

September 25, 2012

“Compensation that Shareholders and Employees Will Embrace”



THE VISIONLINK
ADVISORY GROUP



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Today's Presenter:

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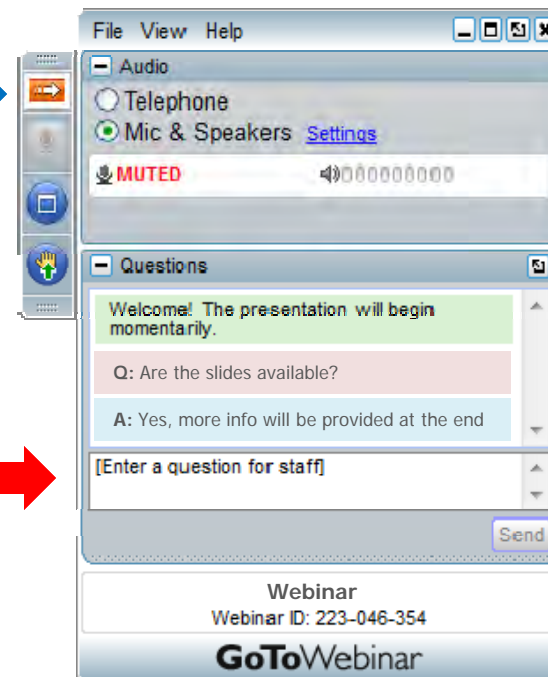
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Previously on our Webinar



Value Creation and Sharing

What Does it Really Mean?

Case Study

(Source: Chief Executive Magazine, May/June 2012 Edition)



**Underwriters
Laboratories**

Keith Williams



Keith Williams



- Assumed leadership of UL in 2005
- Company carrying considerable debt
- Losing market share
- Low employee morale
- UL had become bureaucratic and “siloed”
 - Regional divisions undercutting each other

5 Core Changes



Compensation (Value Sharing):

- Took away local measurements driving management incentive plans—all paid on same metrics
 - “We live together and we die together”
- Aligned everyone behind company success
 - “I call it ‘pay the company first.’”

Williams clearly defined what value creation meant and how it would be shared

Pay the Company First



“Basically, up to the company’s operating profit target, all of the profits go to the company; and only after that target is met, do we start funding the incentive pool.”

Example: If UL’s target is \$80 million--

- 100% of first \$80 in profit goes to company
- The next \$20 million goes to the incentive pool
- From there on, 50/50 between company & incentive pool

Pay the Company First



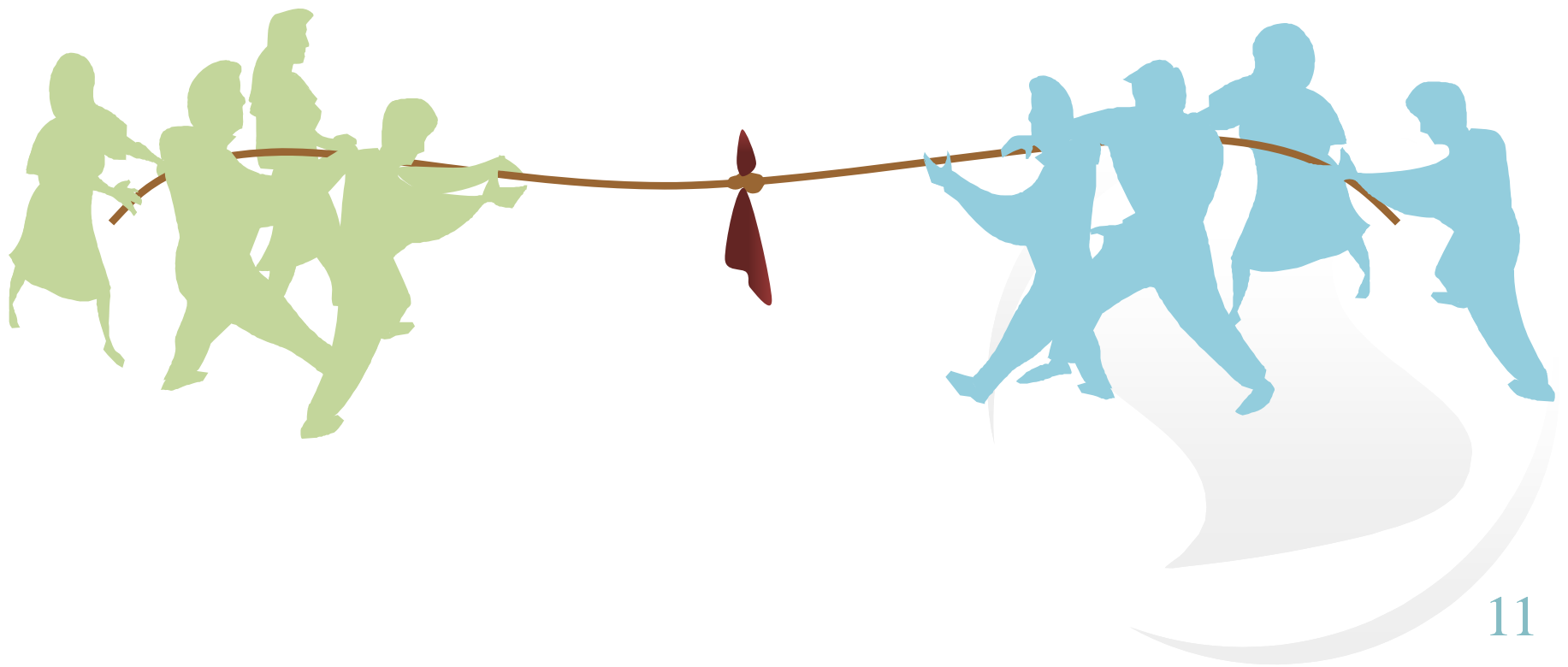
Once value creation is defined, compensation can follow a formula for sharing value in a way that aligns key producers with the company's business plan and priorities.

