Executive Compensation's Role in Driving and Supporting Business Performance

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Linkage Between Pay and Performance is a Mixed Bag

- Common argument by media and some governance and shareholder groups holds there is no meaningful relationship between executive pay and company performance
  - If there is no meaningful relationship between pay and company performance then executive compensation (EC) cannot be driving or supporting business performance
- There are numerous cases where pay and performance linkage is not effective, and these cases are repeatedly highlighted by media and governance groups
- But there are a growing number of cases where pay and performance linkage is alive and well

A Multitude of Pay Design Issues Eliminate, or Substantially Reduce, the Linkage Between Pay and Performance

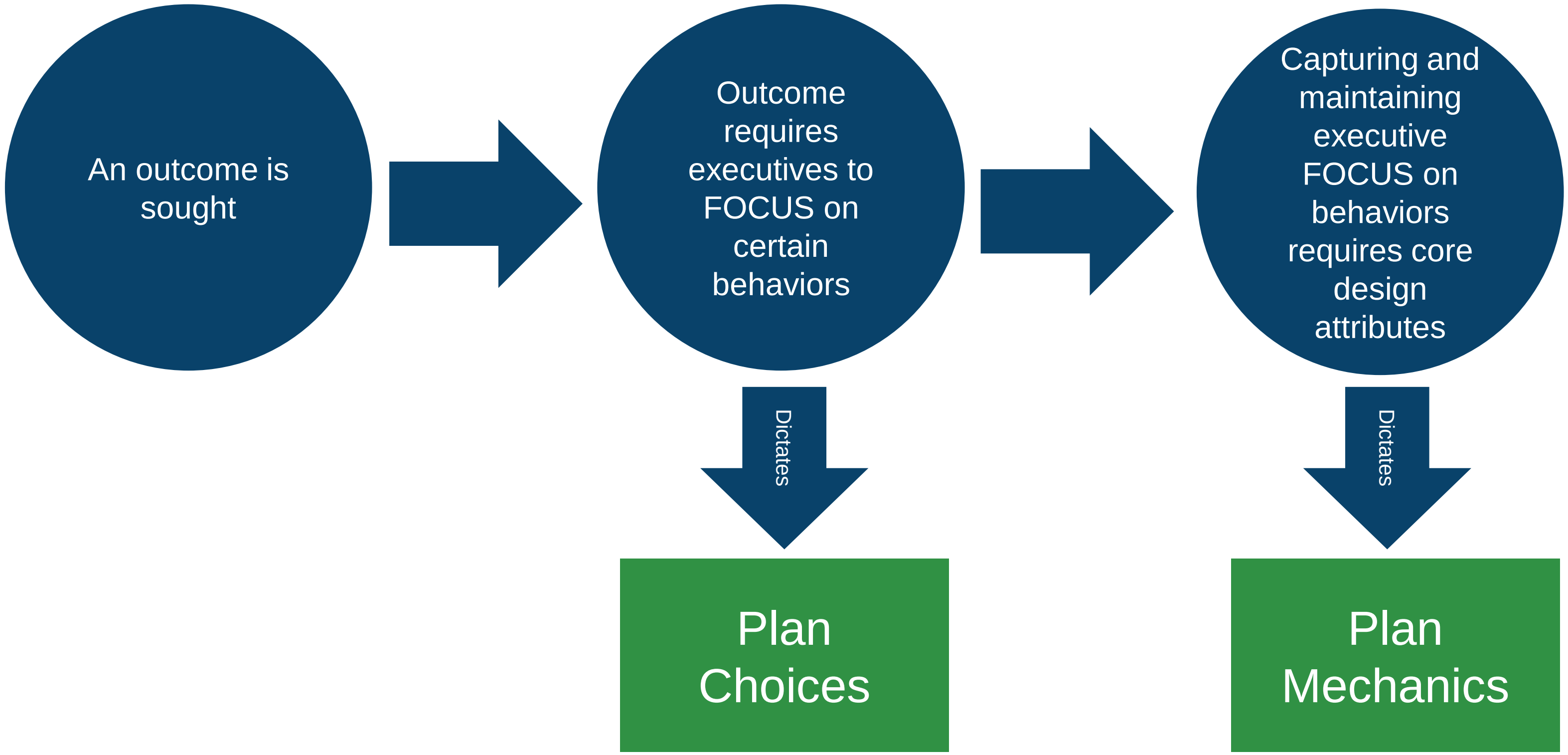
- **The wrong performance measures**
  - Disconnected from business strategy
- **Too many performance measures**
  - What is the business strategy?
- **Obscured performance measures**
  - Buckets of adjustments
- **Poor goal setting**
  - Targets too high or too low, range too narrow or too wide
- **Lack of commitment to the plan**
  - Discretion/need to achieve street profit expectation determines result

