

Compensation Peer Groups: Everything You Need to Know Right Now

A Compensation Committee Series Webinar

Presented by NACD and Pearl Meyer

April 23, 2024

Presenters



Greg Stoeckel
Managing Director, Pearl Meyer



Kim Neil
Principal, Pearl Meyer

Housekeeping



- Submit a question and receive your answer directly from the presenters, either during today's webinar or as a follow-up. You will also be opted-in to receive future executive compensation thought leadership from Pearl Meyer.
- Presentation slides are available today at www.pearlmeyster.com/compensation-peer-groups and within the webinar console.
- The replay will be available early next week at www.nacdonline.org/webinars and www.pearlmeyster.com/compensation-peer-groups.

Your participation in today's webinar earns you credit toward maintaining your NACD credentials.

NACD Board Leadership *Fellowship*[®]

If you're working toward maintaining your NACD *Fellowship*[®] credential, you will receive 1 credit.



NACD Directorship Certification[®]

If you're working toward maintaining your NACD Directorship Certification[®] credential, you will receive 1 credit.



Agenda



- 1) The Role of Peer Groups in Executive Compensation
- 2) Selecting Peer Group Companies
- 3) Assessing the Resulting Peer Group
- 4) Traditional and Non-Traditional Peer Group Analyses

The Role of Peer Groups



Benchmarking Peer Groups

- Executive Compensation Levels
- Incentive Plan Designs
- Policies & Practices

Performance Peer Groups

- Relative Performance Measurement/TSR
- PvP Table Disclosure

“Aspirational” Peer Groups

- Pay Sensitivity Analysis

There are a variety of peer group types and uses in executive compensation

*With today’s focus being on the **Benchmarking Peer Group***

Polling Question #1

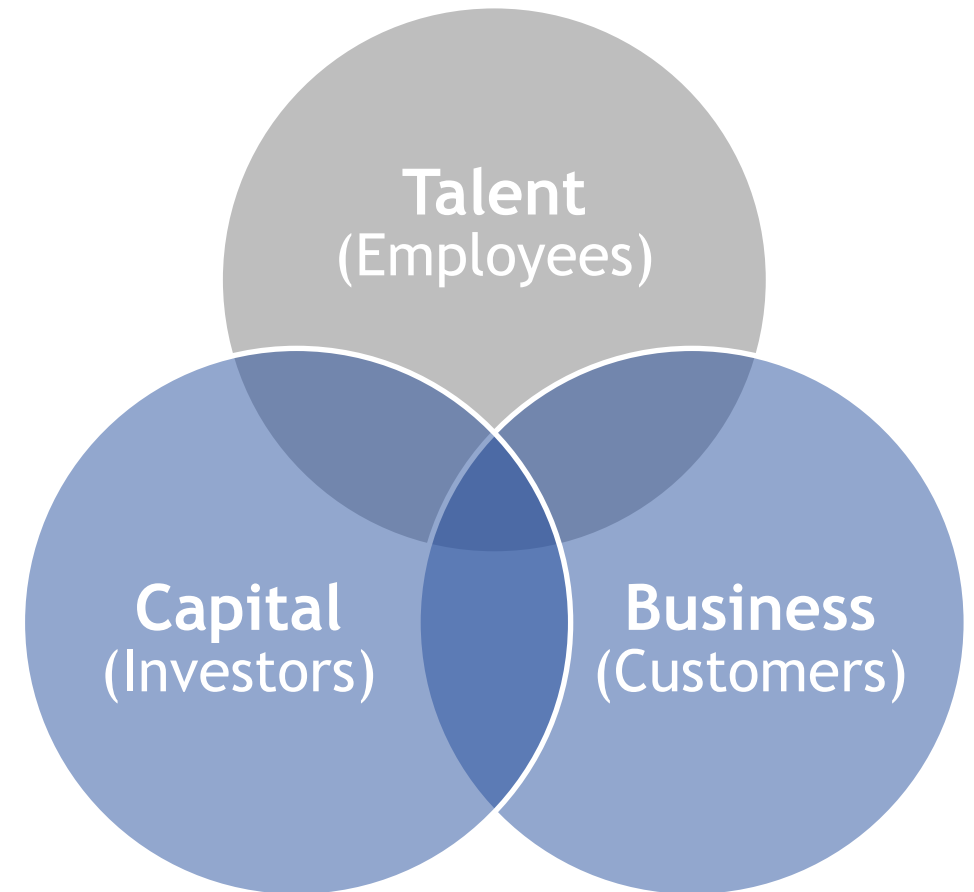


Q: Which types of peer groups do you use for executive compensation?

1. Benchmarking Peer Group Only
2. Benchmarking and Performance Peer Groups
3. All 3 Peer Groups
4. None (We don't use peer groups)

