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# *Executive Compensation & Corporate Governance*

*2011 survey examining  
compensation structures  
in SMI and SMIM  
companies as well as  
SIX disclosure*



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# 1 The Survey

We are delighted to present the fifth edition of our survey “Executive Compensation & Corporate Governance”. The survey is one of the most comprehensive Swiss studies available on the level and structure of board and executive compensation for the years from 2007 to 2010. This report provides a comprehensive picture of executive compensation for SMI and SMIM companies in Switzerland today, and we hope you find this breadth of perspective helpful.

In the light of an increasing demand for transparency and disclosure we also analyse how well SMI and SMIM companies comply with the disclosure requirements of the Directive Corporate Governance. The SIX Exchange Regulation pays significant attention to these matters, and so should all listed companies.

All data used in this survey are based on disclosed compensation information in the annual reports of the companies reviewed. We have not made any assumptions or adjustments to the disclosed values and methodologies used, in particular with regard to variable compensation (valuation, vesting clauses, timing of disclosure and earning periods, etc.).

We trust you find the 2011 “Executive Compensation & Corporate Governance” survey to be an insightful and innovative read that supports you in answering key questions and provides ideas for addressing today’s reward challenges. As always, we welcome your feedback and hope to have the opportunity to discuss these issues with you.



Dr. Robert W. Kuipers  
Partner  
HRS Consulting



Remo Schmid  
Partner  
HRS Consulting

## 2 Executive Summary

Building on the results from the surveys of the last three years, the 2011 issue of “Executive Compensation & Corporate Governance” examines the changes from 2007 to 2010 in total compensation for boards of directors and CEOs. The key findings are:

- Looking at the median, the pay of chairmen in SMI companies has been relatively stable (from CHF 1.2 million in 2007 to around CHF 1.3 million in 2010), whereas it has increased in SMIM companies (from CHF 430,500 in 2007 to CHF 603,100 in 2010). Across SMI companies we have observed some divergence (except in the extremes of the pay scale), whereas the distribution of chairmen’s pay across SMIM companies has remained fairly constant over time.
- Compensation levels of SMIs and SMIMs for other board members have been stable or slightly increasing in a relatively small band over the years 2007 to 2010. The levels remain relatively low (median compensation: CHF 328,694 for SMI and CHF 172,555 for SMIM companies).
- For both SMI and SMIM companies, the average total CEO compensation decreased from 2009 to 2010. The average compensation 2010 amounted to CHF 7.2 million for SMI CEOs (–12.5% compared to 2009) and to CHF 2.8 million for SMIM CEOs (–6.5% compared to 2009). For both groups, the median total CEO compensation increased. The median SMI (SMIM) CEO earned CHF 7.5 million (CHF 2.5 million) in 2010. For average and median total compensation, however, it has not reached the levels of 2007. Also in both samples, the lower quartile increased and the upper quartile decreased from 2009 to 2010, resulting in a convergence within each sample. Overall, the asymmetry of the distribution of CEO pay has decreased – the average and the median are more similar in 2010 than in previous years in both samples.
- For CEOs, cash bonuses as a portion of total compensation have increased in importance from 2009 to 2010, while long-term incentive plans now make up a smaller portion of total compensation. In 2010, the average total compensation of an SMI (SMIM) CEO was split into a base salary of 24% (37%), a cash bonus of 24% (25%), long-term incentives of 41% (29%) and other compensation forms of 11% (9%).
- In 2010, the median CHF wealth change due to ownership was around zero or slightly positive for all chairmen, other board members and CEOs. The median CEO has not yet made up the loss from 2008 (CHF –900,000) despite gains in 2009 and 2010 (CHF +480,000 and CHF +230,000, respectively). Overall, our findings suggest that stock ownership helps align managers to the shareholders’ welfare.

In this survey, we also put a spotlight on SIX Exchange Regulation mandatory compensation disclosure requirements. Our review of compliance with these requirements suggests a mixed picture. In the sample of SMI and SMIM companies, overall disclosure quality has increased from 2009 to 2010, but there is significant variation in compliance, at least according to the strict standard of our scorecard.

Finally, as Swiss policymakers prepare to make decisions as regards the implementation of various “say-on-pay” proposals that have been put forward over the past few years, we recommend that companies and regulators carefully consider the benefits and costs of such proposals. It is striking that stock prices of Swiss public companies reacted negatively when it was announced that the “Abzocker-Initiative” had collected sufficient signatures to force a constitutional referendum. The average firm lost nearly 1.5% in market capitalisation over a three-day window around the announcement. Stock prices dropped in a particularly pronounced fashion in firms that have performed well in the past. These and other results suggest that binding say-on-pay (as put forward by the “Abzocker-Initiative”) has limited potential benefits in terms of better managerial decisions, but incurs substantial implementation costs, at least from a shareholder perspective. More generally, the empirical analysis cautions that more shareholder power may not always and unambiguously be a good thing, even for the shareholders themselves.

## 3 Survey Results

For a number of years now, compensation data has been disclosed as a consequence of the Transparency Act, which came into force in 2007. In this section, we analyse and comment on the level and structure of compensation for chairmen of the board of directors, other board members and CEOs for both SMI and SMIM companies.

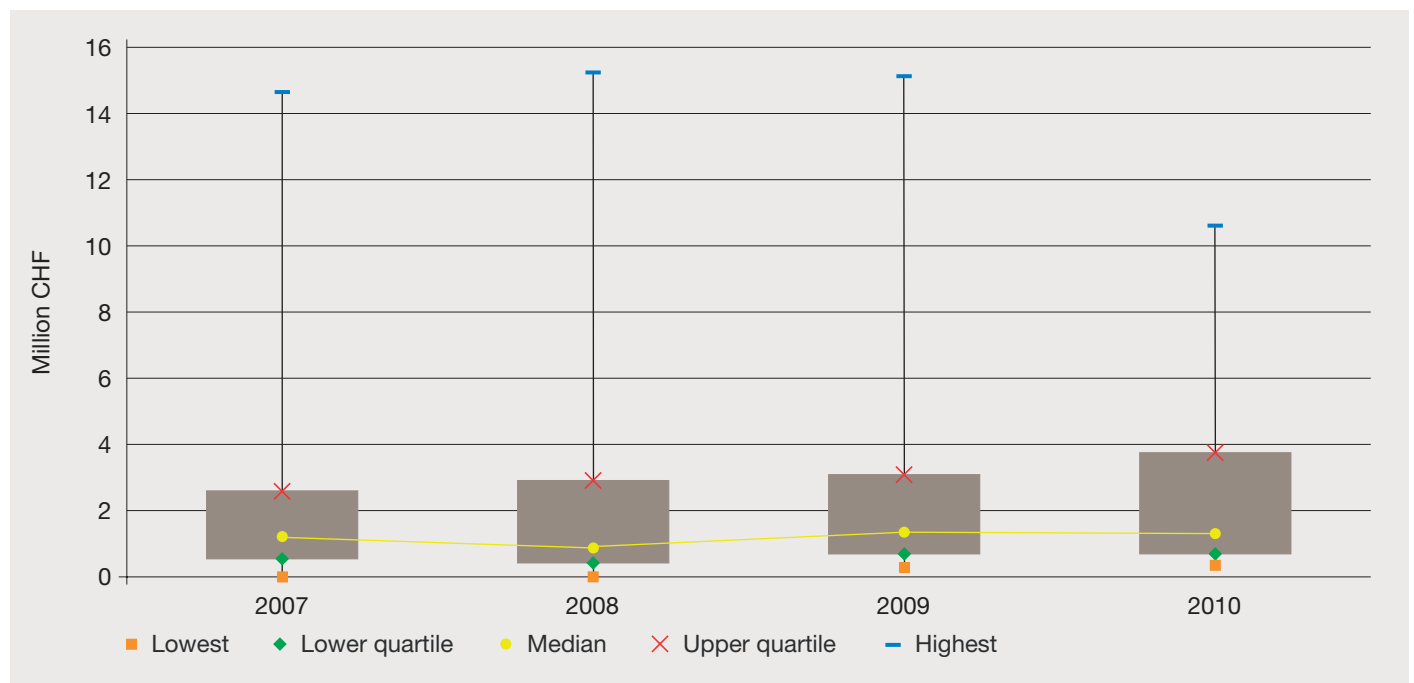
### 3.1 Chairmen of the board of directors

As the structure of the board of directors and the related responsibilities and tasks for members of the board of directors vary, for the chairman in particular, a one-to-one comparison among SMI and SMIM companies proved difficult. Nevertheless, a comparison was made based on compensation data disclosed, whereby only the non-executive chairman function was considered.

