

August 28, 2012

# “How to Build Long-Term Value for Key Producers”



THE VISIONLINK  
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Today's Presenter:

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

**For questions during today's presentation:**

Use the question panel  
to the right of your screen

# Today's Focus

How to use long-term value sharing as a tool of business transformation



Key Producer  
Compensation

# Key Questions

1. What is meant by value creation and value sharing?
2. Does long-term value sharing really matter?
3. If so, what does it impact? What does it change?
4. How is long-term value shared most effectively with those who produce it?



# Value Creation and Sharing

## *What Does it Really Mean?*

### Case Study

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



**Underwriters  
Laboratories**

Keith Williams





**Underwriters  
Laboratories**

- Global independent safety science company
- Validates the safety of certain products and processes
- Puts the UL stamp of approval on products that have met its standards
- The company is 118 years old

# 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



**EVA=Economic Value Added.** UL's definition of value creation.

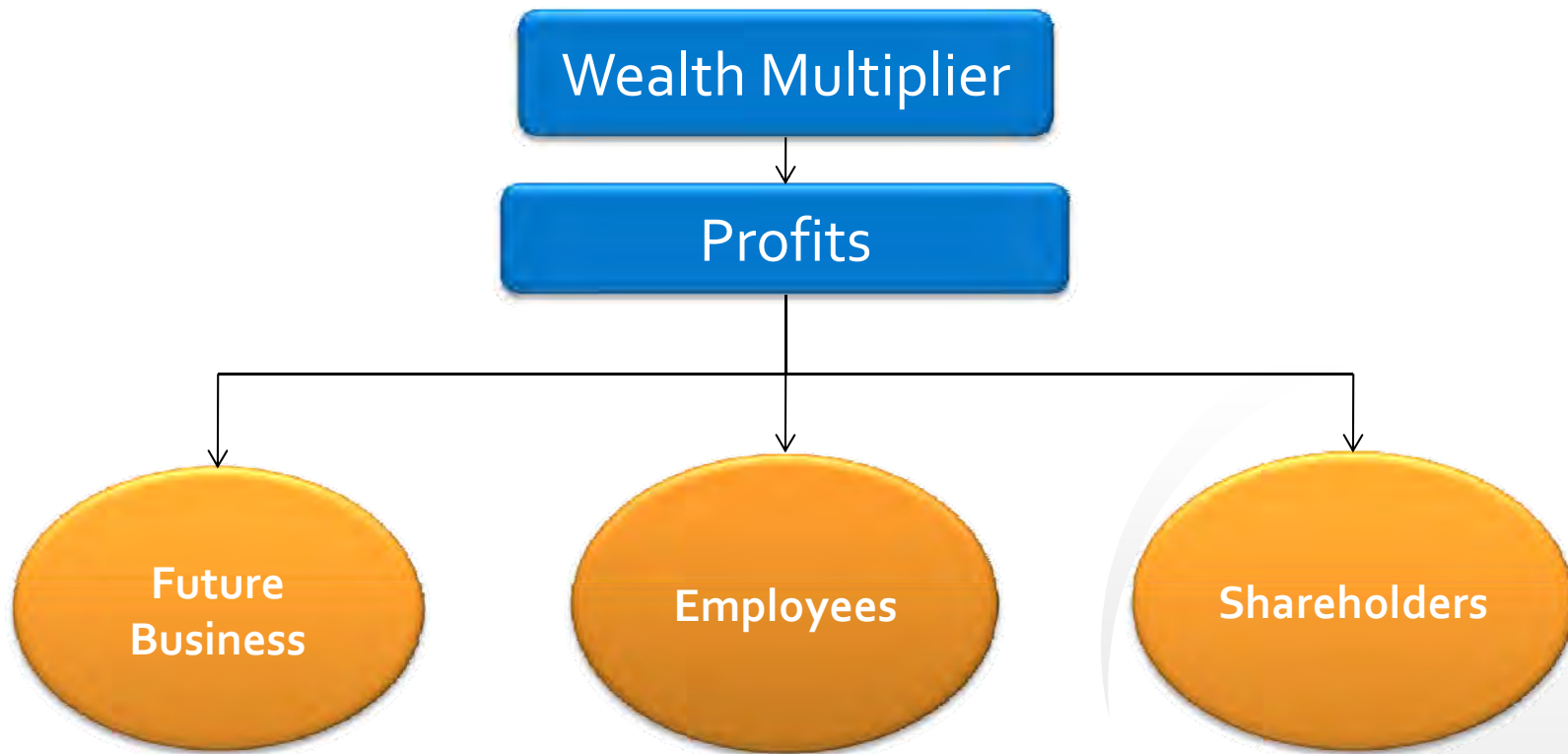


# Pay the Company First

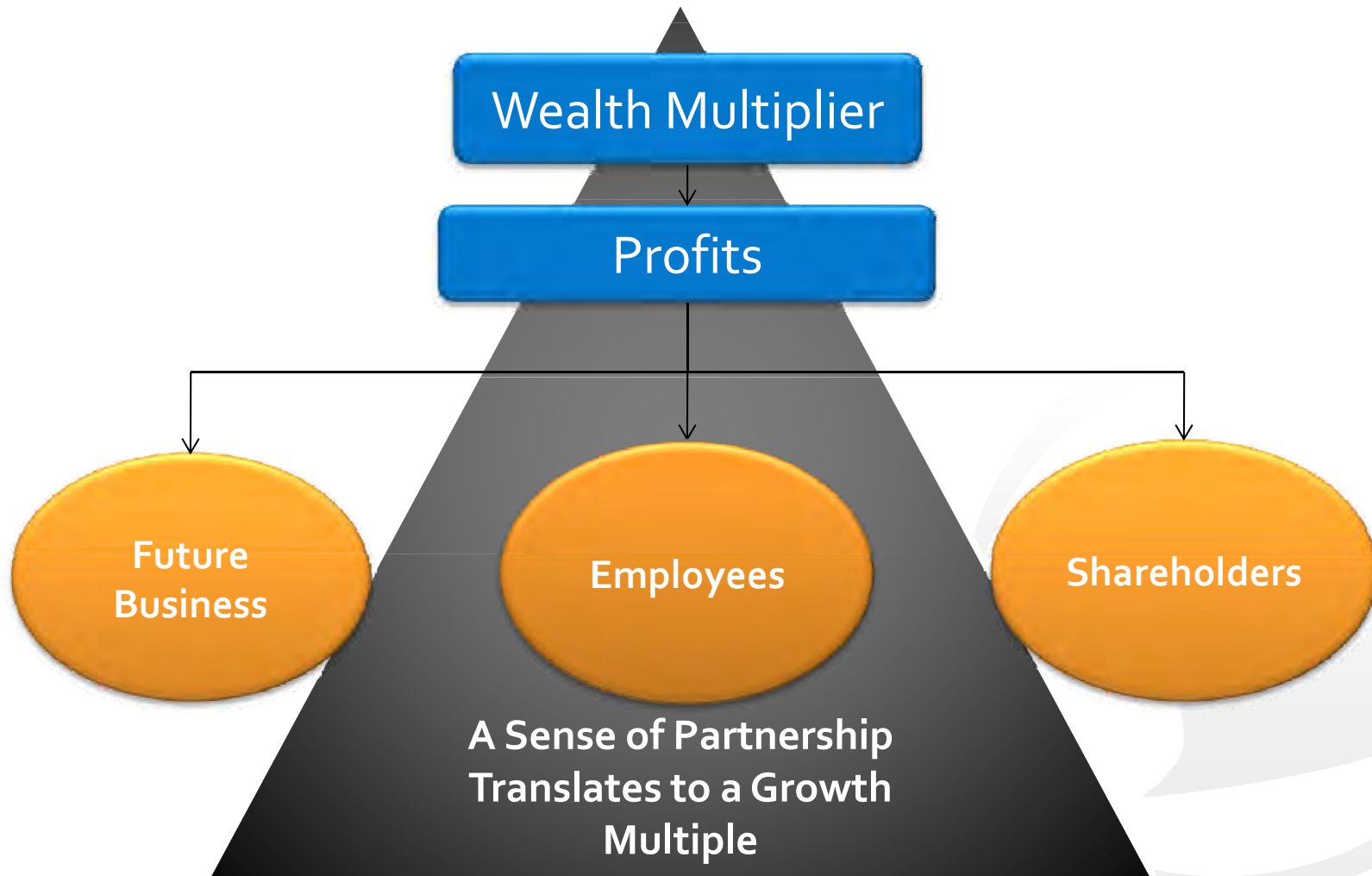


Once value creation is defined, compensation can follow a formula for sharing value in a way that aligns key producers with the company's business plan and priorities.

# The Value of Profit



# The Value of Profit



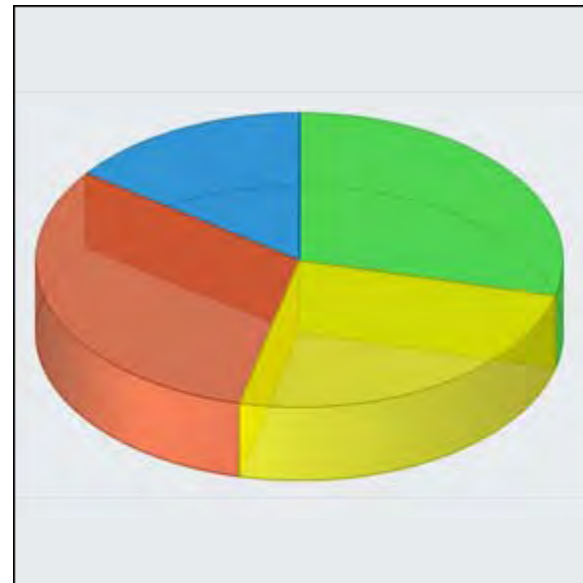
# Profits Generate additional Capital

Wealth Multipliers *continually* look for ways to deploy that capital more productively.



# Capital Deployment “Portfolios”

- Product Portfolio
