

What You are Likely to Hear in the Boardroom

Key Developments Facing Compensation Committees for the 2025-2026 Cycle

LANE RINGLEE AND STEVE DEMARIA

Takeaways

Our firm's partners and consulting staff have participated in more than 250 board compensation committee meetings in the first half of 2025. Through these engagements and internal firm collaboration, we have identified several key issues gaining prominence in boardroom discussions. These key developments, in no particular order, include:

1. *Enhanced Executive Security*
2. *Potential Impact of Tariffs on Incentive Plans*
3. *One Big Beautiful Bill Act – Proposed Impact on Executive Pay*
4. *Navigating Shifting Pressures on ESG and DEI Goals*
5. *Balancing Pay Decisions in Challenging Sectors*
6. *Incentive Plan Alternatives Amid Uncertainty*
7. *Heightened Scrutiny on Goal-Setting Practices*
8. *Alignment of Incentive Plan Payouts and TSR*
9. *Long-Term Incentive Vehicle Mix*
10. *Diverging Say-on-Pay Perspectives: Institutional Investors vs. Proxy Advisors*
11. *Shareholder Outreach Challenges*
12. *Talent Retention and Succession Planning*

Introduction

In the first half of 2025, Pay Governance partners and consulting staff have participated in more than 250 meetings with the compensation committees of corporate boards of directors. These engagements and interactions with key stakeholders in the executive pay arena provide us with a unique vantage point into the evolving landscape of executive compensation and corporate governance.

We regularly convene as a firm to exchange perspectives on the trends shaping the industry, the challenges our clients face, institutional investor perceptions, and the key issues emerging in boardroom discussions. These discussions help us gain a collective, comprehensive understanding of the current priorities and concerns of compensation committees.

This Viewpoint is intended to share our perspectives on the key developments we anticipate will be focal points for board compensation committees during the 2025-2026 meeting cycle. The section below highlights these anticipated trends, accompanied by our insights into how they may influence executive pay practices in the coming year.

Key Developments

The topics are not presented in any order of prominence. Each represents a significant development we expect to emerge in compensation committee discussions and priorities will likely be unique to each company.

1. **Enhanced Executive Security**

Following the fatal shooting of UnitedHealthcare CEO Brian Thompson in December 2024, executive security has become a heightened priority for many organizations. Discussions around executive security benefits are now more frequent in compensation committee and board meetings. These benefits typically include home security systems, personal protection security, secure transportation arrangements (*i.e.*, drivers and personal use of company aircraft), and enhanced protection at company meetings involving leadership. Program enhancements made in 2025 will be disclosed in 2026 proxy filings.

2. **Potential Impact of Tariffs on Incentive Plans**

The design and execution of 2025 incentive plans have been complicated by the uncertain impact of tariffs, which can vary significantly across companies and industries depending on supply chain structures, among other things. Many boards that finalized their budgets in early Q1 have adopted a range of strategies to account for the potential impact of tariffs.

Common approaches include:

- a) Planning for year-end adjustments to account for actual tariff impact
- b) Incorporating a “best estimate” of tariff effects into goal-setting
- c) Establishing wider performance ranges to accommodate uncertainty
- d) Delaying goal-setting until more information becomes available
- e) Maintaining a shadow schedule to monitor parallel performance metrics.

When tariff-related adjustments materially impact incentive plan payouts, companies should clearly articulate the rationale behind these changes and disclose any adjustments/exclusions. Companies may also expect increased scrutiny, particularly if incentive outcomes appear misaligned with the shareholder experience.

3. **One Big Beautiful Bill Act – Proposed Impact on Executive Pay**

The 2021 American Rescue Plan Act (ARPA) modified the definition of covered employee under Section 162(m) to include the next five highest-paid employees in addition to the original list (CEO, CFO, and next three highest-paid), effective for tax years beginning after December 31, 2026. The proposed One Big Beautiful Bill Act includes a provision to aggregate compensation paid to a specific employee across a controlled group, thus treating entities as a single employer for this purpose (which already applies for employee benefit purposes). The proposal would apply for tax years beginning after December 31, 2025.

For tax-exempt organizations, the Act also expands the definition of covered employee for purposes of applying the Section 4960 excise tax to include any current or former employee with compensation above \$1 million, not just the five highest-paid employees.

4. Navigating Shifting Pressures on ESG and DEI Goals

Amid shifting political and regulatory pressures, many companies are re-evaluating their approach to and disclosure of ESG and DEI initiatives. While these goals were actively promoted under the previous administration, the current environment has prompted some organizations to soften publicly disclosed language, delay the rollout of new programs, or reframe existing initiatives under broader business strategy or talent objectives. In some cases, companies are maintaining core commitments but reducing prominence in disclosures, incentive plans, or charters to avoid drawing scrutiny. This repositioning reflects a careful effort to balance evolving external trends with internal priorities and long-term reputational considerations.

5. Balancing Pay Decisions in Challenging Sectors

In sectors experiencing prolonged downturns—such as biotech and renewable energy—compensation committees are challenged with how to reward and retain critical talent (including executives) amid multi-year stock declines that have significantly reduced realizable pay. Companies must carefully balance the tension in executing their pay programs within the broader context of turnaround efforts and evolving business strategies. A key priority is to maintain transparent and compelling shareholder communications—through proxy disclosures, shareholder letters, and active engagement—while upholding strong governance standards around executive compensation. Achieving this balance is essential in turnaround situations, where credibility and consistency are critical to maintaining investor confidence.

6. Incentive Plan Alternatives Amid Uncertainty

Companies operating in uncertain environments or challenging sectors often face significant difficulty in setting reliable incentive plan goals. When incentive awards fail to deliver payouts, particularly in situations involving uncontrollable external forces, it can undermine momentum, morale, and retention. To address this, organizations may consider adopting less traditional, more flexible approaches to incentive design.

