

December 10, 2013

The Compensation of the Future: Where is Pay Headed?



THE VISIONLINK
ADVISORY GROUP



THE VISIONLINK
ADVISORY GROUP

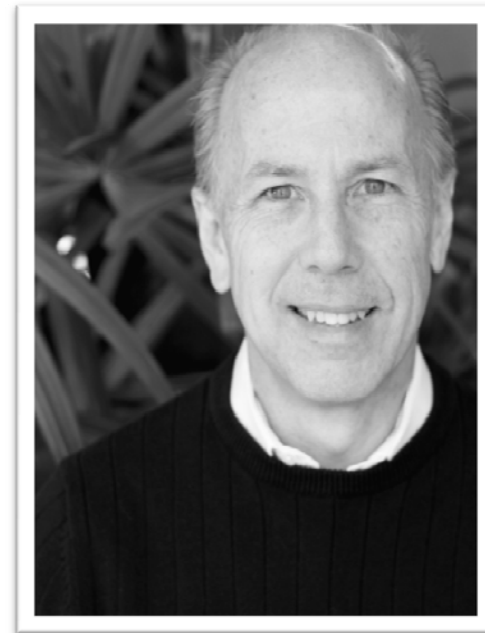
Today's Presenter:

Ken Gibson

Senior Vice President

(949) 265-5703

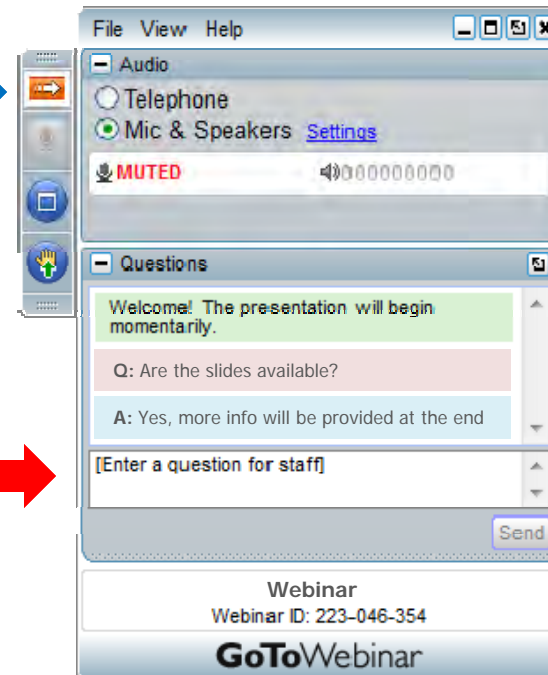
kgibson@vladvisors.com



We're happy to provide a copy of today's slides.
Information will be provided at the close
of the presentation.

**To open or close
the control panel:** →
Click the red arrow

**For questions during
today's presentation:** →
Use the question area
on your control panel



Key Questions

- How will growth-oriented businesses compete in the future?
- What kind of talent will those businesses need?
- What kind of value proposition will attract and retain that kind of talent?



Competitive Advantage



Continuous Value Creation

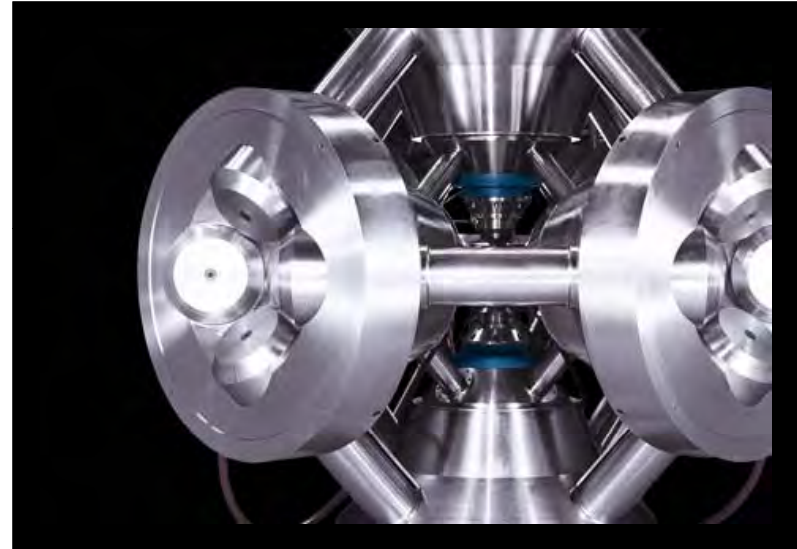
How do you keep an organization creating value for the long-term?

U.S. Synthetics--Rob Galloway, CEO

Friend: "What do you look for in a CFO?"

