TODAY’S SPEAKERS

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<table>
<thead>
<tr>
<th>TABLE OF CONTENTS</th>
</tr>
</thead>
<tbody>
<tr>
<td>• Participant Profile</td>
</tr>
<tr>
<td>• Planned Changes to Compensation Programs</td>
</tr>
<tr>
<td>• The Changing Employee Value Proposition in Financial Services</td>
</tr>
<tr>
<td>• Advances in Building A Sound Risk Culture</td>
</tr>
<tr>
<td>• Experiences With Applying Malus And Clawback Conditions</td>
</tr>
<tr>
<td>• Performance Management in Financial Services</td>
</tr>
<tr>
<td>• The Way Forward</td>
</tr>
<tr>
<td>• Q&amp;A</td>
</tr>
</tbody>
</table>
PARTICIPANT PROFILE

68 ORGANIZATIONS ACROSS 20 COUNTRIES

BY INDUSTRY

- Banks: 50%
- Insurance: 28%
- Investment / Asset Management: 13%
- Other Financial Services: 9%

BY REGION

- Europe: 47%
- North America: 32%
- Growth Markets: 21%
PLANNED CHANGES TO COMPENSATION PROGRAMS
Most organizations who have role-based allowances are not planning to make changes to them:

- Nearly three-quarters of banks are using role-based allowances but only 6% are making changes by moving role-based allowances into base salary, and the remaining banks are not making any changes.
- None of the organizations are planning to eliminate role-based allowances at this point.
- Most insurance organizations (63%) do not have role-based allowances in place.

![Chart showing planned changes to role-based allowances by region and industry]
EFFECT OF MORE FIXED COMPENSATION ON ABILITY TO ATTRACT AND RETAIN TALENT, AND MOTIVATE

- The majority of organizations reported that fixed compensation had little to no impact on their ability to attract and retain talent (68%) whereas 22% of the organizations saw some or substantial positive impact:
  - Banks in particular have made changes to their pay mix and placed more emphasis on fixed compensation due to regulations over the past years.
  - 24% of the banks saw some or substantial positive impact and 18% saw some negative impact on their ability to attract and retain talent.
  - None of the organizations noted any substantial negative impact.

- The majority of organizations reported that more fixed compensation had little to no impact on their ability to motivate performance (67%):
  - 21% of the organizations saw some or substantial positive impact.
  - 25% of the banks saw some or substantial positive impact.
  - 19% of the banks saw some negative impact on their ability to motivate talent.
  - None of the organizations noted any substantial negative impact.
PLANNED CHANGES TO CORPORATE ANNUAL INCENTIVE DESIGN

The majority of organizations are not planning to make changes to their 2016 corporate annual incentive design. Most prevalent changes to corporate annual incentive design include:

- Increasing the link to conduct/compliance behaviors (37%).
- Increasing the individual differentiation in bonus distribution (28%).
- Increasing the link to performance ratings (24%).

Changes to annual incentive design vary significantly by region:

- North American organizations predict far less changes than organizations elsewhere.
- Increasing the use of risk-adjusted measures at business unit level (31%) and at individual level (28%) are significantly more prevalent in Europe than elsewhere.
- Increasing the link to conduct/compliance behaviors is the most prevalent change in both Europe (41%) and Growth Markets (57%).

Changes to annual incentive design in 2016 are more common in banks than other industries:

- More than half of the banks (56%) are increasing the link to conduct / compliance behaviors.
- 32% of banks are increasing the link to performance ratings and use of scorecard with both financial and non-financial criteria.
- 16% of insurance organizations are lowering the weight of financial performance measures, whereas only 3% of banks are considering the same.
PREVALENCE AND PLANNED CHANGES TO MANDATORY DEFERRAL

- 68% of organizations have mandatory deferral programs in place. Nearly all banks (88%), 67% of investment/asset management firms and approximately half of insurance firms have a mandatory deferral mechanism in place. Some organizations are planning to make changes to their mandatory deferral program design in 2016:
  - The most prevalent change is increasing focus on conduct and compliance (22%).
  - In Europe, increasing the mandatory deferral period (performance/vesting period) is more prevalent (32%), than elsewhere.
  - Increasing the focus on conduct and compliance and increasing the mandatory deferral period (performance/vesting period) are among the most cited changes to mandatory deferral design for banks (both 30%).

