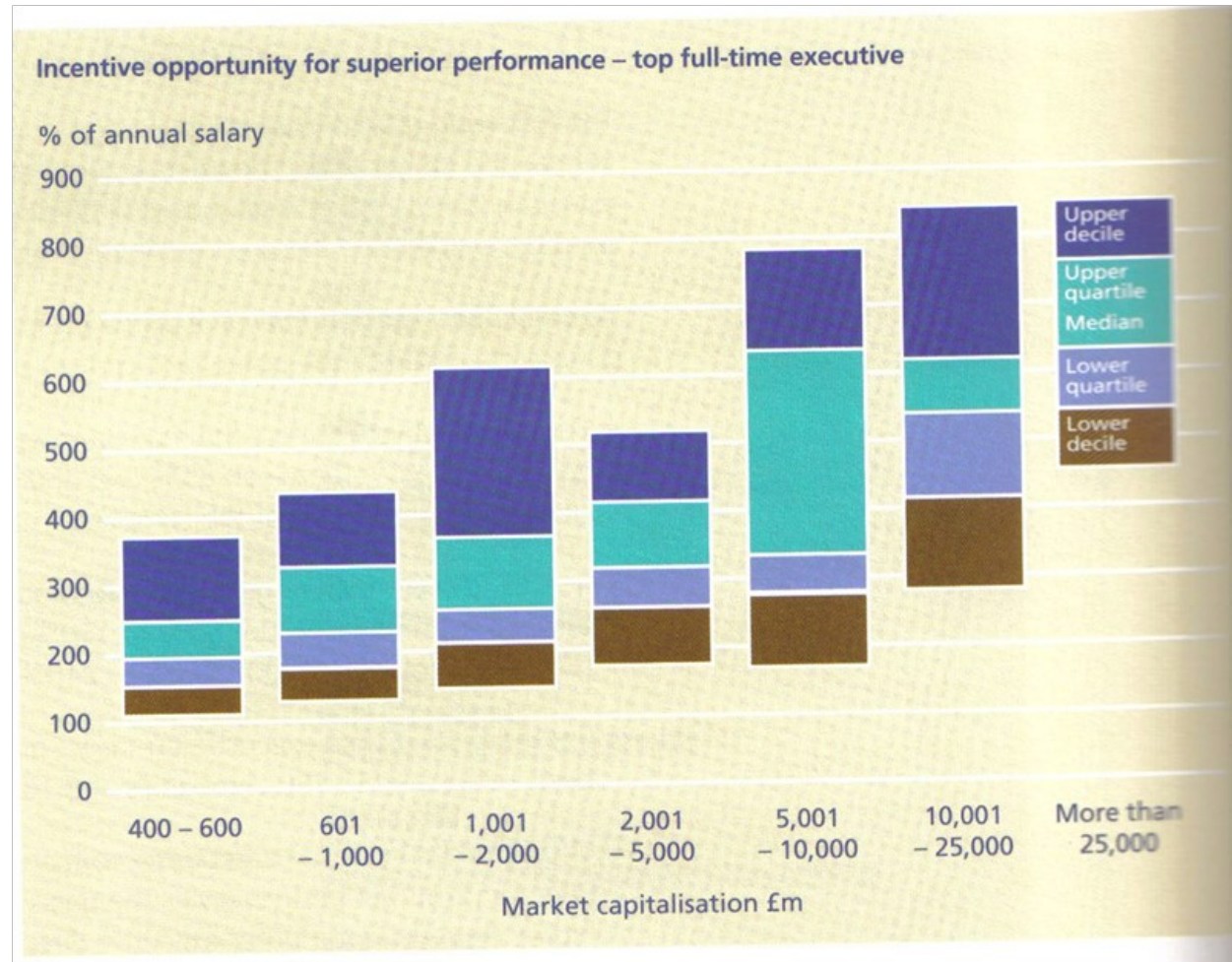
## FTSE 100 – CEO Source KPMG's Survey of Directors' Compensation 2007

- 2007 Median total actual remuneration moved by 12% from £2,329m to £2,617



# Incentive opportunity for superior performance – top full time executive

Source Deloitte Executive director' remuneration – September 2007



Strategic Remuneration



# How demanding are they?

- **Annual incentives**
  - Target – 50% of maximum
  - Maximum – 140% of salary at median (was 60% in 2001), 180% at UQ
- Actual bonuses paid steady at 85% of maximum
- **Long-term incentives**
  - Target – 160% of salary at median
  - Maximum – 565% of salary for superior performance



# How demanding should they be?

- **Annual incentives**
- Achievable but stretching
- No incentive if clear cannot be attained after the first month of the year
- Actual bonuses paid steady at 85% of maximum
- **Long term incentives**
- Designed to pay out at maximum 2-3 years in every 10
- Upper quartile to upper quintile performance
- Should not be a reward for failure
- Significant contrast with position in the US