Better Pay Design Principles Can Increase Likelihood of Strong Pay and Performance Linkage

- **Link indirectly to shareholder value experience**
  - Search for metrics that correlate with shareholder experience and may therefore be leading indicators of forward total shareholder return (TSR)
- **Or directly link to shareholder experience with absolute TSR**
  - Benefits of absolute versus relative TSR
  - New design, leveraged performance units (LPUs), depending on the fact pattern
- **Whatever the metrics and rationale, create FOCUS**
  - Avoid underweighted or frequently changing performance metrics
- **Business strategy driven performance metrics**
  - Don’t forget FOCUS
  - You likely will get what you reward – is it the right strategy?

Well designed executive compensation plans sharpen participant FOCUS on behaviors that drive business performance

- An organization's strategy dictates which behaviors to focus on in the executive compensation plan
- Impacting behavior requires several attributes be included in the design, implementation, and administration of executive incentive plans



Capturing and Maintaining Executive Focus on Behaviors Requires Several Design Attributes be Present in all Incentive Plans

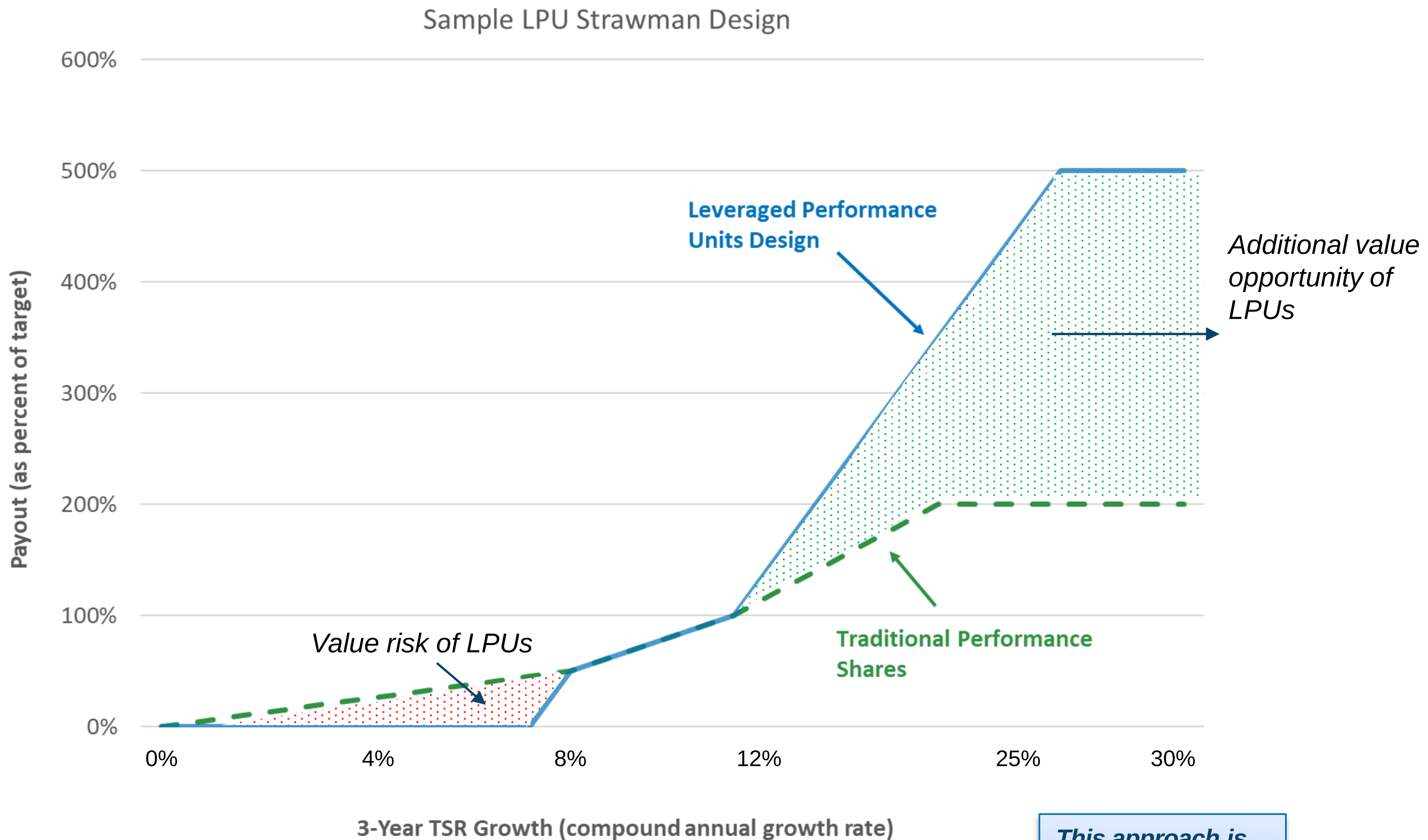
- **Understandable**: plan designs that are effectively communicated (and reinforced through education/training)
  - *The participant understands the mechanics of the plan*
- **Achievable**: plans that are viewed as having a reasonable probability of achievement (supported by a collaborative and rigorous goal setting process)
  - *The participant views the outcome as achievable*
- **Relatable:** plans that contain sufficient line of sight between participant behaviors and performance outcomes (reinforced by education/training)
  - *The participant understands how they can contribute to the outcome*
- **Equitable**: final award outcome will be fairly assessed
  - *The participant believes that if they hold up their end of the bargain, they will receive the award they're due*
