Executive pay adaptations in a transforming tech sector

Executive compensation, board compensation, and equity usage trends in 2024 filings

Introduction

- Grant Thornton has collected executive compensation, board of director compensation, and share usage statistics from recent proxy and 10-K filings for companies in the Russell 2000 Index. Compensation and financial details are generally current for companies’ 2023 fiscal year.
- The following slides provide an industry specific view of Russell 2000 companies in the 4510 Global Industry Classification Standard (GICS) Software and Services code. There are approximately 80 companies in our sample.
- The table below details the 25th, 50th, and 75th percentiles of revenue and market capitalizations for companies in our sample:

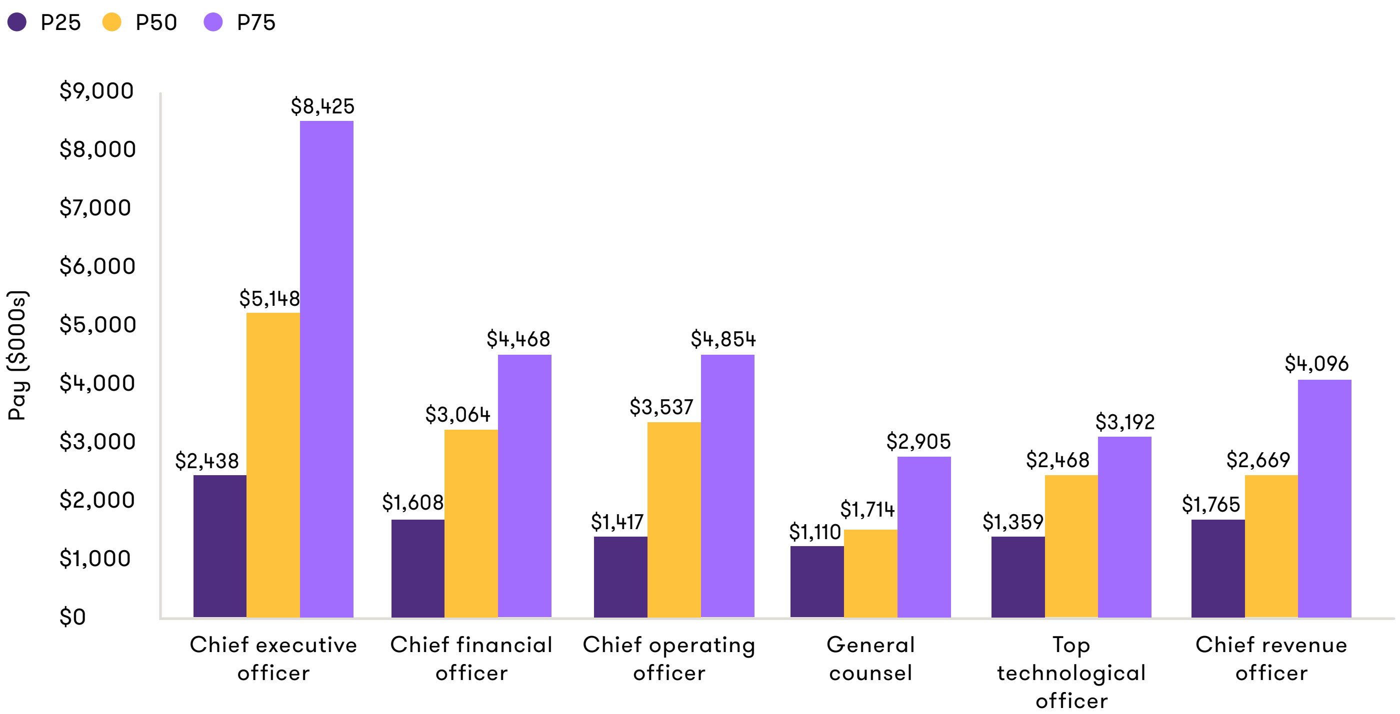
Measure	25th percentile	50th percentile	75th percentile
Revenue	$212M	$389M	$623M
Market cap	$513M	$1,877M	$3,312M