#### SMI companies

From 2009 to 2010, the compensation of the highest paid chairman decreased by 29.9% to CHF 10.6 million whereas the compensation of the lowest paid chairman increased by 29.1% to CHF 331,275. These observations suggest a convergence of pay in terms of extreme values. However, the virtually unchanged lower quartile (increase of 0.7% to CHF 675,175) and the significantly higher upper quartile (increase of 21.6% to CHF 3.7 million) imply an increase in dispersion of total compensation over the years in the middle 50%. Except for 2008 when it was lower, the median remained relatively stable around CHF 1.3 million over the years.

Figure 1: Total compensation of chairmen in SMI companies<sup>1)</sup>



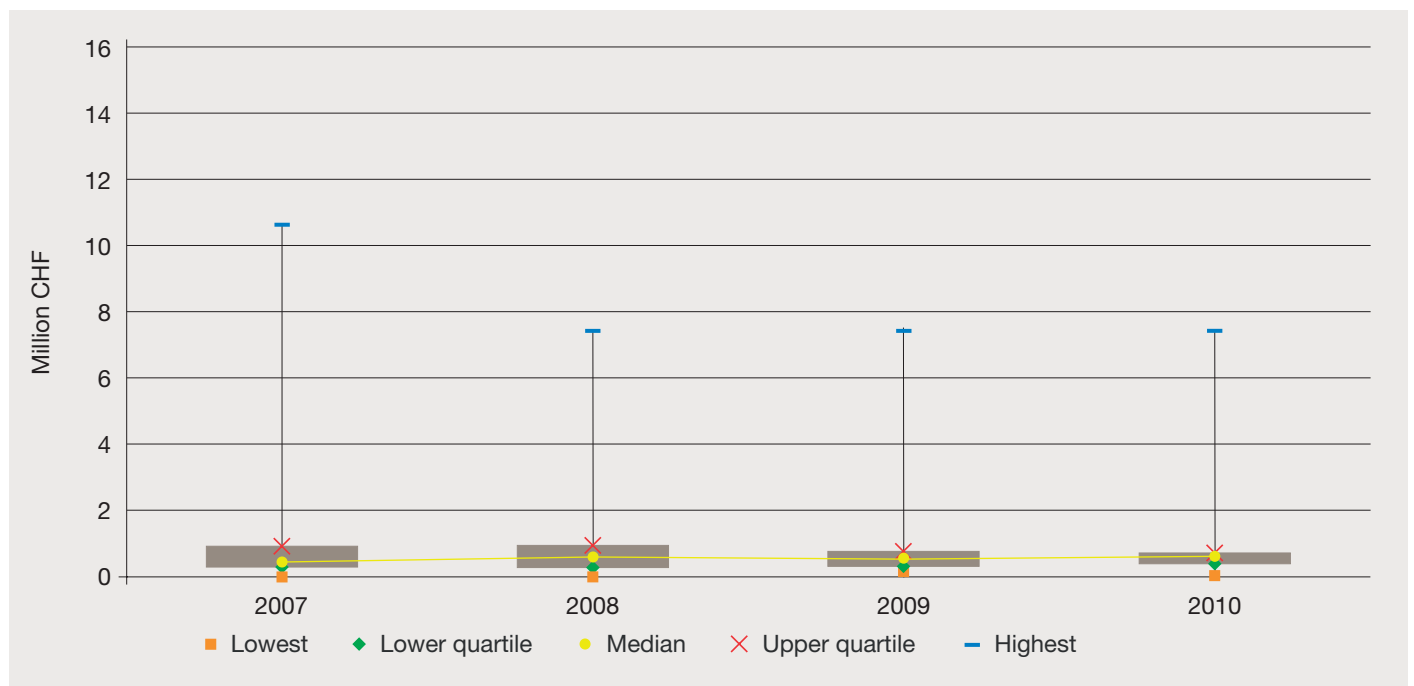
<sup>1)</sup> Compensation for non-executive function (n=16)

### SMIM companies

As in the previous year, compensation levels remained relatively unchanged in 2010. While the lowest and the highest amounts paid show very little to no variance, the lower quartile increased substantially by 23.1% to CHF 376,250 and the upper quartile decreased by 7.1% to CHF 697,994. The median increased by 7.6% to CHF 603,100.

Based on the developments of 2007 to 2010, a convergence of compensation of chairmen of the board of directors of SMIM companies can be observed. In contrast, levels of total compensation have been diverging on a higher level within SMI companies over the years. Looking at the median, chairman pay in SMI companies has been relatively stable over the years, whereas it has increased in SMIM companies over time.

Figure 2: Total compensation of chairmen in SMIM companies<sup>2)</sup>



<sup>2)</sup> Compensation for non-executive function (n=20)

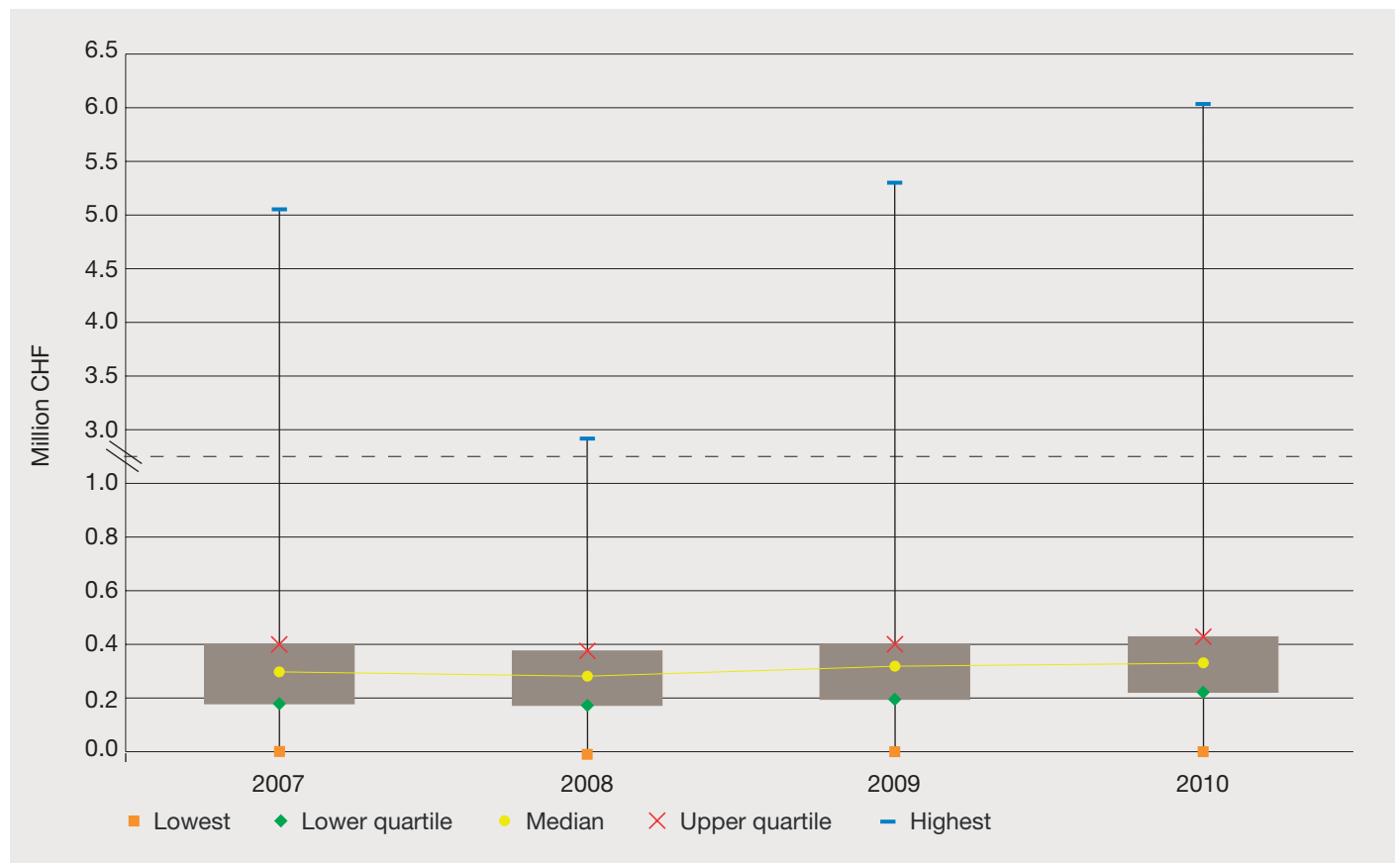
## 3.2 Other members of the board of directors

### SMI companies

The lower quartile amounted to CHF 219,440 and the upper quartile to CHF 427,975, i.e., half of the SMI board members were paid in this range for the year 2010. In 2007 this interval ranged from CHF 176,265 to CHF 400,000. The median amounted to CHF 296,030 in 2007 and to CHF 328,694 in 2010.