3 Key Distinctions

- Willing to tie all executive incentives to the same metrics
- Willing to identify a minimum return on equity threshold that must be met before any incentives are paid
- Willing to share significant upside beyond the threshold (no cap)



Expectations



Expectations



Pay the Company First



ROTRI™

Return on Total Rewards Investment™

Measuring the return on your compensation investment



How much is the Total Rewards Investment?

- Salaries
- Commissions
- Bonuses
- Deferred award accruals (LTIP)
- Core benefits
- Executive benefits
- Retirement contributions
- Payroll taxes



What return do you get on that investment?

____%



ROTRI™ Example:

Capital Account	\$ 20,000,000
Cost of Capital	12%
Capital Charge	\$ 2,400,000
Operating Income	\$ 10,000,000
Productivity Profit	\$ 7,600,000
Total Rewards Investment	\$ 25,000,000
ROTRI™	30.4%

(ROTRI™ = Productivity Profit/Total Rewards Investment)

ROTRI™ Example:

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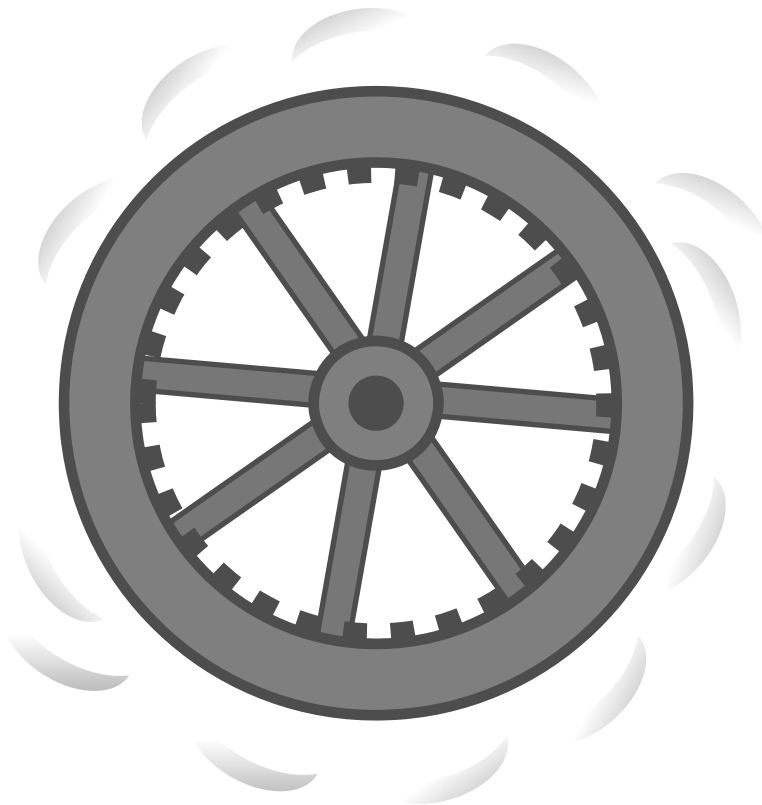
Variable Pay Plans (Value Sharing) are financed from Productivity Profit

When do employees have an “Ownership Mentality”

They have to “get” the following:

- We have a business model and strategy that are sustainable over time and produce a competitive advantage
- We all have to do our part to be productive (do things faster, easier, cheaper, bigger)
- Owners are committed to sharing the financial value we help create—after we’ve produced an appropriate return for them
- That value will be meaningful if we reach our full capacity





Who would object?

Traditional Approach

- Salaries based on market standards (the “tyranny of the median”)
- Bonuses are then based on a percentage of salary (with a cap)
- Ownership is restricted to a small group
- Compensation is tightly budgeted

Value Sharing Approach

- Salaries based on your unique skills and expected contribution
- “Bonuses” reflect value you help create (short-term value sharing plan, with no cap)
- Ownership is something to be nurtured in everyone (and a long-term value sharing plan is essential)
- Compensation is a reflection of the return on human capital

