

# FINDING THE BALANCE



A five-year  
review of  
compensation

December 2019

# With over US\$20 billion paid out in total over the past five years, discretionary compensation has become a systemic compensation issue that needs to be addressed.

Since 2014, at least US\$3.7 billion has been paid in discretionary compensation to executives in any given year. Not only are the amounts substantial, around 80% of all awards are not performance based. This means that for over US\$16 billion of the discretionary awards there were no additional performance conditions required. We believe that given the exceptionality of these awards, it is appropriate they be conditional upon the executives achieving some specific performance objective that is tied to strategic objectives. The absence of performance conditions runs contrary to a pay-for-performance objective. Furthermore, discretionary awards fall outside the regular compensation program and may not be captured in a say-on-pay analysis.

For a number of companies it appears that discretionary compensation has become a regular compensation tool – the exceptional is becoming the acceptable. Finally, about 60% of all awards dollars are directed at sign-on and retention, raising questions about management of succession planning. Also, awarding discretionary compensation for retention purposes is at odds with the claim that the compensation program (i.e. salary, short- and long-term compensation components) is designed to attract and retain.

We believe there is a place for discretionary compensation in a compensation program. However, the frequency, size, and structure we have observed raises concerns that discretionary compensation is not being used in a manner consistent with good compensation governance.

# US\$20 BILLION systemic compensation issue

**34%**  
of companies in the study (882 in total) have granted discretionary compensation in at least three of the five years

frequent users of discretionary compensation paid **US\$11.5 BILLION**, or 57% of the value of all discretionary compensation awards

Annual total discretionary compensation has exceeded **US\$3.7 BILLION** annually



These five sectors accounted for the bulk of reported discretionary compensation in each year

The top five sectors paid **74%** of all discretionary compensation

over **80%** of all awards are not tied to performance

Over the past five years... **89%** of all dollars paid in discretionary compensation came from US-based companies

**54%** of annual discretionary compensation awards granted have been classified as one of sign-on or retention



### calls to action

#### Issuers

Discretionary awards should be:

- infrequent;
- tied to the individual achieving specific and measurable performance targets linked to strategy;
- supported by a compelling rationale describing the need to make the award.

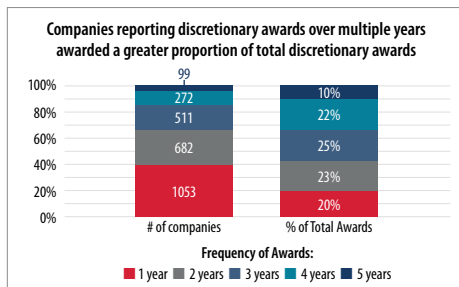
#### Investors

Investors should review discretionary compensation to ensure these awards are:

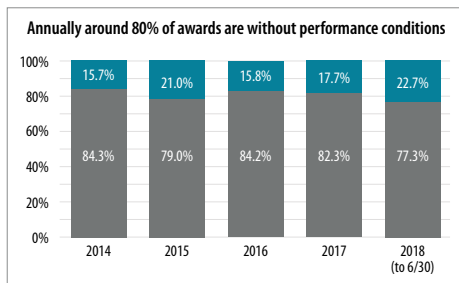
- used infrequently and to address exceptional circumstances;
- supported by a strong rationale in support of making the award;
- tied to the executive achieving specific and relevant performance conditions.



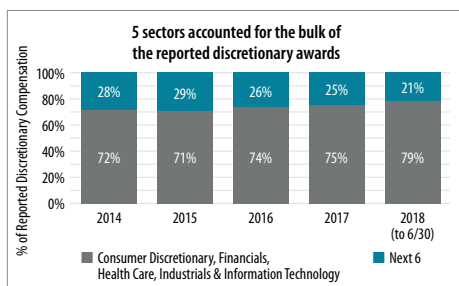
**WE HAVE EVALUATED  
FIVE YEARS OF DATA AND  
HAVE FOUND THAT...**



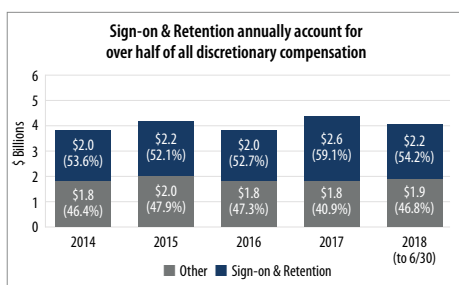
A disproportionate amount of discretionary compensation was paid by the companies using the awards most frequently.



The bulk of awards continue to be made without performance conditions attached.



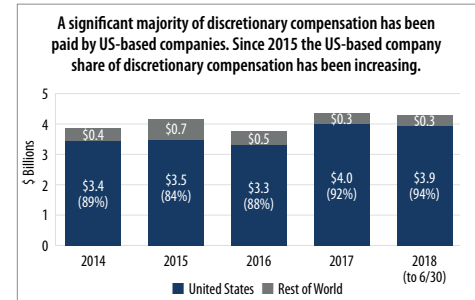
Consumer Discretionary, Financials, Health Care, Industrials, and Information Technology are by far the most frequent sectors where discretionary compensation decisions are made.



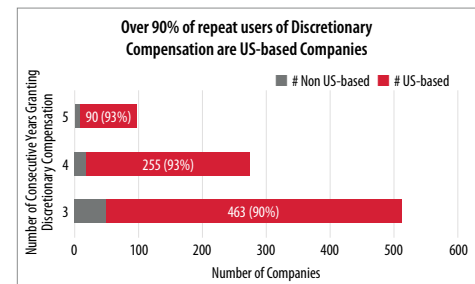
The most frequent use of discretionary compensation is for sign-on and retention purposes.

**DATA TO SUPPORT THAT  
DISCRETIONARY COMPENSATION IS A  
SYSTEMIC ISSUE IN THE UNITED STATES**

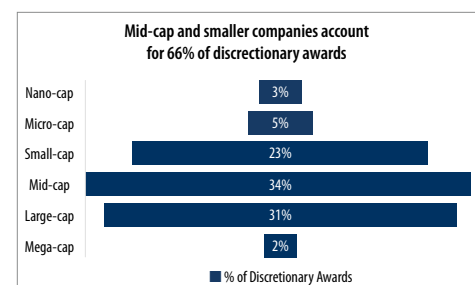
In each of the 5 years of the study, US-based companies awarded a significant portion of the annual compensation payments.



The majority of frequent users are US-based companies.



Companies with smaller market capitalizations are more likely to grant discretionary compensation than their larger peers.



Opinions, estimates and projections contained herein are Ontario Teachers' as of the date hereof and are subject to change without notice. The information and opinions contained herein have been compiled or arrived at from sources believed reliable but no representation or warranty, express or implied, is made as to their accuracy or completeness. Neither Ontario Teachers' nor any of its officers, directors, partners, employees or affiliates accepts any liability whatsoever for any direct or consequential loss arising from any use of this report or its contents. Information may be available to Ontario Teachers' or its affiliates that is not reflected in this report.

This report is provided to you for informational purposes only. This report does not constitute investment advice. This report is not, and is not constructed as, an offer to sell or solicitation of any offer to buy any financial instrument, nor shall this report be construed as an opinion as to whether you should enter into any swap, investment or trading strategy involving a swap or any other transaction. Ontario Teachers' may engage in transactions or have positions that are inconsistent with the views discussed in this report and may have positions, or be in the process of acquiring or disposing of positions, referred to in this report.

This information may not be reproduced without the prior express written consent of Ontario Teachers'.