CHRO PRACTICE GUIDE

The CHRO's Guide to Compensation Committee Chair and Director Onboarding

Best Practices for Selecting, Transitioning, Onboarding, and Educating Compensation Committee Chairs and Board Directors

HRPA
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CENTER ON EXECUTIVE COMPENSATION

AS THE COMPENSATION COMMITTEE CHAIR ROLE BECOMES increasingly complex and public-facing, the selection of an incoming chair as well as onboarding and ongoing education for both the chair and other board directors are critically important. An onboarding program that is well thought out and executed will increase the odds that a new chair or director will be able to make meaningful contributions to the organization sooner rather than later.

Although historically this process has been primarily the purview of the Lead Director and the General Counsel or Corporate Secretary, CHROs are finding that their deep knowledge of their company and industry and their skills and expertise with regard to talent, compensation, and company culture are highly prized by new directors. Given the increased focus on board governance by investors, proxy advisors and other stakeholders, many CHROs have found themselves intimately involved in the director onboarding and education process.

GUIDE CONTENTS

The CHRO's Guide to Compensation Committee Chair Onboarding is based on interviews conducted by the Center On Executive Compensation of 18 Compensation Committee Chairs, CHROs, and Heads of Total Rewards from large companies across multiple sectors regarding their experiences with director onboarding. Although the guide is targeted at newer CHROs or those who have not experienced many Compensation Committee Chair successions, we hope it will also be useful to experienced CHROs as a "checklist" for current practice and some ideas for how to make succession and onboarding even more effective.

We have provided the prevailing practices based on our interviews, plus a number of trend-forward or "cutting-edge" practices.

In the following pages we provide a summary of the chief learnings from our interviews in the form of a list of best practices for how to effectively select, transition, onboard and educate Compensation Committee Chairs and board directors. As we learned during the interview process, companies differ greatly in the formality and style of their director succession and onboarding programs. Throughout the document, we have provided the prevailing practices based on our interviews, plus a number of trend-forward or "cutting-edge" practices that may not have hit the mainstream, but that work well for the companies using them.

INDIVIDUALS INTERVIEWED INCLUDE:

COMPENSATION COMMITTEE CHAIRS

Robert A. Eckert *Compensation and Management Development Committee Chair; Amgen Inc. / Human Resources Committee Chair; Levi Strauss & Co.*

Richard P. Lavin *Compensation and Organization Committee Chair; USG Corporation / Compensation and Personnel Chair; ITT Inc.*

Richard H. Lenny *Compensation Committee Chair; Illinois Tool Works Inc.*

John "Jack" T. Mollen *Leadership and Compensation Committee Chair; Alexion Pharmaceuticals, Inc.*

Nancy A. Reardon *Compensation Committee Chair; Big Lots Stores, Inc.*

Patricia F. Russo *Compensation Committee Chair; General Motors Company*

Laurie A. Siegel *Human Resources and Compensation Committee Chair, CenturyLink, Inc. / Compensation and Talent Committee Chair; FactSet Research Systems Inc. / Compensation Committee Chair; Volt Information Sciences, Inc.*

Kimberly K. Underhill *Compensation Committee Chair, Foot Locker, Inc.*

CHIEF HUMAN RESOURCE OFFICERS

Marcia J. Avedon *Compensation Committee Chair; GCP Applied Technologies Inc. / Senior Vice President, Human Resources, Communications and Corporate Affairs; Ingersoll-Rand plc*

Dennis G. Berger *Executive Vice President and Chief Human Resources Officer; AutoNation, Inc.*

Lisa G. Bisaccia *Executive Vice President and Chief Human Resources Officer; CVS Health*

Brian J. Cook *Executive Vice President and Chief Administrative Officer; USG Corporation*

Julie G. Duffy *Executive Vice President, Human Resources; Textron Inc.*

Tracy Keogh *Chief Human Resources Officer; HP Inc.*

Mara Swan *Executive Vice President, Global Strategy and Talent; ManpowerGroup*

HEADS OF TOTAL REWARDS

David Kasiarz *Executive Vice President, Global Total Rewards & Medical; American Express Company*

Jeffrey Kridler *Corporate Vice President, Total Rewards; United Technologies Corporation*

Janice K. Uhlig *Vice President, Global Compensation & Benefits, Human Resources; General Motors Company*

COMPENSATION COMMITTEE CHAIR SELECTION AND SUCCESSION

Almost all companies we interviewed noted that the Nominating and Governance Committee took the lead in recruiting and selecting new directors and committee chairs, while the ultimate decisions were made by the full board. In addition, the CEO, CHRO, and Corporate Secretary are typically involved in the process as well.