- Training Portfolio
- Finance Portfolio
- Innovation Portfolio
- Marketing Portfolio
- Compensation Portfolio





# Capital Deployment in Compensation

Compensation is a deployment of capital—an investment.

- Investments must be properly allocated
- Investments must be properly measured (ROTRI)
- Investments in human capital should improve productivity



# Compensation Allocation “Portfolios”

- Performance Class
  - Paid to help company meet its “budgeted” or targeted level of performance
  - Today focused
- Growth Class
  - Paid for helping company achieve superior levels of performance
  - Future-focused
- Transformation Class
  - Paid for fundamentally altering the course of the industry through unique breakthroughs
  - Wealth-multiplier mindset
  - Most highly productive class

# Key Concept



The Future

Companies that work on compensation in their transformation portfolio have a wealth multiplier and not just a wealth creator mindset. They envision people—both the customers they serve and the workforce they employ—experiencing life in a whole different realm. (Think Apple, Disney, Amazon and others.) As a result, they don't just create compensation programs. **They market a future to their employees on all levels**—product development, market penetration, innovation expectations and yes, rewards—so that all company “portfolios” are completely aligned.

# Why Long-Term Value Sharing Matters



# Why Long-Term Value Sharing Matters

#1 Value sharing attracts the best talent and magnifies results

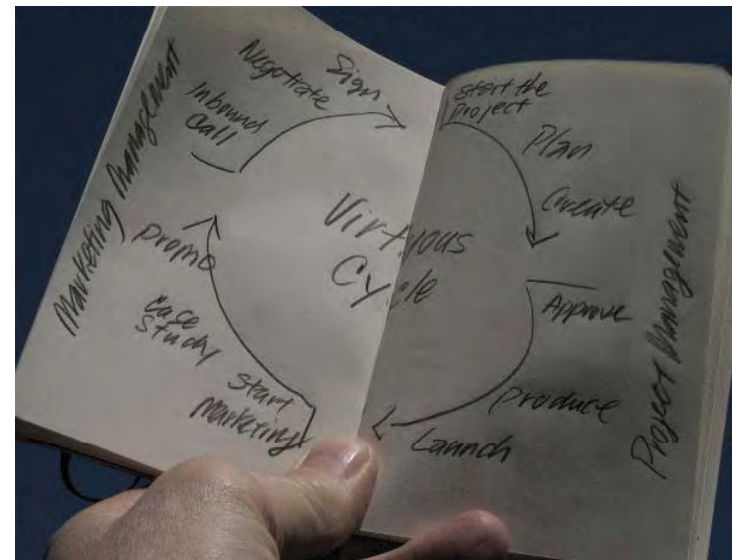


- Attracting the “right” people
  - Willing and able to compete
  - Assume stewardship role in safeguarding shareholder interests
  - Willing to share in risks and rewards of value creation
  - Seek mini-entrepreneurial experience