Summary trends and observations

- CEO pay decreased for the second straight year. There are several factors contributing to the change, including:
  - For many of the companies included in the sample, share prices decreased by roughly 30% between the beginning of 2021 to the beginning of 2023 (i.e., when pay decisions were being made). This broader decline in stock prices contributed to lower compensation levels as a means of aligning pay and performance.
  - 2021 and 2022 were outlier years, with 2023 representing a return to normal. For many companies, 2021 and 2022 were the first two fiscal years after the primary business shocks of the COVID-19 pandemic in 2020. Many compensation committees approved executive pay increases during these years to recognize the extraordinary efforts of returning business to normal. Pay levels in 2023 likely provide a better representation of "true" compensation levels as any elevated pay levels or strategies from post-COVID years fall to the wayside.
- Equity vehicle usage had noticeable changes between 2021 and 2023. RSUs increased in prevalence, moving from 76% to 82% after a slight dip in 2022. performance-based RSUs also increased significantly, moving from 28% in 2021 to 44% in 2023. Options, conversely, decreased by 3%. Going into 2024, we expect performance-based RSUs to continue their wider adoption as companies (i) engage with proxy advisors and institutional shareholders, (ii) tighten the alignment between their compensation and business strategies, and (iii) look for the ability to deliver outsized payouts for above market performance.

Summary TDC — All NEOs (named executive officers)