SELECTION CRITERIA FOR COMPENSATION COMMITTEE CHAIR Nearly all companies reported that the preferred candidate for Compensation Committee Chair is a current member of the Compensation Committee who has previously been a CEO. Indeed, according to Spencer Stuart, 52% of S&P 500 Compensation Committee Chairs are active or retired CEOs, board chairs, presidents, and COOs[1].

> **52%**
> of S&P 500 Compensation Committee Chairs are active or retired CEOs, board chairs, presidents and COOs

Companies explained that sitting or retired CEOs "understand what it's like to be a CEO," are "accustomed to making tough decisions," and "understand the

[1] Spencer Stuart 2017 U.S. Board Index, https://www.spencerstuart.com/research-and-insight/ssbi-2017

importance of connecting the business and rewards strategies."

In addition, companies look for directors with strong communication and people skills, since so much of the chair's role involves understanding how compensation both motivates and serves as a tool of communication with executives. Compensation Committee Chairs engage frequently with shareholders and require a deep understanding of how company pay reflects performance relative to peers and the ability to communicate this effectively to investors.

> ***CUTTING-EDGE PRACTICE:*** Although current practice suggests that relatively few Compensation Committee Chairs have **CHRO experience**, based on the interviews conducted with those that did, the combination of strong business acumen and extensive experience leading compensation and governance programs resulted in a significant ability to quickly move up the learning curve as a new chair. In addition, as one director noted, **"The #1 job of the board is to hire the right CEO.** Having directors with a good nose for talent is incredibly valuable." Another chair added, "as more CHROs and Chief Administrative Officers become directors, they will bring deep compensation knowledge and an understanding of motivation and culture to the role."

SUCCESSION PROCESS The majority of companies we interviewed did not have a formal process for Compensation Committee Chair succession, nor did they have a policy imposing term limits for chairs. This is not unusual, as only about 5% of S&P 500 boards set term limits for directors.[2] However, a few companies described a formal succession process in which the Nominating and Governance Committee works with the CEO, CHRO and sitting Compensation Committee Chair to identify the succession candidate six months to a year in advance.

> "The **#1** job of the board is to hire the right CEO"

Once a succession candidate is identified, the process of transitioning from the outgoing to the incoming chair can take place. Companies and chairs differed in their opinions on the appropriate timeline for this. One company has a formal hand-off process over a longer period of time, in which the outgoing and incoming chairs jointly establish the agenda for the two committee meetings preceding the change of chairs, and the incoming chair runs the final meeting with the outgoing chair in attendance to provide a smooth transition. Other companies warned that if the transition period is too long, it runs the risk of making things awkward for the incoming chair, so this should be considered in the context of the company culture and the particular succession in question. Either way, it is important to have a clear understanding of how the "off-boarding" of the outgoing chair will work to avoid potential conflict.

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[2] Spencer Stuart 2017 U.S. Board Index, https://www.spencerstuart.com/research-and-insight/ssbi-2017

Cutting-Edge Practice: Consider a **periodic formal or informal review of committee assignments** led by the Nominating and Governance Committee with an eye toward refreshing or rotating them where appropriate (*e.g.*, every 5 years).

Cutting-Edge Practice: **Determine the next compensation committee chair 6-12 months ahead of time** to allow proper planning and a smooth transition, including formal education of the incoming chair.

Cutting-Edge Practice: If appropriate for your company's culture, **consider a transition period of six months where the outgoing chair gradually transitions responsibilities to the incoming chair** and provides guidance and background where needed.

COMPENSATION COMMITTEE CHAIR ONBOARDING

All the companies we interviewed agreed that a thorough, tailored onboarding process for new Compensation Committee Chairs is critical to the success of both the chair and the committee.