Based on these figures and trends we conclude that compensation levels of SMI board members have been slightly increasing over the years 2007 to 2010 and have stayed within a relatively small band.

Figure 3: Total compensation of other members of the board of directors in SMI companies<sup>3)</sup>



<sup>3)</sup> Chairman and executive functions excluded (n=178)

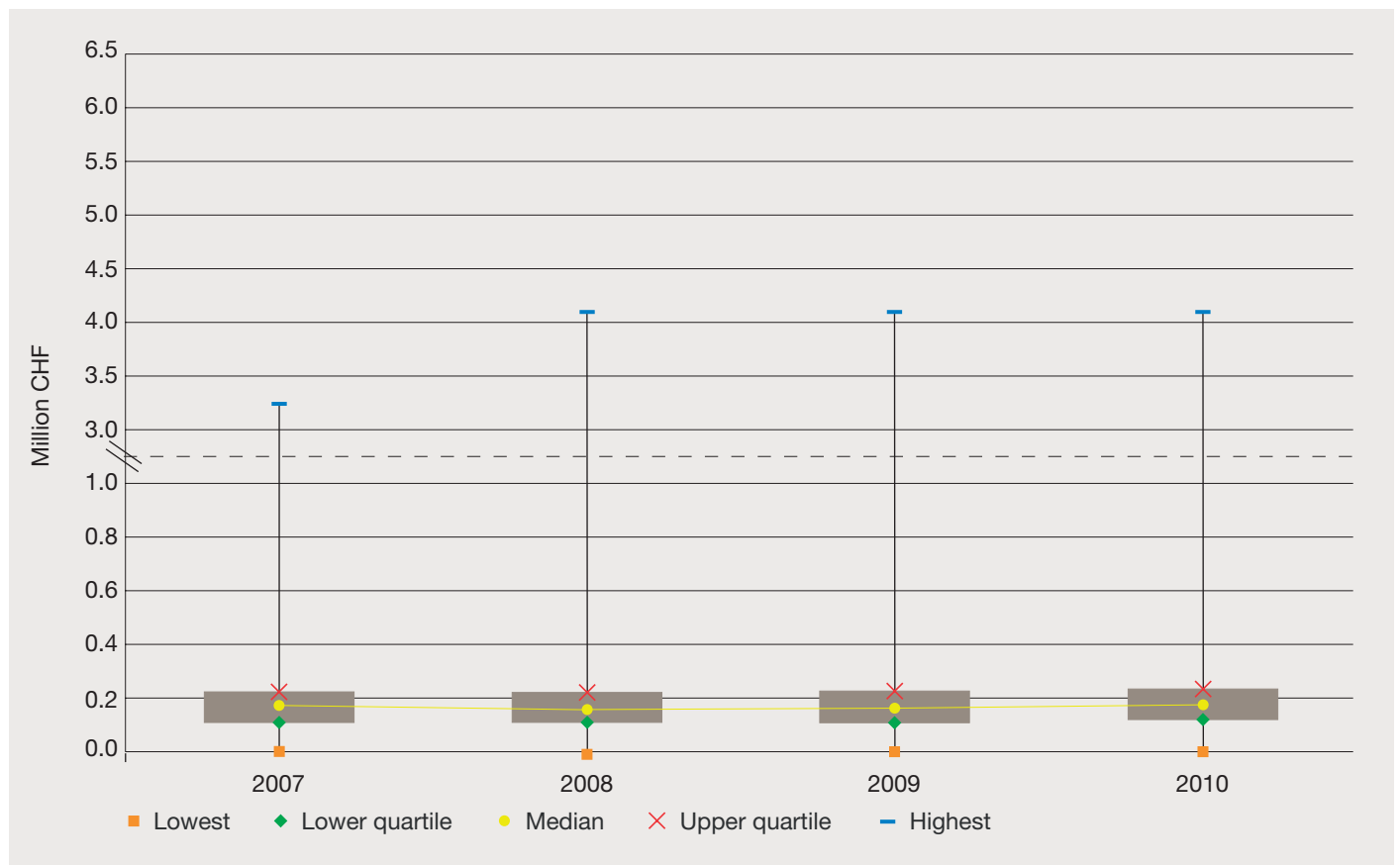


### SMIM companies

The lower quartile amounts to CHF 117,000 and the upper quartile to CHF 231,823, i.e., half of the SMIM board members were paid in this range for the year 2010. The changes from the previous years are marginal; e.g., the median remained virtually unchanged from CHF 169,000 in 2007 to CHF 172,555 in 2010.

Based on these figures and trends we conclude that compensation levels of SMI and SMIM board members have been stable or slightly increasing in a relative small band for the years 2007 to 2010.

Figure 4: Total compensation of other members of the board of directors in SMIM companies<sup>4)</sup>



<sup>4)</sup> Chairman and executive functions excluded (n=198)

### 3.3 CEOs

In this section we analyse and comment on the level of compensation for CEOs of SMI and SMIM companies. For both SMI and SMIM companies, median total compensation increased from 2009 to 2010; however, it has not reached the levels of 2007. Also for both groups, the average compensation decreased from 2009 to 2010.

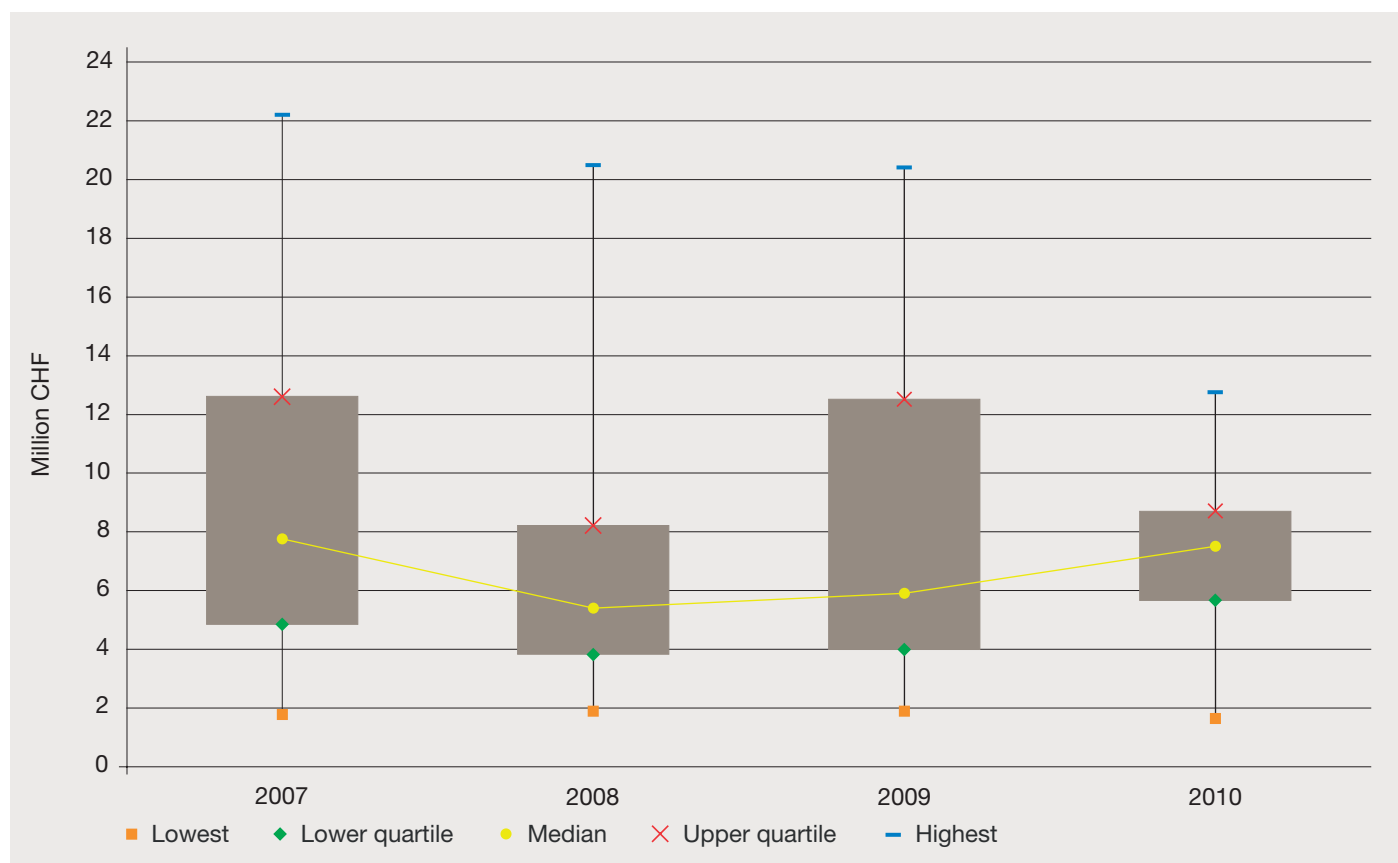
Furthermore, for both SMI and SMIM companies the lower quartile increased and the upper quartile decreased from 2009 to 2010, resulting in a convergence within each sample. Notably, the highest as well as the average CEO total compensation in SMI and SMIM companies have dropped when comparing 2009 to 2010 and also 2007 to 2010. Overall, the asymmetry of the distribution of CEO pay has decreased – the average and the median are more similar in 2010 than they were in previous years.