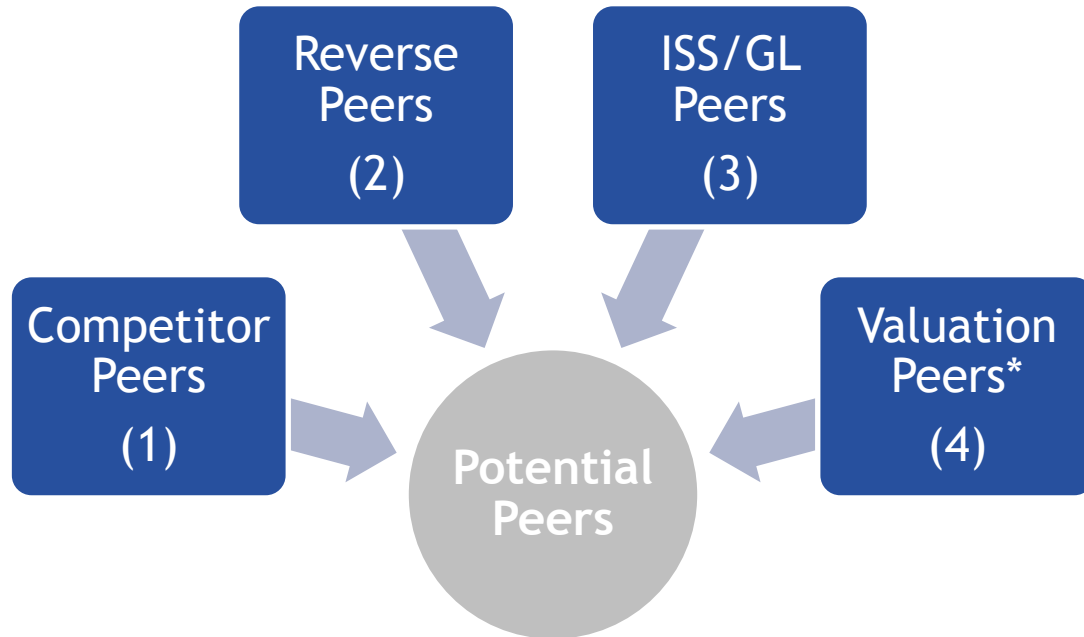
The Benchmarking Peer Group

- Seeking a group of companies that are competitors for talent, capital, and business
- Talent competitors take precedent, but need to be “lateral” competitors



Identifying Individual Peer Companies

Potential Sources of Peer Companies

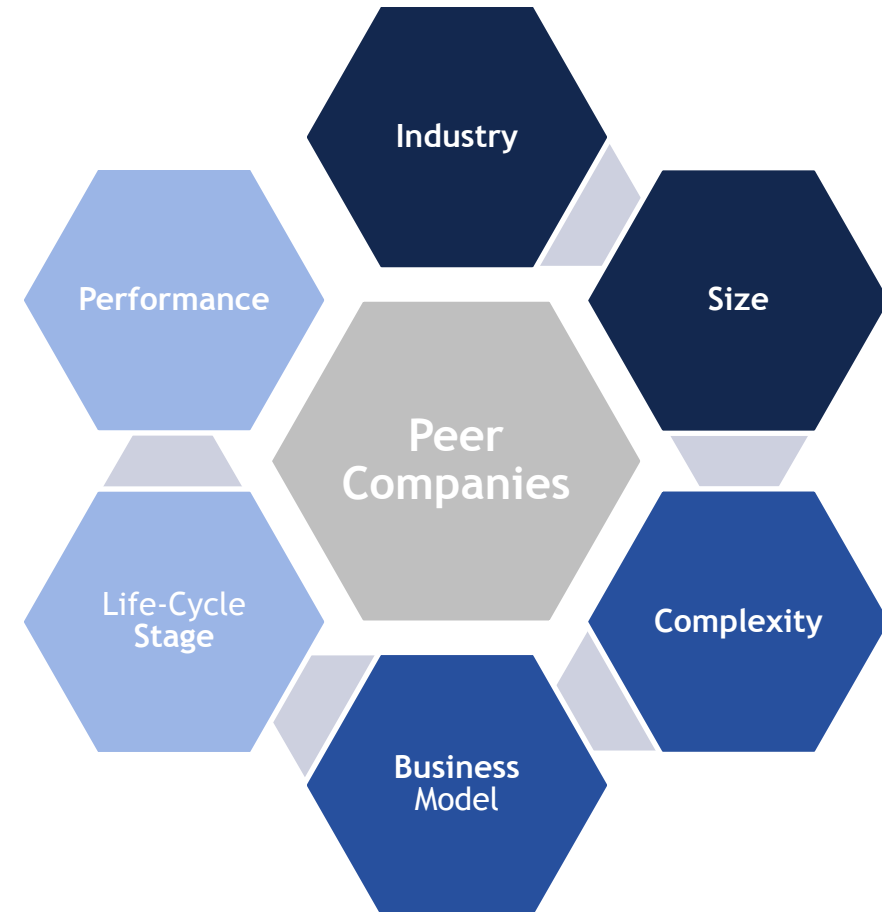


- 1) Who do your direct competitors include in their peer group?
- 2) Which companies include you in their peer group?
- 3) Which companies are included by ISS/GL in their peer groups?
- 4) Which companies are used for valuation purposes?*

 - Need to screen for size

Selecting Individual Peer Companies

- Industry and size are the primary factors to focus on
- Complexity and business model are important considerations
 - e.g., global footprint, multi-division, percent franchised, etc.
- Life-cycle stage and performance can be relevant
 - e.g., turnaround, high growth, etc.



Important Size Criteria and Parameters



Size Criteria	Qualifying Range
Revenue	0.50x - 2.0x
EBITDA	0.50x - 2.0x
Market Cap	0.25x - 3.0x
Enterprise Value	0.25x - 3.0x
Number of Employees	0.50x - 3.0x

- Revenue is the primary factor given its impact on pay levels
 - EBITDA is an important factor with respect to “ability to pay”
 - Market Cap is important with respect to equity-based pay
 - Enterprise Value neutralizes capital structure with respect to size
 - Number of Employees can be indicative of business model

Polling Question #2



Q: How do you feel about the peer group selection criteria you use?

1. We use most of the criteria/factors mentioned
2. We use some of the criteria/factors mentioned
3. We use none of the criteria/factors mentioned, but we should!
4. We use none of the criteria/factors mentioned

Assessing Peer Groups



Assessment Category	General Guidance
Sample Size	<ul style="list-style-type: none">• Between 10 and 20 companies (more is acceptable)
Company Positioning	<ul style="list-style-type: none">• Near the median on a majority of size metrics• Revenue and Market Cap comparability often the most important
Dispersion	<ul style="list-style-type: none">• The ratio between the highest and lowest company in the group• Lower dispersion results in greater statistical significance
ISS/GL Overlap	<ul style="list-style-type: none">• Some degree of overlap, where appropriate (e.g., 50%)• Viewed as a “nice to have” as opposed to a “need to have”
Industry Representation	<ul style="list-style-type: none">• If in multiple industries, ensuring proper representation based on the Revenue and/or EBITDA of each division
Complexity Representation	<ul style="list-style-type: none">• Seeking similar complexity in terms of business model, geographic scope, multiple business units/brands/etc.

