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DIRECTOR'S PAY CHAPTER 17 ABSTRACT

BOARD OF DIRECTORS TOTAL REWARDS STRATEGY COMPETITIVE LEVELS, MIX, AND MESSAGES THAT MAKE GOOD BUSINESS SENSE

Over the past few years, the role of director has become more demanding and fraught with risk. Not surprisingly, director compensation has increased over this time. And while the increase in director compensation is noteworthy, far more meaningful and fascinating is the shift in focus from how much directors are paid to what they do and how that pay is delivered.

The compensation level of reward for any individual on the Board should first reflect the organization's environment, key stakeholders, and business strategy. Secondly, it should reflect the role those board members play and the responsibilities they have and finally it should reflect the total number of directors carrying the load.

No two organizations are the same and no two organizations have the same relationship with—or expectations of—their Board of Directors. That demands that a Board's role and the way it is paid will vary from company to company. The relationship, responsibilities, and roles should be the starting point for Boards as they set the amount and form of compensation they receive for the Total Reward Strategy. New notions of corporate governance demand that director compensation be separate from operating management, and be treated differently. Directors who are elected by shareholders to serve as stewards of their investments have broad reward components focusing on long-term success factors consistent with the various shareholders interests, be it risk adjusted returns, or organization sustainability for example. In this context, director total reward strategy should visibly reflect this distinct role.

When thinking about mix and messages portions of the reward architecture for director's pay, it is best to capture the five different categories of rewards:

Membership Rewards or Retainers send a message that regardless of the company's performance or the director's contribution in terms of hours or expertise, all directors will be paid a straight dollar or share amount.

Performance based rewards, most often seen in the form of company equity but also occasionally in the form of cash, are an attempt to tie the director's rewards to both the shareholders' interests and the performance of the company.

Contribution rewards for directors take the form of fees. Fees for: Board or committee meetings, chairmanships of the Board or various committees, and committee membership in general.

Benefits such as retirement programs, deferred compensation, medical, dental, and life insurance programs are becoming less common but are still provided in some organizations.

Prestige, gratuitous, or status-based rewards have to do with special rewards that range from airplane travel, contributions made to a Board member's favorite charity, all the way to discounts on the companies products.

Each of the above categories of director's rewards carry very different messages by themselves, but that different mixes or combinations of rewards from the above categories would send different messages to not only the directors, but also the entire list of other organizational stakeholders (executives, employees, customers, partners, suppliers and yes ultimately the owner investors!).

Additionally, we believe that in many cases it is appropriate—in spite of the editorials of many pundits to the contrary—to pay the Board for performance.

THE FUTURE

So what does the future hold when it comes to director responsibility, roles, and rewards?

Director responsibilities, roles, and rewards will become more dramatically defined in the future.

The total cost of the Board will be a discussion subject.

Director roles will be better defined.

Director total reward strategy will be dramatically restructured.

Retainers for Board service will continue to increase

Committee chair retainers, particularly premiums for audit and compensation committee chairs, will increase to reflect the additional time these roles now require.

Committee meeting fees will increase modestly.

Lead director compensation will continue to grow.

Equity compensation will continue to shift from options to full value shares.

Stock ownership guidelines for directors will continue to spread.

Finally, holding requirements for directors will and should become increasingly prevalent.