# Why Long-Term Value Sharing Matters

#2: Value sharing plans (effectively designed) reinforce the company's business model

- Nurture a culture invested in the business model
  - Reinforce virtuous cycles
  - Reinforce leverage points
  - Reinforce roles and expectations



# Why Long-Term Value Sharing Matters

#3: Value sharing protects against bad profits and promotes good profits



- Everyone has an interest in good profits if everyone's wealth multiplier rises or falls on the ability of the company to sustain the right kind of profitability.
- Pay people in a way that communicates long-term profitability expectations
- Protect company's interest in generating good profits

# Why Long-Term Value Sharing Matters

## #4: Value sharing promotes an ownership mindset

- Build a rewards system that communicate “what’s important.”
  - Keep performance engine working *while* moving the company forward towards growth goals
  - Define “what’s important” the same way ownership does—revenue/EBITDA growth, profit/margin improvement, cost management





# Why Long-Term Value Sharing Matters



## #5: Value sharing builds trust and accelerates results

- Turn key people into “partners” in building the future business
  - Value sharing communicates a sense of fairness
  - Create a unified financial vision for growing the company
  - Validate your trust in their unique abilities

# 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



# From Why to How



# How to Share Long-Term Value Effectively



- Focus on transformation, not just growth
  - Be a wealth multiplier not just wealth creator
- Match growth goals of company with growth goals of key producers
  - Focus on employee “hierarchy of needs”
- Explore appropriate options
  - Employ a decision tree process
- Project outcomes
  - Develop an effective financial model
- Communicate and promote the plan
  - View employees as “customers” of your value proposition
- Evaluate and refine
  - Make sure you’re achieving “line of sight”

# Transformation not just Growth

## Wealth Multipliers not just Wealth Creators

### Wealth Creators

- Profitability focus
- Recruit to skills and experience
- Comp is an important expense to be managed
- Salaries and total pay should be “at market”
- “Pay-for-performance”

### Wealth Multipliers

- Transformation focus
- Recruit premier talent that relates to our culture
- Comp is an investment that should produce a growing return
- Salary benchmarking can be helpful but pay should be tied to positional value
- “Share wealth created”