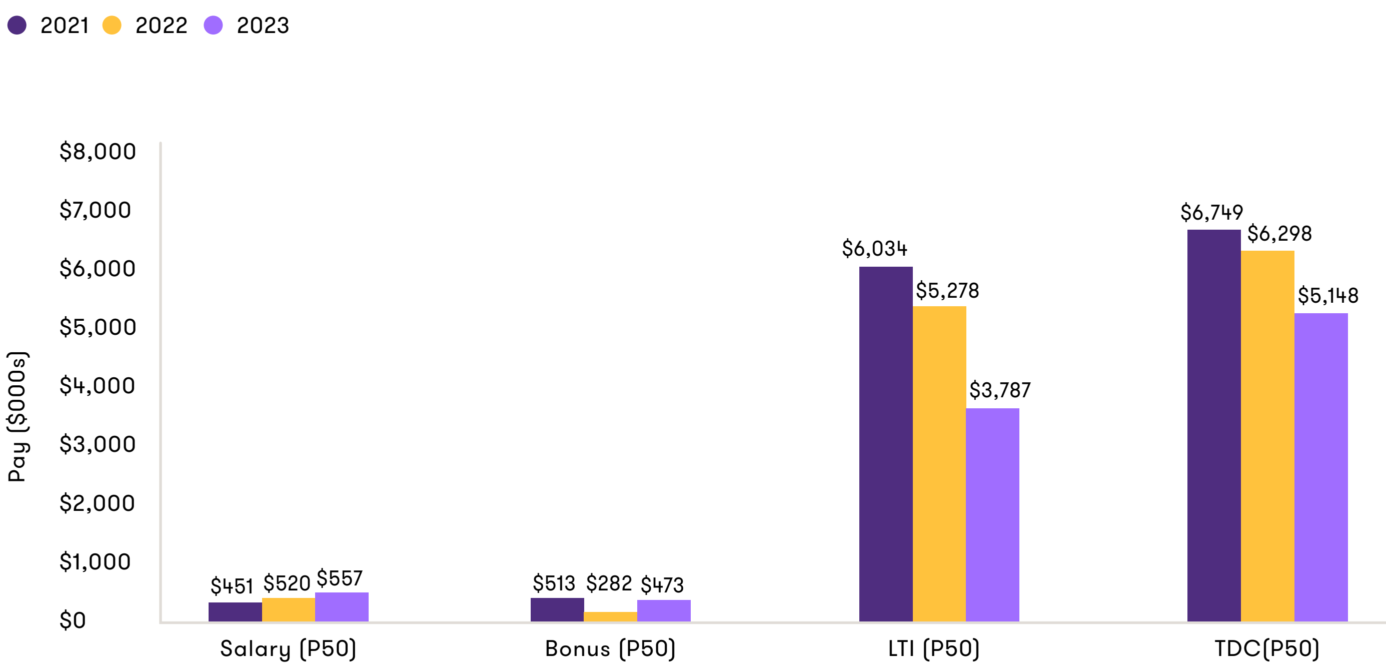
2023 total direct compensation



- The chart above details total direct compensation (TDC), which is inclusive of salaries, annual bonuses, and long-term incentives (LTI). We have reported compensation for the six most common named executive officer (NEO) roles in the Software and Services sector.

CEO pay — 2021 to 2023

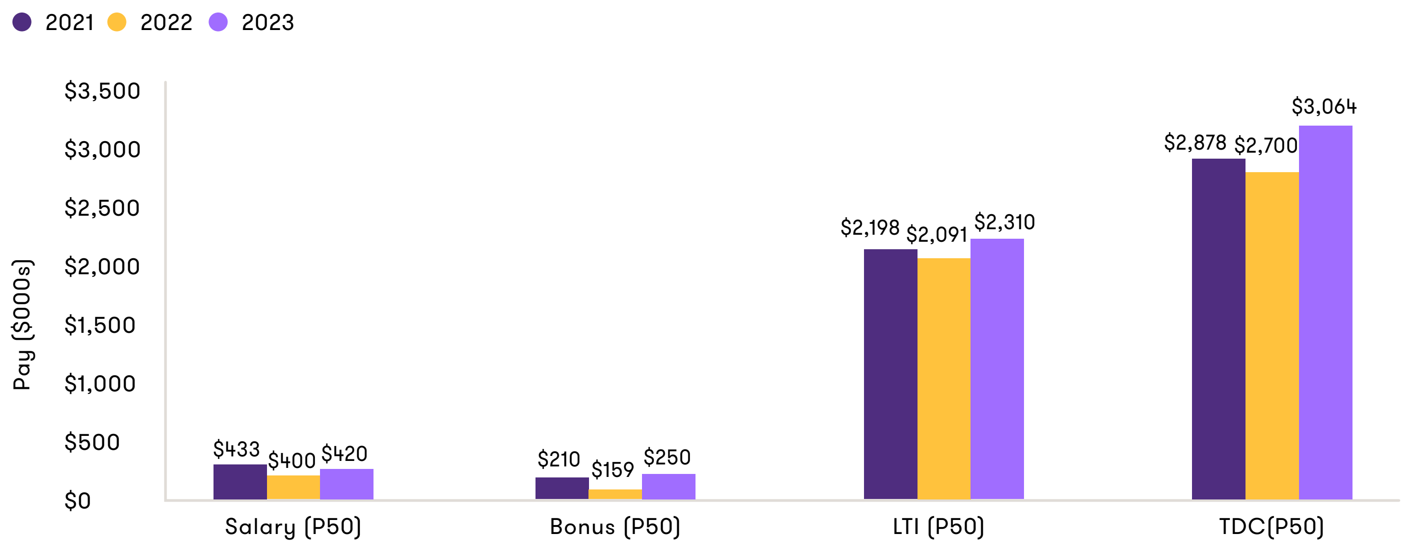
Median CEO compensation 2021-2023



- The chart above details CEO TDC from the Russell 2000 Software & Services sector over the last three years.
- Salaries increased by 7% between 2022 and 2023. Annual bonuses increased by 68%, but this is likely attributable to the sector returning to more normal levels after a sharp drop between 2021 and 2022.
- Long-term incentives have significantly decreased the last few years with a drop of 28% between 2022 and 2023. The resulting TDC decreased by 18% between 2022 and 2023 and decreased by 7% between 2022 and 2021.

