

Rethinking Long-term Incentives: Adapting to Evolving Standards

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Introducing Today's Speakers



Brett Herand

Managing Director, Pearl Meyer

- + Brett is a managing director at Pearl Meyer. Specializing in executive compensation, he works with boards and management on issues related to performance measurement and value creation, incentive plan design, and technical advisory work with respect to tax, accounting, and SEC regulatory issues.
- + Brett works with public and private companies across many industries, including financial and diversified services, technology, and manufacturing. He has been quoted in various publications, including Workspan and Directorship magazines, Agenda, and Bloomberg.
- + Prior to joining Pearl Meyer in 2008, Brett spent five years in Mercer's human capital practice, working in executive remuneration. He holds a bachelor's degree in finance from the W.P. Carey School of Business at Arizona State University.



Brooke Fernandez

General Manager, Main Data Group

- + Brooke is the General Manager of Main Data Group (MDG), a provider of executive compensation benchmarking and corporate governance analytics. The MDG team continues to innovate upon a comprehensive proxy database and offers custom research services to top-tier companies and Executive Compensation firms worldwide.
- + MDG's mission is to empower executive compensation professionals with meaningful, comprehensive total rewards and corporate governance information through the industry's most cost-effective and easy-to-use data platform.
- + She holds a bachelor's degree from UCLA and a master's degree from the Stanford Graduate School of Business.

Rethinking Long-term Incentives: Adapting to Evolving Standards



How did we get here?



The role of the proxy advisors



What the current data says for S&P 500 CEO LTI design benchmarks



What about different performance metrics?



Where are we now?



What institutional investors say about long-term Incentives



Some interesting case studies across the marketplace



Potential evolution in proxy advisor voting policies and LTI grant practices

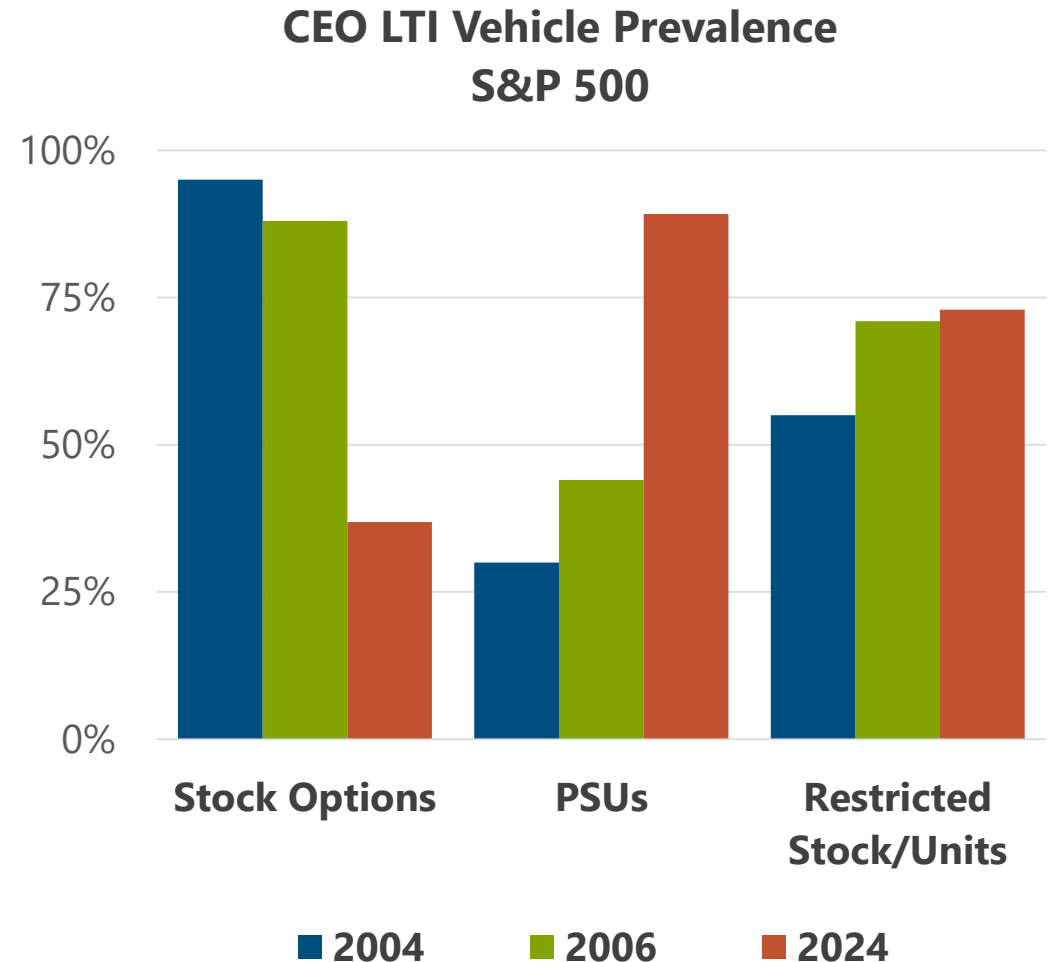
How did we get here?

- + Pre-2005: Options were “free”
 - Expense only required if exercise price less than stock price
 - Other conventional LTI instruments incurred an earnings charge
- + December 2005: FAS 123R leveled the LTI playing field with mandatory stock option expensing
- + SEC Disclosure Enhancements (2006) and the rise of ISS and Glass Lewis
- + The Rise of Relative TSR Plans (and its pitfalls)



Where are we now?