Peer Group Assessment Example



- Start with a list of peers and key criteria
- Summarize and analyze
 - Peer Results
 - Percentile Summary
 - Comparison (You vs. Peers)
 - Percentile Rank
 - Percent of Median
 - Overall Assessment
 - Visual Scorecard

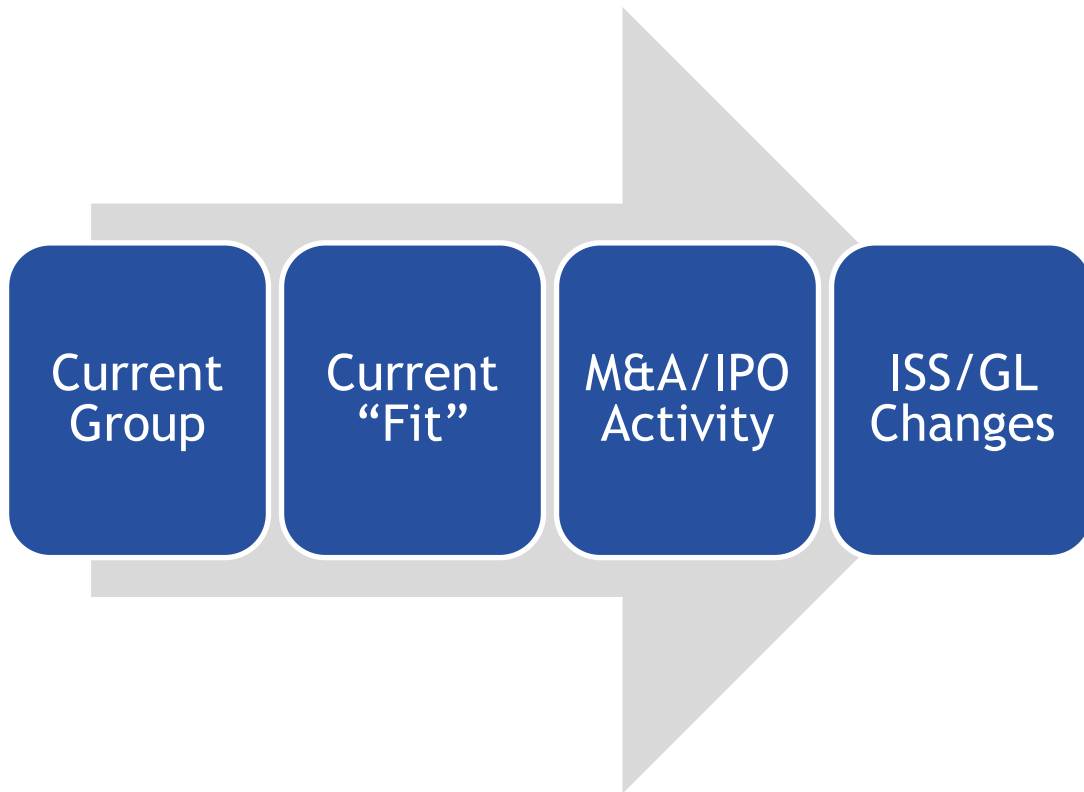
Company XYZ's Current Peer Group

Company	State	GICS Industry Description	Revenue	EBITDA	Market	Enterprise	# of	Peer Overlap				
			LTM	LTM	Cap	Value	EEs	ISS	GL	Reverse		
Company 1	TX	Household Products	\$20,431	\$3,619	\$43,580	\$51,126	41,000		✓	✓		
Company 2	MN	Packaged Foods and Meats	\$20,173	\$4,296	\$39,501	\$51,681	34,000					
Company 3	MI	Household Appliances	\$19,455	\$1,477	\$6,515	\$13,123	59,000	✓	✓	✓		
Company 4	NY	Household Products	\$19,457	\$4,509	\$74,020	\$82,287	34,000		✓			
Company 5	N/A	Household Products	\$18,405	\$5,746	\$40,274	\$49,309	40,000					
Company 6	CT	Industrial Machinery and Supplies and Components	\$15,781	\$1,198	\$15,062	\$22,296	50,500					
Company 7	N/A	Household Appliances	\$12,638	\$134	\$2,440	\$4,849	45,000					
Company 8	CO	Apparel, Accessories and Luxury Goods	\$10,820	\$1,068	\$5,964	\$12,317	26,400	✓				
Company 9	OH	Paper and Plastic Packaging Products and Materials	\$8,364	\$1,271	\$17,976	\$21,168	35,000					
Company 10	MI	Building Products	\$7,967	\$1,517	\$17,335	\$20,193	18,000			✓		
Company 11	OH	Other Specialty Retail	\$7,429	\$1,554	\$11,249	\$15,739	33,069			✓		
Company 12	CA	Household Products	\$7,310	\$1,082	\$19,002	\$21,941	8,700	✓	✓	✓		
Company 13	NJ	Household Products	\$5,868	\$1,258	\$25,442	\$27,703	5,550	✓	✓	✓		
Company 14	CA	Leisure Products	\$5,441	\$818	\$6,815	\$8,220	33,000	✓		✓		
Company 15	WI	Household Products	\$2,898	\$173	\$3,143	\$3,236	3,100			✓		
Company 16	TX	Household Appliances	\$2,000	\$300	\$2,737	\$3,482	1,903			✓		
			75 th Percentile	\$18,667	\$2,070	\$28,957	\$33,104	40,250				
			Median	\$9,592	\$1,265	\$16,199	\$20,681	33,535				
			25 th Percentile	\$6,949	\$1,006	\$6,378	\$11,292	15,675				
			Dispersion (maximum divided by minimum)	10.2	42.8	30.3	25.4	31.0				
Company XYZ			NC	Housewares and Specialties	\$8,000	\$800	\$4,000	\$8,000	15,000			
			Percent of Median	83%	63%	25%	39%	45%				

