Willis Towers Watson

Executive Compensation Bulletin

New analysis reveals moderate increases in *Fortune* 500 outside director pay

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Total pay for nonemployee directors at the largest U.S. companies grew moderately over the last year, driven by increases to elements of both cash and stock compensation. As we saw over the past several years, there continues to be a push toward a fixed approach to director pay components, which enables companies to provide manageable incremental pay adjustments.

To identify trends in 2016 director compensation, Willis Towers Watson's Executive Compensation Resources team analyzed director pay data disclosed in the most recent proxy statements for 250 *Fortune* 500 companies and compared those results to data the same companies reported in 2015. (For our previous annual analysis of director pay trends in the *Fortune* 500, see "Equity-based pay continues to push increases in outside director pay," *Executive Compensation Bulletin,* August 27, 2015.) Following are some of the highlights.

Primary pay components

The median value of total direct compensation for nonemployee directors in our sample increased 3% over the previous year. A typical director in this group now makes $263,500, up from $254,750 in the previous year. The average mix of pay remained at 43% cash and 57% equity, while the total cash and total equity figures increased 6% and 3% at the median, respectively. Thirty-six percent of companies in this sample made a change to one or more core elements of their cash or stock pay program for outside directors, on par with what we typically see in the *Fortune* 500 group each year.

A fifth of the companies studied increased their annual cash retainer, resulting in a 9% increase at the median over the previous year. The median value of these increases was $10,000. The prevalence of variable elements of cash pay continued to shift in opposite directions. Committee attendance fee usage fell from 22% to 18%, while 27% of companies now provide flat retainer-based pay for committee service, up from a quarter of this sample in the prior year. There has also been a slight uptick in the number of companies that no longer provide incremental pay for committee service in favor of a larger base annual cash retainer. Forty-two percent of the companies in our sample provided a base annual retainer as the sole form of cash compensation, up from 40% last year.

Twenty-nine percent of companies disclosed an increase in the annual stock grant portion of their director pay program. Nearly four out of five companies (79%) that made an adjustment to the core pay program included an increase to the annual stock grant. Full-value shares remained the dominant vehicle for delivering stock compensation, with 97% of companies granting one or more types of these shares, up from 95% last year. Meanwhile, stock option usage continued to decline, dropping from 10% a year ago to 8% this year. Ninety percent of all stock grants in this sample were made using a fixed-dollar approach, up from 89% in the prior year.

Figure 1 provides an overview of the change in the median value of all elements of director pay this past year.

Figure 1. Median outside director compensation*[1]

	2014	2015	% change
Sales ($ millions)	$15,874	$14,967	-6%
CASH			
Board cash retainer	$92,000	$100,000	9%
Board meeting fee	$2,000	$2,000	No change
Committee cash retainer	$10,000	$10,000	No change
Committee meeting fee	$1,750	$1,800	3%
Committee chair extra retainer	$15,000	$15,000	0%
Annual Cash Compensation[2]	**$102,500**	**$108,250**	**6%**
ANNUAL/RECURRING STOCK			
Expected Value:			
Common stock	$132,505	$146,251	10%
Deferred stock and phantom stock	$140,000	$148,789	6%
Restricted stock	$135,066	$141,335	5%
Full-value stock[3a]	$139,968	$147,549	5%
Stock options	$79,296	$69,652	-12%
Annual/Recurring Stock Compensation [3,4]	**$145,000**	**$150,000**	**3%**
Total Direct Compensation[5]	**$256,784**	**$263,491**	**3%**
ONE-TIME STOCK	$138,330	$125,000	-10%
One-time stock grants annualized[6]	$17,291	$15,625	-10%
Total Compensation (with one-time stock)	**$258,631**	**$265,748**	**3%**

**See footnotes at end.*

Figure 2 provides an overview of the range of value of all elements of director pay this past year, in addition to the prevalence of these elements.

Figure 2. Outside director compensation — percentile values*[1]