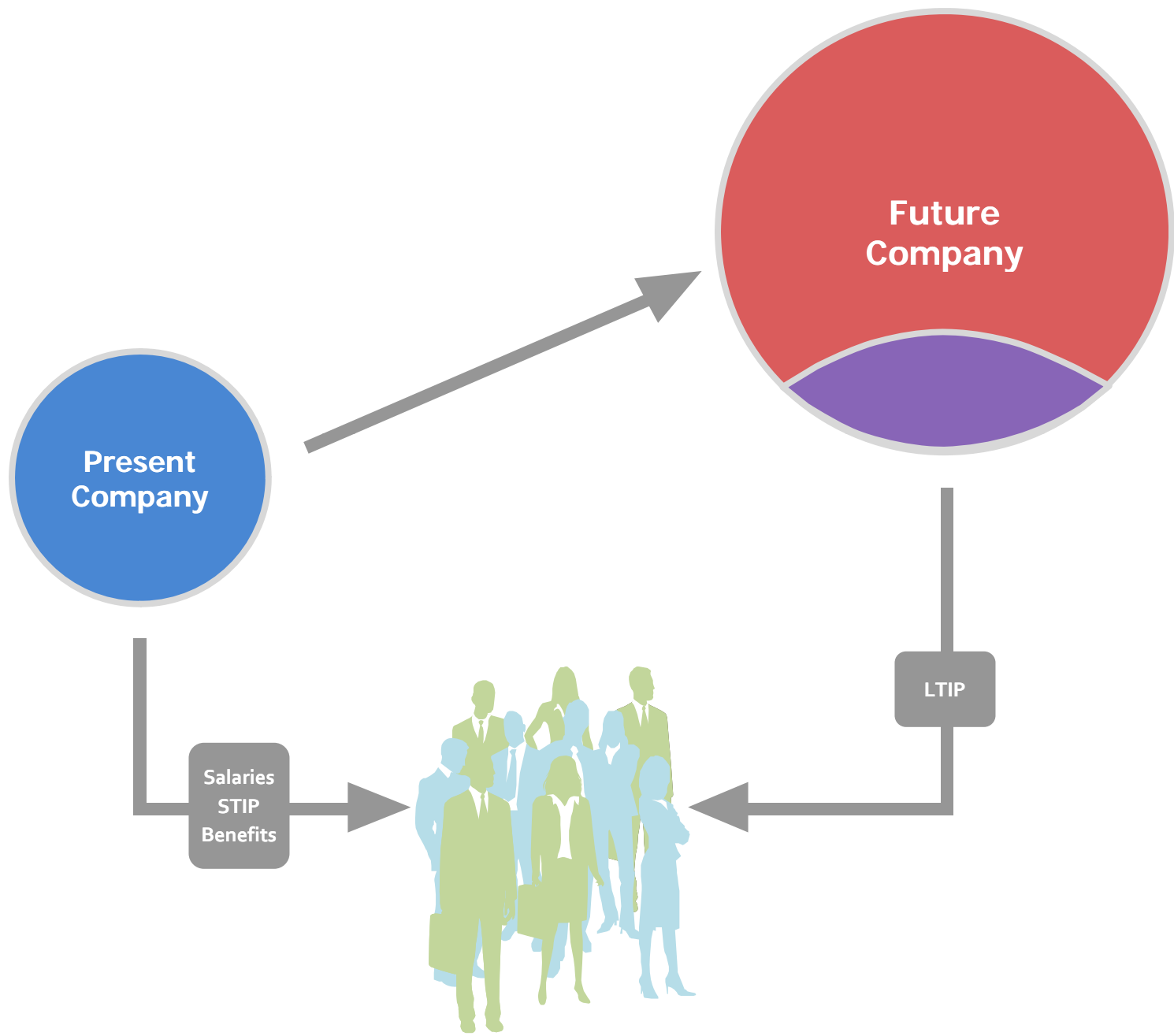
What value do we share?

■ Performance Class

- Paid to help company meet its “budgeted” or targeted level of performance (short-term value sharing plan; bonuses; incentive plans)
- Message: **“Operate our current company successfully”**

■ Growth Class

- Paid for building market (enterprise) value over time (long-term value sharing plan)
- Message: **“Build our future company”**



Why Long-Term Value Sharing Matters



What Happens When You Do It?

1. Value sharing attracts the best talent and magnifies results
2. Value sharing plans (effectively designed) reinforce the company's business model
3. Value sharing protects against bad profits and promotes good profits
4. Value sharing promotes an ownership mindset
5. Value sharing builds trust and accelerates results



When You Don't Do It:

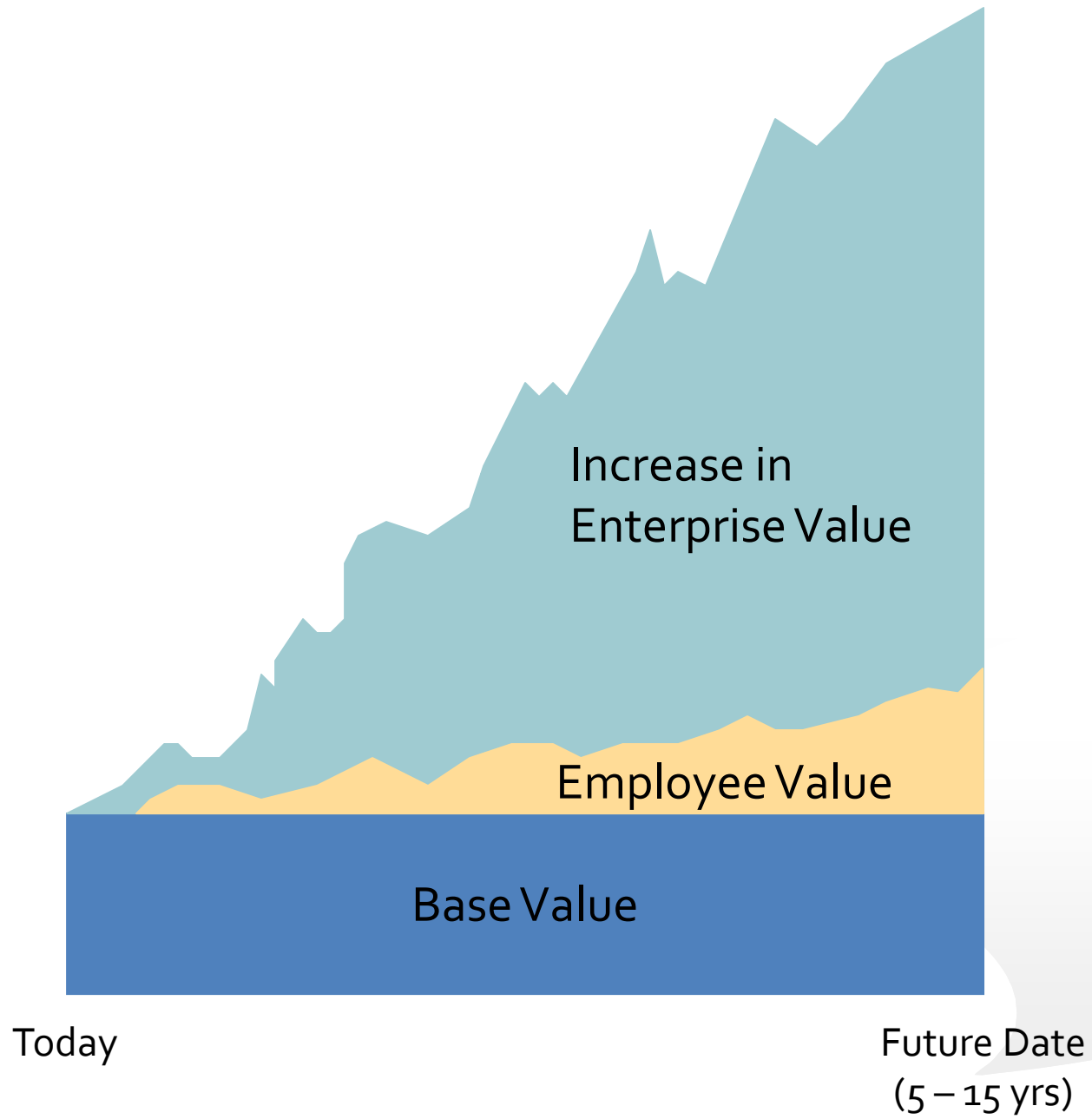
1. You will not attract the best possible talent
2. You can't be certain that pay aligns with the business model
3. You might be promoting bad profits instead of good profits
4. You will not have a complete ownership mindset
5. Employee trust and confidence will not be as strong as possible