<table>
<thead>
<tr>
<th>Requirement</th>
<th>Increase</th>
<th>Decrease</th>
<th>No Change</th>
</tr>
</thead>
<tbody>
<tr>
<td>Focus on conduct and compliance</td>
<td>22%</td>
<td></td>
<td>78%</td>
</tr>
<tr>
<td>Mandatory deferral period (performance/vesting)</td>
<td>20%</td>
<td></td>
<td>80%</td>
</tr>
<tr>
<td>Weight of financial performance measures</td>
<td>13%</td>
<td>2%</td>
<td>85%</td>
</tr>
<tr>
<td>Weight of non-financial performance measures</td>
<td>13%</td>
<td></td>
<td>87%</td>
</tr>
<tr>
<td>Use of malus conditions (prior to vesting)</td>
<td>11%</td>
<td></td>
<td>89%</td>
</tr>
<tr>
<td>Use of clawback provisions (after vesting)</td>
<td>11%</td>
<td></td>
<td>89%</td>
</tr>
<tr>
<td>Eligibility for mandatory deferral</td>
<td>9%</td>
<td>4%</td>
<td>87%</td>
</tr>
<tr>
<td>Required mandatory deferred portion of bonus</td>
<td>9%</td>
<td>4%</td>
<td>87%</td>
</tr>
</tbody>
</table>
PREVALENCE AND PLANNED CHANGES TO FORWARD-LOOKING LONG-TERM INCENTIVES

- 62% have a forward-looking long term incentive program in place. These programs are more common in the insurance industry (84%) than banking (50%) and investment/asset management (33%). However, 9% of banks are planning to introduce one. More North American firms (73%) have forward-looking long-term incentive programs than in other regions.

- Although changes to forward-looking long-term incentive plans are not prevalent, 11% of organizations are planning to increase the rigor of performance conditions, additional required deferral period (after performance period), and target award levels.

- Increasing the additional required deferral period (after performance period) and rigor of performance conditions are more prevalent in Europe (19% and 14% respectively), whereas none of the North American organizations are planning to make these changes.

  - A few banks (16%) are decreasing eligibility for forward-looking long-term incentive.
The far majority of organizations are not planning to make changes to their vehicle mix of multi-year incentives in 2016.

- 10% of organizations are planning to increase the portion of performance shares.
THE CHANGING EMPLOYEE VALUE PROPOSITION IN FINANCIAL SERVICES
CHANGES TO EMPLOYEE VALUE PROPOSITION BEYOND PAY

- Financial services organizations are making or planning to make changes to their employee value proposition beyond pay:
  - Almost half of the organizations are increasing learning and development programs/education and work remotely programs (47% and 43% respectively).
  - Career frameworks, use of flexible work schedules, and use of non-monetary recognition programs are increased by more than one-third of the organizations (37%, 37% and 34% respectively).

Changes to employee value proposition beyond pay vary by region:
- Overall, more organizations in North America and Europe are projecting changes.
- More European organizations are increasing the use of non-monetary recognition programs, employee choice in benefits provided, and company's "noble purpose" communication than in North America.
- More North American organizations are increasing the use of (global) mobility programs than in Europe.
ADVANCES IN BUILDING A SOUND RISK CULTURE
More than half of the organizations are making the following steps to a great extent: penalizing misconduct and/or non-compliance (62%) and showing evidence of setting the right tone at top (60%), top management set and communicate clear (risk) culture objectives (58%), the right values and risk objectives are clearly articulated and reinforced by leadership action (54%), and introducing an annual review of adherence to risk and compliance criteria for all regulated staff (52%).
EXPERIENCES WITH APPLYING MALUS AND CLAWBACK CONDITIONS
APPLYING MALUS

- Over 90% of banks and 72% of insurance organizations have malus policies in place.
- Malus policies are mostly triggered by:
  - Individual misconduct (89%)
  - Individual breach in compliance (89%)
  - Negative business performance (financial) (74%)
  - Malus triggered by a restatement of company or business financial statements is more prevalent in North America (67%) than in Europe (37%).
  - Disciplinary case against individual and negative business performance (financial) are more common triggers in Europe (74% and 89% respectively) than in North America (50% and 56% respectively).