Summary Assessment

Sample Size	16	Green	# Foreign Based	2	Yellow
ISS Overlap	5/16	Yellow	XYZ % Median- Employees	45%	Yellow
Revenue Dispersion	10.2	Red	XYZ % Median - Revenue	83%	Yellow
EBITDA Dispersion	42.8	Red	XYZ % Median - EBITDA	63%	Yellow
Mkt Cap Dispersion	30.3	Red	XYZ % Median - Mkt Cap	25%	Red
EV Dispersion	25.4	Red	XYZ % Median - EV	39%	Yellow

Updating Peer Groups



Absent any significant strategy or industry changes, favor “tweaks” instead of “overhauls”

- 1) Annual refresh process that starts with the current peer group
- 2) Re-assess “fit” in terms of industry, size, complexity, etc.
- 3) Assess potential losses and adds due to M&A and/or IPO activity
- 4) Re-assess ISS/GL overlap

Polling Question #3



Q: How do you feel about your current peer group?

1. It is aligned with most of the factors mentioned
2. It is aligned with some of the factors mentioned
3. It is not aligned with the factors mentioned, but it should be!
4. It is not aligned with the factors mentioned

Traditional Peer Group Analyses



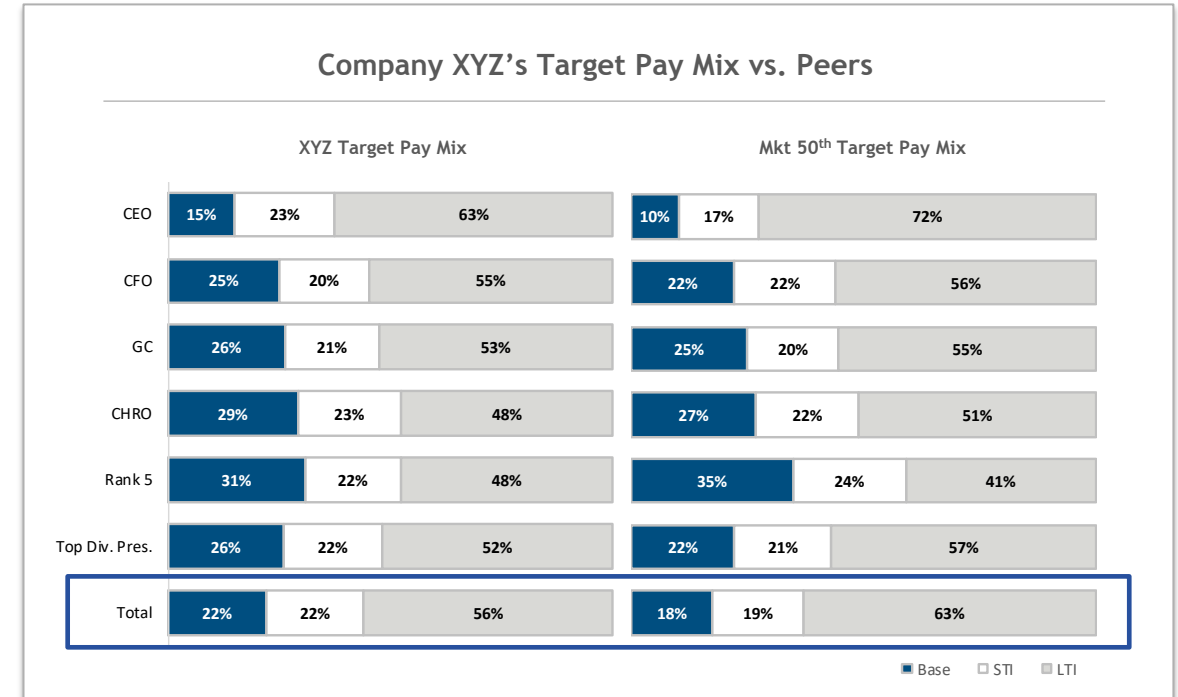
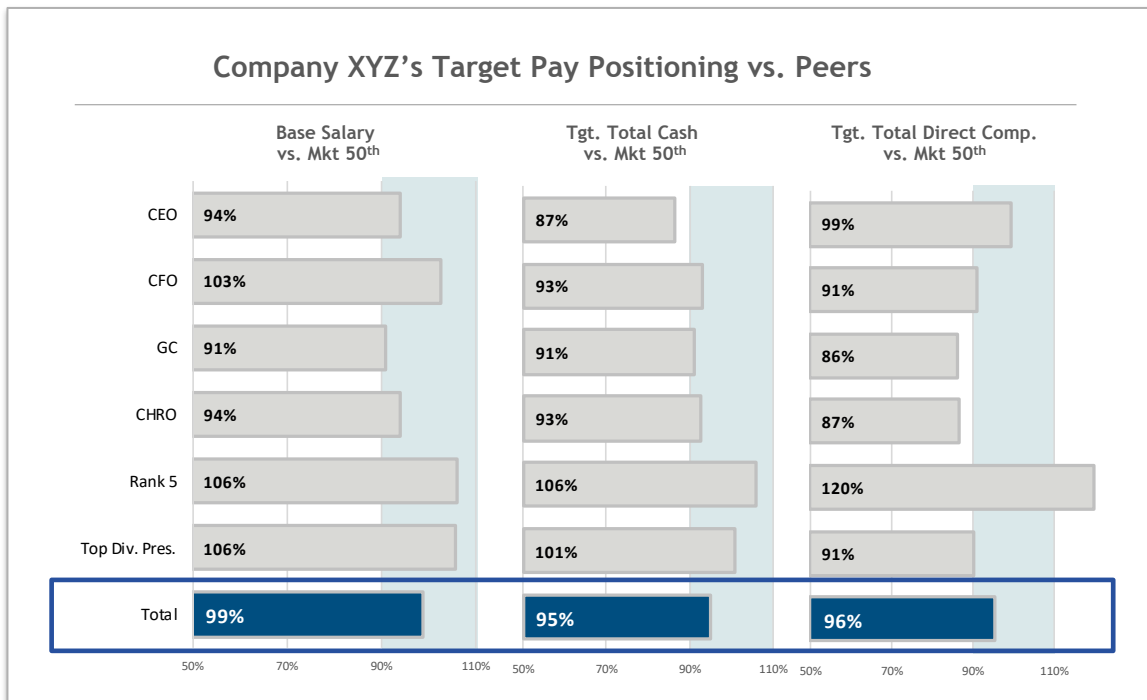
- Target Pay Benchmarking
- Incentive Plan Design Benchmarking
- Pay and Performance Alignment
- Equity Plan Dilution and Grant Rate