Rob: "I need a business partner."

See the business first, then think about the subject matter expertise the talent will need to have.



Continuous Value Creation & Talent

Rob Galloway on the talent component:

- Culture is what we think and how we work today
- Strategy is who we want to be tomorrow
- **People innovate, not systems or machines or tools**
- “What’s your ratio of problem finders to problem fixers?”



The CEO Mindset



PwC's 2012 Global CEO Survey

(reported in Chief Executive Magazine, November/December 2012 Edition)

- Just 12% of CEOs finding it easier to hire today
- 25% reported being unable to pursue a market opportunity or being forced to cancel or delay strategic initiatives because of talent challenges
- 31% feared they would not be able innovate effectively going forward because of skill shortages
- More CEOs plan on changing their talent management strategies this year than adjusting approaches to risk or capital investment—or any other corporate strategies

Key Statistic

A majority of CEOs surveyed by PwC—68% global; 71% U.S.—wish they could spend even more time than they do focused on developing the leadership of their business and their talent pipeline.



Key Implication

In the future, it's likely that while the human resources chief will report directly to the CEO, it is the latter who will have to drive strategy.

“The biggest mistake CEOs can make is to delegate the talent strategy to HR. HR is the enabler of the strategy, but CEOs need to think of themselves as the chief talent officer of their organizations.” (Ed Boswell, PwC's U.S. advisory services people and change practice leader.)



Source of Value Creation

Continuous Innovation



The Business Landscape

The New Corporate Garage

...Apple's inventiveness is no anomaly; it indicates a dramatic shift in the world of innovation. **The revolution spurred by venture capitalists decades ago has created the conditions in which scale enables big companies to stop shackling innovation and start unleashing it.**



Harvard Business Review, September 2012

What Kind of Talent?

“...**entrepreneurial individuals, or ‘catalysts,’** within big companies are using those companies’ resources, scale, and growing agility to develop solutions to global challenges in ways that few others...”



Harvard Business Review,
September 2012 (cont.)

Talent & Business Model Alignment



The competitive environment of the future will require that key people (“catalysts”):

- Work in roles that maximize their unique abilities
- Relieve them of responsibilities that don’t have a strategic impact
- Outsource other duties

Key Talent Trend



- Competitive advantage increasingly coming from hard-to-duplicate know-how of most skilled people
- Not enough knowledge workers to go around

(Source: "Redesigning Knowledge Work," HBR, January-February 2013)



Key Talent Trend

By 2020, the worldwide shortage of highly skilled, college-educated workers could reach 38 to 40 million, or 13% of demand.

(Source: McKinsey Global Institute)



Conclusions Regarding Talent Trends

- Companies will need catalysts to maintain a competitive advantage
- Those individuals need to spend their time on things that have the most strategic impact
 - Especially important due to high comp levels
- These two factors lead to scarcity of high impact talent
- Scarcity creates high competition within the talent pool
- Companies will need a unique and robust value proposition to win the talent wars



The Compensation Landscape

Two Approaches to Retaining Employees

- Expansive
- Selective

Workspan (World at Work)--*The War for Stars*,
May 2012



Expansive Approach

Strives to retain virtually every employee under the theory that everyone is needed or they wouldn't be there. Largely egalitarian.

“Why upset our harmonious culture by creating an elite group that receives special treatment? All our employees are critical and perform well, and most are not going to leave.”



Expansive Approach

- Easy to administer
 - Managers don't have to identify exceptional contributors
 - Managers don't have to differentiate performance messages and rewards
- Does not usually support an organization's efforts to raise overall performance
- Discourages and disengages high performers

"Although I contribute more, I get treated like everyone else. Why bother?"

Selective Approach

Identifies, nurtures and works to retain the high performers at all levels of the organization.

Seeks to produce a cycle that...will...attract more high performers and generate ever-improving standards of performance and organizational results.



Selective Approach

- Sets high performance standards
 - Appeals to high performers; high performers want to “win”
 - Organization wins through improved results and continued retention of high performers
- Acknowledges the company is in a war for stars
- Recognizes high performers always have an opportunity to move



Given the present business landscape...

...which approach makes the most sense?