### SMI companies

In 2010, the highest paid disclosed person was not a CEO. In fact, there were five companies in which a member of the executive board other than the CEO received the highest total compensation. Therefore, for the analysis and to enhance comparability, two graphs were created. The first one includes all the CEOs of the SMI companies; the second one shows all highest paid members of the executive board (i.e., fifteen CEOs and five others).

For the group of CEOs, the lower quartile increased from 2009 by 42.7% to CHF 5.6 million, while the median rose by 27.5% to CHF 7.5 million. All other amounts decreased, with a significant decline of 37.7% to CHF 12.8 million for the highest paid CEO and a decrease of the upper quartile by 30.6% to CHF 8.7 million. Thus, the range of individual total compensation has narrowed amongst SMI CEOs from 2009 to 2010. 50% of CEOs total compensation is between CHF 5.6 million and CHF 8.7 million.

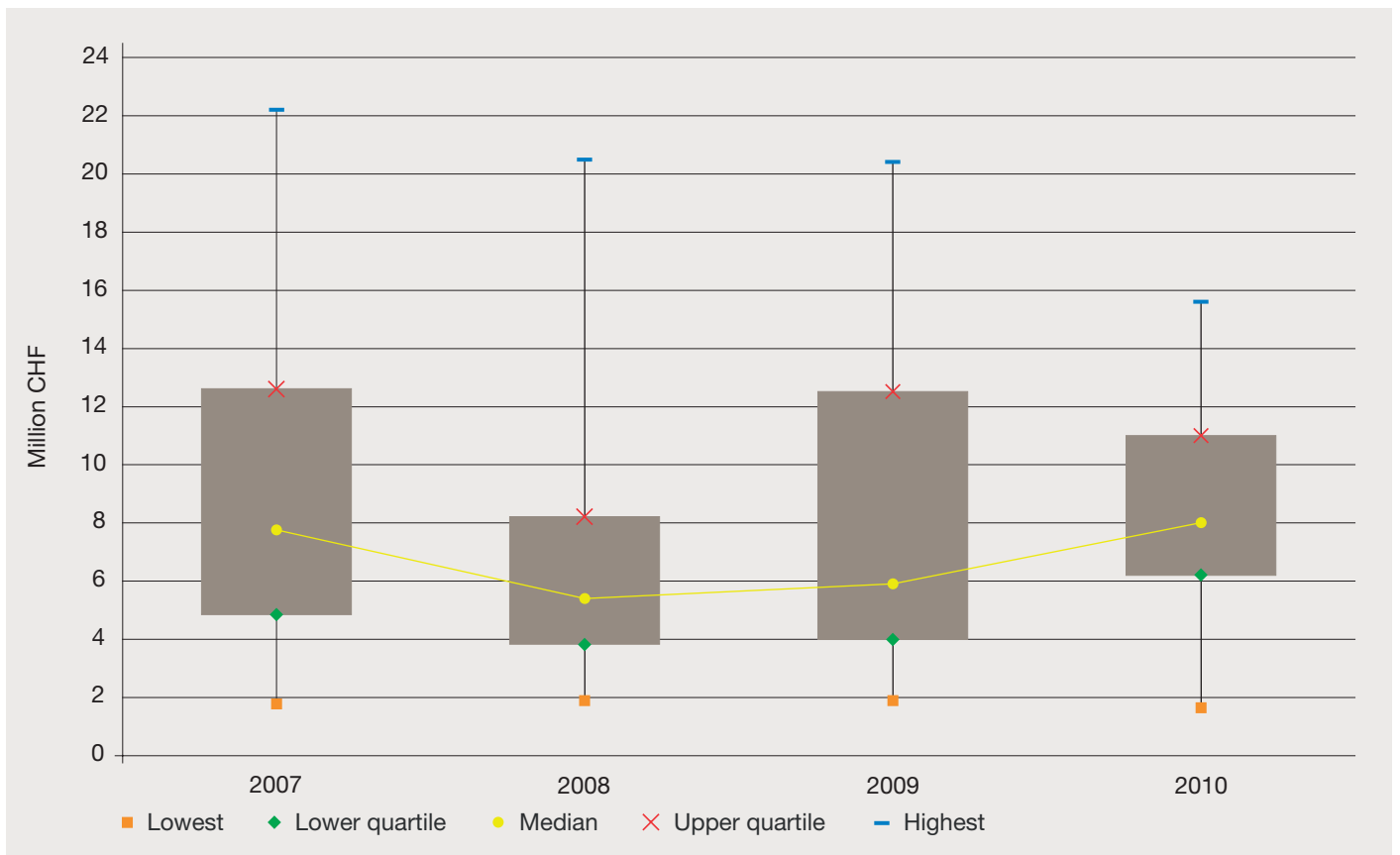
Figure 5: Total compensation of CEOs in SMI companies <sup>5)</sup>



<sup>5)</sup> In 2008, the highest paid disclosed person was not a CEO – in 2010, in 5 companies the highest paid person was not the CEO (n=20)

In 2010, the highest paid disclosed person received a total compensation of CHF 15.6 million, which is CHF 2.9 million, or 22.5%, more than the highest paid CEO. The overall findings as regards the development over time are similar to those for the CEO sample.

Figure 6: Total compensation of the highest paid member of the executive board in SMI companies<sup>6)</sup>



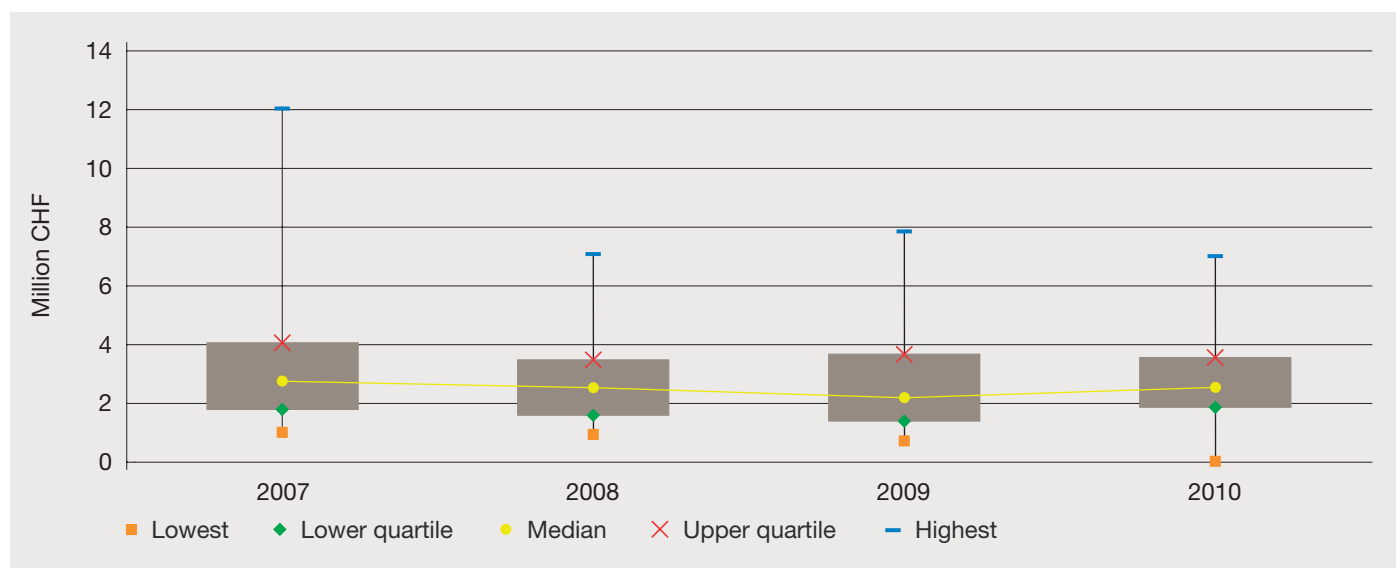
<sup>6)</sup> CEO or the highest paid executive board member respectively (n=20)

## SMIM companies

Within SMIM companies, in 2010 the highest paid individual disclosed was always the CEO.