	25th	Median	75th	Average	Prevalence
Board cash retainer	$75,000	$100,000	$110,000	$93,583	97%
Board meeting fee	$1,500	$2,000	$2,000	$1,983	13%
Committee cash retainer	$7,500	$10,000	$12,000	$9,912	27%
Committee meeting fee	$1,500	$1,800	$2,000	$1,858	18%
Committee chair extra retainer	$10,000	$15,000	$20,000	$14,764	93%
Annual Cash Compensation[2]	**$92,000**	**$108,250**	**$120,500**	**$105,851**	**98%**
ANNUAL/RECURRING STOCK					
Expected Value:					
Common stock	$125,003	$146,251	$174,995	$146,252	14%
Deferred stock and phantom stock	$125,000	$148,789	$168,750	$148,574	25%
Restricted stock	$114,925	$141,335	$175,002	$149,563	60%
Full-value stock[3a]	$122,125	$147,549	$174,997	$151,317	97%
Stock options	$49,797	$69,652	$99,996	$80,317	8%
Annual/Recurring Stock Compensation [3,4]	**$125,000**	**$150,000**	**$175,748**	**$157,304**	**97%**
Total Direct Compensation[5]	**$233,850**	**$263,491**	**$296,626**	**$263,639**	**100%**
ONE-TIME STOCK	$91,370	$125,000	$207,745	$156,935	11%
One-time stock grants annualized[6]	$11,421	$15,625	$25,968	$19,617	11%
Total Compensation (with one-time stock)	**$234,965**	**$265,748**	**$297,627**	**$265,758**	**100%**

**See footnotes at end.*

Board leadership trends

Forty-two percent of the companies in our sample separate the positions of board chairman and chief executive officer, up from 40% in the prior year. Of these stand-alone board chairs, 71% (or 30% of the entire sample) serve in a nonexecutive role, down from 73% (29% of the entire sample) last year. Conversely, the prevalence of companies identifying a lead or presiding director increased from 69% to 71% of the entire sample.

Eighty-six percent of the companies that have a lead director provided an additional fee for such service, up from 83% in the previous year. Early findings show an incremental lead director fee of $30,000 at the median, reflecting a 20% increase. Almost one-fifth (19%) of companies in our sample with an existing lead director fee in place made an increase in that additional fee, the median value of which was $10,000. What's more, 7% of companies that identified a lead director also established an extra fee this year, the median value of which was $30,000. Of the companies in this group that were already providing an additional fee to a nonexecutive board chair, 16% disclosed an increase. However, the fee level for this role did not change significantly at the median.

Stock ownership and retention

Stock ownership and retention mandates remain a fixture of director compensation programs, as 93% of the companies in our sample have one or both requirements in place. Eighty-one percent of stock ownership guidelines are based on a multiple of the board retainer, and two-thirds of those are set at a multiple of five.

The number of companies imposing a requirement that directors retain all or a portion of their stock grants increased slightly, rising from 40% to 41% in the past year. For companies with this mandate in place, 46% require stock to be held until ownership guidelines are met, while 47% stipulate that stock be held until cessation of service from the board. All other companies with a stock retention policy require equity to be held for a specified length of time during the board member's term of service.

Other trends in director pay

In view of the recent shareholder litigation alleging "excessive" compensation of directors, companies have made a concerted effort in the last couple of years to adopt "meaningful" annual limits on awards specific to directors. For example, 42% of the companies in our sample currently have a director-specific award limit in place, with half of these limits having been adopted or amended since 2015.

These annual award ceilings are not necessarily limited to stock-based awards. Fifteen percent of companies that have imposed an annual award limit (6% of the entire sample) have included cash or total compensation as part of the limit. (For recent trends in this area among the full *Fortune* 500, see **"Annual limits for director stock awards gaining steam,"** *Executive Pay Matters,* March 28, 2016.)

Footnotes

1 The sample consisted of 250 publicly owned companies in the *Fortune* 500 that filed their fiscal year 2016 proxy statements by May 15, 2016.

2 Annual cash compensation is calculated as follows:

a. Values reported for fees earned or paid in cash in the Director Summary Compensation Table are identified for each director.

b. Directors who did not serve the entire fiscal year, as well as directors in leadership positions receiving supplemental compensation (e.g., board chair, lead director) and chairs of the three primary committees (audit, compensation and nominating/governance) are removed.

c. The median value is identified for the remaining directors to determine the total cash compensation for "typical" directorial duties.

d. The value of the retainer is eliminated from the total cash compensation for the "typical" director to determine the value, if any, of total variable cash fees.

e. Annual cash compensation is the combined value of the annual cash retainer and the median value of variable cash fees.

3 Stock compensation is determined using ASC 718 values reported in company proxy statements.

a. Full-value stock represents the combined value of all full-value grants, regardless of the form of the award.

4 All board/committee meeting fees and retainers that are paid in stock are included under annual/recurring stock compensation.

5 Total direct compensation includes annual cash compensation plus annual/recurring stock compensation.

6 One-time stock includes initial and discretionary stock-based grants. The values reflect the incremental additional value above that of the annual grant. One-time stock grants are annualized over eight years, based on the average term of an outside director as disclosed in the NACD's *Director Compensation Report*.

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