# Link Company & Employee Goals

## Employee "Hierarchy of Needs"

5 Wealth Accumulation

Wealth Multiplier Philosophy

4 Value Sharing

Short & Long-Term Incentive Plans

3 Retirement Planning

Qualified & Executive Retirement Plans

2 Risk Protection

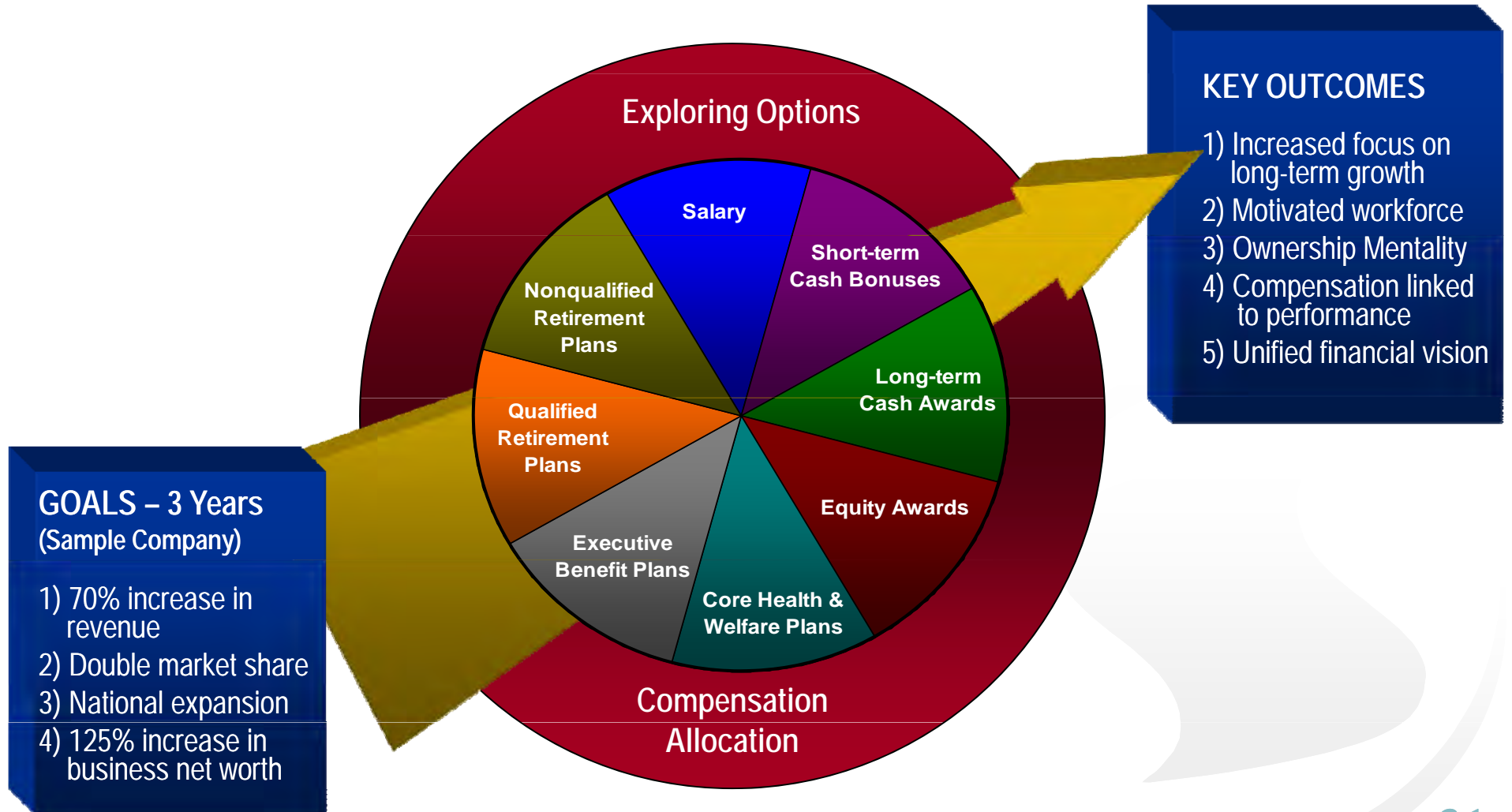
Comprehensive, Flexible Benefits Plan

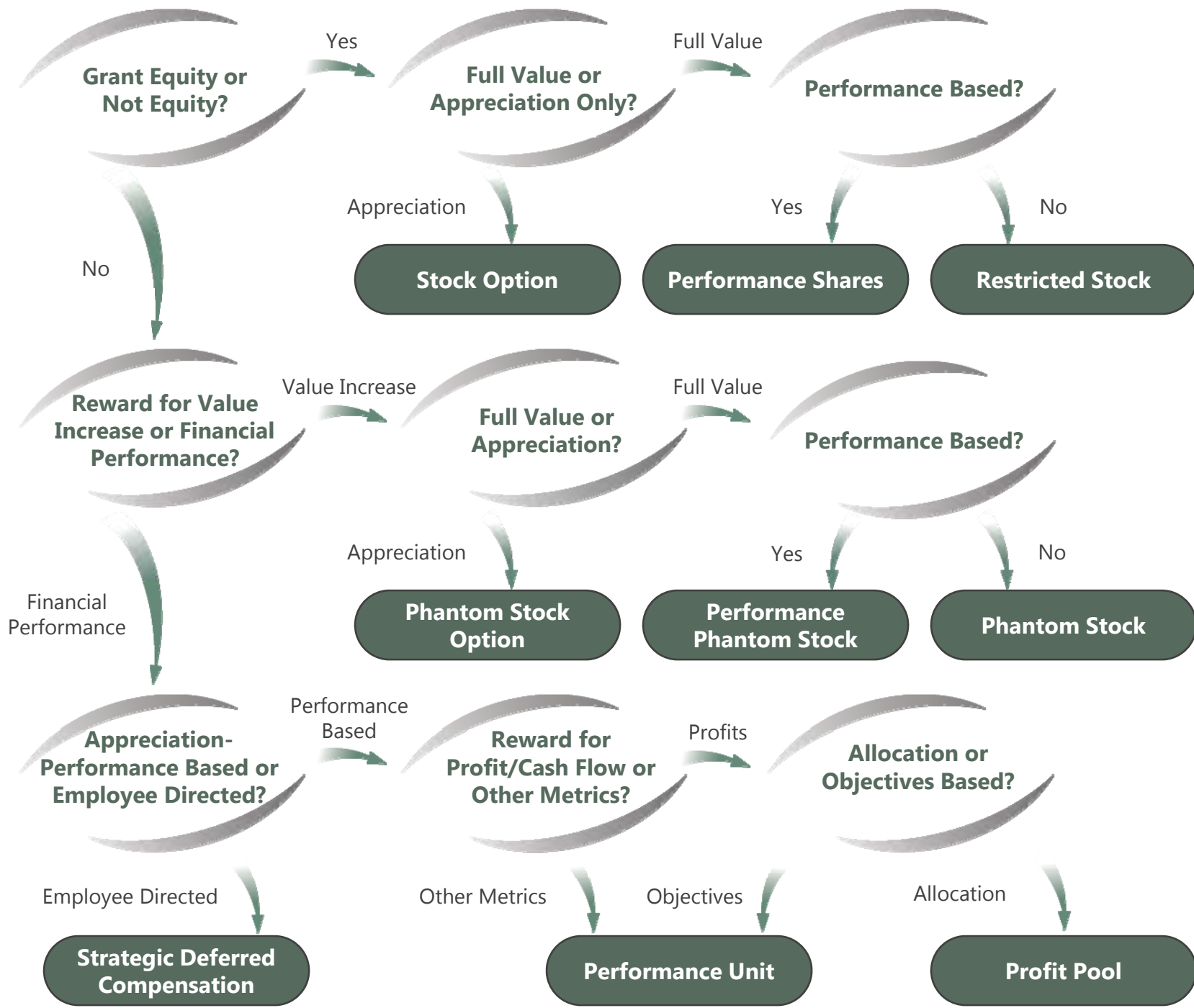
1 Cash Flow & Living Standard

Salary & Bonus

Clear Pay Philosophy

# Explore Appropriate Options







# Project Outcomes

Develop and Effective Financial Model

# Sample LTIP Model – P&L Forecast

	C	E	F	G	H	I	J	K	L	M	N	O	P	Q
1	Target	P&L Forecast												
2	P&L FORECAST	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
3		Actual	Actual	Actual	Projected	Projected	Projected	Projected	Projected	Projected	Projected	Projected	Projected	Projected
4	Net Sales	35,015,667	32,524,143	39,156,444	45,000,000	49,000,000	52,000,000	55,000,000	60,000,000	66,000,000	72,600,000	79,860,000	87,846,000	96,630,600
5	Cost of Goods Sold	19,375,516	17,230,214	21,541,211	24,750,000	26,950,000	28,600,000	30,250,000	33,000,000	36,300,000	39,930,000	43,923,000	48,315,300	53,146,830
6	<b>Gross Profit</b>	<b>15,640,151</b>	<b>15,293,929</b>	<b>17,615,233</b>	<b>20,250,000</b>	<b>22,050,000</b>	<b>23,400,000</b>	<b>24,750,000</b>	<b>27,000,000</b>	<b>29,700,000</b>	<b>32,670,000</b>	<b>35,937,000</b>	<b>39,530,700</b>	<b>43,483,770</b>
7	Selling Expenses	466,785	455,120	483,803	546,750	595,350	631,800	668,250	723,000	801,900	862,090	970,299	1,067,329	1,174,062
8	G&A	5,367,425	5,653,767	6,100,910	6,986,250	7,607,250	8,073,000	8,538,750	9,315,000	10,246,500	11,271,150	12,398,265	13,638,092	15,001,901
9	Interest Expense	48,176	45,388	35,503	36,213	36,937	37,676	38,430	39,198	39,982	40,782	41,597	42,429	43,278
10	<b>Income from Operations</b>	<b>9,757,765</b>	<b>9,139,654</b>	<b>10,989,211</b>	<b>12,680,787</b>	<b>13,810,463</b>	<b>14,657,524</b>	<b>15,504,570</b>	<b>16,916,802</b>	<b>18,611,618</b>	<b>20,475,978</b>	<b>22,526,839</b>	<b>24,782,850</b>	<b>27,264,530</b>
11	Interest & Dividend Income	81,135	52,187	14,171	14,454	14,744	15,038	15,339	15,646	15,959	16,278	16,604	16,936	17,274
12	Gain (loss) on Sale of Investments	(15,596)	1,061	-	-	-	-	-	-	-	-	-	-	-
13	Gain on Disposal of Equipment	9,202	1,750	(9,559)	-	-	-	-	-	-	-	-	-	-
14	Increase in Cash Surrender Value of Life Insurance	67,622	72,272	62,044	63,285	64,551	65,842	67,158	68,502	69,872	71,269	72,694	74,148	75,631
15	Other Income	705	29,525	384	-	-	-	-	-	-	-	-	-	-
16	<b>Earnings Before Taxes</b>	<b>9,900,833</b>	<b>9,296,449</b>	<b>11,056,251</b>	<b>12,758,526</b>	<b>13,889,757</b>	<b>14,738,404</b>	<b>15,587,068</b>	<b>17,000,949</b>	<b>18,697,448</b>	<b>20,563,525</b>	<b>22,616,137</b>	<b>24,873,934</b>	<b>27,357,435</b>