- ✓ Portfolio approach to long-term incentives
- ✓ Heavy emphasis on performance-based LTI
- ✓ Decline of stock options as the primary LTI vehicle
- ✓ Rise of performance shares as the primary LTI instrument
- ✓ Continued use of time-based RS/RSUs as a balancing tool
- ✓ Increased scrutiny from proxy advisors



Proxy advisors don't make the rules...But they hold the pen

Say-on-Pay Impact



- + A "NO" vote recommendation from ISS is worth ~25% of investor support (GL has less influence, a "NO" vote recommendation is worth ~10%)
- + Companies deliver LTI with an eye toward ensuring shareholder support

Investor Influence



- + Many investors rely on proxy advisor research to guide voting
- + Amplifies their influence across the asset managers

Trend Acceleration



- + Drive adoption of what they view as "best practices"

Establish Standards and Red-flag Practices

- + Standards: 50%+ of LTI in performance-based equity, strong metrics, payout caps
- + Standards become industry "best practice"
- + We don't consider stock options as performance-based compensation



Constraints on Innovation

- + Pressure to conform has increased design homogeneity, making it challenging to consider atypical approaches
- + Cost of going against the grain



Global Impact

- + ISS and Glass Lewis advise across the globe. Will "one-size-fits-all" policies be further standardized across countries?



Considering the Opinions of Institutional Investors and Issuers

- + Annual policy surveys provide an opportunity for issuers and investors to shape proxy advisor voting policies

- + A particular focus in the policy surveys for 2025 and 2026 related to executive pay:

- Mix of performance-based and time-based equity
- Whether extended vesting or holding period requirements can mitigate pay for performance concerns
- The types of circumstances in which granting time-based equity is acceptable

Q: What is a vesting requirement?

A: A vesting requirement is the time and/or performance condition that must be met before an executive gains full ownership of the equity award (or other compensation/benefit).

Q: What is a holding period requirement?

A: A holding period requirement means that even after an award has vested, the executive must continue to hold some portion of the shares received from vesting/option exercises for a period of time before the shares can be sold.

- + What kind of feedback did the proxy advisors receive for the 2025 policy survey???

A spotlight on Norges Bank Investment Management (NBIM) – A leading advocate to drive change in executive LTI arrangements

What is NBIM?



- + NBIM, Norway's pension fund manager, is one of the world's largest sovereign wealth funds (\$1.6T in assets)
- + Owns ~1.5% of global equity markets

NBIM's Position on LTI Design



- + Advocates for simple, transparent pay structures
- + Prefers time-based share grants vesting over 5–10 years with rigorous holding period requirements
- + Skepticism around performance-based equity (funds above target, overly complex, benefit management at the expense of shareholders)

Rationale for NBIM Preferences

- + **Long-Term Alignment:** Long-term shares drive long-term value alignment
- + **Reduce Complexity:** Avoid poorly calibrated, easily adjusted performance metrics that are management-friendly
- + **Transparency:** Clearer, more predictable compensation outcomes



NBIM in Action

- + Engages with proxy advisors and investors on alternative pay models
- + Voted against management Say on Pay 90+ times in 2024
- + Across investment managers, one of the loudest voices in on-going debates about executive pay



The survey says.!!!

ISS Policy Survey Respondents

- + Many investors want long-vesting time-based equity treated as a mitigating factor in pay for performance assessments (similar to performance awards) but ultimately, feedback was somewhat mixed
- + Extended vesting: Majority say ≥ 5 years is sufficient; some prefer longer (7+ years)
- + Post-vesting holding: Most investors support requiring it; non-investors less so

Glass Lewis Policy Survey Respondents

- + Strong majority of investors favor performance-based equity as the primary long-term incentive
- + Time-based awards generally disfavored, except when:
 - Award sizes are reduced
 - Vesting is 5+ years
 - Post-vesting holding requirements apply
- + Key concerns: overly complex metrics, unclear goals, dilution, weak alignment

Due to the mixed investor feedback, changes to proxy advisor voting policies for FY25 around performance-based equity were modest

ISS

- + No formal policy changes. Offered clarifications around its assessment of executive pay:
 - Greater focus on performance-based equity, particularly where there is a PFP disconnect
 - Red flags: no disclosure of forward-looking goals, poor disclosure of vesting results, excessive pay opportunities, non-rigorous goals, overly complex PSU structures
 - Stock options still not considered performance-based