Traditional Peer Group Analyses

Sample - Target Pay Levels and Mix



- Peer data moves, view “competitive” as a range vs. specific data point



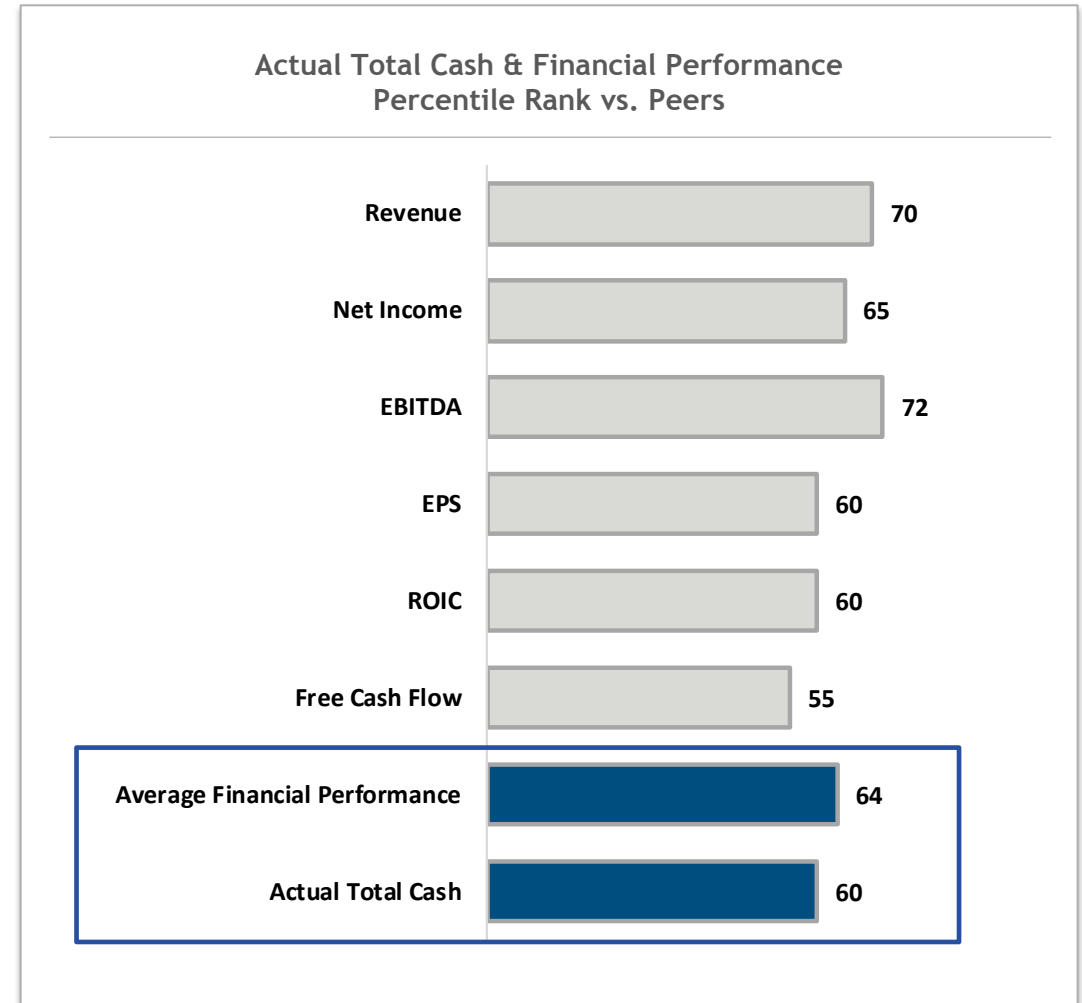
- Factor in pay element combinations
 - Fixed (Salary) vs. Variable (STI plus LTI)
 - Short (Salary plus STI) vs. Long-term (LTI)

Traditional Peer Group Analyses

Sample - Pay and Performance Alignment



- Are pay levels commensurate with performance?
 - Compare key financial performance and resulting pay levels against peers
 - Misaligned? Investigate disparities to identify areas for program improvement