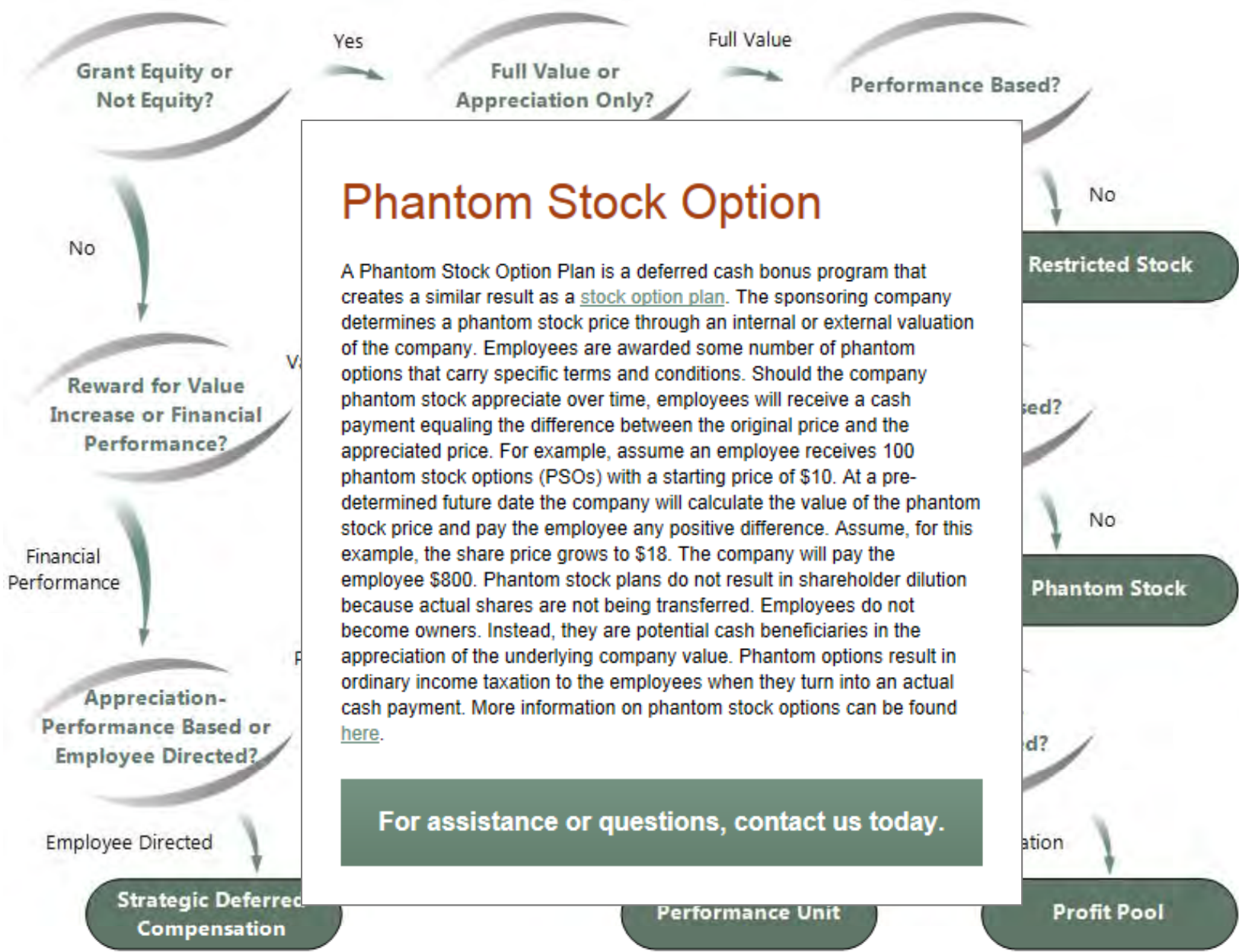


How to Share Long-Term Value Effectively

- Picture your future company
- Determine the right value to share with those who help create it
- Select the right plan
- Build it with care and know-how
- Communicate and promote it







Phantom Stock Option

A Phantom Stock Option Plan is a deferred cash bonus program that creates a similar result as a [stock option plan](#). The sponsoring company determines a phantom stock price through an internal or external valuation of the company. Employees are awarded some number of phantom options that carry specific terms and conditions. Should the company phantom stock appreciate over time, employees will receive a cash payment equaling the difference between the original price and the appreciated price. For example, assume an employee receives 100 phantom stock options (PSOs) with a starting price of \$10. At a pre-determined future date the company will calculate the value of the phantom stock price and pay the employee any positive difference. Assume, for this example, the share price grows to \$18. The company will pay the employee \$800. Phantom stock plans do not result in shareholder dilution because actual shares are not being transferred. Employees do not become owners. Instead, they are potential cash beneficiaries in the appreciation of the underlying company value. Phantom options result in ordinary income taxation to the employees when they turn into an actual cash payment. More information on phantom stock options can be found [here](#).

