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Your Short-Term Incentive Plan: Why Communication Matters

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With Q1 behind us and 2025 annual incentive metrics and goals likely in place, many companies are focused on ensuring their leaders understand how those goals connect to performance expectations, especially in light of today's uncertainties. But as we look ahead, it's worth reflecting on a key insight from a recent Pearl Meyer survey which found that 94.4% of directors believe their executives have a strong grasp of their annual incentive opportunities. At face value, that suggests effective communication. But understanding alone doesn't guarantee results.

Consider that approximately 37% of CEOs in the Russell 3000 received below-target payouts for 2024 performance, according to early proxy data—a figure that may reflect a range of challenges, including execution, market conditions, or goal-setting. Of course, CEO results do not tell the whole story, and many performance outcomes are outside of management's control. However, shortfalls at the top can still serve as an early signal of potential breakdowns in execution or communication. That is why it's worth exploring how the plan is being communicated, and whether that communication is providing the clarity and direction leaders need to stay focused on what they can influence.

The Pearl Meyer survey also highlighted a more fundamental challenge: 43.3% of directors viewed communication as effective, compared to just 12.7% of management. This disconnect can undermine a plan's potential impact. Business performance is shaped by both internal decisions (e.g., resource allocation, pricing, and operational priorities) and external forces (e.g., market volatility, shifting demand, and macroeconomic pressure). That's exactly why communication matters. If executives don't clearly understand how their annual incentives work or how their daily decisions influence outcomes, it becomes much harder to translate goals into action. Even well-designed plans can fall short without the clarity needed to guide decision-making, maintain focus, and lead teams through uncertainty.

What the committee can do without overstepping

Compensation committees are not responsible for communicating incentive plans, but they do play an important role in ensuring the plans are operating as intended. Financial results offer one view, but they don't fully capture how the plan influences leadership behavior, shapes decision-making, or reinforces strategic priorities.

Gaining perspective on how well an incentive plan is resonating among participants can provide additional context for evaluating whether it is delivering on its purpose and driving the behaviors needed to produce results that create value. Committees can do this without stepping into management's role, by engaging in occasional dialogue with leadership. These conversations don't need to be overly formal or frequent, but they can offer helpful context for understanding how incentive plans are landing with the people they're designed to motivate.

One area worth exploring is whether there are any risks in how the plan is being received by senior leaders. Committees might ask whether there are signs of confusion, frustration, or misalignment related to key elements of the plan, such as performance metrics, goals, or payout expectations. These discussions aren't about second-guessing the design, but about identifying concerns that could help management fine-tune how the plan is being communicated and reinforced.

Another practical step is gaining visibility into how expectations are being managed over the course of the year. Clear communication at the launch of an incentive plan is important, but it's not enough on its own. Without regular reinforcement, participants can lose sight of priorities, become disengaged, or misinterpret what outcomes are likely. Understanding how the organization is keeping the plan visible and relevant can help committees stay connected to how the plan is functioning in practice and how it's being experienced by participants over time. Again, it's not to question management's approach, but to have an outlook on how communication may be shaping engagement, focus, and ultimately, the effectiveness of the plan.

This annual performance cycle may be more important than most

Understanding alone won't drive performance. With goals set and execution underway for this performance year, the real test is whether the annual incentive plan is influencing leadership decisions, reinforcing priorities, engaging participants, and staying relevant as the year unfolds. In a year marked by uncertainty and change, it is even more important for committees to stay informed about how the plan is communicated and experienced—not to direct those efforts, but to maintain perspective on how it's being received and understood by participants. That awareness can offer valuable context for whether the plan is operating as intended and supporting the outcomes it was designed to achieve.

About the Author

Sharon Podstupka is a managing director at Pearl Meyer. She is a trusted advisor to boards and executive management teams in the areas of executive and broad-based employee compensation communication and change management. With over 25 years of consulting experience, she is one of the original pioneers of executive compensation disclosure best practices and has proven success in creating effective strategies and delivering content in challenging business environments and under intense scrutiny from investors and proxy advisory firms. Sharon has extensive experience in a broad range of industries, including financial services, manufacturing, oil and energy, retail, biopharma/biotech, and healthcare.

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