

# Incentive Design Changes in Response to Covid-19

*Russell 1000*

SEMLER BROSSY REPORT

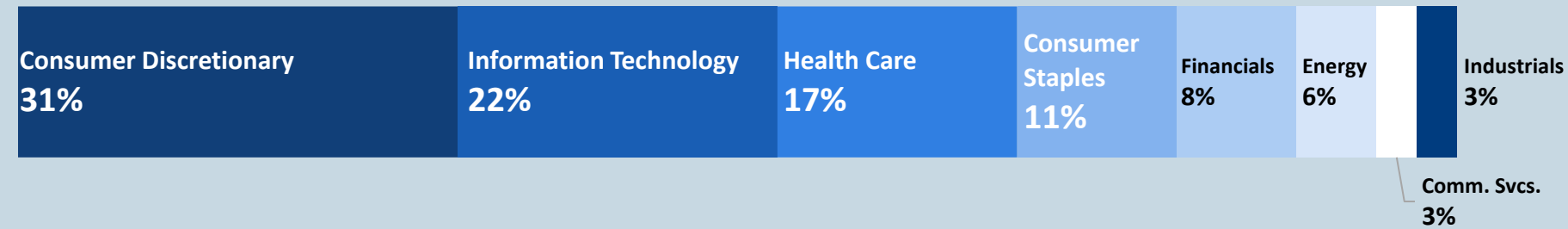
AS OF SEPTEMBER 10, 2020

*NOTE: Semler Brossy Consulting Group does not provide tax, legal or accounting advice and does not provide regulatory guidance in the jurisdictions being considered. The Company should consult its respective experts in those fields on such matters, as appropriate.*