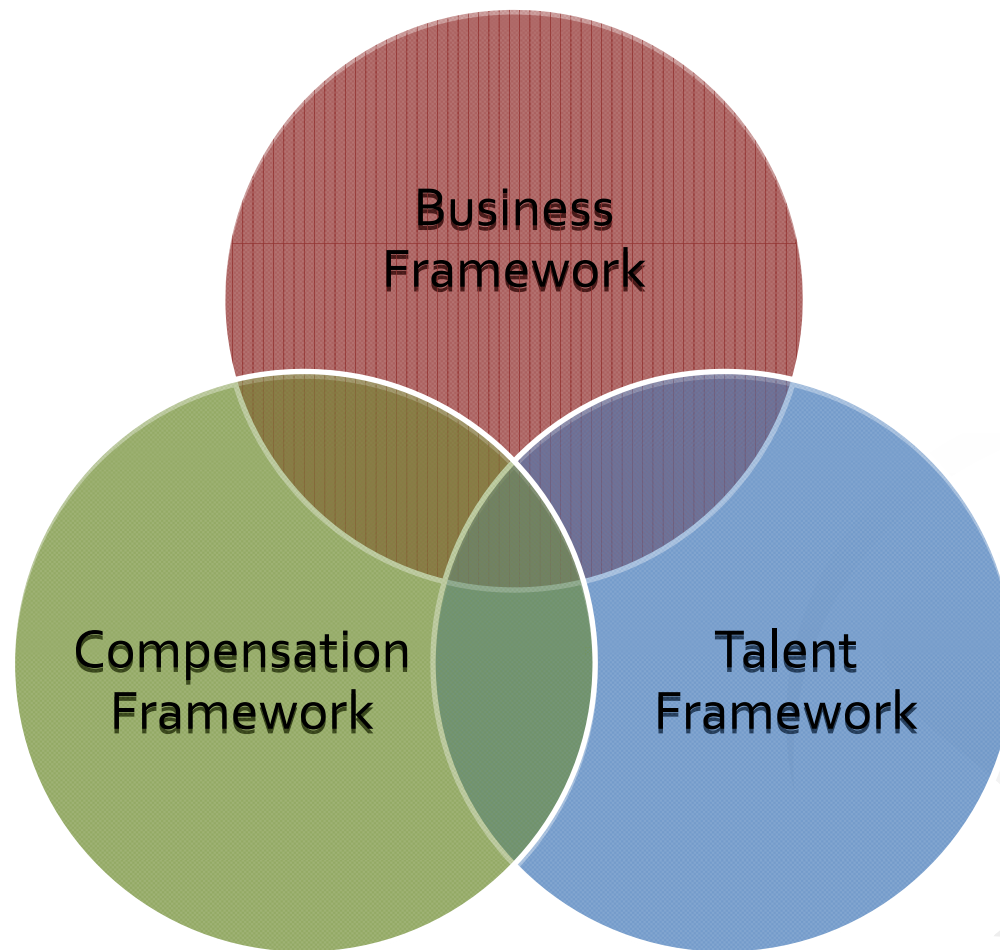
Expansive



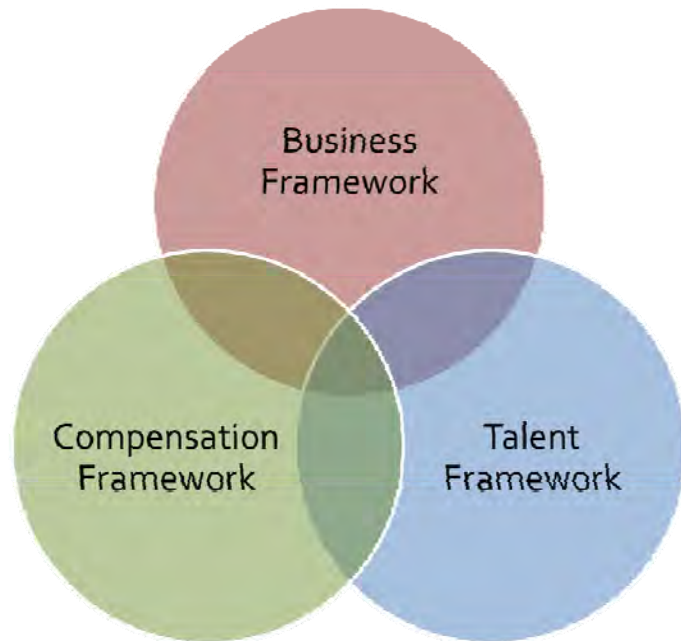
Selective



Establish a Performance Framework



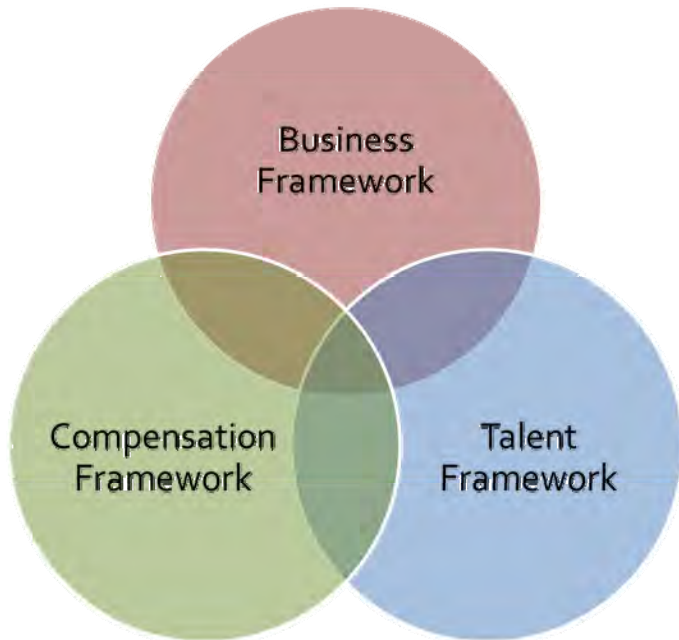
Establish a Performance Framework



Phase One—Business Framework

- Define Growth Expectations (Vision)
 - Key outcomes that must be achieved
- Define Business Model and Strategy
 - Performance Engine
 - How the company will compete
 - Where are growth opportunities?
- Identify Roles and Expectations
 - Establish Performance Criteria
 - Define "Success"

Establish a Performance Framework



Phase Two—Compensation Framework

- Establish a pay philosophy
 - Expansive vs. Selective—or Hybrid
 - Define what the company is willing to pay for
- Engineer a pay strategy
 - Structure
 - Mindset
- Adopt a “Total Rewards” Approach

Total Rewards Approach



Establish a Performance Framework



Phase Three—Talent Framework

- Identify Key Producers
 - Meeting “success” standards
- Identify Talent “Gaps”
 - Recruiting Strategy
- Communicate Expectations
 - Define success
- Communicate Rewards
 - Philosophy
 - Programs
 - Value Statement

Future Criteria for Pay Strategies

- Must attract top talent (particularly entrepreneur-oriented people)
- Must promote and reinforce innovation