CONDITIONS TRIGGERING MALUS POLICY TO REDUCE AWARDS

- Individual misconduct: North America 94%, Europe 93%
- Individual breach in compliance: North America 89%, Europe 96%
- Negative business performance (financial): North America 56%, Europe 89%
- Disciplinary case against individual: North America 50%, Europe 74%
- Restatement of company or business financial statements: North America 37%, Europe 67%
- Firm-wide regulatory fines: North America 39%, Europe 37%
- Individual on performance improvement plan: North America 28%, Europe 26%
**APPLYING MALUS**

- Typically, amounts reduced under malus conditions are determined on a case-by-case basis (45%).
  - Prevalent practices in North America are to recuperate all outstanding unvested awards (42%) or determined on a case-by-case basis (42%).
- The majority of organizations (69%) do not retain individuals involved in malus cases.

### PART OF AWARDS REDUCED BY MALUS CONDITIONS

- **All outstanding unvested awards (multiple years)**: 42% (Europe) vs. 13% (North America)
- **Only awards that would vest that year**: 19% (Europe) vs. 13% (North America)
- **Depends case by case**: 42% (Europe) vs. 56% (North America)
- **None, no malus in place**: 16% (Europe) vs. 13% (North America)
### Applying Clawback

- North American (80%) and European (71%) firms tend to have a clawback policy in place.
  - Policies are also prevalent in the banking (76%) and insurance (65%) industries.

- Policy effectiveness differs across regions. 35% of European companies indicated that labor laws prevent an effective application compared to just 5% in North America and 7% in Growth Markets. The majority of North American firms (65%) find that their clawback policy works effectively, compared to just 23% of European organizations.
  - Differences in effectiveness between industries are small.

- In the rare instance a clawback policy was applied, nearly 90% of employees were not retained following the incident. This is common across all regions and industries.

#### Prevalance and Effectiveness of Clawback Policies

- Yes, the policy works effectively: **65%**
  - North America: 23%
  - Europe: 35%
- Yes, but labor laws prevent an effective application: 5%
  - North America: 10%
  - Europe: 13%
- Yes, but other challenges prevent an effective application: 10%
- No such policy in place: 20%
  - North America: 29%
  - Europe: 29%
MALUS & CLAWBACK CASES APPLIED

• Three-quarters of companies have not applied their malus policy in the past 2 years for company or business performance reasons
  – Banks have applied malus for company or business performance reasons more than insurance firms (39% vs. 18%).
  – 9% of banks have done so in 4 to 20 cases.
  – 6% of European organizations have had 21 or more cases of malus in the past two years, whereas none of the North American and Growth Market organizations have.

• 63% of companies have not applied their malus policy in the past 2 years for individual performance reasons or misconduct
  – Banks have applied malus for individual performance reasons more than insurance firms (52% vs. 29%).
  – 35% of banks have done so in 1 to 9 cases and 13% percent of banks have done so in 10 to 49 cases, compared to only 24% of insurance firms in 1 to 9 cases.
  – Europe had the most cases of malus policies being applied due to individual performance (59%), compared to just 15% in North America. Almost half of European firms (45%) applied malus due to individual performance in 1 to 9 cases only, and 13% in 10 cases or more.

• Over the past 2 years, clawback policies were rarely applied (10%), with little difference between industries and regions:
  – In cases where clawback policies were triggered, most instances were typically limited to 1 – 3 cases.
PERFORMANCE MANAGEMENT IN FINANCIAL SERVICES
**TENURE OF CURRENT PERFORMANCE MANAGEMENT PROCESSES**

- Many organizations (41%) have had their current performance management processes in place without making any key decision changes or revisions for 1-3 years, followed by 4-6 years in 24% of the organizations.