17	Provision for Income Taxes	145,400	26,200	104,000	191,378	208,346	221,076	233,806	255,014	280,462	308,453	339,242	373,109	410,362
18	<b>Net Income</b>	<b>9,755,433</b>	<b>9,270,249</b>	<b>10,952,251</b>	<b>12,567,148</b>	<b>13,681,410</b>	<b>14,517,328</b>	<b>15,353,262</b>	<b>16,745,935</b>	<b>18,416,987</b>	<b>20,255,072</b>	<b>22,276,895</b>	<b>24,500,825</b>	<b>26,947,074</b>
19	Interest Expense	48,176	45,388	35,503	36,213	36,937	37,676	38,430	39,198	39,982	40,782	41,597	42,429	43,278
20	Depreciation	966,850	875,917	853,121	878,715	905,076	932,228	960,195	989,001	1,018,671	1,049,231	1,080,708	1,113,129	1,146,523
21	<b>EBITDA</b>	<b>10,915,859</b>	<b>10,217,754</b>	<b>11,944,875</b>	<b>13,673,454</b>	<b>14,831,770</b>	<b>15,708,308</b>	<b>16,585,693</b>	<b>18,029,149</b>	<b>19,756,102</b>	<b>21,653,538</b>	<b>23,738,442</b>	<b>26,029,493</b>	<b>28,547,237</b>
30	Share Price multiple			5	5	5	5	5	5	5	5	5	5	5
31	Formula Value			\$ 55,930,151	\$ 62,750,482	\$ 69,966,626	\$ 75,481,459	\$ 80,077,599	\$ 85,879,065	\$ 93,380,533	\$ 102,228,885	\$ 112,056,874	\$ 122,856,160	\$ 134,723,536
32	Formula Share Price (EOY)			\$ 6.28	\$ 7.00	\$ 7.55	\$ 8.01	\$ 8.59	\$ 9.34	\$ 10.22	\$ 11.21	\$ 12.29	\$ 13.47	
33	Annual Increase in Formula Value				\$ 6,820,330	\$ 7,216,144	\$ 5,514,833	\$ 4,596,140	\$ 5,801,466	\$ 7,501,468	\$ 8,848,351	\$ 9,827,989	\$ 10,799,286	\$ 11,867,378
34	Annual Increase in Formula Value Since Plan Inception				\$ 6,820,330	\$ 14,036,479	\$ 19,551,308	\$ 24,147,448	\$ 29,948,914	\$ 37,450,382	\$ 46,298,734	\$ 56,126,722	\$ 66,926,009	\$ 78,793,384
37	Assumptions				2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
39	Increase in Net Sales				14.3%	8.3%	6.1%	5.8%	9.1%	10.0%	10.0%	10.0%	10.0%	10.0%
40	Cost of Goods Sold as % of Net Sales				55.0%	55.0%	55.0%	55.0%	55.0%	55.0%	55.0%	55.0%	55.0%	55.0%
41	Selling Expenses as % of Gross Profit				2.7%	2.7%	2.7%	2.7%	2.7%	2.7%	2.7%	2.7%	2.7%	2.7%
42	G&A as % of Gross Profit				34.5%	34.5%	34.5%	34.5%	34.5%	34.5%	34.5%	34.5%	34.5%	34.5%
43	Annual Increase in Interest Expense				2.0%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%
44	Annual Increase in Interest Income				2.0%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%
45	Annual Increase in Gain/Loss on Investments				0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
46	Annual Increase in Gain/Loss on Disposal of Equipment				0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
47	Annual Increase in Cash Surrender Value				2.0%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%
48	Annual Increase in Other Income				0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
49	California Franchise Tax				1.5%	1.5%	1.5%	1.5%	1.5%	1.5%	1.5%	1.5%	1.5%	1.5%
50	Annual Increase in Depreciation				3.0%	3.0%	3.0%	3.0%	3.0%	3.0%	3.0%	3.0%	3.0%	3.0%