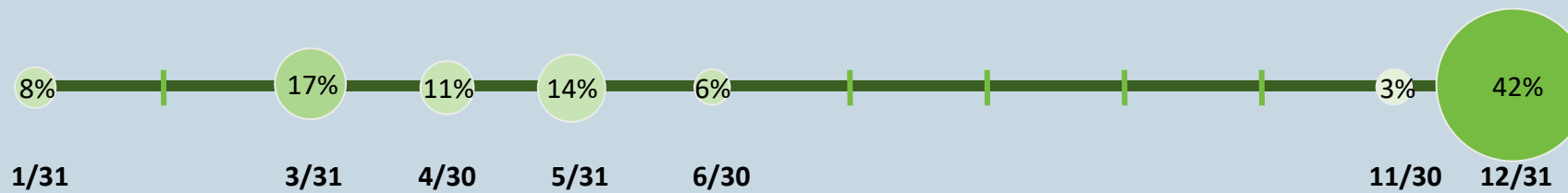
# Sample Overview

N = 36 COMPANIES

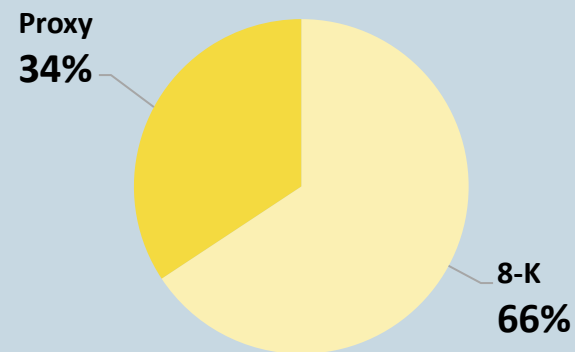
## SECTOR BREAKDOWN



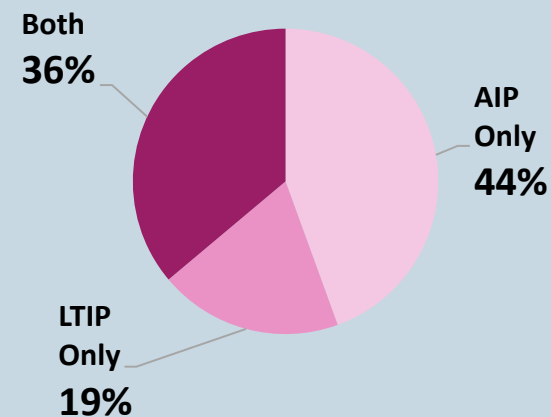
## FYE DATE BREAKDOWN



## FILING BREAKDOWN



## ACTIONS TAKEN





## Observations

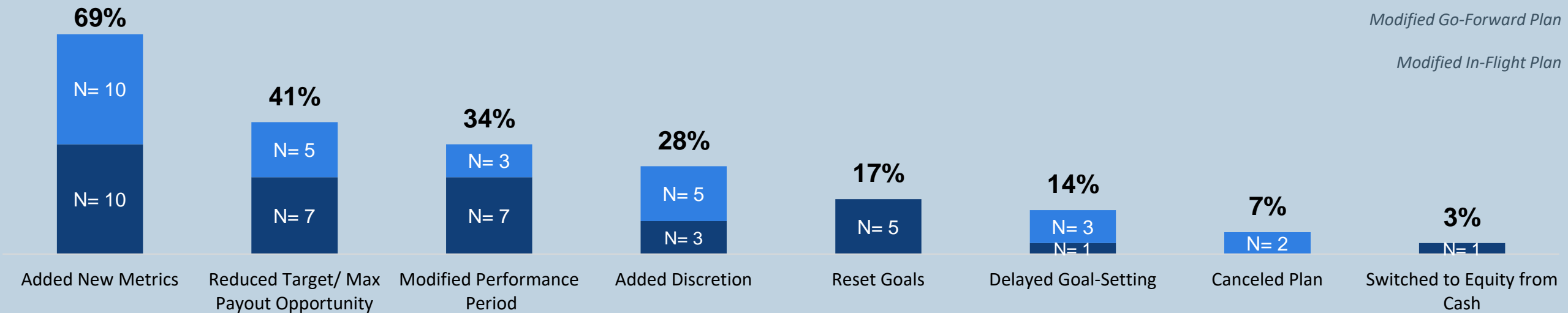
- Between June 1<sup>st</sup> and September 10<sup>th</sup>, 36 Russell 1000 companies announced changes to their in-flight and/ or go-forward incentive programs to address Covid-19's impact:
  - Consumer Discretionary (31%) and Information Technology (23%) companies make up slightly more than half the sample
  - Changes have been disclosed more often in 8-K filings (primarily 12/31 and 1/31 FYE companies with an in-process FY) than proxy filings (primarily 3/31 and 6/30 FYE companies with a recently started FY)
  - Consumer Discretionary (33%) and Information Technology (33%) make up two-thirds of 3/31 FYE companies that have disclosed changes
  - About half the sample announced changes to their annual incentive plan only and about one-third announced changes to both the annual and long-term incentive plans
- 42% of companies in the sample previously announced temporary reductions to executive base salaries as an immediate response to Covid-19

# Annual Incentive Plan Changes

COVERS IN-FLIGHT AND GO-FORWARD PLANS

(N=29 Companies Disclosed Annual Incentive Plan Changes)

Modified Go-Forward Plan   
Modified In-Flight Plan 



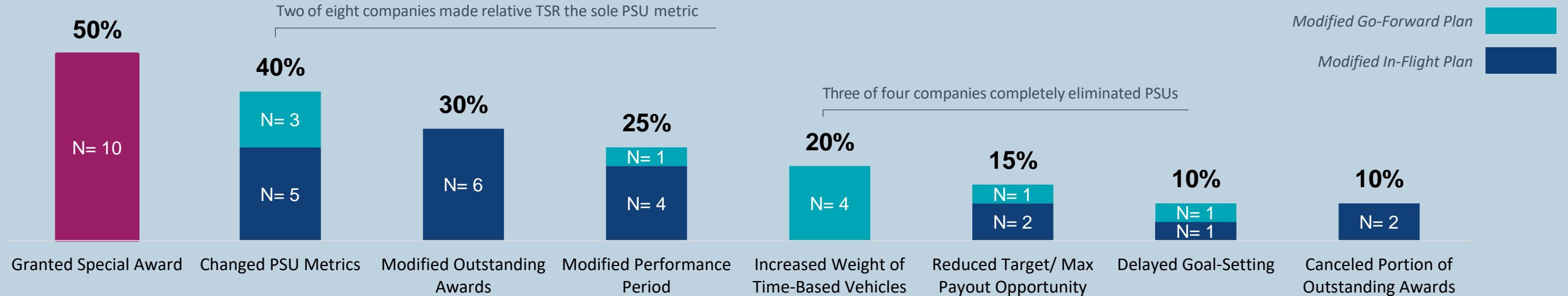
## Observations

- The most common annual incentive plan change has been to add new metrics (69%); commonly added metrics have been cash flow, EBITDA, and strategic/ operational health measures
- The second most common change has been to reduce target or max payout opportunities (41%), both for the in-flight plan and the go-forward plan
- Ten companies modified the annual incentive plan performance period (typically to measure partial year performance), and eight companies explicitly added Committee discretion to determine payouts (although, this approach may be more prevalent in practice given the qualitative measurement of certain additional metrics)
- Five companies reset performance goals for the in-flight plan based on updated forecasts and four companies delayed goal-setting
- Two companies elected to cancel the annual incentive plan for the recently started fiscal year
- Since our last report, Lions Gate Entertainment was the first Russell 1000 company to pay a portion of the annual incentive bonus, as determined by the plan's formula, in RSUs instead of cash