Glass Lewis

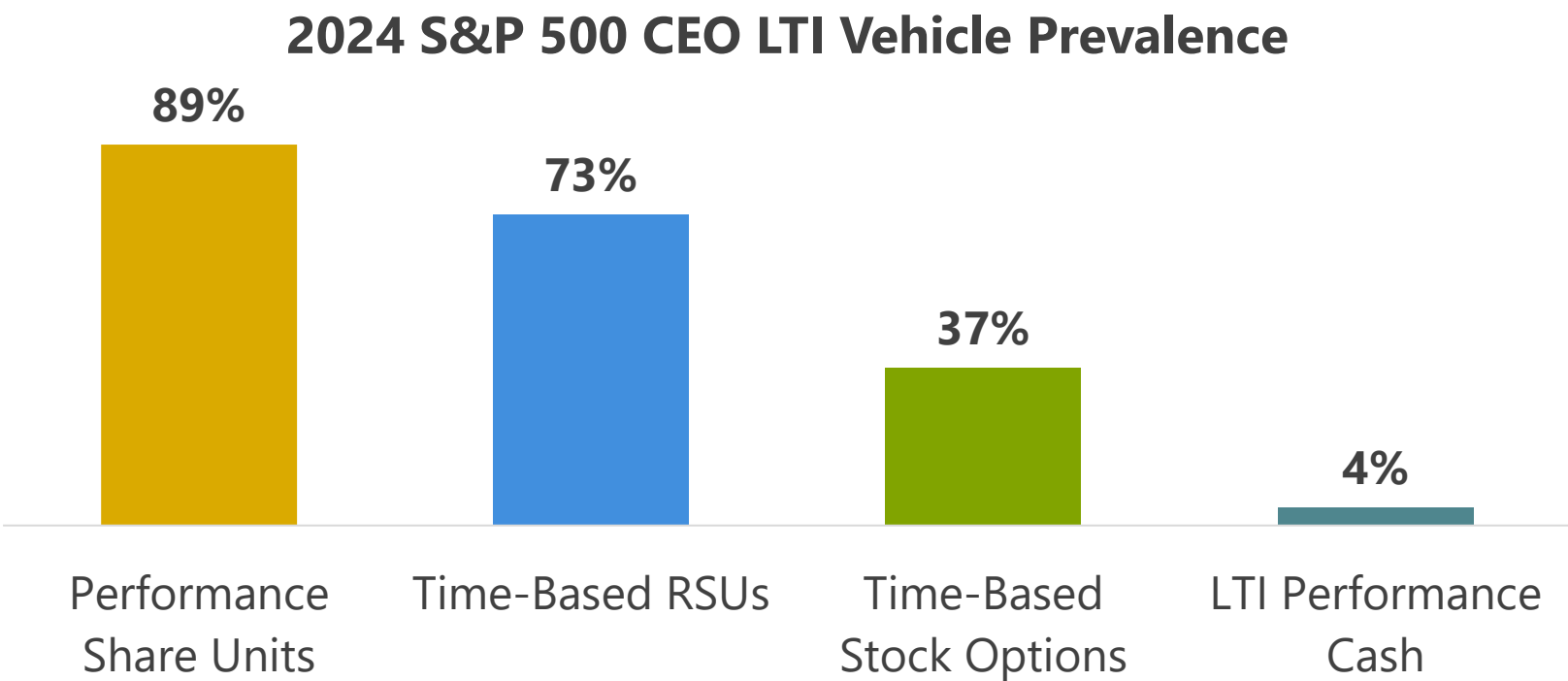
- + Limited formal policy changes to underscore a holistic approach and that analysis of executive pay occurs on a case-by-case basis
- + Added post-vesting holding periods to the list of favorable design elements
- + Stock options still not considered performance-based

More extensive changes to proxy advisor voting policies are expected in 2026

Client Advice: Focus on transparent disclosures and how plan designs and compensation decisions support business and human capital needs

Current S&P 500 CEO Market Data: LTI Vehicle Prevalence

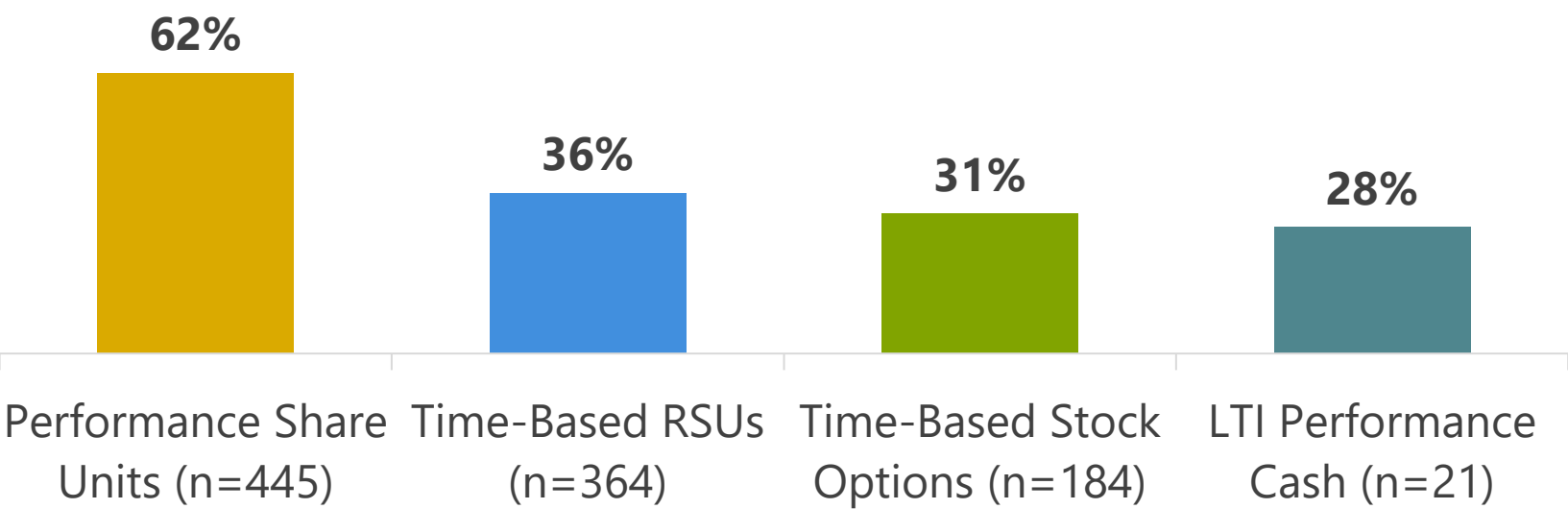
- + Nearly 90% of companies in the S&P 500 grant the CEO PSUs while almost 75% grant time-based RSUs
- + Stock options are used by less than 40% of companies and just 4% of companies grant cash LTIP awards