- **Meaningful**: award opportunities with sufficient relative magnitude to drive participants to *want* to work towards the outcome
  - *The participant views the size of the potential award as large enough to focus their attention on working towards the outcome*

LPUs are a new type of special grant that can significantly strengthen alignment with shareholders

- **Design Attributes:**
  - Opportunity for participant to increase Company value and share in the growth – *direct shareholder alignment*
  - Measured based on company TSR over a 3-year period
  - TSR peer group or index serves as a modifier to further balance participant and shareholder interests
  - Greater leverage than traditional performance shares; less dilutive than stock options
  - Similar to stock options, LPUs have no value if the stock price does not grow. Unlike stock options, there is no intrinsic value until TSR rises above a pre-established level
  - Viewed as performance-based by ISS, contrasted with stock options which are not
  - Target value of awards disclosed in SEC filings (e.g., proxy) are generally modest

LPUs provide more downside risk, but with much greater upside opportunity than performance share units

LPUs are an innovative approach to LTI (typically issued as a one-time, special grant), designed to strengthen the alignment between management and shareholders during a period of transition by driving operational improvement and increasing share value creation



<u>Sample LPU Performance and Payout Range</u>

Performance is measured based on TSR growth over 3 years

Range	TSR (CAGR)	Percent Target Shares
Maximum	25%	500%
Target	12%	100%
Threshold	8%	50%

Payouts are interpolated between these points.

<u>This approach is now used by:</u>

<u>Carnival</u>
<u>Conagra Brands</u>
<u>Global Payments</u>

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Historical pay and performance alignment are tested by comparing actual pay outcomes to both company and shareholder performance

Example pay-for-performance back testing (banking organization)