For assistance or questions, contact us today.

Go to "Tools" at PhantomStockOnline.com

Build it with care and know-how

Develop an Effective Financial Model



Keys to Success



Clarity

Believability

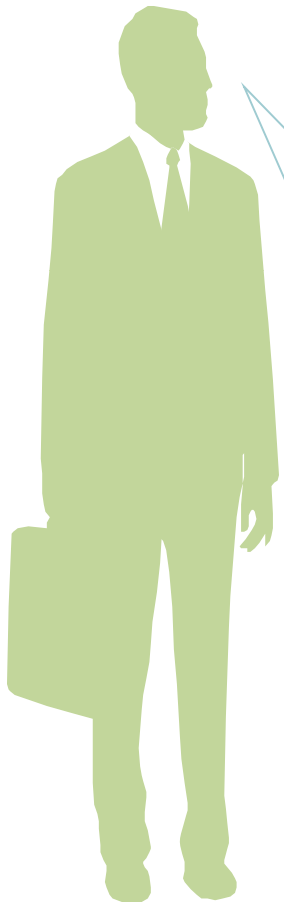
Meaning



CEO

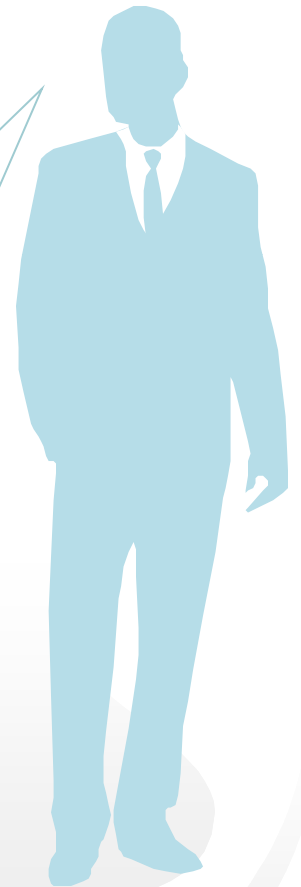
Clarity

Employee



These are the specific results that create enough value to generate bonuses. This is how your plan works.

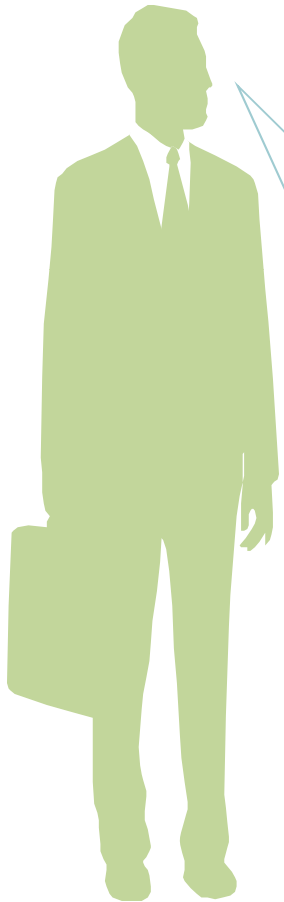
I understand what results we're seeking. I see how I can contribute. I understand how the plan works.



CEO

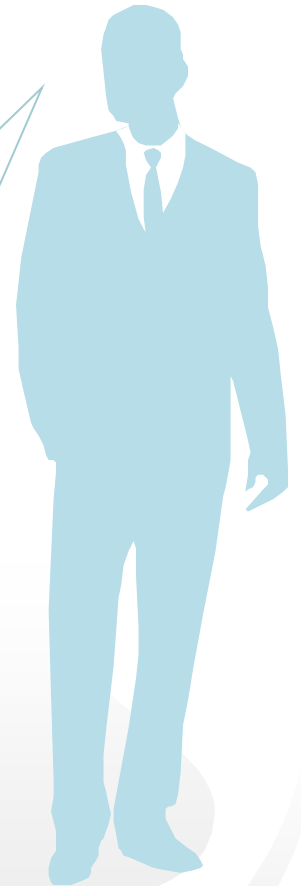
Believability

Employee



Here are the results we're expecting. Here's how we plan to get there. Here's why we're confident these results are achievable.

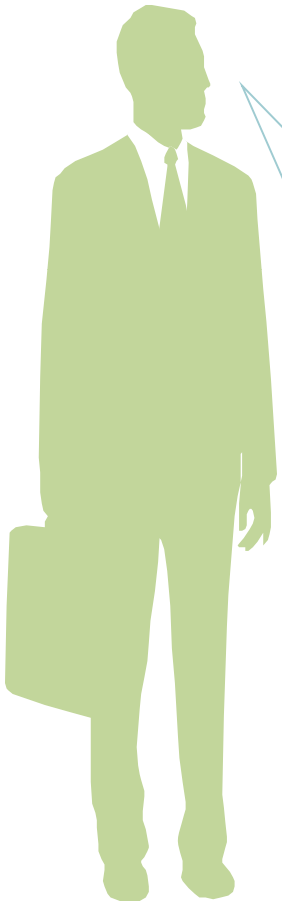
I understand the results. I understand what has to happen to achieve them. I believe we can do it.