Non-Traditional Peer Group Analyses



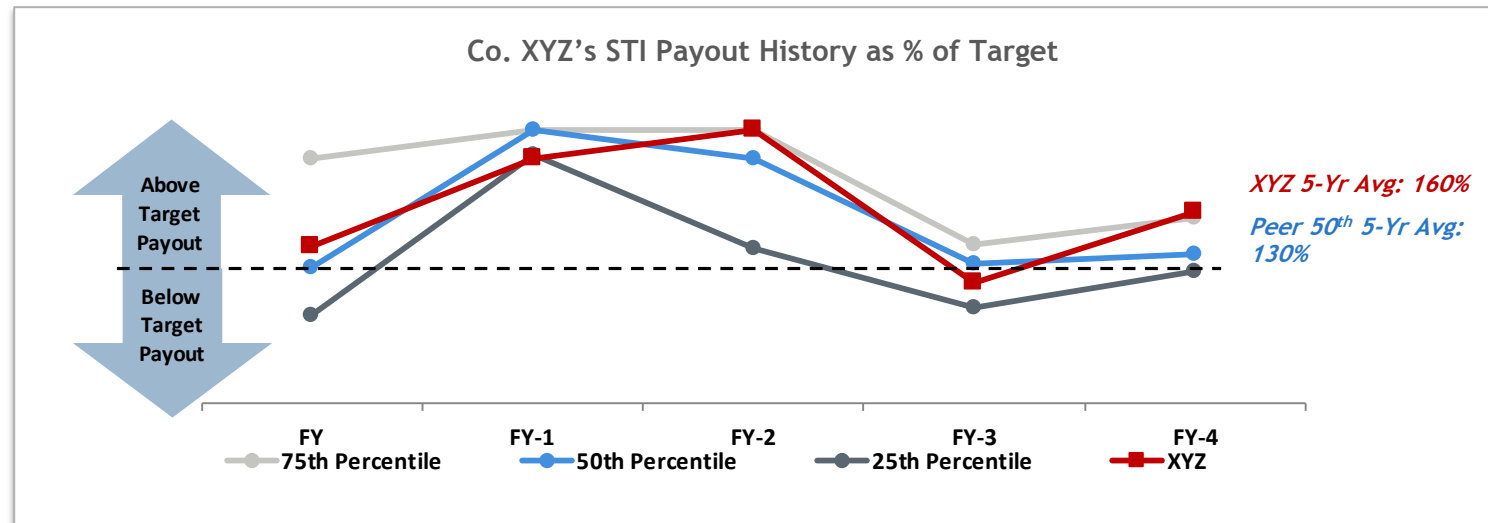
- Incentive Plan Payout History
- Incentive Plan Slopes
- Realizable Pay vs. Performance
- Goal-Setting Rigor

Non-Traditional Peer Group Analyses

Sample - Incentive Plan Payout History



- Are your incentive plans paying out as anticipated?
 - Traditional rule of thumb suggests plans pay out at Threshold 80-90%, Target 50-60%, and Maximum 10-20% of time
 - Compare your payout history with peers to add real world context to the traditional rule of thumb

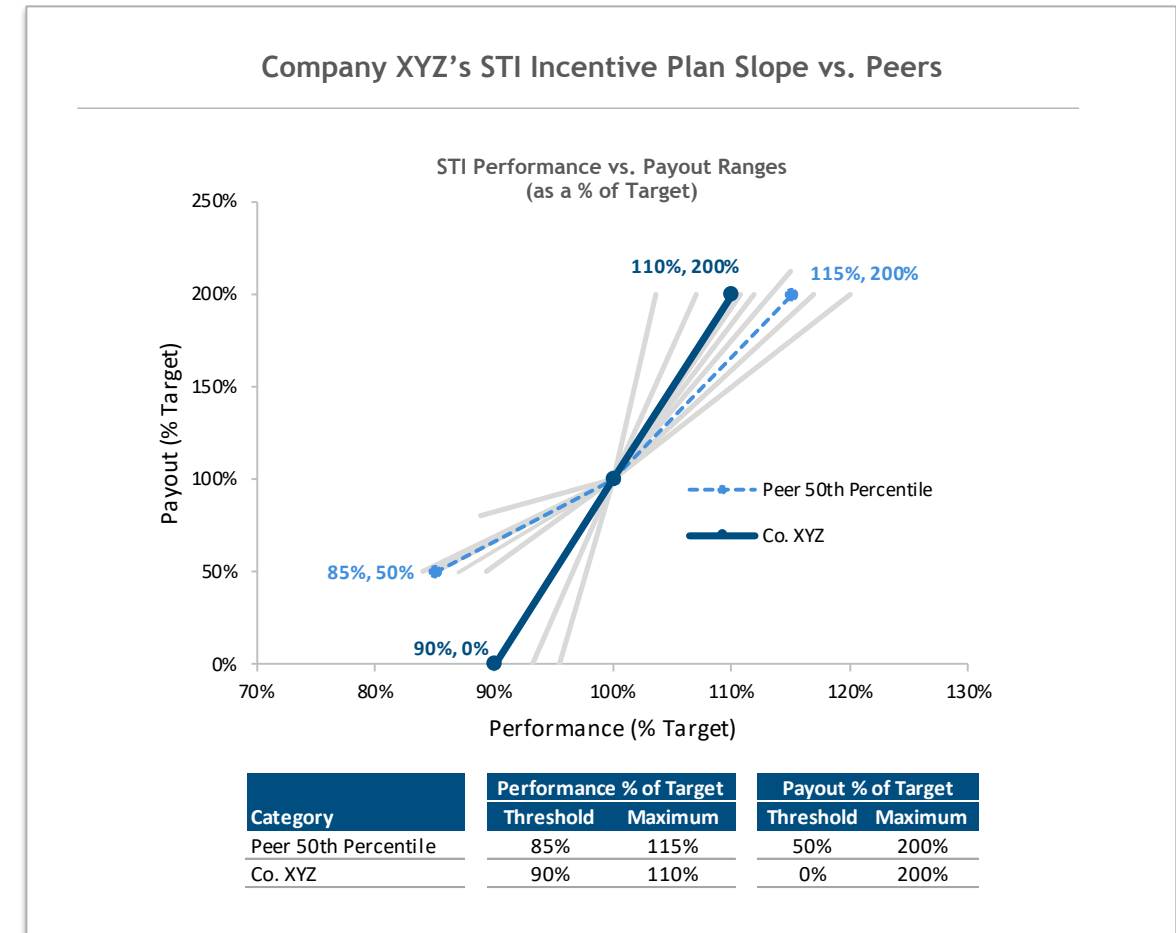


Non-Traditional Peer Group Analyses

Sample - Incentive Plan Slopes



- Test your incentive plan slopes
 - Understand the relationship between performance ranges and payout ranges
 - Assess Threshold and Maximum levels
 - Consider the impact of range width on slope steepness