CFO pay — 2021 to 2023

Median CFO compensation 2021–2023

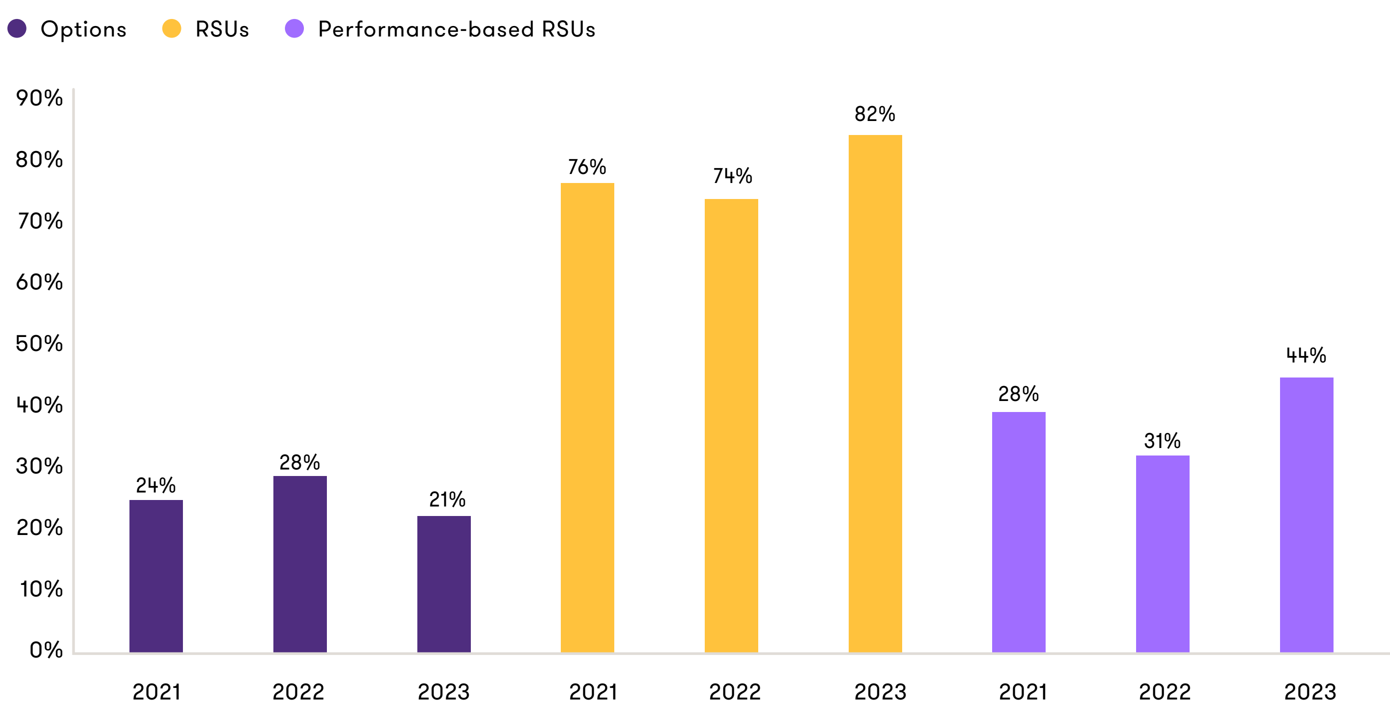


- The chart above details CFO TDC from the Russell 2000 Software and Services sector over the last three years.
- Salaries increased by 5% between 2022 and 2023. Annual bonuses increased by 57%, but this is likely attributable to the sector returning to more normal levels after a sharp drop between 2021 and 2022.
- LTI increased by 10% in 2023 after falling between 2021 and 2022. The resulting median TDC increased by 13% between 2022 and 2023.

Equity vehicle prevalence

- RSUs are the most prevalent vehicle in the Software and Services sector, with usage at 82% of companies.
- Performance-based RSUs are also commonly used with a 44% prevalence.
- Stock options in the Software & Services sector continue to decrease in prevalence and are now used at only 21% of companies in our sample.
- There were fairly sizable changes in vehicle prevalence between 2021 and 2023:
  - Options decreased by 3%, reflecting a move away from appreciation only vehicles.
  - RSUs increased by 6%, reflecting a preference for a more consistent and guaranteed form of compensation.
  - Performance-based RSUs increased by 16%, which likely acknowledges proxy advisors' and institutional shareholders' preference for performance-based compensation.