After the decrease from 2008 to 2009, the median with CHF 2.5 million was in 2010 at the level of 2008 again but still 8.6% below 2007. The lower quartile increased in 2010 by 34% to CHF 1.9 million. The upper quartile decreased by 3.2% to CHF 3.5 million. Consequently, 50% of SMIM CEOs are paid in the range of CHF 1.9 million to CHF 3.5 million.

Figure 7: Total compensation of CEOs in SMIM companies<sup>7)</sup>



<sup>7)</sup> CEO or highest paid executive board member respectively (n=28)

### 3.4 Compensation structure 2010

For board members, the total compensation structure of 2010 within SMI and SMIM companies has not changed significantly compared to 2008 and 2009 as they were predominantly remunerated in the form of fixed compensation. Chairmen received about 60% of their remuneration as fixed compensation, for both SMI as well as SMIM companies. Other board members of SMI companies received 84.8% as fixed compensation whereas SMIM board members were provided with 68.9% fixed compensation. While other board members of SMI companies received only 3.7% of their total compensation as

long-term incentives (LTI) in 2010, SMIM companies remunerated the other board members with 17.5% LTI.

For CEOs and other executives the portion of fixed salary in relation to total compensation remained virtually unchanged from 2009 to 2010 in SMI as well as SMIM companies. The portion of the cash bonus in relation to total compensation increased for all executives in both samples. For the CEOs this increase amounted to about one third. For the other executives the portion of the cash bonus increased by approximately one quarter. In contrast, the portion of long-term incentives decreased for all executives in SMI companies. This also applies for CEOs in SMIM companies but not for other executives where the portion remained basically unchanged.

Figure 8: Overview of compensation structure in SMI companies in 2010

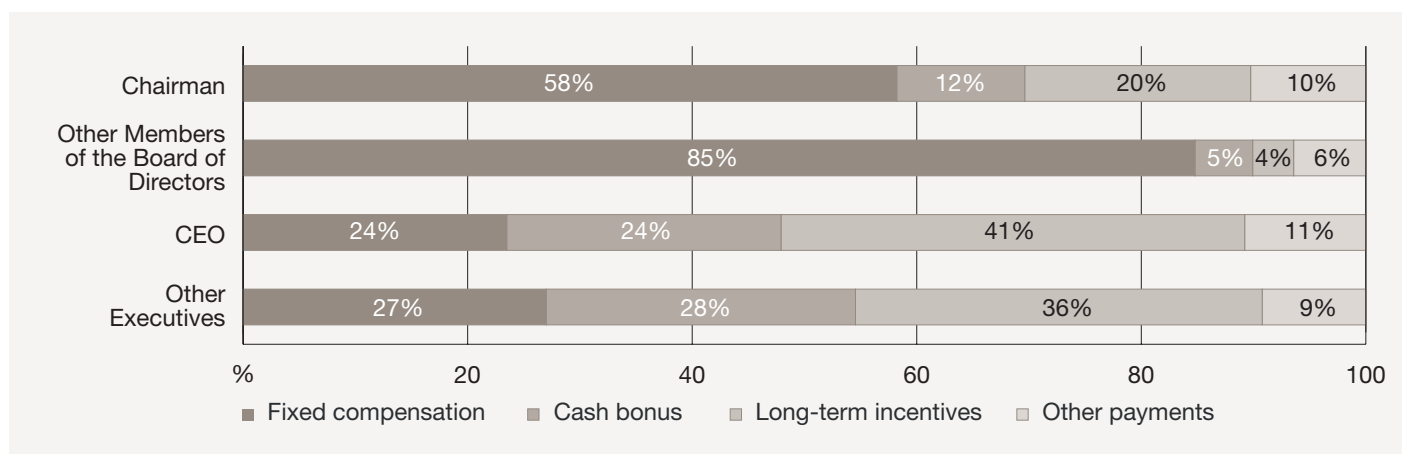
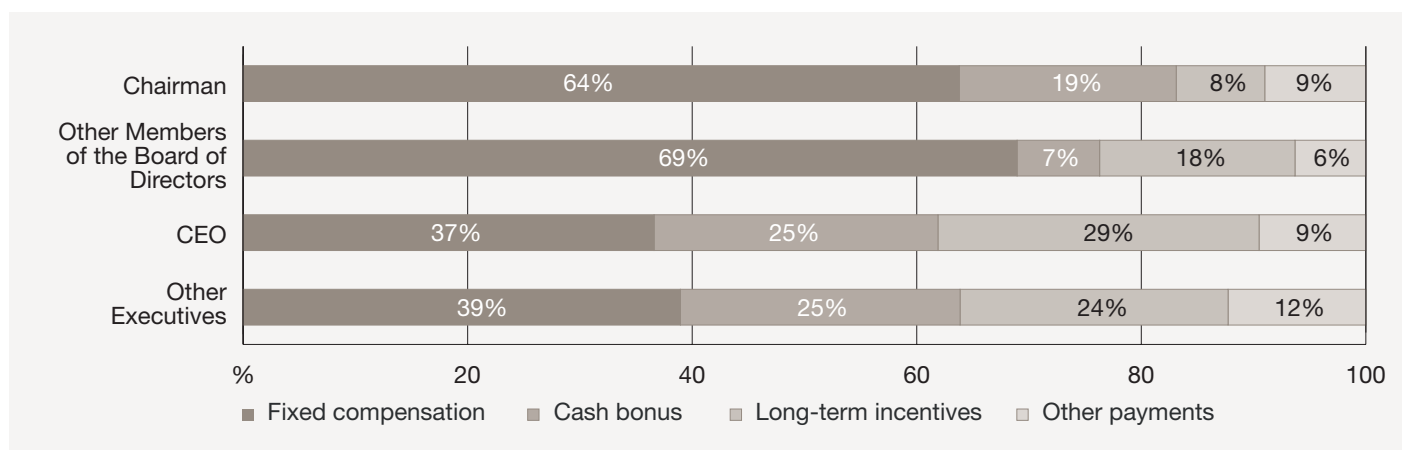


Figure 9: Overview of compensation structure in SMIM companies in 2010



### 3.5 Structure of average total compensation of CEOs<sup>8)</sup>

As in previous years, we have analysed the structure of the average total compensation for CEOs as we believe this provides important insights in addition to the analysis of the level.

#### SMI companies

The average total compensation decreased by 12.5% from CHF 8.2 million in 2009 to CHF 7.2 million in 2010. This happened after the average had increased by 18.0% from 2008 to 2009. With this decrease in 2010, the average total compensation is significantly below the figures of 2007 (CHF 9.3 million).