- Must be flexible
- Must drive business value
 - Reinforce leverage points of virtuous cycle
- Must minimize guarantees
 - Share the risk
- Must provide large “upside” to key producers
- Must employ continuous value creation and sharing philosophy and practices



Future Pay Trends in Business

- Performance Agreements
- Opt-In Plans
- Internal Venture Capital
- Long-Term Value Sharing Plans
- Focus on Productivity Profit—Comp ROI
- Market a Future



Performance Agreements



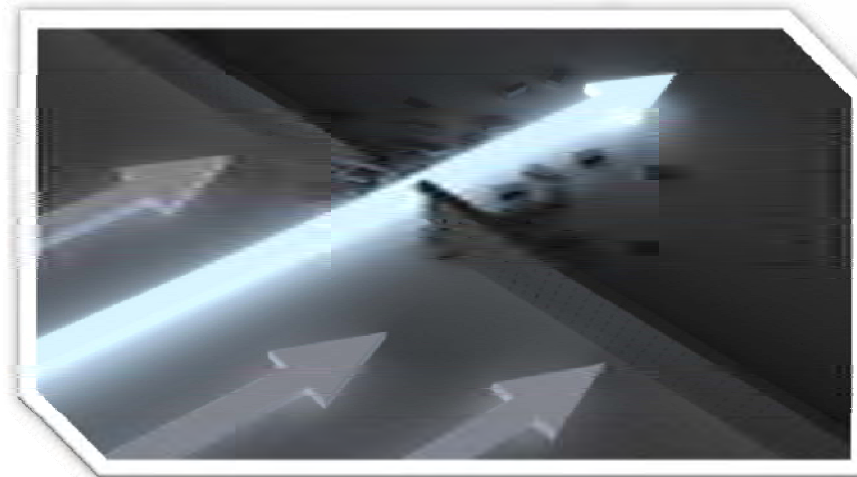
Prominent Media Company

- High performers excluded from company's "egalitarian" profit sharing-type incentive plan
- Annual "deal" negotiated with COO & CFO
- Deal memorialized on a "deal sheet"
 - Defines financial, operational & leadership expectations
 - Defines value of the award that could be generated
- Quarterly self-evaluation against performance expectations with COO & CFO

Performance Agreement

Outcomes:

- Threshold for compensable performance is very high
 - Small or even \$0 payouts can occur
- High-risk, high-reward—high upside
- Self-evaluations create a mentoring environment
- High performers think and feel like owners in the company's success
- Because no competitors offer this opportunity, high performers rarely leave