Current S&P 500 CEO Market Data: LTI Vehicle Weighting

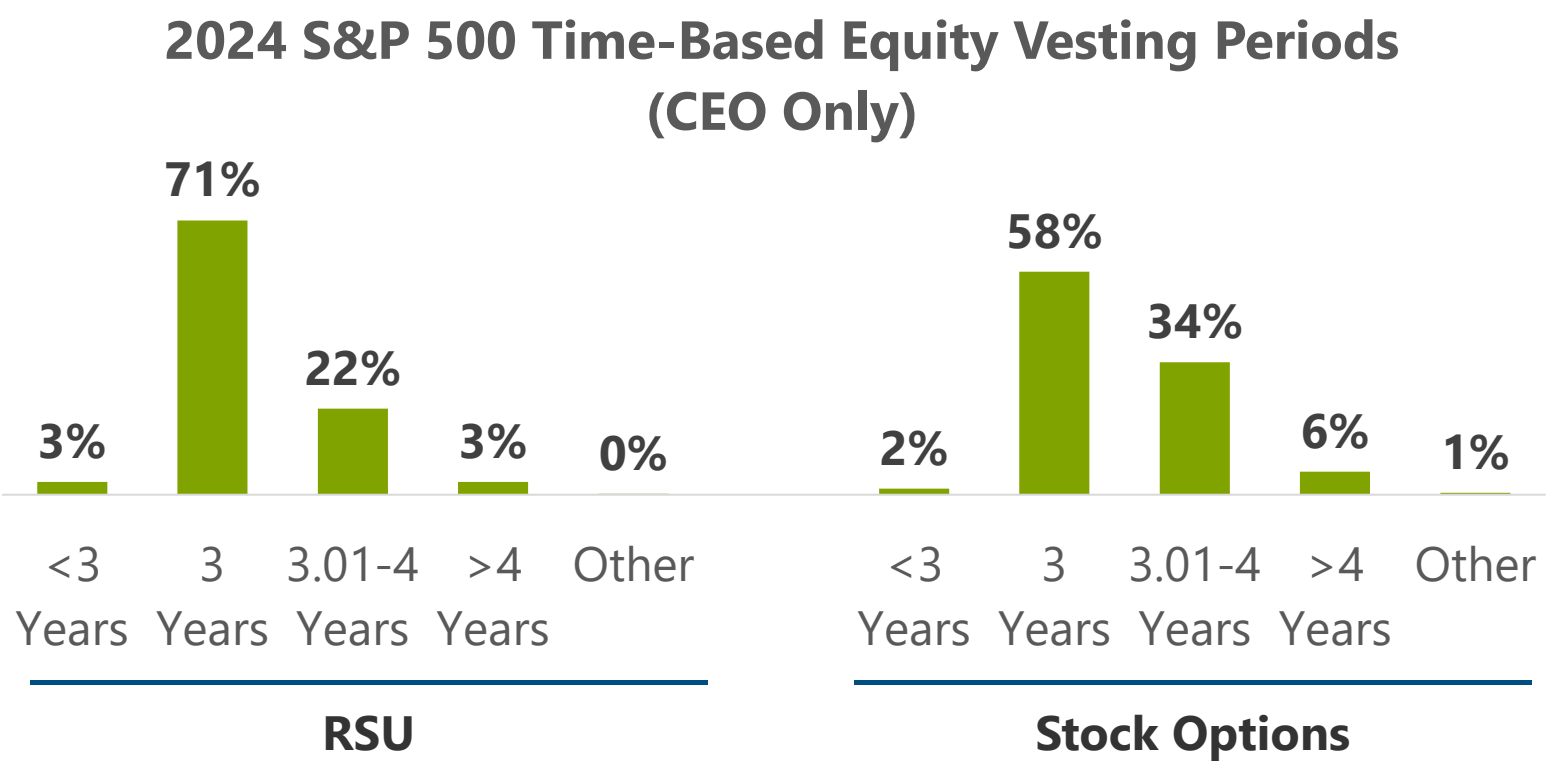
+ On average, companies in the S&P 500 granted 62% of CEO equity in performance stock