Non-Traditional Peer Group Analyses

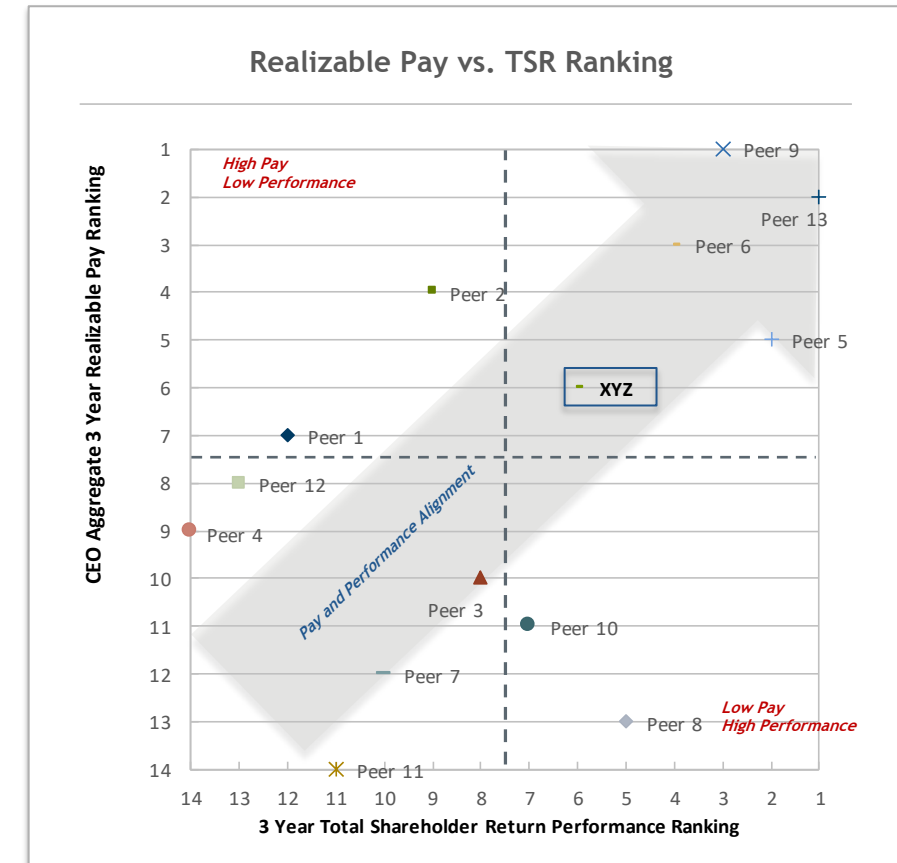
Sample - Realizable Pay vs. Performance



- Exam the relationship between pay outcomes and actual performance achievements
- Are your incentive programs driving the desired results?

Realizable LTI vs. Performance

Element	XYZ Positioning vs. Peers			
	Q1 P0 - P25	Q2 P25 - P50	Q3 P50 - P75	Q4 P75 - P100
3-Year EPS CAGR		40th		
3-Year Average ROIC		35th		
3-Year TSR CAGR				80th
Composite Performance Rank			55th	
CEO Realizable LTI		50th		
Other NEOs Realizable LTI		55th		

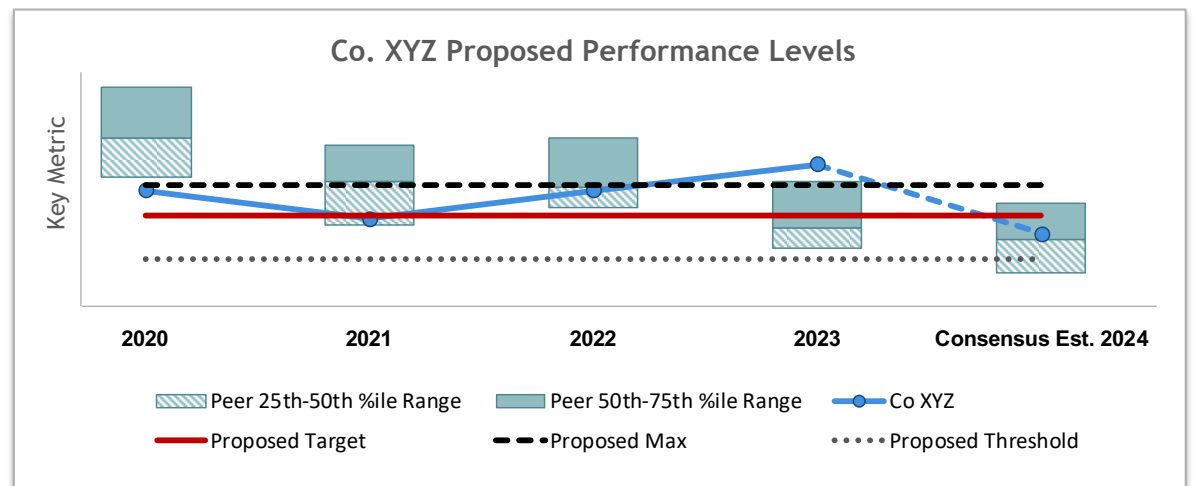
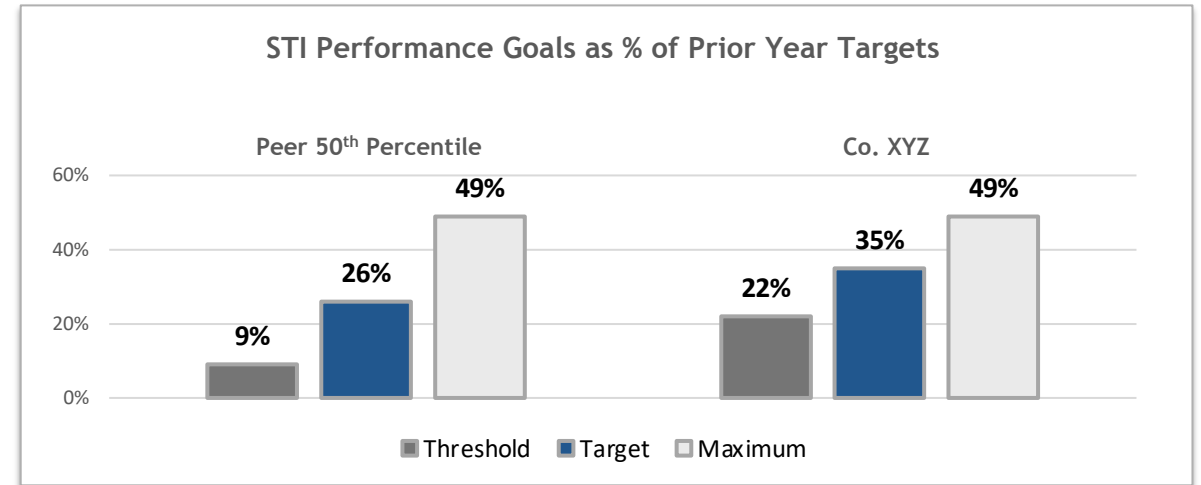