Content of Onboarding

Typically, companies provide an expansive library of reading material along with a half or full-day session that includes meeting with key members of management individually (CEO, CFO, General Counsel, CHRO and Business Unit Heads). The CHRO, often joined by the Head of Total Rewards, will provide orientation on the following topics with the company's most recent proxy as a critical component of the information received, depending on the scope of the committee's responsibilities. Note that if the new Compensation Committee Chair is also a new director, his or her onboarding will need to include the items listed under "Onboarding of New Directors" below:

- Compensation Committee charter, calendar and responsibilities
- Role of the independent compensation consultant
- Shareholder proposals and Say on Pay votes
- Chair's preferences for protocols regarding reviewing agendas and content, preparing for board report-outs, and pre and post-meeting reviews
- Proxy advisory firm policies and shareholder perspectives
- Executive Compensation Program
  - Peer group
  - Plan design
  - Perquisites
  - Key policies (stock ownership, clawbacks, tax gross-ups, etc.)
- Employment contracts and restrictive covenants
- Director compensation
- Health and welfare, retirement and non-qualified plans
- Talent review

In addition to meeting with the CHRO, incoming chairs typically also meet with the rest of the C-suite to gain a better understanding of how each executive views the business and the effectiveness of the compensation plans. These meetings are key, but should be carefully prepared for with pre-reads and communication with the incoming chair regarding his or her desired level of information. In the words of one CHRO, "Trouble comes when there are mismatched expectations of how much information is appropriate and when it should be received. A full reading list is important to avoid surprises later, but don't succumb to information overload, either."

CUTTING-EDGE PRACTICE:
Incorporate input from the **compensation consultant, other members of the committee and members of the management team** specifically on **areas for improvement** within governance, compensation plan design and any other area of committee responsibility.

CUTTING-EDGE PRACTICE:
Design compensation plan reviews to include a **retrospective review of compensation plans and payouts over a three- to five-year period** (including payouts vs. key performance indicators) as well as a **forecast of the next one to two years** of payouts and performance.

COMPENSATION CONSULTANT

Many companies we interviewed stated that the arrival of the incoming Compensation Committee Chair was an opportunity to review the services and fit of the independent compensation consultant, whether or not this led to a formal Request for Proposal process. Given the critical role played by the compensation consultant in advising the chair and the committee and tracking emerging issues, a periodic performance evaluation and market review is an emerging best practice.

An orientation session with the outside consultant can provide the new chair with critical insights regarding past practices and any points of tension with management or board members regarding compensation. In addition, the CHRO and the new chair should discuss the board's preference for interactions with the consultant. Some boards require a total separation with management hiring their own firm for incentive plan design work, while others encourage the use of their own firm to eliminate "dueling" consultants. Either way, the discussion should include agreement on ground rules for access, project work and billings.

ONGOING ORIENTATION: Given the depth and breadth of information covered in the orientation for a new Compensation Committee Chair, it is common to find that the orientation may extend past the initial meetings (often through at least one full annual cycle) where the CHRO, Head of Total Rewards or other members of management make themselves available on a more informal basis to support the new chair.

ONBOARDING OF NEW BOARD DIRECTORS

Our interviews also included a discussion of the onboarding process for new directors in general, both from the perspective of the director and the perspective of the CHRO or Head of Total Rewards.

DIRECTOR ONBOARDING SESSION
Most companies have developed a formal process for new director onboarding which is led by the General Counsel or Corporate Secretary and the Lead Director, typically including the following:

- Review of industry trends and competitors
- Company financial and operating goals and results
- Major shareholder perspectives and engagement
- Executive talent and rewards
- Regulatory and legislative environment
- Essentials of corporate governance
- A review of director pay and benefit plans

In addition to a session with the General Counsel, some companies described a more extensive two-day seminar with the CEO and CEO's direct reports in which the issues above were covered in more detail and involved the relevant members of the company leadership team.

> ***CUTTING-EDGE PRACTICE:***
> If possible, schedule the orientation sessions ahead of the new director's first board meeting.

> ***CUTTING-EDGE PRACTICE:***
> Have new directors attend **investor calls** as well as the annual "Investor Day."

BUILDING RELATIONSHIPS The directors we interviewed expressed a strong appreciation for one-on-one meetings with members of the executive committee other than the CEO, meetings with other directors, and exposure to top talent below the C-suite level as well as meeting employees during site visits. Directors noted that these meetings were the most valuable to them because they were unscripted and provided a close-up look at various operations within the business, in addition to company culture.

It is not an uncommon practice for new directors to spend time with the leaders of each major business unit to get a "deep dive" into the businesses in which the company competes. One director noted that she makes it a point to spend time with group heads in addition to top executives:

"I say, 'Tell me about your business. How long have you been running it? What progress have you made? What keeps you up at night? Who are your competitors?'"