# Communicate and Promote the Plan



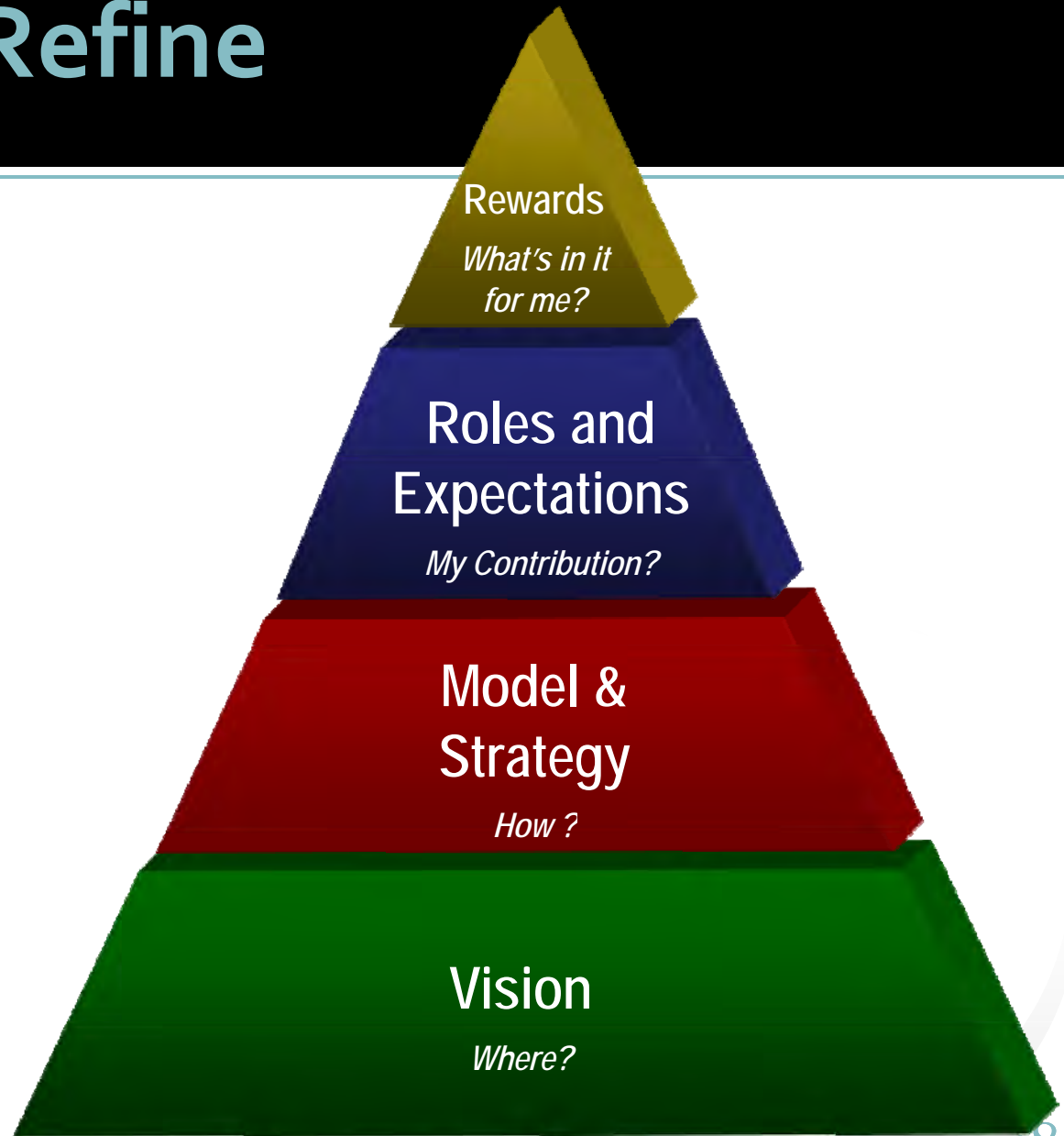
1. Explain, celebrate and reinforce the total value proposition
2. Communicate a sense of partnership
3. Project the wealth multiplier opportunity