Equity Vehicle Prevalence



Board compensation

- The table to the right lists summary statistics for each element of director pay.
- There is a tight alignment across the 25th, 50th, and 75th percentiles of each pay element.
- The largest variance is amongst board chair and lead independent director retainers. Responsibilities for each of these leadership roles is highly variable and based on a company's governance design and the director's own experience, leading to a larger variation in competitive practices.
- Roughly 75% of companies in our sample provide committee member retainers, which is lower than general industry practices.
- Lastly, RSUs are a nearly universal practice for annual equity retainers. Only two companies granted options, and in both instances, they awarded a combination of options and RSUs.

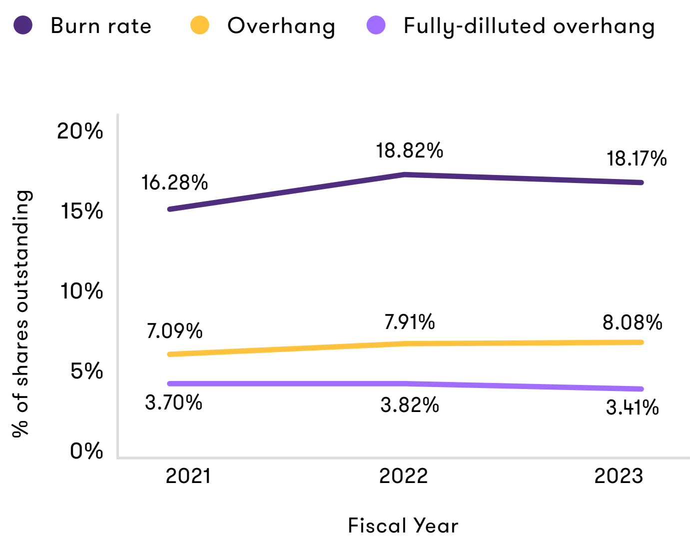
Director compensation summary statistics

Program elements		Prevalance	P25	P50	P75
Board retainers	Cash	99%	$35,000	$40,000	$60,000
	Option Award	2%	$105,938	$120,625	$135,313
	RSU Award	94%	$150,000	$175,000	$200,000
	Equity Total	94%	$150,000	$180,000	$200,000
Leadership retainers	Board Chair	55%	$22,500	$43,000	$70,000
	Lead director	33%	$15,000	$19,500	$30,000
Comittee Chair and Member Retainers	Audit Chair	90%	$20,000	$20,000	$20,000
	Audit Member	77%	$10,000	$10,000	$10,000
	Comp Chair	85%	$13,500	$15,000	$18,000
	Comp Member	76%	&6,000	$7,500	$8,000
	Nom & Gov Chair	81%	$8,000	&10,000	$10,000
	Nom & Gov Member	74%	$4,000	$4,000	$5,000
Average total director compensation		-	**$214,979**	**$242,250**	**$273,125**

Company-wide equity dilution

- The chart and table to the right illustrate three common measures of equity dilution.
- In general, burn rate represents the proportion of shares granted each year. Overhang represents the proportion of shares that are outstanding at the end of the year, and fully diluted overhang is the proportion of shares outstanding and shares that have been reserved for future issuance.
- The median values for each measure were generally consistent between 2022 and 2023:
  - Burn rate decreased by 41 basis points
  - Overhang was nearly flat, with a slight increase of 17 basis points
  - Fully diluted overhang decreased by 65 basis points

Equity usage and dilution measures



Measure	Calculations
Burn Rate	Options granted+ Restricted stock granted / Weighted avg. common shares outstanding
Overhang	Options outstanding+ Restricted stock outstanding / Common shares outstanding at fiscal year end
Fully diluted overhang	Options outst.+ Rest. stock outst.+ Shares reserved / Common shares outstanding at fiscal year end

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