Two companies described "Board Buddy" programs they administer – one pairs board directors with high-potential executives, while another pairs new directors with more experienced directors to help them acclimate to the board. Another company reported that when any director comes to town, they are scheduled for a lunch with 5-8 high potentials for an open-ended discussion.

CUTTING-EDGE PRACTICE: Assign new directors a "buddy" in the form of a **more experienced director to provide coaching** and feedback. Almost every director we spoke to said this was valuable to them, especially with regard to providing **history and context to agenda items** or other aspects of the company's briefing materials. As one director noted, "It's extremely helpful to understand the context around specific items; how that decision came to be made, whether there was pushback, what the conversation was and who the main players were."

CUTTING-EDGE PRACTICE: Consider pairing directors with **high-potential executives** below the C-suite level. As one director put it, "It's a great opportunity to visit sites and experience the business without the CEO. Talk about the executive's strategy and leadership; learn about his or her business." However, other directors cautioned that a program like this could place an **undue burden on management**, and should only be pursued if the directors state that they value in it.

CUTTING-EDGE PRACTICE: Separately from the "buddy" initiative described above, have new directors **accompany the CEO on site visits** to manufacturing facilities, call centers, or meetings with key customers. One company asks all directors to spend at least one day deeply engaged in some element of the business such as a **product launch meeting, manufacturing site, research initiative, or diversity program**.

EXTERNAL OPPORTUNITIES FOR EDUCATION Although most companies were happy to pay for any outside training or education that individual directors requested, a small number of companies stated that they proactively send new directors (particularly those who have never served on a public board) to corporate governance seminars at company expense. Interestingly, one company even paid for sitting executives to attend corporate governance training to make them better board members, since an executive board member's performance reflects on the company at which they are an executive as well as the company on whose board they serve.

CUTTING-EDGE PRACTICE: Offer directors access to company-paid external seminars such as:

- Harvard Business School: "Making Corporate Boards More Effective" program
- Stanford Graduate School of Business: Directors' Consortium
- NACD: Director Professionalism foundation course

- Northwestern's Kellogg School of Management: Corporate Governance Program

ONGOING BOARD EDUCATION AND FEEDBACK

Although the majority of companies reported they do not have a formal ongoing education or director feedback program other than the typical annual survey, almost all directors said it would have been helpful for them.

One company does an annual two-hour "refresh" of company compensation and benefit plans without reference to payouts, inviting Legal, Finance and HR to prepare and present a series of materials, plus a full session on talent with the CEO and CHRO. Directors noted that meetings that focus only on plan design and market trends, without the distraction of having to make pay decisions, are very useful and provide context for later meetings where pay decisions are necessary.

With regard to ongoing feedback, a Compensation Committee Chair described an effective process in which he schedules annual face to face visits with each committee member to discuss their performance and that of other members of the committee (and offers to share specific, anonymous feedback with other directors if desired). This builds relationships between him and the rest of the committee while providing each director with individual feedback at the same time.

CUTTING-EDGE PRACTICE: Consider scheduling **follow-ups with each new director six months to a year after his or her first meeting** to fill any gaps in knowledge or information and ensure the transition is running smoothly.

CUTTING-EDGE PRACTICE: Encourage the lead director or committee chairs to conduct **annual feedback sessions with individual directors** in addition to the typical annual self-evaluation survey.

CUTTING-EDGE PRACTICE: Seek out opportunities where the **full board is apprised of developments/ challenges in both talent and rewards**, such as dedicating time for this review as a formal agenda item at least once per year.

FURTHER READING

- EY Center for Board Matters, "Improving Board Performance Through Effective Evaluation," October 2018.
- PwC and Cleary Gottlieb, "Serving On – And Chairing – the Compensation Committee," July 2018.
- Russell Reynolds, "Enhancing Director Performance and Impact," July 2018.
- Spencer Stuart, "New Director Onboarding: 5 Recommendations for Enhancing Your Program," September 2018.

Appendix One: Sample Orientation Meeting Table of Contents

During the course of our interviews for the preparation of this Guide, we received several examples of orientation agendas for one-on-one meetings between the CHRO/Head of Rewards and a new Compensation Committee Chair or board member. The following sample Table of Contents is based on the various examples we received, erring on the side of more rather than fewer items, thus allowing members to modify the template to suit their needs.