Opt-In Plans



Most Ideal in Start-Up Environment

- Opt for:
 - “Higher” salary plus modest incentives
 - “Low” or no salary and high upside through short and long-term value sharing
- Opt-In payments tied to a revenue or profit-sharing formula
- Volatility: payments lowered and/or deferred
 - Deferred payouts made when economics permit
- Opt-In periods may differ
 - Quarterly, semi-annual, annual

Opt-In Plans

Outcomes

- Employees feel more in control
- Owners can limit guaranteed payouts
- Highly flexible—can adjust to rapidly & frequently changing economics
- Provides a “shared” entrepreneurial experience
- Promotes an ownership mindset
- “Self-identifies” key performers



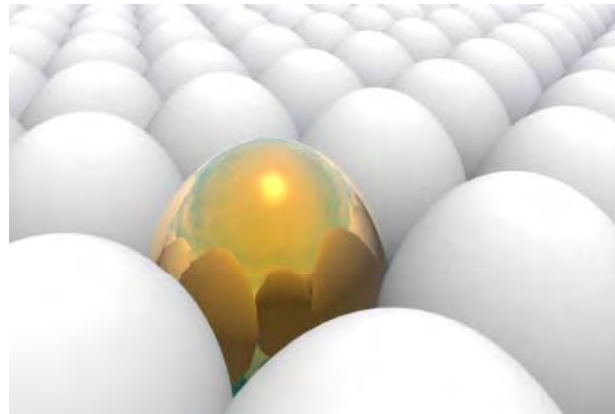
Internal Venture Capital



Highly Entrepreneurial Approach

- Most common in larger organizations
- Venture capital account established
- Criteria for access is defined
- Innovative ideas “funded” and financed through venture capital account
- Performance criteria set
- Value sharing plan tied to performance criteria
- Often accompanied by performance agreements or “opt-in” comp plans

Internal Venture Capital



Outcomes

- Attracts entrepreneurial employees
- Creates a “start-up” environment within larger organization
- Places a large emphasis on innovation
- Creates ability to move quickly with new ideas
- Allows mini-entrepreneurs to leverage resources and scale of larger organization

Long-Term Value Sharing Plans

Broad Application

- Used in every size organizations
- Can be tied into any of the previous approaches
- Creates “wealth multiplier” mindset
- Ties employees to vision and business plan of the company



Why Long-Term Value Sharing Matters

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



President—Logistics Company



Just Hired:

- CFO
- COO
- CRO (Chief Revenue Officer)

“These guys are seasoned and experienced. They want to know that if they help grow this thing, there is something in it for them.”

