Customize Your Long Term Incentive Plans to Attract and Reward Top Talent

by Scott Cahill and Linda Parker

"Deferral Account Measurement. When measured as phantom stock, each award is deposited into a nonqualified 409A account. The dollar award is divided by the current share price of the company stock. Each year, after the company valuation, the share price of the Phantom units is marked to the current share price. This ownership of Phantom equity in a 409A plan is economically tantamount to holding actual shares in a tax-deferred account. The mandatory deferral (hold period) has wide latitude and design.

Deferral can also be measured in mutual funds, similar to the way a 401(k) is handled. During the hold period, participants manage the investment allocation of their LTIP balance in much the same way as they manage their 401(k), until a distribution year or event occurs"

For executives seeking a place in the c-suite, the vacation ownership industry can be extremely attractive. However, for timeshare and resort companies, University of Central Florida Rosen College of Hospitality Management Assistant Professor, Amy Gregory, Ph.D., RRP, points to indicators that suggest competition for top talent in the timeshare sector will get even tougher in the years ahead.

"Research," said Amy, "continually shows that compensation and benefits are key attractors and retainers for employees at all levels of organizations across a wide spectrum of industries. It is critical that the timeshare industry understands current trends and offerings in compensation in order to effectively compete in the ongoing bid for talent.

"The relatively low penetration rate of qualified consumers that are timeshare prospects, as well as the evolution of the timeshare industry to a more flexible vacation product, signal strong future growth for the segment. This growth will continue to require strong talent that is committed to the industry and interested in its success. That success typically yields benefits in terms of bonuses, profit sharing and salaries that are historically among the highest in the greater hospitality industry."

As attractive as bonuses and higher salaries are, they may lack strategic differentiators to help protect the interests of the company and of the executive. On the surface, two benefits packages can seem highly comparable. Without professional guidance to evaluate the flexibility and usability of the plans and the long-and short-term tax implications for both the company and the executive, the plans may only be adequate in an environment where exemplary plans are essential for competitive positioning.

The following five components offer guidelines for establishing a long-term incentive plan (LTIP) for top executives:

1. **Determine the business drivers that will trigger awards.** For private companies, drivers may include

Return on Equity. Once annual pre-tax returns exceed a predetermined yield on shareholder equity (hurdle rate), then a portion of this "excess" is shared. Typical hurdle rates are in the 12-20 percent range, depending upon the capital requirements of the business.

PTI/EBITDA/EBIT. Regardless of the term used to describe it, profit determines this measurement. The hurdle is set in advance and is usually a fixed target or percentage of increase year over year.

Company Performance vs. Outside Index. An outside index can be the measurement for determining success of company performance. The index may be narrowly defined, such as a self-compiled comparator group of peer public companies, or broadly defined, including indices such as the S&P.

Economic Value Added or EVA is a measure of how large an increase in value is attributable to management. While typically complicated to develop and challenging to explain, the logic behind this method is sound even though the mechanics may not have readily identifiable lines of measurement.

2. **Determine the level(s) of executives eligible to participate.** Often, the LTIP starts at the top one or two

levels within a company. Assuming the LTIP is a successful method for driving desired performance, over time, it may cascade by a few levels at lesser bonus opportunities.

3. **Determine share rates.** Assuming the company meets the minimum threshold to trigger an award, the company must determine what share rate will create the award pool. Step 4 (below) creates the target awards for the group; this information is helpful in modeling the pool's share rate.

4. **Allocation of award within eligible group.** Companies choose methods of allocation that are consistent with each participant's responsibilities and contributions, meaning that the allocation criteria for CEO, COO and CFO may differ, depending upon the focus a company desires from the executive. The award amount may be determined as a multiple of the executive's base salary.

Examples

POSITION	THRESHOLD	TARGET	MAXIMUM
CEO	50%	125%	200%
COO	50%	75%	100%
CFO	50%	75%	100%

(These samples represent an average of how companies determine the amount of award; however, each company is unique.)

5. **Award Distribution.** In order to accomplish typical LTIP purposes of "retain and reward," a company may choose mandatory **award deferrals** and **unique vesting** to align with its corporate objectives.

Examples

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Deferral can also be measured in **mutual funds,** similar to the way a 401(k) is handled. During the hold period, participants manage the investment allocation of their LTIP balance in much the same way as they manage their 401(k), until a distribution year or event occurs

A **fixed credit rate** is another way of measuring deferral. Often the rate is tied to the company's cost to borrow some bond index or other fixed crediting reference.

Typically, **automatic deferral periods** (mandatory) are a minimum of three years to a maximum of retirement, with multi-year payout at retirement. Many companies use a mix of timings for deferral periods. For example, fifty percent of annual award is deferred for three years, with the individual option to re-defer, and fifty percent of annual award is deferred to retirement.

Vesting and deferral periods do not have to coincide. Frequently, a three-year rolling cliff, vesting on each award, is a good plan with super vesting in the event of death, disability, retirement (age determined by company) and other pre-established circumstances.

This summary is broad and non-specific regarding the unique features to consider in building a competitive private company Long Term Incentive Compensation Plan. Although the five steps outlined do not provide a specific plan, they should motivate executives, compensation committees, CFOs and human resource executives to seek the guidance of a professional executive benefits consultant to assist in driving desired performance and remaining competitive for the top talent in vacation ownership.

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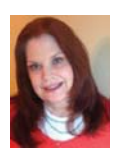

Linda Parker has been writing professionally since the 1980s. With clients in finance, sports, technology, change enablement, resorts and nonprofit global initiatives, Linda helps organizations communicate their stories in meaningful ways to the people they most want to reach. She has authored, ghostwritten or contributed to more than a dozen nonfiction books. Linda is a member of the Authors Guild and the Golf Writers Association of America. You can connect with her on Facebook at: www.facebook.com/GlindaCreative

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