Possible design considerations include:

- a) Exercising judgement/discretion
- b) Increasing the weighting of MBOs (individual and/or corporate) or incorporating other non-financial metrics
- c) Widening performance ranges to better accommodate uncertainty and volatility
- d) Splitting annual incentive plans (AIPs) into two six-month performance periods with aggregate payout at the end of the year
- e) Structuring performance share units (PSUs) as three discrete one-year performance periods with aggregate payout at the end of three years (and combining with a three-year relative TSR modifier to preserve long-term alignment)
- f) Using long-vesting restricted stock units (RSUs) or stock options to avoid the complexities of goal-setting altogether.

For any such change, clear disclosure and proactive shareholder engagement are critical to building trust and demonstrating continued alignment between incentive design, business strategy, and shareholder value.

7. Heightened Scrutiny on Goal-Setting Practices

Proxy advisors are placing increased emphasis on the alignment between incentive plan goals and company performance. Specifically, the large proxy advisors (*i.e.*, ISS and Glass Lewis) are scrutinizing situations where annual or long-term incentive (LTI) goals are set below prior-year targets or actual outcomes. Without a strong and well-communicated rationale—such as a major strategic shift, macroeconomic disruption, or turnaround context—goal “reductions” may be viewed as misaligned with shareholder interests. Companies that make such adjustments should be prepared to clearly explain their reasoning in proxy disclosures to mitigate potential investor and proxy advisor concerns.

8. Alignment of Incentive Plan Payouts and TSR

Some stakeholders have expressed concern that incentive plan goals may lack sufficient rigor, potentially resulting in elevated payout levels. However, a recent Pay Governance study found that actual incentive payouts are generally aligned with shareholder outcomes—a dynamic that may help explain the consistently strong shareholder support for Say on Pay (SOP). By implementing a disciplined goal-setting process, companies can improve the alignment between payouts, operating performance, and shareholder experience, while also reinforcing motivation and retention. (See Viewpoint [*“Are Executive Incentive Plan Payouts for AIP and PSUs Aligned with Shareholder Returns?”*](#) April 23, 2025.)

9. Long-Term Incentive Vehicle Mix

As companies continue to evaluate the effectiveness of their LTI programs and alignment of metrics with strategy, the mix of vehicles utilized is coming under renewed scrutiny. Among S&P 500 CEOs, the current LTI mix is ~60% PSUs, ~25% RSUs, and ~15% stock options.

While PSUs remain the dominant vehicle, they have drawn increasing criticism from proxy advisors, particularly around the use of non-GAAP adjustments and the potential resulting misalignment between pay and performance. Proxy advisor perspectives have also started to differ on the use of PSUs and RSUs with lengthier vesting schedules (our firm’s upcoming Viewpoint on institutional investor perspectives will address some of these issues). Stock options, though often categorized as non-performance-based by proxy advisors, still appeal to many boards and investors due to their direct link to shareholder value through stock price appreciation.

As perspectives of proxy advisors and institutional investors evolve and potentially become more differentiated, it will be increasingly difficult to design LTI programs to conciliate all external stakeholders.

10. Diverging Say-on-Pay Perspectives: Institutional Investors vs. Proxy Advisors

SOP support from large institutional investors has remained consistently strong in recent years. However, recent data reveal a decline in alignment between institutional investors and proxy advisors on SOP voting outcomes. This suggests that institutional investors may be placing less reliance on proxy advisor guidance and increasingly forming independent judgments on executive compensation matters. It may also highlight an emerging shift in how executive pay practices are evaluated and signal a broader rebalancing of influence in shaping SOP results.

11. Shareholder Outreach Challenges

Recent SEC guidance has added new complexity to shareholder engagement by cautioning that certain forms of outreach, particularly those perceived as influencing control over corporate strategy, may trigger more burdensome filing requirements for investors. As a result, some institutional investors have become more hesitant to ask direct questions or engage deeply on sensitive topics such as executive compensation. In this environment, many companies continue to adopt a more proactive approach to outreach, anticipating the concerns and informational needs of major shareholders, even when those concerns are not explicitly raised.

One increasingly important communication tool is a letter from the compensation committee chair included in the proxy CD&A, which enables companies to clearly articulate pay decisions, governance principles, alignment with strategy, and responsiveness to shareholder feedback in a transparent and structured format.

12. Talent Retention and Succession Planning

These areas have become increasingly central to compensation committee charters, particularly during this period of record executive turnover. Executive transitions can be disruptive and expensive, with average CEO transition costs among S&P 500 companies exceeding \$10 million. More effective succession planning supported by effective compensation decisions can help minimize these costs while also reducing the uncertainty and volatility that often accompany leadership changes.

Many committees are addressing succession planning throughout the year, rather than limiting it to annual reviews, to ensure a strong pipeline of internal candidates. One ongoing challenge is managing pay increases for internal promotions, where compensation must balance market competitiveness, internal equity, and performance justification. Similarly, many are reviewing and, in some cases, increasing the formalization of board-approved emergency succession plans.

Closing Remarks

As the 2025-2026 cycle brings heightened complexity across a range of executive compensation and governance issues, open communication and proactive planning are essential. At Pay Governance, we encourage clients to foster constructive, transparent dialogue—within compensation committees, across the full board, involving management, and with key external stakeholders, including shareholders, institutional investors, and proxy advisors. We believe that thoughtful engagement and disciplined governance foster the trust and flexibility needed to effectively navigate this dynamic environment.

General questions about this Viewpoint can be directed to Lane Ringlee (lane.ringlee@paygovernance.com) or Steve DeMaria (stephen.demaria@paygovernance.com).