- Tenure of performance management processes is similar between regions, but differences by industry exist:
  - 22% of insurers indicated to have used their processes for 7 years or more, compared to only 3% of banks.
  - 30% of banks have made changes in the past 12 months compared to just 11% of insurers.
PLANNED CHANGES TO PERFORMANCE MANAGEMENT PROCESSES

• 46% of organizations across all industries indicate that they do not have key design changes or revisions planned for their performance management processes:
  – Half of all banks are planning to change their performance management processes in the next 12 months, compared to just 16% of insurers.
  – 32% of insurers want to change their processes but are unsure when.
  – 37% of European organizations are planning to change their performance management processes in the next 12 months with an additional 13% after one year compared to 28% and 5% of North American organizations.
PERCEIVED EFFECTIVENESS OF PERFORMANCE MANAGEMENT APPROACH

- Only a small portion of the participating organizations indicated that their performance management approach delivers exceptional value.
  - More than half of participants responded that the performance management approach works well. Reinforces a sound risk culture, involvement of Control Functions, linkage to compensation and use of performance rating scale were cited as most effective.

- There are differences in the perceived effectiveness of performance management approach across regions and industries.
  - 30% of North American organizations reported that the involvement of control functions delivers exceptional value compared to just 3% of European organizations.
  - Around half of the European and banking organizations indicated feedback process and linkage to development needs work compared to 40% and 30% in North America and 44% and 24% of insurers.

<table>
<thead>
<tr>
<th>Category</th>
<th>Needs work</th>
<th>Works well</th>
<th>Delivers exceptional value</th>
</tr>
</thead>
<tbody>
<tr>
<td>Reinforces a sound risk culture</td>
<td></td>
<td>11%</td>
<td></td>
</tr>
<tr>
<td>Involvement of Control Functions (e.g., Compliance, Risk Management)</td>
<td>14%</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Linkage to development</td>
<td>5%</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Linkage to compensation</td>
<td>9%</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Use of performance rating scale</td>
<td>8%</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Evaluation process</td>
<td>6%</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Feedback process</td>
<td>3%</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Setting expectations / Planning process</td>
<td>5%</td>
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PERFORMANCE MANAGEMENT APPROACH AND PROCESS COMPONENTS

The top 4 most cited components that are included in a company’s performance management approach are:

1. Individual goals (99%)
2. Formal year-end review discussions (96%)
3. Overall performance ratings (85%)
4. Link individual performance ratings and compensation decisions (85%)

European organizations are also planning for compliance and conduct review

The top 3 components that companies indicate they are planning to introduce are:

1. Competencies / behaviors (12%)
2. Frequent feedback throughout the year rather than only periodic performance review (12%)
3. 360-degree or multi-source feedback (10%)

European organizations are also planning for compliance and conduct review

The top 3 components that companies indicate they do not have:

1. Managers receiving a separate rating on "people management" (69% do not have this)
2. Grid rating of goal results and behaviors ("9-box") (60%)
3. Year-end feedback and compensation decision occurring in the same meetings (59%).

74% of banks indicated they do not have year-end feedback and compensation decision occur in the same meeting, which is more than 20% higher than the other industries

– North America and Growth Markets have the same top 4 most cited components
– European organizations have calibration of performance ratings as one of their top 4 most cited components
– A majority of banks (82%) indicated they have performance scorecard with financial and non-financial criteria
FUNCTIONS INVOLVED IN PERFORMANCE MANAGEMENT PROCESS

- Human Resources and Finance have significant involvement throughout the performance management process. The role of Risk Management is meaningful particularly in selecting performance measures, performance goal setting, and performance evaluation.
  - Across all four performance management processes, more banks have a major involvement of their Risk Management function compared to insurers.
  - More European organizations have major involvement of their Finance function in the performance evaluation and bonus determination process.
TOOLS AND PROCESSES USED FOR DIFFERENTIATING PERFORMANCE

• The predominant tool used for differentiating performance is guidelines regarding expected ratings distribution (69%)
  – Relative ranking of employees is more prevalent in North American and Growth Markets organizations (35% and 43%) than European (23%)
  – The use of "forced" distribution of ratings is limited to about one quarter of organizations across regions, however, more prevalent in the insurance industry (33%) than banking (25%), as is the relative ranking of employees (56% vs. 22%)

• Most firms use a 5 point rating system to determine employee performance rating

