

ClearBridge

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# CLEAR*thinking*

Pay vs. Performance Trends from 2023 Proxy Season



ClearBridge  
Compensation Group

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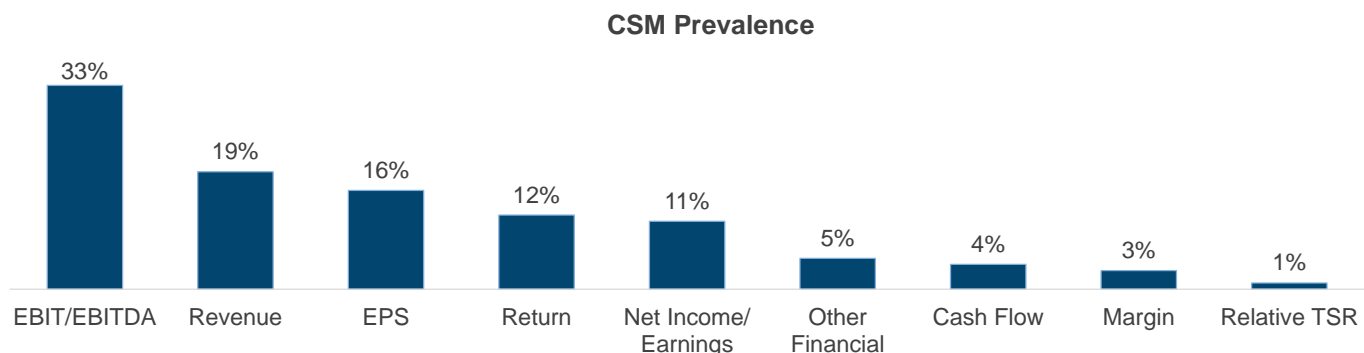
Over ten years after the Dodd-Frank Act directed the SEC to develop disclosure requirements regarding the alignment of pay and performance, the SEC finalized and implemented the rules in late 2022. In 2023, we saw the first season of proxies filed with the new Pay vs. Performance (“PvP”) requirements, which provided insights into companies’ initial interpretations and decisions regarding the disclosure rules. ClearBridge examined the PvP disclosure of 100 mid-cap and large-cap companies to provide insights into disclosure trends and the relationship between pay and performance in accordance with the new requirements.

## PvP Disclosure Trends

### *Company Selected Measure*

The PvP requirements include disclosure of performance for a metric that the company believes to be the most important financial performance measure used to link compensation actually paid (“CAP”) to company performance for the most recently completed fiscal year (“Company Selected Measure” or “CSM”).

Earnings metrics were the most common CSM among our sample, specifically EBIT/EBITDA (33%).

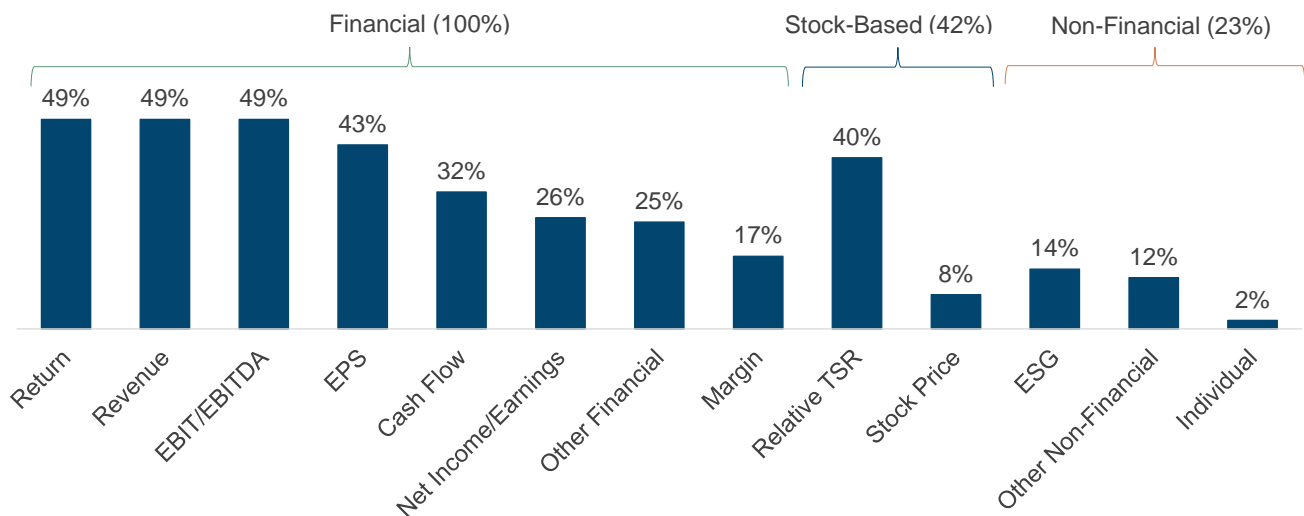


CSMs were most commonly a metric used in a company’s annual incentive plan (77%), and a little under half (47%) were used in the long-term incentive plan. In addition, four companies in our sample voluntarily disclosed more than one CSM.