# Key Producer 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

# Evaluate & Refine

Line of Sight



# First Step

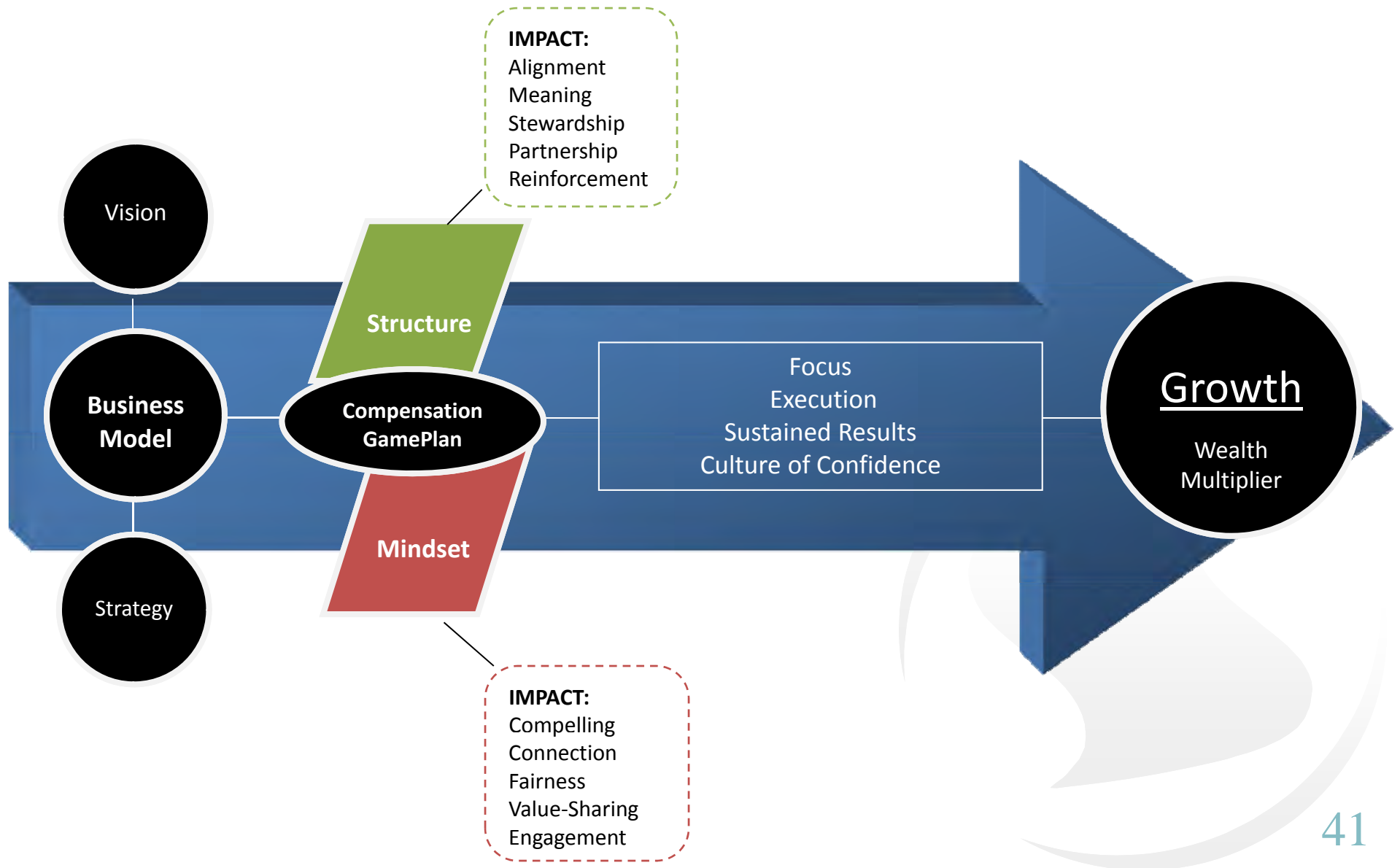
- Alignment Appraisal™
  - A focused look at your current practices with a comparative eye on whether your company is building a “Unified Financial Vision for Growing the Business”
  - Process—online employee survey

# 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



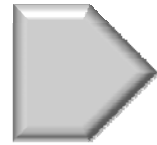
# Building a Unified Financial Vision for Growing the Business



# 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

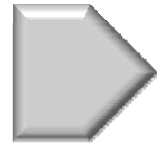


Are we excellent communicators of the value and purpose of our rewards programs?

# 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\*

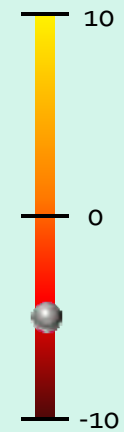
\*Scale of 100

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\*

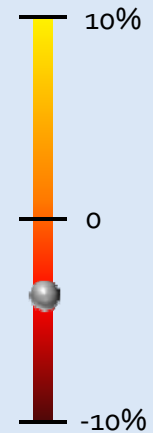
\*Scale of 100

Employee Appraisal

30.2

Net Score

-32.0%



Compelling

7.0

Connection

6.4

Fairness

5.4

Value-Sharing

5.0

Engagement

6.4

# Special Offer

This Appraisal is typically \$1,800.

For today's webinar attendees only:

*No cost*

Indicate interest on final survey

## Focus: Creating a Unified Financial Vision

Wealth  
"Multipliers"  
5%



### The Wealth Multiplier

- Partnership Relationship
- Shared Vision
- Engaged Employees
- Effective Practices
- Sustained Productivity

---

Missing  
Structure

---

## Focus: Fulfilling Ownership Vision

Wealth  
"Creators"  
95%



### The Wealth Creator

- Subordinate Relationship
- Divided Visions
- Loyal Employees
- Inconsistent Practices
- Bursts of Productivity

# Creating Long-Term Value for Premier Talent

- They will find non-traditional pay structures alluring and differentiating
- The pay structure will respect their entrepreneurial mindset and appeal to their interest in wealth accumulation opportunities
- They will accept the responsibilities and accountability associated with true value creation (i.e., they won't "expect" higher pay without creating results)