CEO

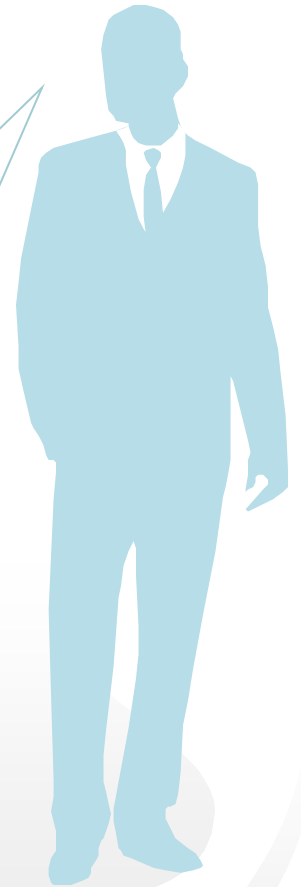
Meaning

Employee



Here's how much you should expect to receive if we hit our minimum, expected and superior result levels.

Each of those amounts is fair for the results achieved. I'm enthused and grateful to be a part of this plan.



Communicate and Promote the Plan

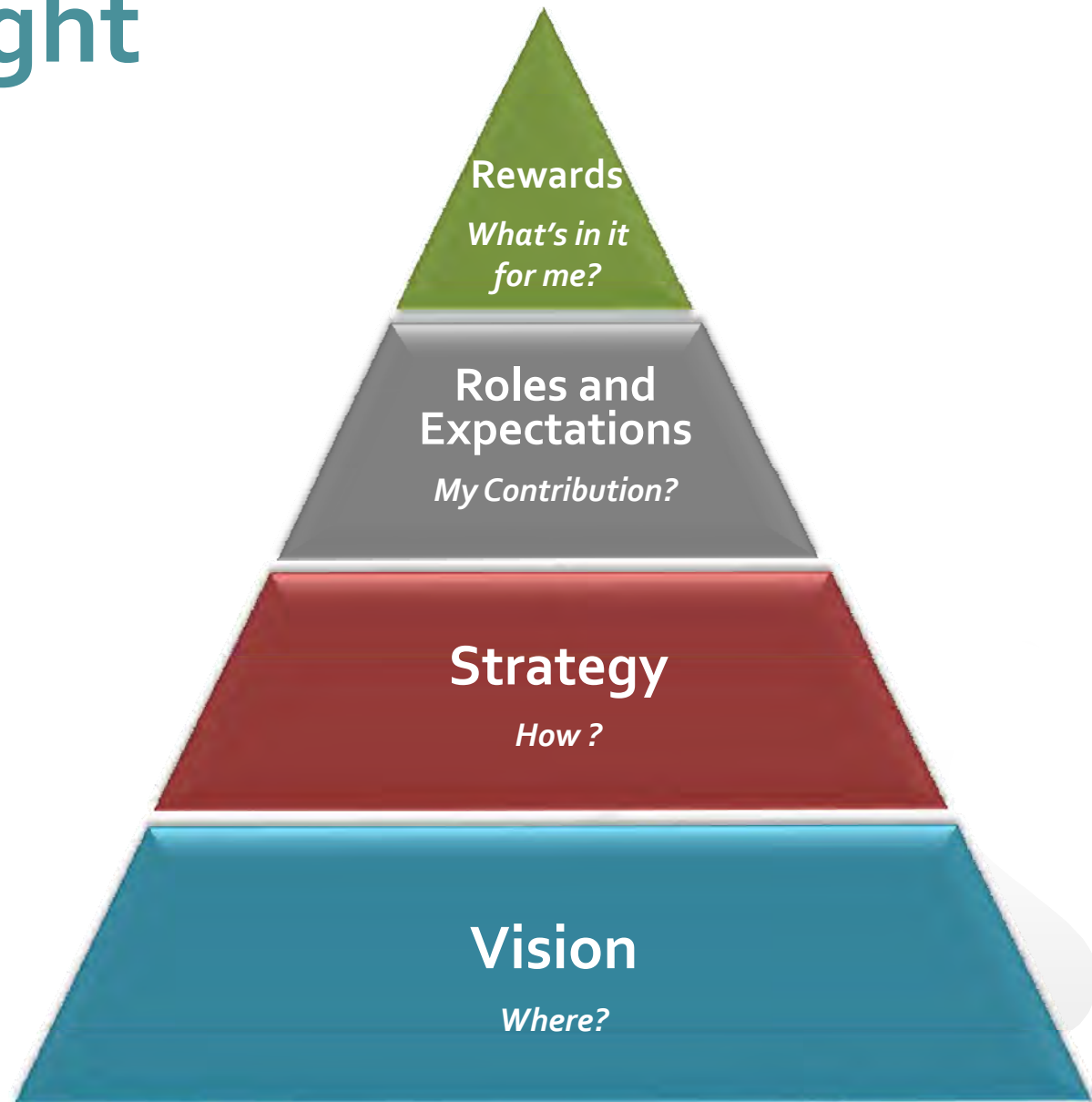


1. Explain, celebrate and reinforce the total value proposition
2. Communicate a sense of partnership
3. Project the wealth multiplier opportunity

Employee Value Statement



Line of Sight



Where to Begin

- Alignment Appraisal™
 - A focused look at your current practices with a comparative eye on whether your company is building a “Unified Financial Vision for Growing the Business”
 - Process—online employee survey

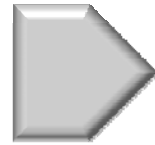
Alignment Appraisal™

- A focused look at your current practices with a comparative eye on “World Class Compensation” standards. “Is your total rewards program enhancing or slowing growth?”
- The AA is broken into two categories: Structure (are we constructing our pay plans in the best possible way?) and Mindset (are we creating the best possible perception of our plans by our employees?)
- Process—simple online survey

Compensation Practices (Structure)

The Alignment Appraisal™ assesses the pay philosophy and practices of the company relative to world-class standards.

