Managing through the COVID-19 crisis: Adopting responsible Executive Compensation strategy

COVID-19 is first and foremost a human crisis. As a result, in the current economic downturn, organisations are increasingly being asked to effectively manage human capital risks and support discussions with shareholders.

This crisis is proving to be one of the most defining leadership moments for top executives, as organisations strive to stay true to their purpose, values, principles and culture, while continuing to deliver the best possible outcomes for all stakeholders.

At times like this, organisations must reflect upon their current executive pay programmes to review their effectiveness to:

- Create alignment with organisation goals
- Clarify objectives and establishing priorities
- Align rewards strategy in line with changed organisational strategy
- Define accountability and motivate performance

Business-driven, principles-led decision making is required for making compensation decisions in response to COVID-19. Key things to consider include:

1. **Ensure consistency and fairness**: In terms of their rewards actions in response to COVID-19 crisis, it is important for organisations to be consistent and fair from bottom to top. If the wider business actions have had a negative impact on employees, more favourable reward actions for executives will attract scrutiny from investors and other stakeholders.

2. **Adapt the reward interventions to the industry:** Companies facing great degrees of distress are considering or have taken actions to reduce/defer executive salaries. It is anticipated that this trend will increase as organisations finalise their annual reports and make decisions on their executive pay programmes for the next year. Industries which are significantly impacted by the COVID-19 crisis, such as Aviation, Hospitality, Travel & Tourism and Automotive, had to take some tough decisions such as executive pay cuts, bonus pay deferrals and cancellation of salary increases etc. In other moderately impacted sectors such as Media, FMCG, Energy, Construction & Engineering, Retail & eCommerce etc., a mix of cost saving measures have been adopted by organisations.

3. **Take a long-term perspective**: There is a large, significantly negative impact anticipated by more than 46% of Indian organisations on their business in the coming 12 months. This has led to about 59% of the organisations to consider deferral or reduction in their executive salary increase budgets, and more than 68% of the organisations have adopted cost control measures such as temporary hiring and promotion freeze. Any such tough reward programme decisions are driven from the top, starting from executive compensation programmes.

4. **Consider shareholder experience and expectations:** As variable pay forms a significant part of executive compensation, this crisis is expected to negatively impact executive variable compensation payouts for 2020, at a much higher level than the rest of the organisation. Making any positive adjustments to such variable payout calculations should be in line with the experience of shareholders (dividend payouts) and other stakeholders such as rest of the employees. While some of the organisations have contemplated the decision of adjusting their annual bonus payout plan, majority (68%) of the organisations are not changing their annual bonus plans for calculating payouts for their executives. Additionally, 78% of the organisations which offer performance based LTI awards are not considering any changes to the performance

goals or metrics for their 2020 vesting of such awards.

Guiding principles for Remuneration Committees – a roadmap

Although this crisis is unprecedented, it is recommended to not lose sight of the long-standing executive compensation principles (alignment, attract, retain, incent, hold accountable) as they continue to be relevant.

The key guiding principles for Remuneration Committees towards 'Restoring Stability' in the area of Executive compensation programmes:

- Engage proactively and effectively with shareholders, proxy advisors, employees and public (reporting frameworks to monitor and track key human capital measures, e.g., employee health)
- Model business performance scenarios (including key human capital and ESG measures) to assess current compensation and governance programmes (interim/ongoing) to align with performance outlook
- Assess short-term and long-term incentive goals and performance metrics in the context of economic conditions and business performance. Balance affordability of compensation programmes relative to profitability, cash flow, and share price
- Communicate and implement human capital management metrics into incentive plans and/or governance oversight; review oversight and management of ESG elements with Board/ Management
- Develop a retention programme for critical talent, as well as special award programmes for essential workers
- Modify pay rates for jobs that may have changed (e.g. cyber security, business continuity);
- Update reward strategy and/or programmes considering changes in organisation and workforce strategy
- Evaluate solutions to address underwater stock options as needed; promote employee and management stock ownership plans, as an alternative to deferring cash payments

Finally, we do acknowledge that aligning executive pay programmes with the new and changing business strategy is a journey, and each company will have a different way to address these issues over time.

Also, we see a need for Boards to maintain their strategic and oversight, and work with their management teams to ask the right questions and to develop ways to monitor progress as the businesses move forward.

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