

Board pay has always been an interesting — and sometimes uncomfortable — topic for outside directors.

It's uncommon to set one's own pay level, and doing so as a steward of a corporation and its shareholders can be uncomfortable. Add to this the December 2017 Investors Bancorp lawsuit — which brought a new challenge to protections under the "business judgement" rule — and a subsequent ruling by the Delaware Supreme Court, and board pay has even the most coolheaded outside directors wringing their hands in anticipation of potential criticisms of their best efforts at getting it right.

We offer here three simple rules for stress-free board pay, even where the long-standing and board-favorable business judgment rule has taken a major hit. By following these rules (which are reflective of leading practice today), outside directors are unlikely to become a target for plaintiffs' lawyers.

Pay responsibly

- Target your total director pay to the mid-range of the competitive market.
- In order to do so, you need to know your competitive market. For most companies, the right "market" definition for director pay is the same as for executive pay: a peer group of one to two dozen companies of comparable size and business focus; and broader-market, survey-reported information.
- Further, you need to test the market regularly. For most companies, this means

comprehensive benchmarking of director pay levels and structure every other year. Why every other year? Director pay should remain fairly consistent year to year, and therefore market benchmarks are fairly stable over time.

ier to identify (especially for the plaintiffs' attorneys who seek them out).

Practice great hygiene

• Establish meaningful limits on director pay. Many companies have done this by setting annual limits on

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• In recent years, the range from highest- to lowest-paying boards has narrowed considerably. It's common in peer groups today to see high-low spreads that range only about 20% from the median. This reversion to the midpoint means that "outliers" are that much eas-

equity to directors. Generally, the new model for "meaningful limits" sets a dollar-based maximum on equity grants between \$500,000 and \$1m. Some companies have extended these limits to director pay, overall, inclusive of cash and equity.

- Beware of fixed-share grants. Today, most companies grant a dollar value of equity each year to directors. This approach makes it easy to manage total pay consistently year to year. Some companies grant a fixed number of shares the value of which will vary depending on share price. The "noise" inherent with a fixed-share approach can draw external attention, particularly where strong price performance drives a significant uptick in the reported value of director grants. Again, director pay outliers are easy to identify.
- Establish a deferral mechanism to allow directors flexibility in managing their individual tax expe-

- rience. At the same time, maintain a healthy mix of cash and equity pay no less than 40% cash for most to avoid director stock sales to cover tax bills.
- Finally, you want to plan ahead for hazard pay. Too often boards find themselves paying in arrears for periods of extraordinary service (e.g., a major M&A transaction; a leadership change). The easy approach here is to stipulate that board and committee cash retainers cover a preset number of meetings each year. If a given year requires more, then per-meeting fees automatically kick in.

Tell your story

• For many companies, director pay disclosure is

compliance-oriented and intentionally bare bones. Today, you want to approach director pay disclosure much more akin to compensation discussion and analysis discourse of executive pay. In your public disclosure, be sure to make clear how you apply the rules above, from target-pay positioning through to the benchmarking approach, along with the "pay hygiene" features of your program.

Following these simple rules will help protect your board from external challenge. Director pay can be simple and safe. By establishing clear parameters for director pay, boards can proactively communicate

with the external audience the what, how, and why of director pay. And in doing so, boards can protect themselves from potential legal challenge — even where the business judgment rule has been softened by the Investors Bancorp decision.

Barry Sullivan, Managing Director at Semler Brossy Consulting Group, has 15 years of experience advising boards and management teams on executive and strategic pay issues. He can be reached at bsullivan@semlerbrossy.com. Kathryn Scherich is a consultant with the firm and is experienced in designing a broad range of reward programs. She can be reached at kscherich@semlerbrossy.com