Select the Right Plan Type

Phantom Stock
Option

Restricted Stock

Profit Pool

Performance Shares

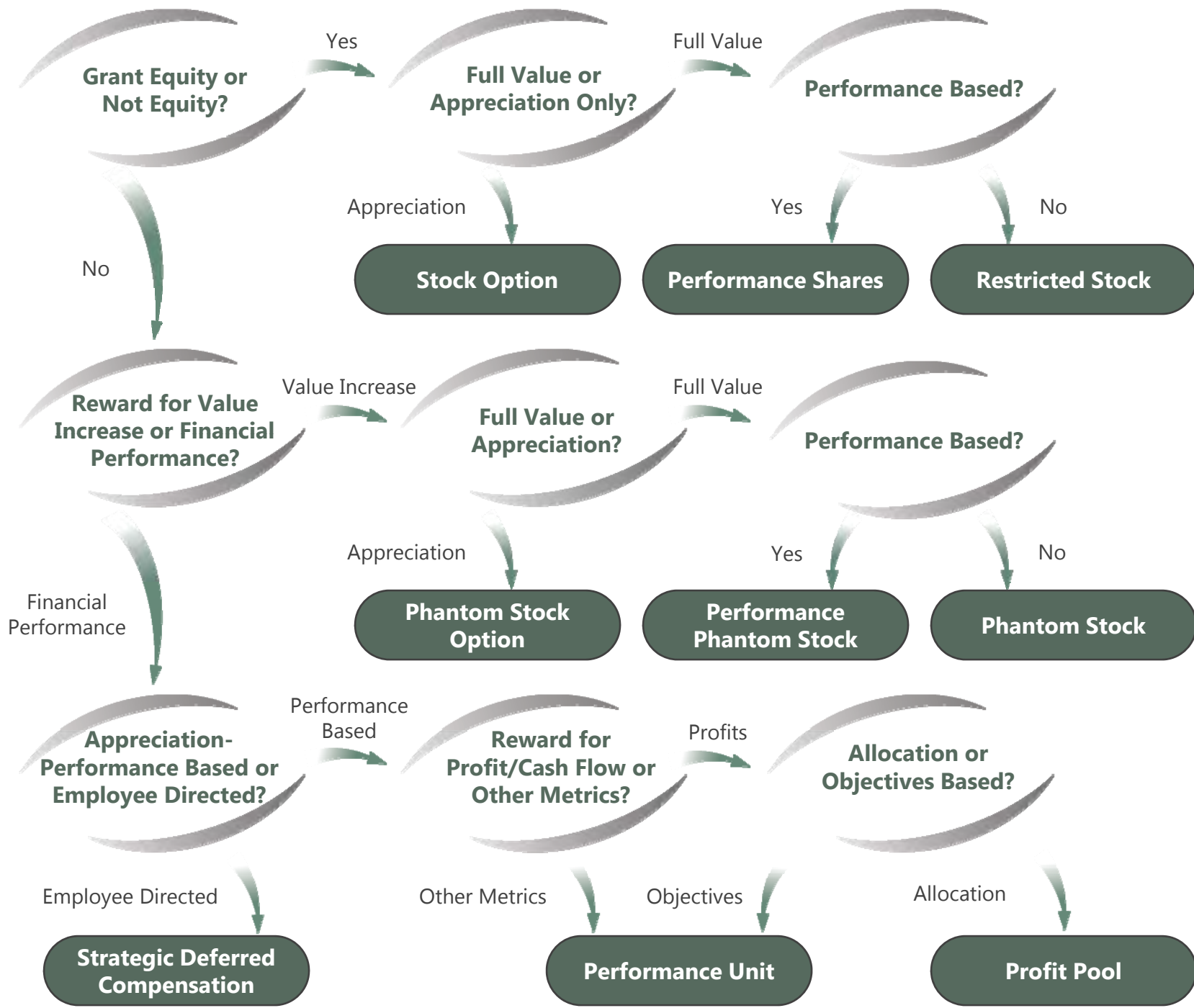
Phantom Stock

Strategic Deferred
Compensation

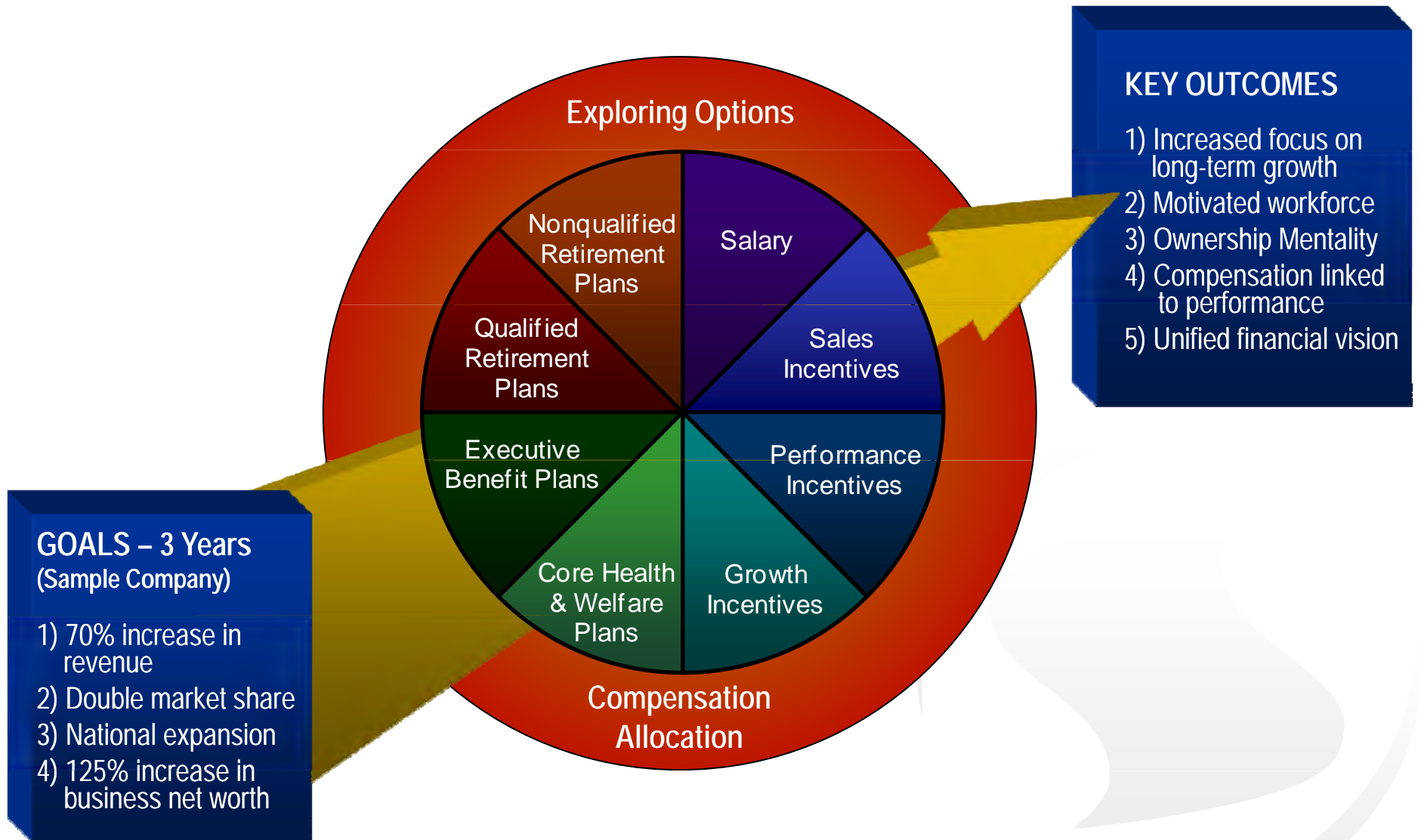
Performance
Phantom Stock

Stock Option

Performance Unit



Examine Alternatives



Form of Pay	Purpose	Standard	Investment	ROI
Salaries	Provide for the current cash needs of our executives	40-50th percentile for peer group	\$500,000	Achieve ROA standard of 0.75%
Short-term Incentives	Enhance current cash payments to executives for achieving top and bottom line annual goals	30-40% of base salary	\$168,000 (Target)	15% revenue growth and 12% margin
Long-term Incentives (Cash)	Retain execs; focus them on long-term earnings growth; align with shareholder interests; meet wealth accumulation needs	15-20% of base salary	\$84,000 (Target)	Long-term growth in earnings (double earnings = share 13% of new value)
Long-term Incentives (Equity)	Retain execs; focus them on long-term earnings growth; align with shareholder interests; meet wealth accumulation needs	15-20% of base salary	\$84,000 (Target)	Long-term growth in earnings (double earnings = share 13% of new value)
Core Benefits	Meet basic security needs of the executives	50th percentile for peer group	\$25,500	ROA of 0.75%
Executive Benefits	Enhance basic security needs and meet market standards for perquisites	50th percentile for peer group	\$24,000	ROA of 0.75%
Qualified Retirement	Provide wealth accumulation opportunity for executives	40th percentile (3% of salary)	\$15,000	ROA of 0.75%
Supplemental Retirement	Strengthen rewards value proposition to help recruit and retain executives; meet wealth accumulation needs	30th percentile compared to banks that have plans	\$135,000	ROA of 0.9%

Link Company & Employee Goals

Employee "Hierarchy of Needs"