Alignment



Do we align our pay strategy with our business strategy?

Meaning



Does our pay strategy offer fair and meaningful value to our top contributors?

Stewardship



Are we effective stewards of the compensation investment being made by shareholders?

Partnership



Do the design components of our incentive plans promote a value-sharing, partnership philosophy?

Reinforcement

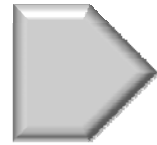


Are we excellent communicators of the value and purpose of our rewards programs?

Compensation Impact (Mindset)

The Alignment Appraisal™ assesses the impact of your pay practices on your employees' perception of how well they fit in your company.

Compelling



Do your employees perceive themselves as belonging to a dynamic organization with a compelling future?

Connection



Do your employees see the connection between company success and personal rewards?

Fairness



Do your employees feel that your pay practices are fair, consistent and purposeful?

Value-Sharing



Are the design components of your incentive plans based on a value-sharing, partnership philosophy?

Engagement



Do your employees feel fully engaged in their jobs?

Structure Index = 52*

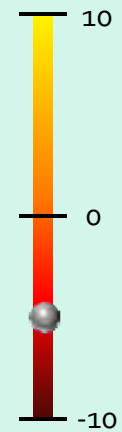
*Scale of 100

Leadership Appraisal

25.9

Net Score

-55.0%



Alignment

6.2

Meaning

5.3

Stewardship

5.8

Partnership

4.8

Reinforcement

3.8

Mindset Index = 60*

*Scale of 100

Employee Appraisal

30.2

Net Score

-32.0%

10%

0

-10%

Compelling

7.0

Connection

6.4

Fairness

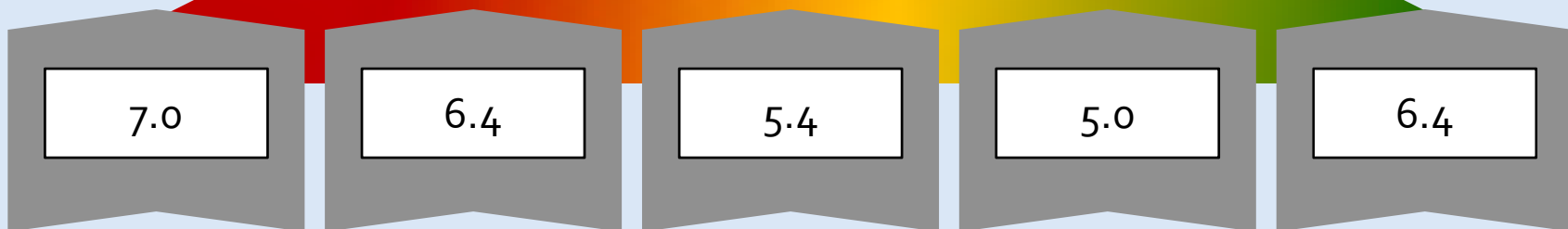
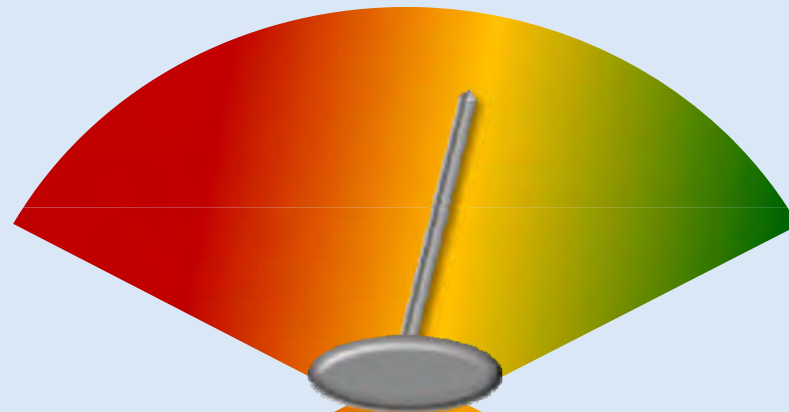
5.4

Value-Sharing

5.0

Engagement

6.4



Creating Long-Term Value for Premier Talent

- Pay the company first; tie this to your explanation to employees about how you define value creation
- Share the upside value in clear, believable and meaningful ways
- Make sure a long-term plan locks them in
- Communicate, communicate, communicate