COMPENSATION COMMITTEE – NEW MEMBER ORIENTATION AGENDA

I. Company Overview

a. Corporate Structure
b. Business Model
c. Company Culture
d. Impact on Talent and Compensation Strategy

II. Compensation Committee Overview

a. Committee Members and Charter
b. Role of Independent Consultant
c. Role of Management
d. Compensation Committee Calendar
e. Annual Compensation Committee Core Agenda
f. Timing and Approach to Committee Materials

III. Section 16B Officers

IV. Deep Dive on Key Compensation Committee Responsibilities

a. Administer Executive Pay Plans
b. Assist Board of Directors in Risk Management Oversight
c. Monitor Investor and Proxy Advisor Views of Executive Pay
d. Approve Incentive Design and Performance Against Pre-established Goals
e. Approve Compensation, Discussion and Analysis (CD&A) for Proxy Statement

V. Historical Review of Executive Compensation

a. Executive Compensation Philosophy
b. Market Comparators (Peers)
c. Summary of Plan Design Changes
d. Historical Payouts
e. Proxy Advisory Firm and Shareholder Feedback
f. Historical Concerns/Issues

VI. Senior Management Team Compensation Design and Payouts

a. Base Pay
b. Annual Incentive Plan (Targets and Payouts)
c. Long Term Incentive Plan (Targets, Grants and Payouts)
d. Executive Perks
e. Employment/Change-in-Control Agreements
f. Total Wealth Analysis (Tally Sheets, etc.)
g. Stock Ownership & Guidelines
h. Restrictive Covenants
i. Recoupment Policies
j. Summary of Health & Welfare Plans
k. Retirement and Nonqualified Plans

VII. Director Compensation

VIII. Talent Review

a. Succession Planning
b. Leadership Development
c. Diversity and Pay Fairness
d. Engagement Survey Results
e. Practices & Programs

Appendix Two: Questions for the Compensation Committee Chair

The following set of questions is designed to help the CHRO or Head of Rewards get the most out of meeting with a new Compensation Committee Chair. The questions are based on the experiences of Center Subscribers and have been used in real-life situations to ensure alignment of expectations and make the transition for a new chair as smooth as possible.

We suggest that where asking the Compensation Committee Chair about changes they'd like to make, you first set the context by summarizing the current state of affairs. For example, for question #1 below, it would be effective to begin by reviewing the topics currently included in the committee charter before moving on to desired changes.

Committee Charter and Calendar

1. Are there any topics you wish to add or delete from the committee charter (e.g., talent review)?

2. Is there anything you would like to see changed on the committee calendar? At which meeting would you prefer to finalize the calendar for the year?

Pre-Meetings

3. Should pre-meetings be face-to-face or via phone?

4. Which individuals should be included in the pre-meetings in addition to the Compensation Committee Chair and CHRO?

5. How far in advance of the meeting should our pre-meeting be scheduled?

Meetings

6. When we have significant recommendations for the committee, how many meetings do you prefer we dedicate to discussing them?

7. Are you comfortable scheduling additional committee meetings if we need one off-cycle?

8. Which members of management should attend committee meetings in addition to the CHRO and Corporate Secretary? Should the CEO always attend?

9. How far in advance of each meeting would you like us to send out the materials?

10. If there are questions from the committee members on the materials sent in advance, how do you prefer we respond?

11. How do you prefer to assign responsibilities for presenting the committee materials at meetings?

12. Do you wish to have executive sessions scheduled for every committee meeting, even if there is no particular agenda item under review?

13. We will provide an executive summary of each committee meeting for you to use for your "report-out" to the full board. Can you give us an idea of how much detail you would like the summary to include?

Committee Responsibilities

14. How do you prefer to handle development of the CEO pay recommendation? What level of involvement do you want from the CHRO?

15. What is your philosophy on the influence that proxy advisory firms should have over our program design and delivery?

16. What role do you envision playing on shareholder outreach, should it be requested?

17. What are your thoughts on director education specific to those serving on the Compensation Committee?

Compensation Consultant

18. What is the appropriate protocol for management to work with the committee's compensation consultant?

19. How important is it for the compensation consultant to attend every meeting, either in person or via phone?

20. How should we proceed if there is a disagreement between the committee's compensation consultant and management?