5

Wealth Multiplier

Internal Venture Capital

4

Value Sharing

Long-Term Incentives, Opt-In,
Performance Agreements

3

Retirement Planning

Qualified & Executive
Retirement Plans

2

Risk Protection

Comprehensive, Flexible
Benefits Plan

1

Cash Flow & Living Standard

Salary & Bonus

Clear Pay Philosophy

Market a Future



- Think transformation, not just change
- Build a sense of partnership
- Demonstrate commitment
 - To the future business
 - To key contributors
- Promote don't just communicate
- Be consistent

Employee Value Statement

Year	1	2	3	4	5
5-Year Plan Achievement Level	100%	100%	100%	100%	100%
Current and Inflated Salary	\$ 160,000	\$ 166,400	\$ 173,056	\$ 179,978	\$ 187,177
Cash Incentives Paid at Target	\$ 64,000	\$ 66,560	\$ 69,222	\$ 71,991	\$ 74,871
LTIP Vested Value at Year End	\$ -	\$ 74,000	\$ 186,000	\$ 311,000	\$ 448,000
Retirement Plan Value (at 7%)	\$ 17,120	\$ 36,123	\$ 57,169	\$ 80,428	\$ 106,086
Total Cash Received	\$ 224,000	\$ 232,960	\$ 242,278	\$ 251,970	\$ 262,048
Total Wealth Accumulation	\$ 17,120	\$ 110,123	\$ 243,169	\$ 391,428	\$ 554,086
Total Paid or Accumulated	\$ 241,120	\$ 567,083	\$ 942,407	\$ 1,342,636	\$ 1,767,343

Key Conclusions



- Businesses need to innovate for continuous value creation
- Companies need to attract “entrepreneurial talent” to meet innovation demands
- Counter intuitively, marketplace has a scarcity of *skilled* talent
- Businesses will have to compete for *premier* talent
- Innovative employee value propositions will be needed to compete
- CEOs must become the chief talent officer of the company



Type Your Questions

Special Offer

One hour consulting call with a VisionLink principal at no charge

(CEO or other senior leader)

Indicate interest on final survey

Next Online Seminar:

“Do Incentive Plans Really Work?”