Non-Traditional Peer Group Analyses

Sample - Goal-Setting Rigor



- How challenging are your performance goals?
 - Compare your goal structure to prior year targets and actuals
 - Assess absolute goals against historical and estimated peer performance for market context



Polling Question #4



Q: Which of the non-traditional analyses is the most interesting to you?

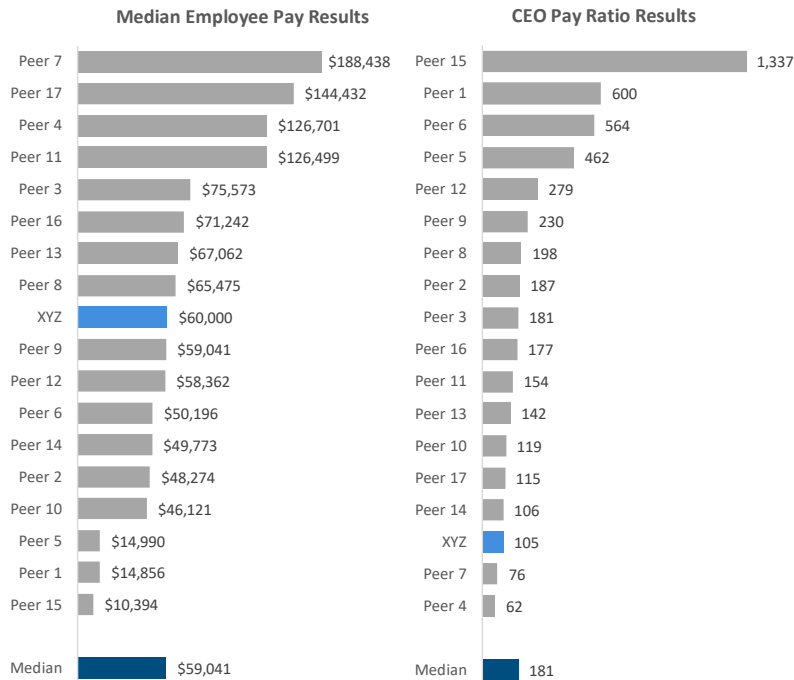
1. Incentive plan payout history
2. Incentive plan slopes
3. Realizable pay vs. performance
4. Goal-setting rigor analysis

But wait, there's more!

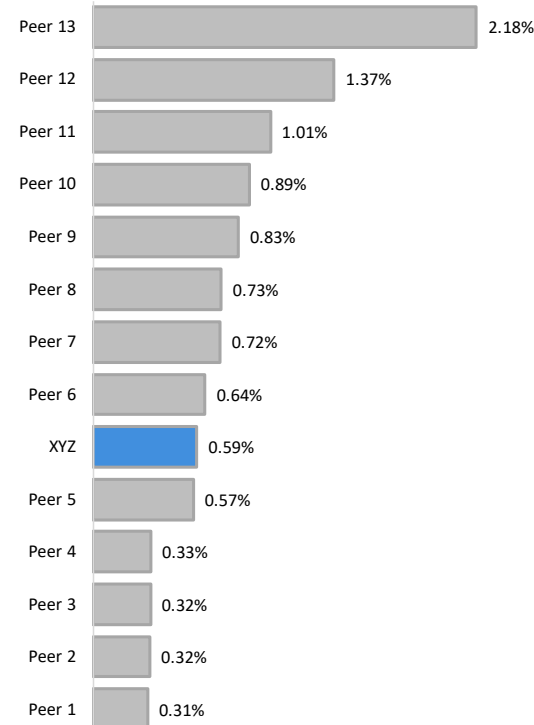


- These additional peer analyses provide another perspective on pay reasonableness...

CEO Pay Ratio Results vs. Peers



Actual Total Cash Spend for Top 5 NEOs vs. Peers (as % of EBITDA)



NEO Perquisite Research - Security Benefits

Item	CEO	Other NEOs
Security Benefit Prevalence	29%	16% *
<i>* 87% of companies providing benefits to Other NEOs also provide benefits to the CEO</i>		
Of those companies providing Security Benefits...		
Security Benefit Category Prevalence		
Home Security Systems	68%	79%
Personal Security/Services	36%	21%
Personal Security/Services During Travel	11%	15%
ID Theft	7%	15%
Home Cyber Security	4%	0%
Security Benefit Total Value		
75th %ile	\$ 219,812	\$ 32,910
50th %ile	\$ 50,840	\$ 7,938
25th %ile	\$ 9,027	\$ 1,680
Average	\$ 771,692	\$ 236,048

Closing Thoughts



- It's important to be thoughtful about (i) the selection of individual companies and (ii) the structure of the resulting peer group
- There's no “perfect peer group,” it always requires some degree of trade-offs between the primary factors being considered
- There are more ways to use peer group data to support pay decisions, beyond traditional benchmarking of pay levels and plan designs

Q&A

Please submit your questions in the Q&A box below.

Don't Miss Our Next Webinar



Join NACD and Pearl Meyer for our next *Compensation Committee Series* webinar:

July 23, 2024

Archives of earlier webinars in this series are available at
www.nacdonline.org/webinars or
www.pearlmeyer.com/insights-and-research