2024 S&P 500 CEO Average LTI Mix Weighting for Companies Granting that Vehicle



Current S&P 500 CEO Market Data: LTI Vesting

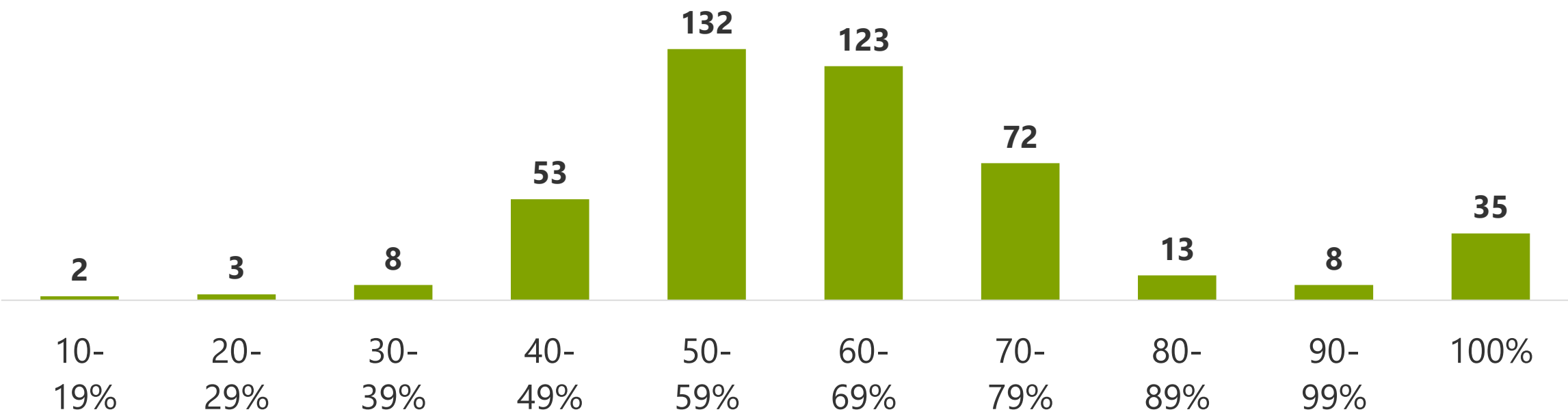
- + It is slightly more common for stock options to have longer vesting periods than restricted stock and RSUs
- + Only 3% and 7% of companies had vesting periods longer than four years



Current S&P 500 CEO Market Data: % of Performance-based LTI

+ Of the 449 S&P 500 companies that granted performance-based LTI to the CEO, 383 (85%) granted at least 50% of LTI in performance-based awards*, consistent with ISS and Glass Lewis practice standards

2024 S&P 500 CEO Performance-Based LTI Prevalence (CEO Only)



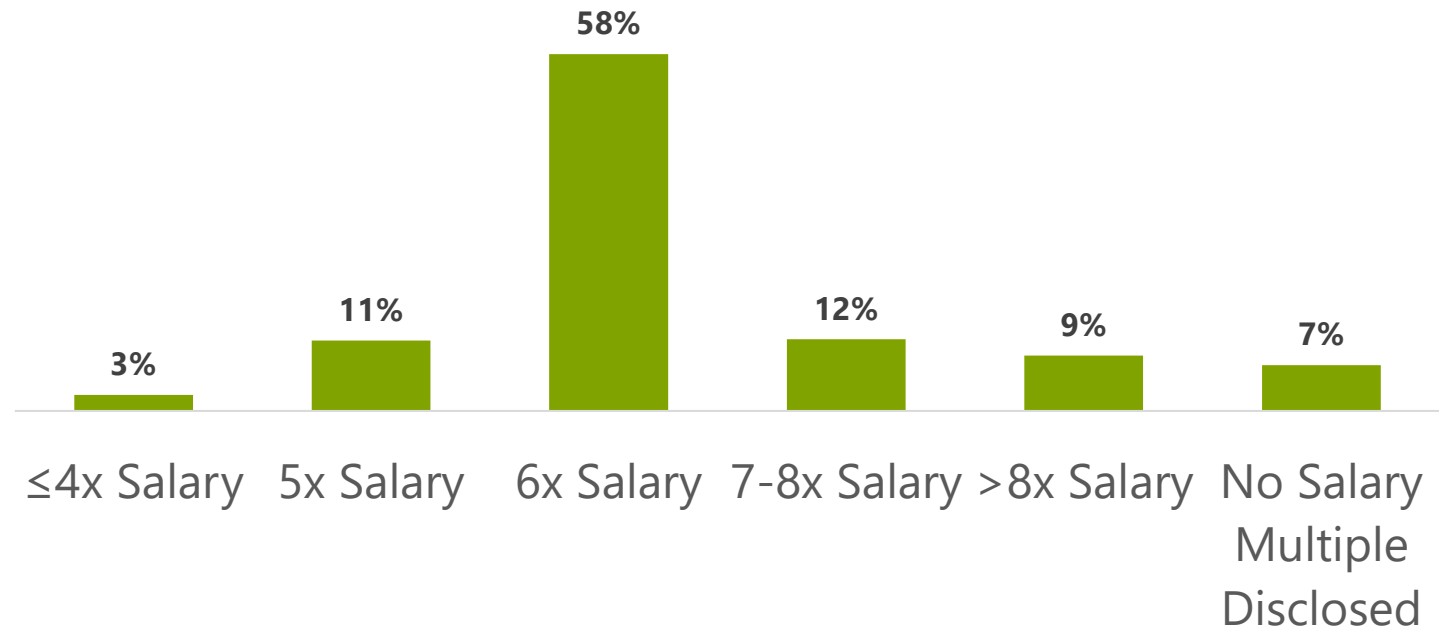
**To align with ISS and Glass Lewis methodology, this chart treats stock options as not performance-based*

Current S&P 500 CEO Market Data: Stock Ownership Guidelines (Multiple of Salary)

+ Within the S&P 500, 477 companies (96%) disclose CEO stock ownership guidelines with 461 companies referencing the CEO's salary in the guideline construct