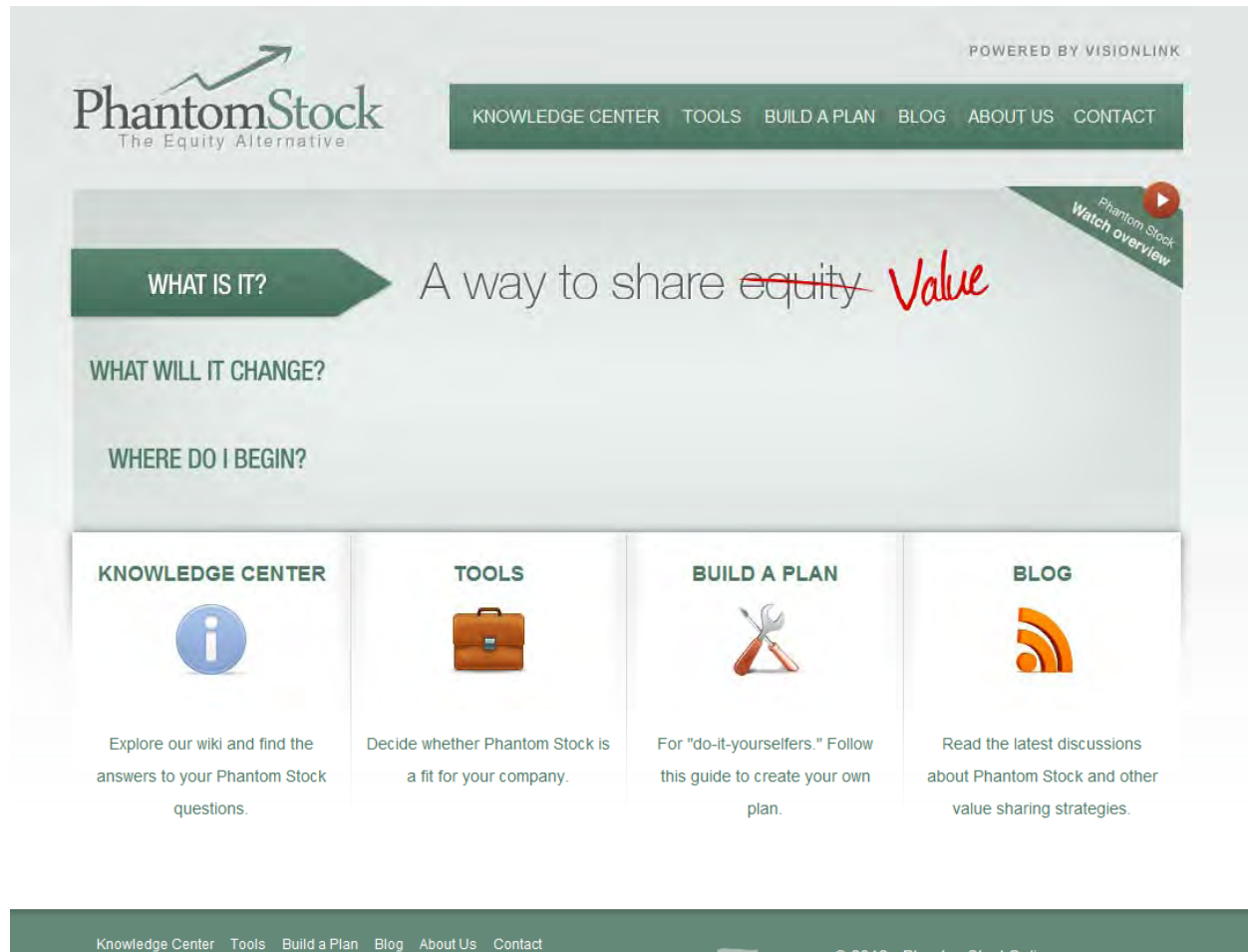


Next Online Seminar:

“What is Phantom Stock and Why do I Keep Hearing About It?”

To be held on:
Tuesday, October 23rd, 2012

Check out our NEW website:
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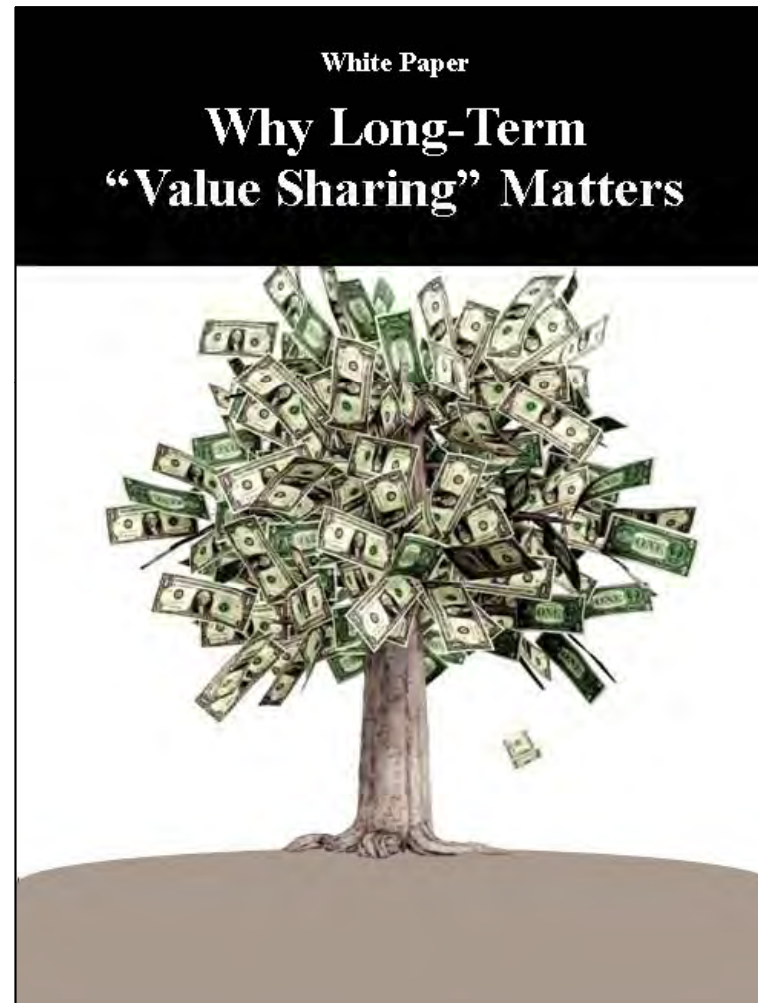
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Questions

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We value your input.

You may request a copy of our slides, the White Paper and more information about the Alignment Appraisal.



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