# The corporate governance framework – extracts from ABI Guidelines of 2007

- Bonuses
- Annual bonuses should be demonstrably related to performance. Both individual and corporate performance targets are relevant and should be tailored to the requirements of the business and reviewed regularly to ensure they remain appropriate.
- Where consideration of commercial confidentiality may prevent a fuller disclosure of specific short-term targets at the start of the performance period, shareholders expect to be informed of the main performance parameters, both corporate and personal, for the financial year being reported on.
- Following payment of the bonus, shareholders will expect to see a full analysis in the Remuneration Report of the extent to which the relevant targets were actually met.
- Maximum participation levels should be disclosed and any increases in the maximum from one year to the next should be explicitly justified. Shareholders will expect increases to be subject to correspondingly more stretching performance



# Aviva plc

Frequently asked questions

## Annual General Meeting 2007

- **Q4 Salaries and bonuses paid to directors continue to increase year on year above the rate of inflation. Why is this, especially when returns on policies are poor? What systems are in place to ensure that employees share in the success of the Company?**
- A The Company's remuneration policy seeks to provide remuneration packages which attract and retain high calibre employees and encourage and reward superior performance. Senior executives are rewarded on the basis of performance and their remuneration packages are set at median against external comparator data for on target performance, and upper quartile for superior performance.
- The annual bonus plan, which was approved by shareholders at the 2005 AGM, is geared towards incentivising and rewarding superior performance and returns to shareholders. When Aviva announced its 2006 full year results, they were at a record level and widely regarded as very good and therefore the Company's reward structure has done what was promised and rewarded excellent performance appropriately.
- Executive pay and staff pay operate as completely different "markets", moving at different rates. Having said that, all Aviva staff are on performance-related pay structures and therefore salary progression depends on individual performance. Additionally many UK staff received bonuses for 2006 which reflected the good results delivered by the business units.



# Executive pension provision

- Funding issues
  - Investment returns prior to retirement
  - Salary increases during employment
  - Annuity rates at retirement
  - Longevity
- Tax simplification
  - Earnings Cap replaced by lifetime allowance
  - FURBS no longer tax efficient



# Executive pension provision

- Solutions to funding issues
  - Investment returns prior to retirement
  - Salary increases during employment
  - Annuity rates at retirement
  - Longevity
- Tax simplification
  - Earnings Cap replaced by lifetime allowance
  - FURBS no longer tax efficient
- Spectrum of plans
  - Final salary
  - Career Average Revalued Earnings CARE
  - Cash Balance Plan
  - Pure Defined Contribution
- Dealing with tax issues
  - Maximise LTA
  - Employer Financed Retirement Benefit Schemes EFRBS – unfunded but secured
  - Cash alternative



# Executive pension provision – new ABI guidelines – Source ABI 3 December 2007

- 2.2 Payments in lieu of pension scheme participation should be clearly disclosed and treated as a separate non-salary benefit. Accordingly, they should be excluded from the calculation of bonus entitlements and share scheme grants.
- 2.4 Changes in pension benefit entitlements or to transfer values reflecting significant changes in actuarial and other relevant assumptions should be fully identified and explained. Where changes to pension benefit entitlements or transfers are of a discretionary nature, these should be made clear and justification provided.



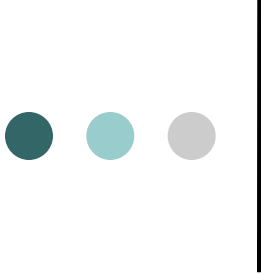
# Myners hits out at governance specialists

Source: FT December 5 2007

- Paul Myners, chairman of Guardian Media Group and Land Securities, has hit out at “the open-toed sandal brigade”, his description for corporate governance experts, because of their obsession with pay and board structure.

In a View from the Top interview published on FT.com on Wednesday, Mr Myners – who has also chaired Marks and Spencer and Gartmore – accused sticklers for corporate governance of losing sight of the economic value a company might create and called for breathing space from a series of reviews of UK corporate governance standards.

He said the UK system “was probably the best in the world”, but warned investors against being too rigid in their interpretation of the UK’s combined code on good governance.



# Terry Smith slams 'Swampy does corporate governance' activism

Source: Financial Times Published: Jun 15, 2007

- Terry Smith, the chairman of Collins Stewart, has lashed out at shareholders who complain about uncapped bonuses and demand "platitudes" on environmental commitments and other such "tosh".

Writing in a typically forthright manner in today's Financial Times, he argues that some investors' corporate governance demands waste the time of public companies and give an advantage to private rivals, which are free from such scrutiny. Mr Smith, who is also chief executive of inter-dealer broker Tullett Prebon, said investors who pester him with paperwork before annual meetings have "an approach to business [that] might be described as 'Swampy does corporate governance'." Among those singled out are churches, charities, Co-operative Insurance and the Association of British Insurers.



# Conclusion

- You can achieve a balance between need to attract retains and motivate, and not rewarding failure
- It helps if both annual incentive and LTIP are aligned with business strategy and linked to relevant performance
- Dialogue with shareholders and disclosure beyond the letter of the law is essential
- With shareholder consent public companies can design incentives to compete with the world of private equity