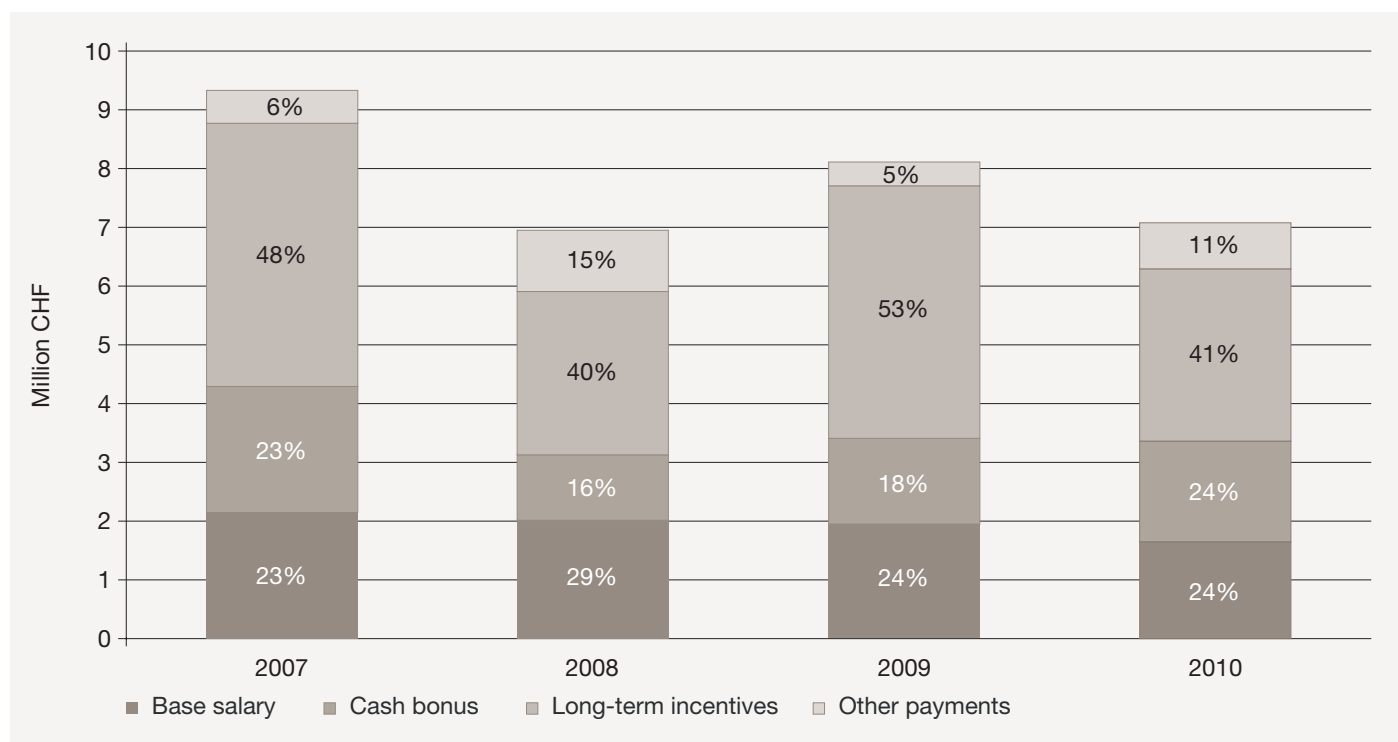
For 2010, the average total compensation was split into 24% as the base salary, 24% as a cash bonus, 41% as long-term incentives, and 11% as other compensation. The average base salary amounted to CHF 1.7 million, decreasing from CHF 2.1 million in 2007, which

corresponds to a decrease of approximately 20%. For the year 2010, 50% of CEOs received a base salary ranging from CHF 1 million to CHF 2 million.

The average cash bonus amounted to CHF 1.8 million in 2010 which is an increase of 20.1% compared to 2009. The average cash bonus did not reach the level of 2007 (CHF 2.2 million). Total average cash compensation (base salary + cash bonus) remained unchanged at CHF 3.4 million comparing 2010 to 2009.

The average of long-term incentives decreased from CHF 4.4 million in 2009 to CHF 3.0 million in 2010 which represents a significant drop of 31.8%.

Figure 10: Structure of average total compensation of CEOs in SMI companies



<sup>8)</sup> The comments in this section are based on the data for the CEOs (according to Figure 5) and not the highest paid member of the executive board.

### SMIM companies

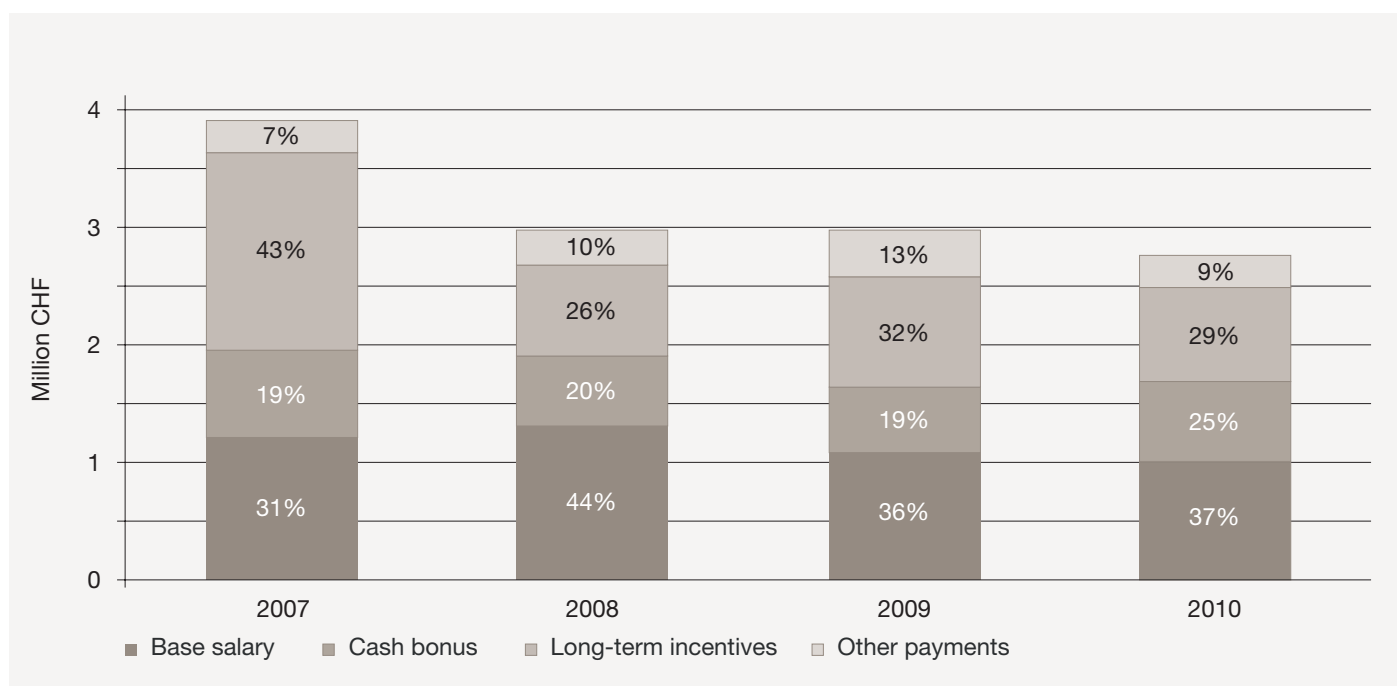
The average total compensation of CHF 2.9 million in 2009 remained at a similar level in 2010 with a decrease of 6.3% to CHF 2.8 million. However, from an overall perspective, the average total compensation has decreased over time by 27.6% from CHF 3.8 million in 2007 to CHF 2.8 million in 2010.

For 2010, the average total compensation was split into 37% as the base salary, 25% as a cash bonus, 29% as long-term incentives, and 9% as other compensation. The base salary decreased by 5.1% from 2009 to 2010 and by 13.5% from 2007 to 2010 (from CHF 1.2 million in 2007 to CHF 1.0 million in 2010).

The cash bonus increased from CHF 562,634 in 2009 to CHF 698,227 in 2010 which equals +24.1%, nearly reaching the levels of 2007 again. In contrast, the long-term incentives dropped from CHF 936,566 in 2009 to CHF 789,823 in 2010 (-15.7%).

Overall, the level of total variable compensation remained unchanged at approximately CHF 1.5 million, when comparing 2009 to 2010. But a shift has taken place from long-term incentive plans to cash bonuses, i.e., the portion of cash bonus within variable compensation has increased in 2010 at the expense of the long-term incentive portion.

Figure 11: Structure of average total compensation of CEOs in SMIM companies



### 3.6 Wealth changes due to share ownership

In addition to analysing the total compensation, it is also important to understand net wealth changes in the share ownership of board members and executives resulting from share price changes. These can be substantial in case of volatile markets. Table 1 lists these changes and developments. It is important to note that the highest gains and losses relate to chairmen and other board members that have significant share holdings (in particular as founders or founding family members).

In 2008, at least 75% of chairmen, other board members and CEOs suffered net wealth reductions resulting from falling share prices. In 2009, we observed the opposite, i.e. at least 75% of the persons surveyed benefited from rising share prices.

In 2010, an intermediate result occurred. The median CHF wealth change due to ownership was around zero or slightly positive for all three groups. The median CEO has not yet made up the loss suffered in 2008 (CHF -900,000) despite gains in 2009 and 2010 (CHF +480,000 and CHF +230,000, respectively).