+ 58% of S&P 500 companies set the CEO ownership multiple at 6x salary

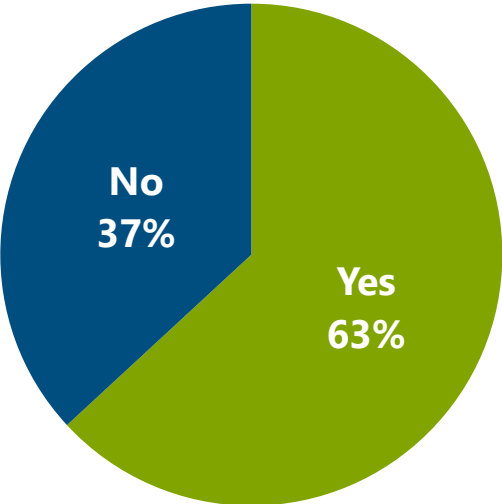
2024 S&P 500 Stock Ownership Guidelines (CEO Only)



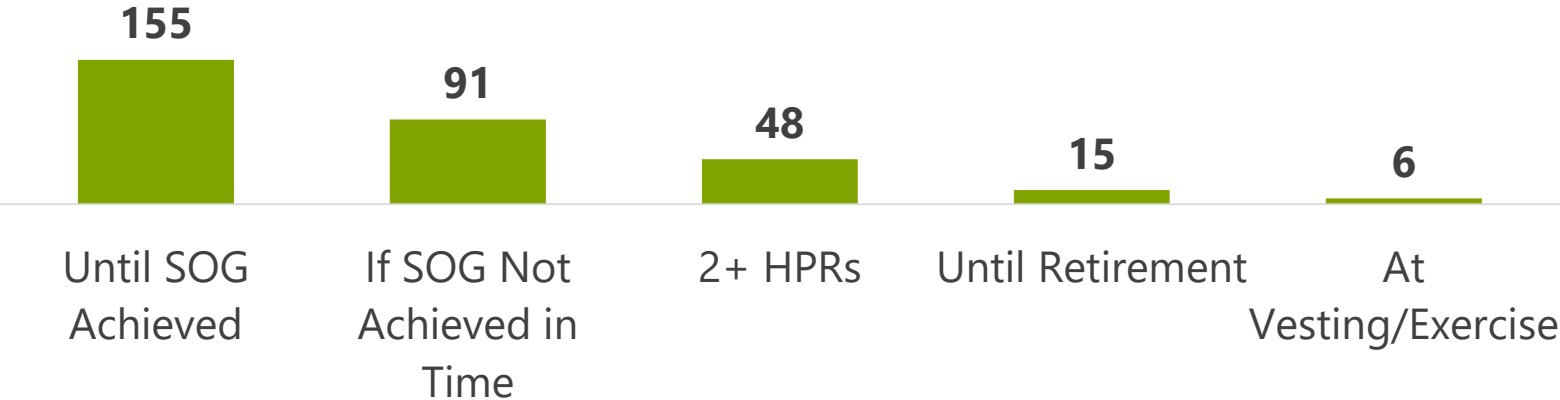
Current S&P 500 CEO Market Data: Holding Period Requirements (“HPRs”)

- + Within the S&P 500, 315 companies (63%) have HPRs for the CEO and other senior executives
- + Most commonly, the HPR is effective until the ownership requirement is achieved (~50% of cases) or if the ownership requirements is not achieved within the specified time period (~29% of cases)
- + A minority of companies use multiple HPRs (i.e., 50% of net shares until guideline is met. If guideline not met in 5 years, HRP increases to 100% until guideline met)

**2024 S&P 500 CEO Holding
Period Requirement Prevalence**



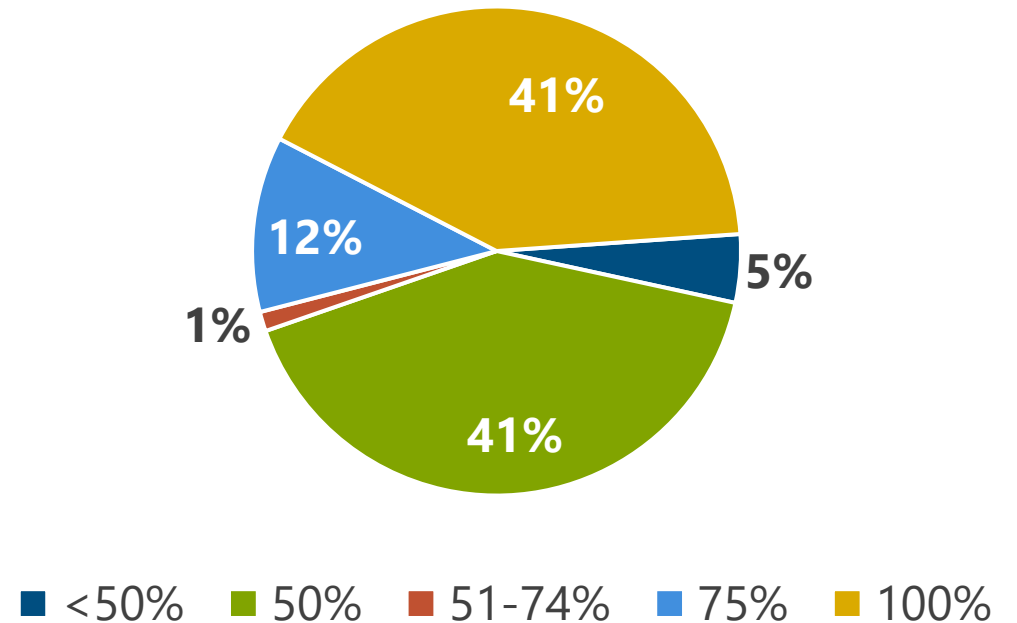
CEO Holding Period Requirement Applicability