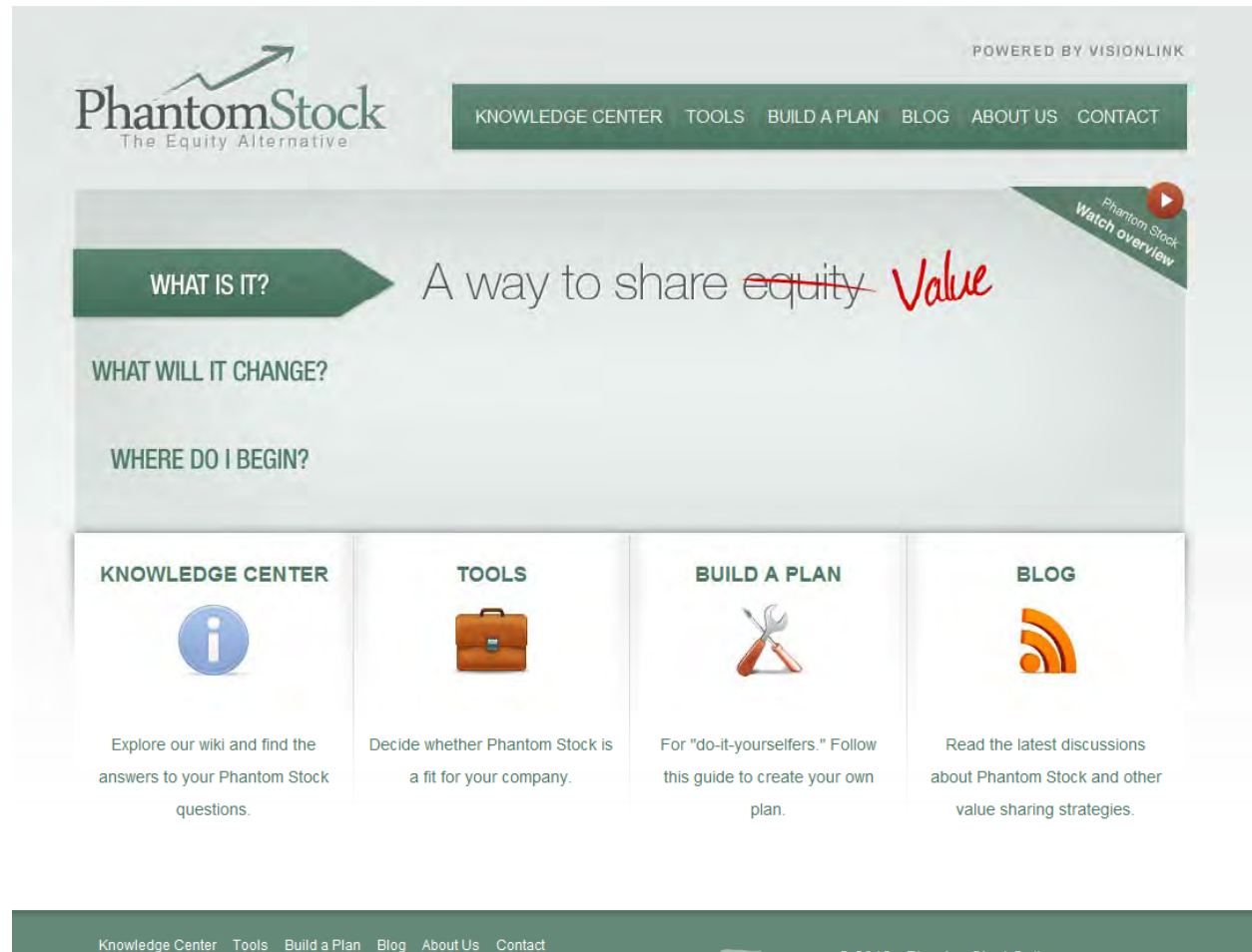


# Next Online Seminar:

**“Compensation Standards that both Shareholders and Employees will Embrace”**

To be held on:  
Tuesday, September 25<sup>th</sup>, 2012

Check out our NEW website:  
[www.PhantomStockOnline.com](http://www.PhantomStockOnline.com)



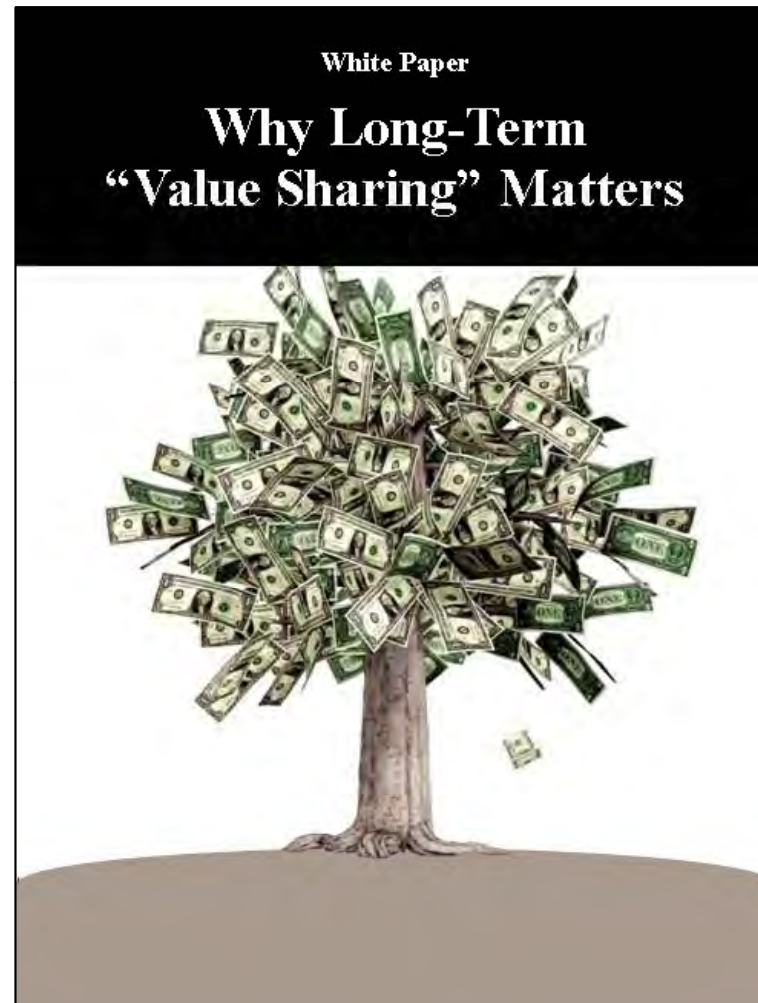
You can also subscribe to our blog

# UPDATED website: [www.VLadvisors.com](http://www.VLadvisors.com)

The screenshot shows the homepage of The VisionLink Advisory Group. At the top left is the logo, and at the top right is a 'Client Login' button and the phone number (888) 703 0080. A navigation bar includes links for Home, About Us, Client Profile, Knowledge Center, Speaking Engagements, Events, Blog, and Contact Us. The main content area features a large image of a mountain peak with a sidebar article titled 'How should I Share Value?' with a 'Learn More' button. Below this are three smaller article teasers: 'WHAT IS PHANTOM STOCK?', 'HOW SHOULD I SHARE VALUE?', and 'HOW DO I END ENTITLEMENTS?'. An 'Events' section lists four dates with descriptions, and a 'Join our webinar invitation list' form is present. At the bottom, three columns provide advice: 'ASK THE RIGHT QUESTIONS', 'FOLLOW THE RIGHT PROCESS', and 'CHOOSE THE RIGHT COACHES'.

You can also subscribe to our blog

# NOW AVAILABLE!



Express interest on the final survey



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# Questions?



# Thank you for attending

*Please complete our brief survey immediately following our presentation.*

*We value your input.*

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

# Thank you!



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ADVISORY GROUP