### *List of Most Important Measures*

In addition to the CSM, companies are also required to disclose a list of the three to seven most important measures in linking CAP to company performance. Most companies selected three to four measures for this list (inclusive of the CSM). The vast majority of companies disclosed only one list of measures, applicable to all Named Executive Officers (“NEOs”) (96%), as opposed to separate lists applicable to individual NEOs.

### List of Most Important Measures Prevalence

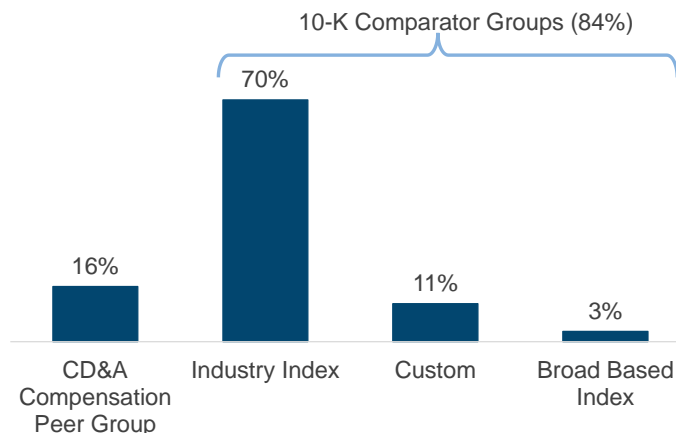


### Total Shareholder Return (“TSR”) Comparator Group

In addition to presenting their own TSR performance, companies are required to present TSR performance for “peer” companies, which can either represent the 10-K performance graph comparator group (industry/line-of-business index) or the peer group used for executive compensation benchmarking purposes as disclosed in the Compensation Discussion & Analysis (“CD&A”).

A significant majority of companies (84%) used the 10-K performance graph comparator group, as opposed to the peer group used for executive compensation benchmarking purposes. This is largely driven by the additional complexities involved in updating the compensation peer group for changes made over the applicable years when calculating TSR.

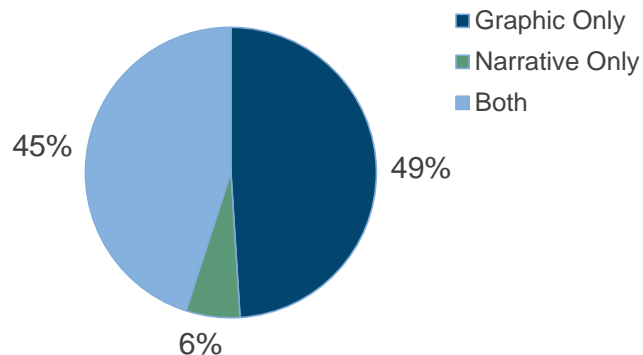
### TSR Comparator Group Prevalence



### *Graphic vs. Narrative Disclosure*

The PvP rules provide flexibility in how companies may disclose the required descriptions of the pay and performance relationships. Almost all companies included graphic descriptors, often in connection with narrative descriptors.

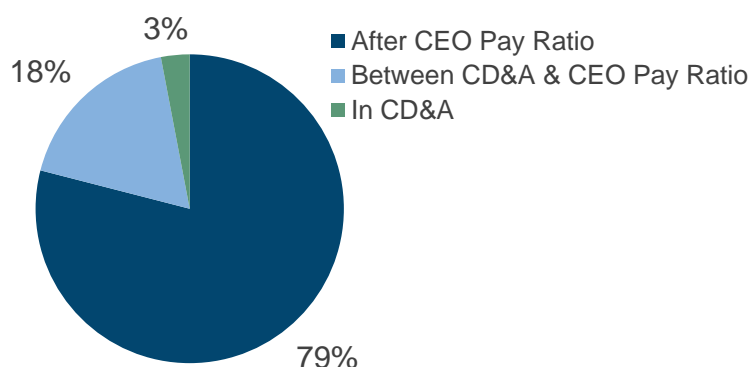
**Graphic & Narrative Descriptor Prevalence**



### *Location of Disclosure*

The PvP rules do not specify where disclosure should fall within the proxy statement. Almost all companies positioned the PvP disclosure outside of the CD&A, most commonly after the CEO Pay Ratio in the proxy statement, such that the PvP disclosure is not subject to the Say on Pay vote.