Current S&P 500 CEO Market Data: Holding Period Requirements (“HPRs”)

- + For the 155 companies that provide for a HPR until the SOG is achieved:
 - 41% of companies require 50% of net shares to be retained and 41% of companies require 100% of net shares to be retained
 - 12% of companies require 75% of net shares to be retained

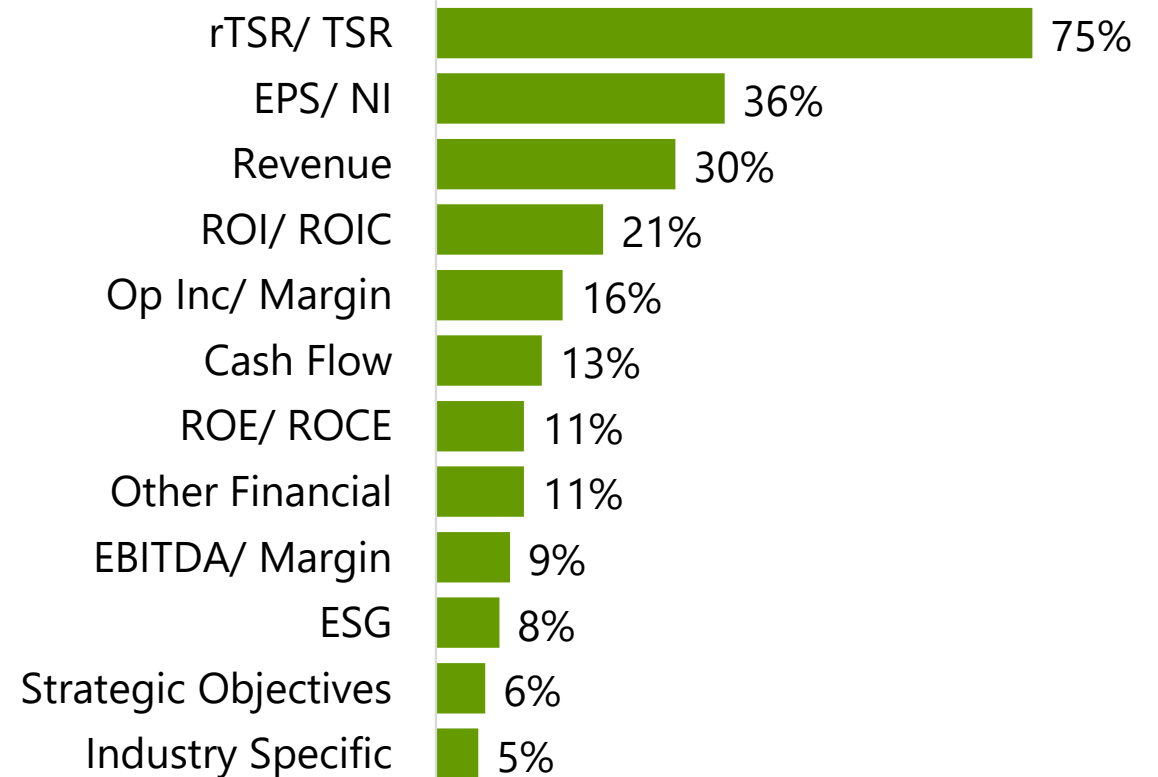
2024 S&P 500 CEO % of Shares Subject to HPR Until SOG Met



We review metric prevalence for performance-based equity

- + It is worth reviewing metric prevalence for performance-based equity although the discussion is separate from those related to vesting provisions and holding period requirements
- + Data indicates that TSR and other stock price-based metrics continue to be most common
- + Metric usage beyond TSR and other stock price-based metrics is varied

2024 S&P 500 CEO PSU Performance Metric Prevalence



We have not discussed performance metrics. Unfortunately, there are no metric selection silver bullets

+ Business strategy and context, rather than market prevalence or fad, should drive metric selection



Focus on the metrics that drive value



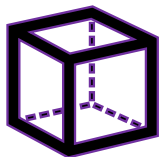
Relative TSR, while simple, has its limitations



Goal calibration is as important, if not more important, than performance metric selection



Too many measures risks dilution of the performance focus



Growth and returns required for sustainable value creation



Measures should be complementary and align with the value chain

Some interesting case studies across the marketplace

These companies were chosen only for their LTI design features and to spark discussion. No criticism or value judgments are intended

Company	Equity Practices in Place
Old Dominion Freight Line	+ <u>CEO FY24 equity mix</u>: 53% RSUs and 47% PSUs + <u>Vesting on time-based equity</u>: 3-year ratable on RSUs + <u>Stock ownership guidelines</u>: 6x CEO base salary + <u>Holding requirement</u>: 50% of net shares until SOG achieved. 50% of net shares from vesting/exercise for 1 year
Keurig Dr. Pepper Inc.	+ <u>CEO FY24 equity mix</u>: 100% time-based RSUs (introducing PSUs at 25% weight in FY25) + <u>Vesting on time-based equity</u>: 5-year ratable on RSUs (60% after 3 years, then 20% in each of years 4 and 5) + <u>Stock ownership guidelines</u>: 10x CEO base salary to be obtained within 1 year + <u>Holding requirement</u>: 50% of net shares until SOG achieved

