COMPENSATION

Assessing Your Say-on-Pay Vote

Susan O'Donnell is a partner with Meridian Compensation Partners.

Daniel Rodda is a lead consultant with Meridian Compensation Partners.

As banks prepare for their annual shareholder meetings, most will have a say-on-pay vote where shareholders indicate whether they support the executive compensation program. This process has pressured companies to improve their compensation disclosures and clearly explain their pay practices and decisions. Today's bank boards should engage with shareholders to understand their evolving perspectives on compensation and governance practices.

Meridian Compensation Partners' Susan O'Donnell and Daniel Rodda discuss how to interpret your say-on-pay results and how to prepare for next year's vote.

What do directors need to understand about the results of their 2015 say-on-pay vote?

Directors should know what percentage of their shareholders voted in favor of their executive compensation programs, and how that level of support compared to prior years. Receiving majority support isn't enough. Over 70 percent of banks last proxy season received a favorable shareholder vote on their programs of 90 percent or more, so any result below that level suggests potential concerns. If your bank receives less than 70 percent support, shareholders and advisory firms such as Institutional Shareholder Services (ISS) will expect to hear specific details on how the company responded to feedback, and they will conduct a more rigorous assessment the following year. Strong shareholder support one year does not guarantee future success. We have seen the result change swiftly when not monitored.

How can directors understand what drove the results of their say-on-pay vote?

Directors should understand the makeup of their shareholder base, as there are differences in what drives the voting patterns of retail and institutional investors. Many institutional shareholders are influenced by ISS and another prominent shareholder advisory firm, Glass Lewis, so it is valuable to review their vote reports. Other institutional shareholders, like Blackrock and Vanguard, follow their own voting guidelines. While pay outcomes are more easily controlled, say-on-pay also reflects how shareholders view performance, primarily based on total shareholder return (both relative to peers and on an absolute basis). Directors need to take an objective look at how shareholders will view the relationship between executive pay and the bank's performance.

How can banks improve the results of their say-on-pay vote?

Ensuring a significant portion of your total pay program is variable and that actual pay outcomes vary based on performance are the best ways to gain shareholder support. It is also important to maintain and disclose policies and practices that reinforce sound governance, such as stock ownership requirements, clawback policies, minimal perquisites and elimination of any tax gross-ups. The Compensation Discussion and Analysis (CD&A) section of your company's annual proxy must effectively communicate the context and rationale for pay decisions, as well as how the programs ensure alignment between pay and performance. Investors want to understand the "how and why" of compensation decisions, including why performance measures were chosen, how pay decisions were made, and how the compensation program is aligned with shareholder value. If the say-on-pay vote receives less than 90 percent support, banks should consider reaching out to large shareholders to understand any concerns they may have. Additionally, banks that received negative recommendations from ISS and Glass Lewis should reach out to these advisory firms to discuss what led to their recommendation and what might address their concerns.

When should banks begin preparing for the following year's say-on-pay vote?

Directors should already be thinking ahead to next year's vote. The board has likely already made pay decisions in 2015 that will be evaluated as part of the 2016 say-on-pay vote. Typically, salary increases and equity awards are made in the first quarter of the year, but shareholders will be evaluating those decisions through the lens of performance through the end of the year. This can at times lead to an unfortunate disconnect. As a result, it is never too early to consider decisions in light of shareholder perspectives and the potential impact on the say-on-pay vote. In addition, ongoing shareholder outreach is viewed positively by investors and can proactively surface potential issues while there is still time to make changes. Being proactive and considering pay in the broader context of bank performance and shareholder perspectives should be an ongoing process.