**Disclosure Location Prevalence**



## PvP Alignment

As expected, CEO 3-year cumulative CAP as a percentage of 3-year cumulative summary compensation table (“SCT”) total compensation directionally tracks with 3-year TSR<sup>(1)</sup>, given that stock price/TSR is inherently a significant driver of equity award value and equity is a significant component of NEO pay.

Our findings also show that year-over-year changes in CEO CAP directionally track with year-over-year changes in Net Income (albeit to a lesser degree than TSR), but alignment is more mixed with CSM performance<sup>(2)</sup>. As illustrated below, CEO CAP did not directionally align with CSM performance in 2022 when the stock market was in a downturn, as opposed to in 2021 when the stock market was strong. While some companies may have had positive financial performance in 2022 as reflected in the CSM, TSR and Net Income were impacted by broader economic factors (e.g., inflation, interest rate increases) that also impacted the value of equity reflected in CAP.



As additional context for the relationship between CEO CAP and TSR, 3-year cumulative CEO CAP as a percentage of 3-year cumulative SCT total compensation increases as 3-year TSR performance increases.

CEO 3-Year Cumulative CAP as a % of 3-Year Cumulative SCT Total Comp				
Percentile	Total Sample	Companies with Ending 3-Yr TSR Value:		
		< \$100	\$100 to > \$150	≥ \$150
75th	141%	114%	135%	213%
50th	119%	93%	117%	167%
25th	100%	82%	102%	143%

(1) CEO 3-year cumulative CAP as a % of 3-year cumulative SCT total compensation (greater or less than 0%) vs. 3-year TSR (greater or less than \$100)

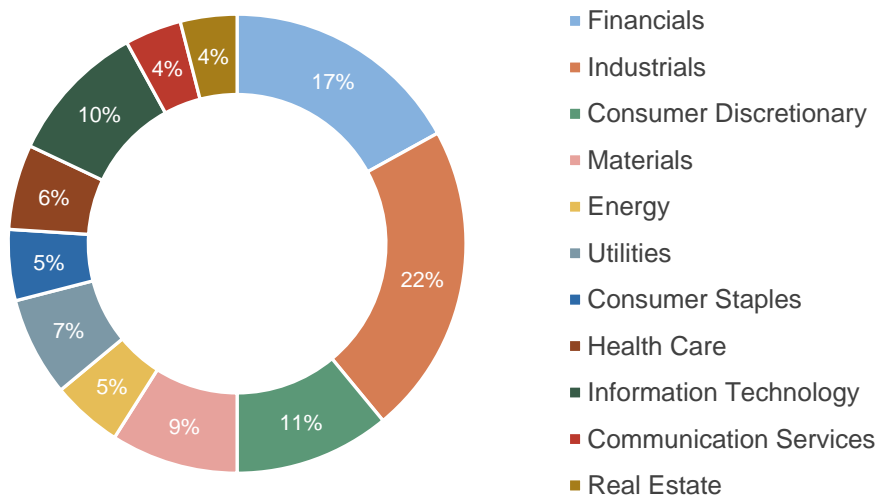
(2) Year-over-year change in CEO CAP (positive or negative) vs. year-over-year change in net income or CSM (positive or negative)

Also of note, the majority of CEO and Other NEO CAP values were positive in each of 2020, 2021, and 2022. Negative CAP values were most prevalent in 2022 (16% of CEOs and 10% of Average of Other NEOs), with the 2022 market environment likely a driving force.

	Compensation Actually Paid					
	2020		2021		2022	
	Positive	Negative	Positive	Negative	Positive	Negative
CEO	95%	5%	100%	0%	84%	16%
Avg. of Other NEOs	95%	5%	98%	2%	90%	10%

## Characteristics of Companies Analyzed (n=100)

(\$MM)	LTM Revenue (12/31/2022)	Market Cap (12/31/2022)
<b>75th %ile</b>	\$17,062	\$36,961
<b>50th %ile</b>	\$5,468	\$9,413
<b>25th %ile</b>	\$2,457	\$4,817



## Contact Us

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