<table>
<thead>
<tr>
<th>Points on Performance Rating Scale</th>
<th>North America</th>
<th>Europe</th>
</tr>
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<tbody>
<tr>
<td>More than 5</td>
<td>16%</td>
<td></td>
</tr>
<tr>
<td>5</td>
<td>62%</td>
<td>56%</td>
</tr>
<tr>
<td>4</td>
<td>24%</td>
<td></td>
</tr>
<tr>
<td>3</td>
<td>9%</td>
<td></td>
</tr>
<tr>
<td>2</td>
<td>5%</td>
<td>6%</td>
</tr>
<tr>
<td>No rating scale is used</td>
<td>10%</td>
<td>13%</td>
</tr>
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</table>
TOOLS AND PROCESSES USED FOR DIFFERENTIATING PERFORMANCE

- The most prevalent processes used to differentiate employee performance levels are mandatory calibration meetings and next-level manager reviews (55%). Next-level manager reviews are more common in North America (70%), than in Europe (44%).
  - Mandatory calibration meetings (72%), next-level manager reviews (72%) and guided distribution (67%) are more prevalent in insurance organizations than banks (48%, 48%, and 36% respectively).

- Looking ahead, 74% of companies foresee continuing with their current performance rating system.
  - 20% of North American organizations are planning to move away from performance ratings and an additional 10% would like to but do not have an alternative yet.

DIFFERENTIATING BETWEEN PERFORMANCE LEVELS

<table>
<thead>
<tr>
<th>Method</th>
<th>Banking</th>
<th>Insurance</th>
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</thead>
<tbody>
<tr>
<td>Mandatory calibration meetings</td>
<td>48%</td>
<td>72%</td>
</tr>
<tr>
<td>Next-level manager review</td>
<td>48%</td>
<td>72%</td>
</tr>
<tr>
<td>Forced rankings</td>
<td>21%</td>
<td>22%</td>
</tr>
<tr>
<td>Guided distribution</td>
<td>36%</td>
<td>67%</td>
</tr>
<tr>
<td>Other</td>
<td>3%</td>
<td>6%</td>
</tr>
<tr>
<td>None of the above</td>
<td>15%</td>
<td></td>
</tr>
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</table>
Financial services organizations see lots of opportunities to improve critical skills of their people managers.

- **65% of North American organizations** are aiming to improve providing career development coaching and direction to employees.
- **60% of North American organizations** are linking individual performance to "actionable" development planning.
- **50% of European companies** would like to improve ensuring performance evaluations are "fair" and "equitable".
- **50% of European companies** are setting "SMART" goals.
- **44% of European companies** are gathering "meaningful" information on employee performance (e.g., multi-source feedback).

- **55% of banks** are focused on setting “SMART” goals, and ensuring performance evaluations are "fair" and "equitable" (52%) than insurers (39% and 39% respectively).
- **94% of insurers** are focused on having candid dialogue with their direct reports about their performance and providing career development coaching and direction to employees (67%) than banks (73% and 52% respectively).
THE WAY FORWARD
THE WAY FORWARD

• Compensation plan design change has continued in the financial services industry (e.g., creating increased fixed compensation for key risk-takers in the EU)

• Recent regulatory proposals in the US and the impact of the UK’s EU referendum vote will likely bring about more changes:
  – Inclusion of non-financial performance metrics in short and long-term incentives;
  – Limitations on maximum awards as a multiple of target;
  – Extended deferral and forfeiture/clawback requirements;
  – Potential changes to pay structures in the UK (a return to CRD III?)

• The emphasis on Employee Value Proposition in financial services is critical in the war for talent, particularly for millennials.

• Reinforcing the “right” behaviors and demonstrating a sound risk culture will be a focus and a challenge

• Performance management reform is a key lever to help manage toward desired culture change

• Efforts to achieve a sound risk culture, create an attractive environment for Talent, and meet shareholder requirements, have to go beyond compensation systems for meaningful change to become embedded

• These initiatives need to be driven by responsible leadership rather than additional regulation
QUESTIONS?
QUESTIONS?

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QUESTIONS

Please type your questions in the Q&A section of the toolbar and we will do our best to answer as many questions as we have time for.

To submit a question while in full screen mode, use the Q&A button, on the floating panel, on the top of your screen.

CLICK HERE TO ASK A QUESTION TO “ALL PANELISTS”