Table 1: CEO and board of director wealth changes due to ownership in the years 2008, 2009, and 2010<sup>9)</sup>

2008	Highest gain	Top 25 % (upper quartile)	Median	Bottom 25 % (lower quartile)	Greatest loss
CEOs	+230,000	-240,000	-900,000	-2,000,000	-220,000,000
Chairman	+6,340,000	-300,000	-1,000,000	-35,600,000	-2,745,000,000
Other Members of the Board of Directors	+42,830,000	-60,000	-200,000	-670,000	-3,015,000,000
2009	Highest gain	Top 25 % (upper quartile)	Median	Bottom 25 % (lower quartile)	Greatest loss
CEOs	+10,300,000	+980,000	+480,000	+60,000	-35,400,000
Chairman	+2,170,000,000	+3,100,000	+240,000	+10,000	-30,000,000
Other Members of the Board of Directors	+1,440,000,000	+240,000	+50'000	+7,000	-318,000,000
2010	Highest gain	Top 25 % (upper quartile)	Median	Bottom 25 % (lower quartile)	Greatest loss
CEOs	+11,600,000	+975,000	+230,000	-10,000	-21,100,000
Chairman	+1,899,000,000	+410,000	+80,000	-110,000	-32,000,000
Other Members of the Board of Directors	+290,000,000	+110,000	+/-0	-30,000	-590,000,000

<sup>9)</sup> All amounts in CHF and rounded. Wealth changes in 2008 are calculated as the difference between the wealth due to the average of the reported stockholdings on 31 December 2007 and those on 31 December 2008, valued on 31 December 2008, minus the value of these average shareholdings on 31 December 2007. For wealth changes in 2009 and 2010, the same methodology is applied. All shares (not only vested shares) are considered. Companies that do not report shareholdings for the respective category of individuals are not considered in this table.



The wealth changes of the middle half of CEOs, chairman, and other board members are in a relatively narrow range around the median. 50% of all CEOs (between lower and upper quartile) experienced wealth changes in the amount of CHF -10,000 to CHF +975,000. For chairmen, this range is narrower this year than last year: from CHF -110,000 to CHF +410,000. For other board members, this range amounts to CHF -30,000 to CHF +110,000 for 2010 compared to CHF +7,000 to CHF +240,000 for 2009<sup>10)</sup>.

In 2008 and in 2009, the distribution of wealth changes of CEOs was heavily skewed. For example, in 2009, the average CEO had lost CHF 550,000 while the median had gained CHF 480,000. In 2010, the distribution is considerably less skewed: On average, the average wealth change of CEOs considered from end of 2009 to end of 2010 that is implied by their average shareholdings was CHF 110,000, only slightly less than the median.

The median share ownership in 2010 was around 0.03 % of the respective company. This shows a generally low share ownership quota of CEOs in their company. It means that a CHF 1,000 change in shareholder wealth in a given year corresponds to CHF 0.30 CEO wealth change. However, the percentage wealth change, defined as the wealth change of a disclosed person expressed as a percentage of the wealth he holds in shares of his company, can be substantial: the median percentage wealth change of CEOs was +12%. For other board members, this number was +6%, for chairmen it was +2%.

All the numbers reported in this section do not reflect implied ownership through options or other instruments similar to equity. They are merely based on what companies report to be the direct alignment of their CEOs with shareholders through the ownership of shares.

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<sup>10)</sup> At one company, three board members have a shareholder agreement regarding a large stock package. In our 2008 analysis, we attributed the wealth change on the whole stock package to one individual. In the 2009 analysis, we divided the total effect by three to account for the agreement between these three shareholders.

# 4 Mandatory Disclosure According to SIX Exchange Regulation

## 4.1 Background

Compensation disclosure is one of the key issues in today's challenging environment for companies. Companies need to be mindful of several mandatory rules before even considering which additional voluntary disclosures could be helpful when communicating with stakeholders. For Swiss listed companies, besides the rules in the Code of Obligations that mainly concern the disclosure of levels of compensation, several new requirements are in place that also concern the process and other substantive issues in management compensation. In particular, the Directive on Information relating to Corporate Governance of the SIX Swiss Exchange requires issuers to disclose important information on their board and executives (or to give substantial reasons why this information is not disclosed).

SIX Exchange Regulation is responsible for the enforcement of issuer regulation in accordance with the SIX Swiss Exchange stock exchange law. Indeed, in its circular 8/2010, the SIX has emphasised that in its 2010 review of annual reports it will pay particular attention to whether the rules are being adhered to. Many companies have, also alerted by a number of sanctions imposed by the SIX on non-compliant companies, expended considerable effort to align their reports with the regulations. However, compliance is not a simple matter when it comes to compensation disclosure. For example, listed companies need to be aware of several different standards in deciding what needs to be disclosed. In particular, the Directive Corporate Governance itself is not particularly detailed. However, there are several additional relevant documents. First, the Commentary to the Directive provides a number of more detailed points. Second, on 24 November 2010, the SIX provided some additional guidance on particular aspects of disclosure. Third, additional information can be read out of the published decisions of the SIX sanctions commission. (Our analysis in this survey is based on guidance published as of July 31, 2011.)

## 4.2 A scorecard for compliance with SIX Exchange Regulation rules

To support listed companies in ascertaining what level of quality they have obtained in their compensation disclosure efforts and to develop a view on overall compliance and best practice in Switzerland today, we have developed a rating system that aims at capturing the rules that companies currently need to comply with as far as the SIX Exchange Regulation is concerned. We emphasise that the resulting scorecard is PwC's reading of the SIX Exchange Regulation's rules. It is not an official rating and was developed without any involvement of SIX Exchange Regulation. However, we believe it accurately and comprehensively reflects the rules that are in place today.<sup>11)</sup>

The general guiding principle that companies need to follow is that the principles and elements of compensation (the design and determining mechanisms, as well as details of any shareholding programme and how it works) must be explained to investors in terms that are as comprehensible as possible. From this general principle follow several more specific requirements, which we have chosen to summarise under three headings. Topic A covers requirements regarding the process of how pay is set. Topic B relates to requirements regarding the substance of the compensation system. Topic C concerns requirements regarding the calculation of payments and other requirements. Our detailed scorecard covers a total of 24 criteria: 7 for Topic A, 11 for Topic B, and 6 for Topic C.

For the purpose of this survey, Table 2 highlights the main issues within each topic group. The full scorecard is available upon request.

<sup>11)</sup> The Directive Corporate Governance also covers other aspects of disclosure not related to compensation; these are not part of this scorecard. The other statutory requirements that exist regarding compensation matters (in particular, disclosure requirements according to OR 663b bis) are also not part of this review, although there is of course some overlap.

**Table 2: Key compliance issues with regard to SIX Exchange Regulation rules on compensation disclosure**

Headings/Topics	Main challenges in practical implementation
<p><i>A: Requirements regarding the process of how pay is set (7 criteria)</i></p>	
<p>The key points of the process used to determine compensation and participation in the shareholding programme must be described. This includes, but is not limited to, issues such as competencies of various bodies, who has a vote in a relevant meeting, whether external advisors are consulted, and whether part of the compensation is given on a discretionary basis.</p>	<p>We have seen a significant improvement in reports on this dimension from 2009 to 2010. Many companies have substantially clarified the process of pay-setting. Occasionally, the difference between rules-based and discretionary bonuses is perhaps not as clear as it could be.</p>
<p><i>B: Requirements regarding the substance of the compensation system (11 criteria)</i></p>	
<p>Companies have to describe which goals are taken into account when structuring compensation and share-ownership programmes, and how strongly individual goals and other components are taken into account. Non-GAAP measures need to be explained. Moreover, companies are required to disclose whether benchmarks or salary comparisons have been used; if so, the benchmarks and salary comparisons selected must be disclosed (sector/function, etc.) and the choice of benchmarks and reference salaries must be explained as transparently as possible. Furthermore, the composition of pay needs to be detailed in various ways, using easy-to-understand quantitative analysis, and share and option plans need to be explained exactly.</p>	<p>Perhaps the most challenging of these requirements appears to be the explanation of the benchmarks used, if any. To some extent, this appears to be difficult because companies have not been very explicit about the process by which benchmarks were selected. Moreover, some companies are reluctant to go into too much detail regarding this issue. Furthermore, some uncertainty exists as to what the SIX Exchange Regulation actually wants to see here. Similar uncertainty surrounds the requirement to explain non-GAAP measures. Generally speaking, the explanation of the substance of compensation systems has significantly improved from 2009 to 2010, although stakeholders still do not always obtain a clear picture of how value-generation is measured and rewarded in a company.</p>
<p><i>C: Requirements regarding the evaluation of payments and other requirements (6 criteria)</i></p>	
<p>This final topic covers the explanation of in-kind payments, special payments, especially those made upon leaving the company, and related topics.</p>	<p>Tricky disclosure questions are sometimes encountered by companies in conjunction with leaving management and board members, in particular when privacy issues can be in apparent conflict with disclosure rules.</p>

### 4.3 A view on compliance and best practice in Switzerland today

Based on our experience, we list some of the main challenges in practical implementation we observed in the right column of Table 2 above. Moreover, using the full scorecard, we have evaluated<sup>12)</sup>, for both 2009 and 2010, all the 48 companies that are part of our executive compensation survey in the first part of this report.