# Long-Term Incentive Plan Changes

COVERS IN-FLIGHT AND GO-FORWARD PLANS

(N=20 Companies Disclosed Long-Term Incentive Plan Changes)



## Special Retention and Recognition Awards

- Ten companies granted special awards meant to retain or recognize select NEOs
  - Seven companies granted special awards to all NEOs (including the CEO) in recognition of the challenging period
  - Two companies granted a recognition award to one specific executive (non-CEO executive)
  - One company (NIKE) paid a discretionary cash bonus to make up for Covid-19's impact on incentive payouts
- Awards generally ranged from \$2.0M to \$7.3M for the CEO and \$330K to \$2.2M for the other NEOs (typically equivalent to less than one-year annual grant value)

## Observations

- Eight companies switched their PSU metrics, typically to measure metrics that are (i) more focused on operational health (e.g., cost reduction); (ii) more easily forecasted; and/ or (iii) relative metrics
- Six companies disclosed modifications to in-flight awards' performance goals; five disclosed changes to the outstanding 2020-2022 cycle and one disclosed changes to the 2019-2021 and 2020-2022 cycles
- Four companies adjusted the long-term incentive vehicle mix to a higher weighting of time-based vehicles (i.e., RSUs or stock options); three companies eliminated PSUs entirely
- Three companies reduced target and/ or max payout opportunities, and two companies (Gap and J.M. Smucker) delayed PSU goal-setting until August
- Since the last report, two companies canceled a portion of outstanding PSUs: Nordstrom replaced each NEO's most recent PSU grant with stock options (1:1 value ratio for the CEO) and Wynn Resorts canceled 140,000 of the CEO's outstanding PSUs to offset dilution associated with the company's retention award

# Case Studies

WE HIGHLIGHT SIX COMPANIES WITH MORE EXTENSIVE ACTIONS — PAGE 1 OF 2

COMPANY **Henry Schein**

FILING **8/12/20**

FYE DATE **12/31**

INDUSTRY **Health Care**

## COVID INCENTIVE ACTIONS

### Annual Incentive Plan

- Suspended the FY20 Henry Schein Performance Incentive Plan (“PIP”) and canceled all corresponding PIP awards
- Adopted 2020 Recovery Performance Plan (“RPP”) designed to reward employees, including NEOs, for contributions to the company’s business recovery strategy
- Individual target bonus amounts for NEOs under the RPP are expected to be materially less than target amounts set under the PIP
- Established performance goals based on a performance period commencing July 1, 2020 and ending December 26, 2020, including:
  - Company-wide profitability goals
  - Functional area/business unit-level operating income and expense management goals
  - Individual performance goals designed to drive toward and support business recovery efforts

COMPANY **Wynn Resorts**

FILING **8/20/20**

FYE DATE **12/31**

INDUSTRY **Consumer Discretionary**

## COVID INCENTIVE ACTIONS

### Annual Incentive Plan

- Established second-half 2020 goals focused on cash generation and preservation in US operations and market share in the Company’s Macau operations

### Long-Term Incentive Plan

- Intend to reset long-term performance targets for named executive officers as business conditions become clearer throughout the remainder of 2020 and early 2021

### Additional Actions

- Approved one-time grant of RSUs for approximately 240 top leaders, including NEOs, which will vest on the 1-year anniversary of the grant date; award value was ~33% of CEO’s and ~70% of CFO and GC’s annual equity grants
- At CEO’s request, canceled 140,000 PSUs previously granted to him based on performance metrics that are no longer relevant in light of Covid-19 to partially reduce equity dilution associated with Retention Award

COMPANY **Pinnacle Financial Partners**

FILING **8/17/20**

FYE DATE **12/31**

INDUSTRY **Financials**

## COVID INCENTIVE ACTIONS

### Annual Incentive Plan

- Established alternative performance measurement under the 2020 Annual Cash Incentive Plan based on an additional metric with reduced payout opportunity
  - Additional performance metric is tied to the Company’s pre-tax, pre-provision net revenue for the year ending December 31, 2020
- Participants will be able to earn a cash incentive payout based on the larger of:
  - Original plan metrics: 80% diluted EPS and 20% deposit volume and rate goals (100% and 125% payouts at target and maximum, respectively); or
  - Modified plan metrics: 15% pre-tax, pre-provision net revenue and 20% deposit volume and rate goals (35% and 50% payouts at target and maximum, respectively)