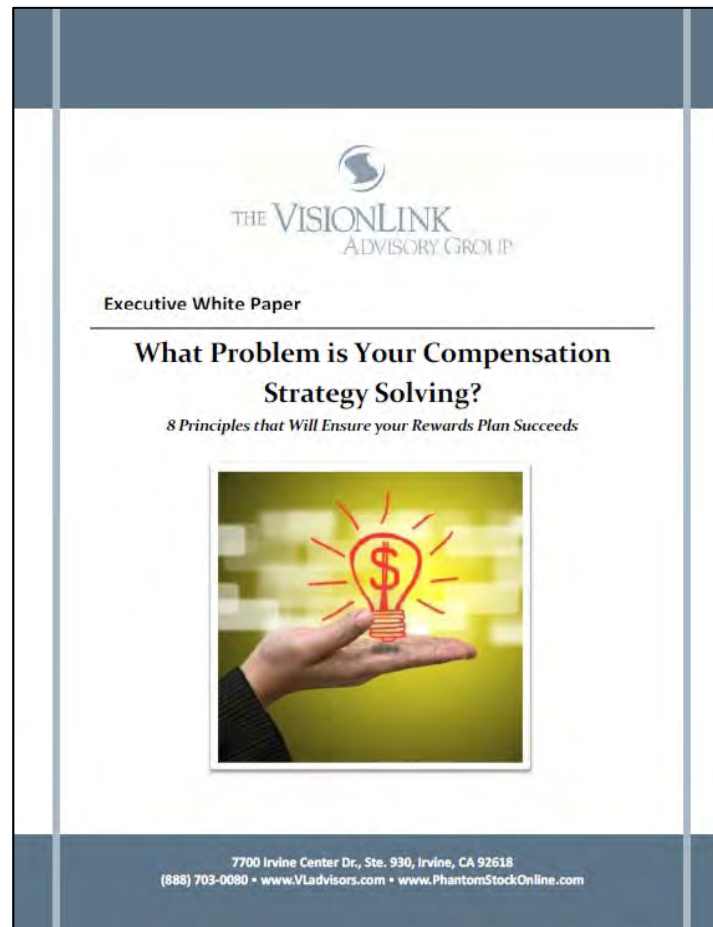
To be held on:
Tuesday, January 28th, 2014

7700 Irvine Center Drive, Suite 930 ♦ Irvine, CA 92618 ♦ 949-852-2288

www.VLadvisors.com ♦ www.PhantomStockOnline.com

NOW AVAILABLE!

New White Paper



Express interest on the final survey

www.VLadvisors.com



[About Us](#) [Capabilities](#) [Knowledge Center](#) [Tools](#) [Blog](#) [Contact Us](#)



(888) 703 0080

Exceed Results - Drive Growth - Increase Value - Multiply Wealth

How Do I End Entitlements?

[Click here to learn more](#)



Learn About
VisionLink's
Capabilities

[CLICK HERE](#)



Register for a
VisionLink
Webinar

[CLICK HERE](#)



Speak to a
Compensation
Expert

[CLICK HERE](#)

You can also subscribe to our blog

www.PhantomStockOnline.com

POWERED BY VISIONLINK

PhantomStock
The Equity Alternative

KNOWLEDGE CENTER TOOLS BUILD A PLAN BLOG ABOUT US CONTACT

WHAT IS IT? A way to share ~~equity~~ Value

WHAT WILL IT CHANGE?

WHERE DO I BEGIN?

Phantom Stock
Watch overview

KNOWLEDGE CENTER

TOOLS

BUILD A PLAN

BLOG

Explore our wiki and find the answers to your Phantom Stock questions.

Decide whether Phantom Stock is a fit for your company.

For "do-it-yourselfers." Follow this guide to create your own plan.

Read the latest discussions about Phantom Stock and other value sharing strategies.

Knowledge Center Tools Build a Plan Blog About Us Contact

© 2012 PhantomStockOnline.com



Questions

Thank you!



Ken Gibson

Senior Vice President

(949) 265-5703

kgibson@vladvisors.com



THE VISIONLINK
ADVISORY GROUP