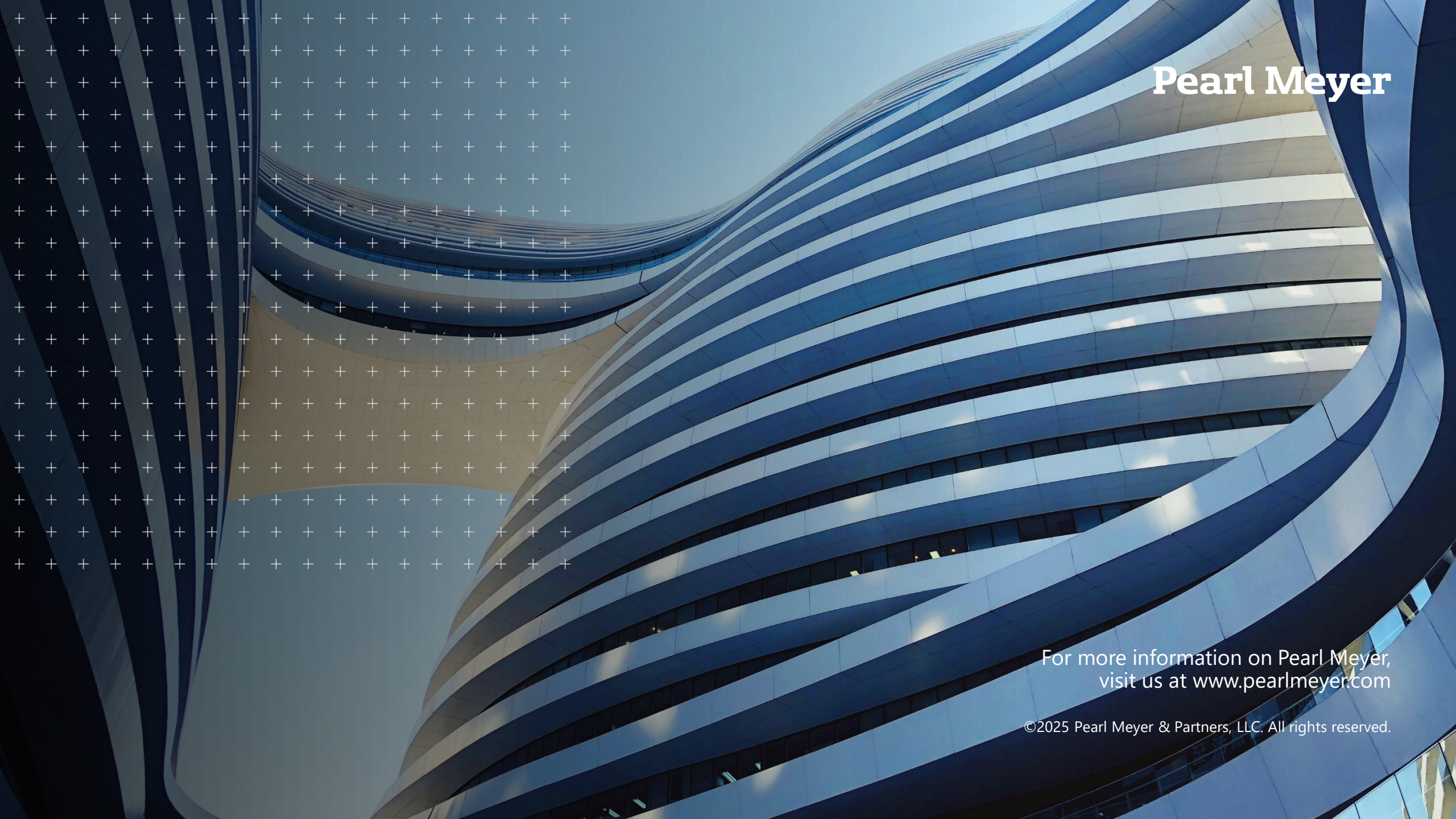
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Company	Equity Practices in Place
Juniper Networks (Recently acquired by Hewlett-Packard Enterprise)	+ <u>CEO FY24 equity mix</u>: 75% time-based RSUs and 25% PSUs + <u>Vesting on time-based equity</u>: 3-year ratable + <u>Stock ownership guidelines</u>: 6x CEO base salary to be obtained within 5 years + <u>Holding requirement</u>: 50% of net shares until SOG achieved. 100% of net shares from vesting/exercise for 1 year
Autozone	+ <u>CEO FY24 equity mix</u>: 100% options + <u>Vesting on time-based equity</u>: 4-year ratable + <u>Stock ownership guidelines</u>: 6x CEO base salary to be obtained within 5 years + <u>Holding requirement</u>: 50% of net shares from vesting/exercise if guideline is not reached within 5 years

Potential evolution in proxy advisor voting policies and LTI practices

Topic	Forecast
Adjustment to ISS & Glass Lewis Voting Policy	+ Both advisors soften standards on delivering 50% of LTI in performance-based awards + For companies delivering more than 50% of LTI in time-based equity, ≥ 5-year vesting restrictions or ≥ 1-year post-vest holding period requirements can mitigate pay for performance disconnects
Simplicity and Back to Basics	+ Investor fatigue with overly complex PSU structures (e.g., layered 1-year goals, etc.) may push adoption of simpler PSU structures or lead to companies delivering more equity in time-based vehicles
A Focus on Disclosure	+ Companies will continue to refine their disclosure strategy, focusing on transparent explanations of the connection between performance and compensation outcomes



Pearl Meyer

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