# Case Studies

WE HIGHLIGHT SIX COMPANIES WITH MORE EXTENSIVE ACTIONS — PAGE 2 OF 2

COMPANY **Nike**

FILING **7/24/20**

FYE DATE **5/31**

INDUSTRY **Consumer Discretionary**

## COVID INCENTIVE ACTIONS

### Annual & Long-Term Incentive Plans

- Adjusted non-executive payouts based on annual incentive plan performance through 3 quarters and long-term cash performance through 11 quarters; the 2020 annual incentive and 2018-2020 Cash LTIP would have both paid 0% but were adjusted to pay out at 100% and 75% of target, respectively
- Granted discretionary cash bonuses to executives to approximate adjusted incentive payouts received by all other eligible employees (CEO's portion was \$6.8M)
- Adjusted their 2020-2022 Cash LTIP metrics to 100% relative TSR based (vs. 50% Revenue and 50% EPS)

COMPANY **Capri Holdings**

FILING **7/22/20**

FYE DATE **3/31**

INDUSTRY **Consumer Discretionary**

## COVID INCENTIVE ACTIONS

### Annual Incentive Plan

- Suspended FY21 annual incentive plan; the Committee will use discretion to determine whether any cash bonus payments outside the plan are appropriate or warranted based on actual performance for fiscal 2021
- Changes for when the plan is reinstated post-fiscal 2021: same financial metrics for all NEOs and no individual performance metric to align with Company performance widen performance and payout range by tying to the Company's operating budget because previous hurdles were too narrow and iii) interpolate annual incentives for all NEOs based on actual performance

### Long-Term Incentive Plan

- Equity awards were granted in the form of solely RSUs due to the difficulty in setting performance targets
- Mr. Idol's (CEO) award was reduced by 20%

COMPANY **WEX**

FILING **6/29/20**

FYE DATE **12/31**

INDUSTRY **Information Technology**

## COVID INCENTIVE ACTIONS

### Annual Incentive Plan

- Added new metrics based 40% on CAPEX, 40% on Cost Containment, and 20% on Operating Income of Health business to replace revenue and operating income metrics
- Shifted the performance period to the second half of 2020, ignoring first half performance
- Reduced maximum payout to 150% from 200%, and positive operating income was established as a threshold goal

### Long-Term Incentive Plan

- Changed metrics from 60% Net Income Earnings Per Share and 40% Compensation Revenue to
- 100% relative TSR (compared to the S&P 400 Index)

### Additional Actions

- Made an additional "Business Continuity Grant" of 75% relative TSR PSUs and 25% RSUs to NEOs and other selected employees










# Sample Detail

(N=36 COMPANIES) — PAGE 3 OF 4

Modified Go-Forward Award  

Modified In-Flight Program 

Company	Sector	Fiscal Year End	Revenue (\$000s) ▼	Filing	Annual Incentive Plan Changes								Long-Term Incentive Plan Changes												
					Added New Metrics	Reduced Tgt./ Max Payout Opp.	Modi. Perf. Period	Added Discretion	Reset Goals	Delayed Goal-Setting	Canceled Plan	Switched to Equity from Cash	Granted Add. Special Award	Changed PSU Metrics	Modified Outstanding Awards	Modified Perf. Period	Increase d Weight of Time-Based Vehicles	Reduced Tgt./ Max Payout Opp.	Delayed Goal-Setting	Canceled Portion of Out. Awards					
Capri Holdings	Consumer Discretionary	3/31	\$4,656	<a href="#">Proxy</a>																					
Wynn Resorts	Consumer Discretionary	12/31	\$4,341	<a href="#">8-K</a>																					
Paychex	Information Technology	5/31	\$4,041	<a href="#">Proxy</a>																					
Lamb Weston	Consumer Staples	5/31	\$3,792	<a href="#">Proxy</a>																					
Lions Gate Entertainment	Communication Services	3/31	\$3,740	<a href="#">Proxy</a>																					
DENTSPLY SIRONA	Health Care	12/31	\$3,439	<a href="#">8-K</a>																					
H&R Block	Consumer Discretionary	4/30	\$3,090	<a href="#">Proxy</a>																					
Sabre	Information Technology	12/31	\$2,668	<a href="#">8-K</a>																					
Viasat	Information Technology	3/31	\$2,303	<a href="#">Proxy</a>																					
WEX	Information Technology	12/31	\$1,681	<a href="#">8-K</a>																					
Pinnacle Financial Partners	Financials	12/31	\$887	<a href="#">8-K</a>																					

Source: S&P Capital IQ; financials as of 9/10/2020



For additional considerations and up-to-date analysis of the impact of Covid-19 on executive compensation, see our other Covid-19 resources at <https://www.semlerbrossy.com/covid-19/>

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