Managing reward through challenging times

COVID-19 and its consequences for business will impact many executive reward matters and will potentially expand the remit of the Remuneration Committee.

In addition to matters relating to executive pay, there will be decisions required on pay and conditions for the wider workforce. Shareholders and the broader community will expect to see consistency across these decisions.

The political and economic context for decision-making will be critically important, with companies needing to plan comprehensively whilst ensuring that they balance multiple stakeholder interests.

Immediate interventions taken

Many companies in the worst affected industries have taken early action in managing reward, including:

- Reductions to CEO fixed annual remuneration (FAR);
- Reductions to executives' FAR;
- Reductions to/temporary suspension of NED fees;
- Nil payment of short term incentive (STI) for CEO/executives/general staff for FY20, regardless of whether these were 'in the money';
- Application of salary freezes; and
- Implementation of recruitment freezes.

Key issues for all to consider

Regardless of whether operating in one of the worst hit industries, many companies are projecting reduced/volatile revenue patterns into FY21. Reward matters to work through in this context include:

Salary reviews:
At what point is it appropriate to release temporary reductions to CEO/executive FAR? How should we explain/defend why we have suspended any executive and general staff reviews? Or conversely, how will we defend going ahead with remuneration increases?

Adjustment to 'in-flight' targets or performance outcomes
How will current year STI targets be dealt with in an environment of volatility? If discretion is applied, on what basis will we do so? What are investors' expectations in this regard?

Setting FY21 STI targets
What approach to target setting will be deemed acceptable to shareholders? Is it defensible to postpone target setting until there is more certainty? Do we change targets or move to a fully discretionary approach for this period? How do we apply discretion?

Award of LTI grants
Should grants be reduced if the share price has fallen materially compared to the prior grant? Should we establish discretion to address any inappropriate windfall gains at vesting (in the context of a market correction)? How should hurdles be set in this context of volatility, compared to those used in prior grant years?

NED fees
In what context is it appropriate to release temporary NED fee decreases? When is it defensible to approach shareholders for an increase to base fees or fee pools again? What rationale should be provided?

What are external stakeholders saying?

NZ State Services Commission (SSC)
Voluntary pay reductions agreed with CEOs in the state sector. "I would not expect to see any pay increases occurring through this period for your tier 2 and 3 leaders." Peter Hughes, SCC Commissioner.

NZ Shareholders Association (NZSA)
"With […] significant cutbacks of dividends and staff, we need to ask if directors and executive remuneration reductions have been enough. Surely they are in a better financial position to weather this storm than most." Tony Mitchell, NZSA Chair.

Australian Council of Superannuation Investors (ACSI)
ACSI's CEO encouraged Boards to use discretion to review all remuneration outcomes in the coming months, taking into account the appropriateness of any payment in light of the experiences of their investors, staff, customers and the broader community.

Australian Securities & Investments Commission (ASIC)
ASIC sees robust governance arrangements as critical to support effective and informed Board decision making, appropriate to companies' changing circumstances. Decisions need to avoid being overly influenced by the views of interested executives and must include consideration of the company's stakeholders.

Prudential Regulation Authority (PRA) UK
Have requested that the seven largest UK banks and building societies do not pay cash bonuses to senior staff and material risk takers and also suspend dividends to be made in and for 2020.

How can PwC assist?

- Providing data on market movement trends and forecasts.
- Reviewing proposed FY20 STI payment/FY21 STI target setting approach in the context of the overall remuneration strategy and market precedent/practice.
- Working through proposed LTI grant options and the implications of alternate approaches.
- Providing guidance on how to articulate in what circumstances discretion will be applied by the Board.

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