We have applied this scorecard approach in the most diligent manner possible, but the procedure is clearly subjective. Different rating systems will yield different results. Moreover, it is possible that violations of some criteria may be regarded as more severe by the SIX sanctions commission than others. We refrained from applying such “value-weighting.” Nonetheless, taking these caveats into account, we believe that the findings are informative.

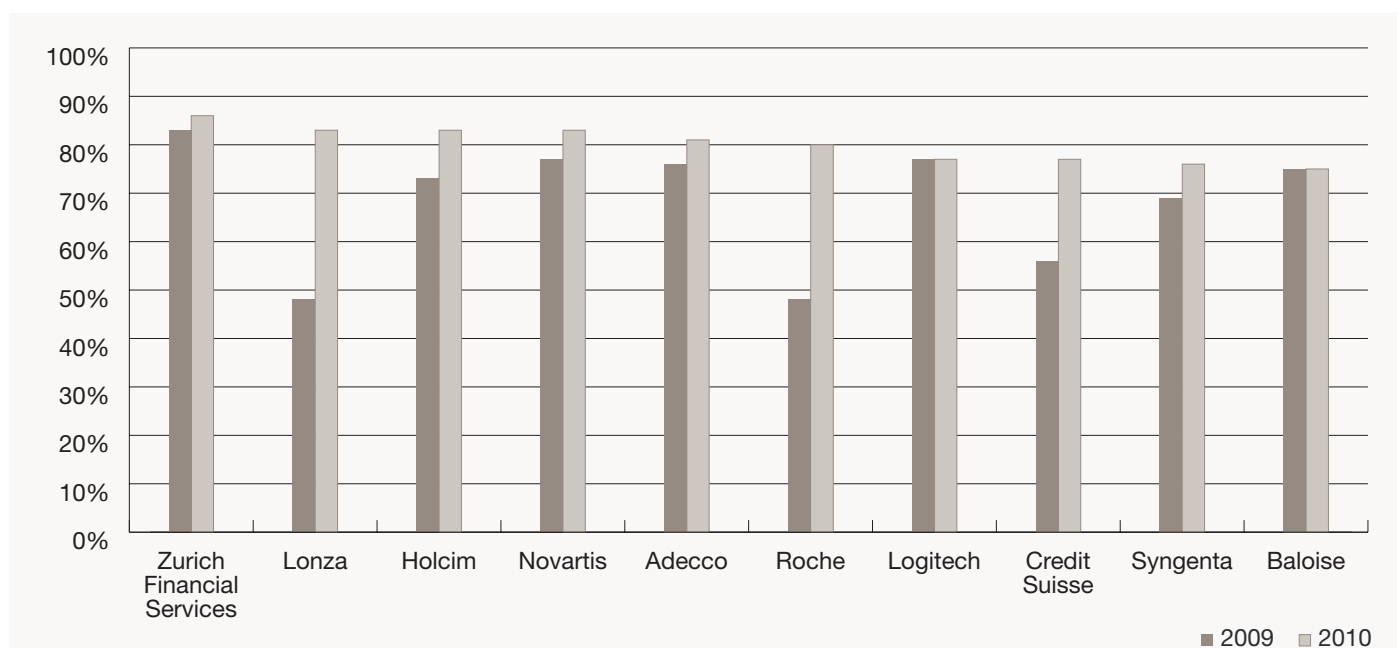
Figure 12 shows the ten companies with the highest disclosure score in 2010, with the scores for both years under consideration. In our view, the reports of these companies in many ways represent what can be regarded as best practice with respect to compliance with SIX Exchange Regulation compensation disclosure requirements in the Swiss market today.

Based on our analysis of the data, we make two observations, one regarding the development over time and one regarding the cross-section of companies.

1. Compliance with SIX rules has substantially increased from 2009 to 2010. In 2010, the median disclosure score was 63%. In 2009, the median score had only been 52%. Although compliance with SIX rules varies from company to company surveyed in 2010 (at least according to our strict grading standard embedded in our scorecard), the good news is that most firms have improved.
2. There is large variation in the quality of disclosure and compliance with SIX regulations. Several points – in particular, the quantitative presentation of compensation levels – nowadays are part of standard disclosure procedures in most (though not all) companies. But there are also some key issues such as, for example, the explanation of benchmarks and non-GAAP measures that are better addressed in some reports than in others.

<sup>12)</sup> In particular, on each of the 24 criteria, companies were rated with a grade of 0, 1, or 2. First, we determined whether a given criterion is addressed at all in a report. If it was addressed, a score of 2 was given if an issuer fully and understandably covered the issue or used the “explain” clause, i.e., did not disclose the issue, but explained why it did so. A score of 1 was given if the criterion was partially addressed. A score of 0 was given if the issuer used too general explanations or incomprehensible prose. If a criterion was not mentioned at all, for those cases which clearly were relevant for a company, we assigned a score of 0 due to the apparent violation of disclosure requirements. However, for some criteria it was possible that they did not apply to a given company (for example, when no “special rules” exist for some managers, they cannot be disclosed), and in this case we did not take this criterion into account for calculation of the total number of reachable points for this company. The total compliance score for a company per year was then calculated as the ratio of the total number of points to the total number of reachable points.

**Figure 12: Degree of compliance with SIX Exchange Regulation compensation disclosure rules**  
**Top 10 companies 2010, out of the SMI and SMIM sample (based on a scorecard developed by PwC)**



# 5 Concluding Remarks

## 5.1 Using disclosure requirements as an opportunity?

Compliance with mandatory disclosure is a critical reputational issue for companies today. As such, companies are forced to think hard about how to describe their compensation systems in ways that fulfil the disclosure and transparency requirements. We suggest that management also sees the opportunities in these requirements, not only the costs. In particular, successful disclosure will require the board and executives to understand explicitly where and how value is generated in a company, and how value generation is rewarded. Modern compensation systems reward either outcomes (in the traditional pay-for-performance sense) or the achievement of strategic goals. In particular when the second approach is employed – as is the case in many companies, at least in a supplementary fashion – it becomes critical to explain to stakeholders why and how the chosen metrics are related to overall firm value. From our experience, this is not always easy as compensation systems have grown organically over time, without an explicit, guiding plan. We recommend that companies think carefully about their overall compensation policy and how it matches with their business strategy.

## 5.2 Is it time to increase shareholder power?

The call for more shareholder power is sounding loud and clear. Our response is: not so fast. In particular, shareholders themselves may not want enhanced power. For example, consider the “Abzocker-Initiative.” As we showed in last year’s survey, stock prices of Swiss public companies reacted negatively when it was announced that the “Abzocker-Initiative” had collected sufficient signatures to force a constitutional referendum.<sup>13)</sup> The average firm lost nearly 1.5% in market capitalisation over a three-day window around the announcement.<sup>14)</sup>

Why would shareholders be angry when they get more power? The point is that the Abzocker-Initiative does not only bring benefits, but also implies costs. The cited study shows that in fact, differences in reactions among firms can be explained well by thinking about differences among firms in terms of these benefits and costs. For example, stock prices dropped in a particularly pronounced fashion in firms that have performed well in the past where more shareholder power has limited potential benefits in terms of better managerial decisions, but still incurs substantial implementation costs. Interestingly, stock prices of the largest companies barely reacted, while the decrease in stock prices of small and medium companies suggests that the market perceives the proposed regulation as particularly value-destroying for these companies.

While the results suggest that the emotional and popular knee-jerk reaction to “increase shareholder power” is, in the worst case, dangerous, they do not imply that governance should not be regulated. Evidence from the U.S. shows, for example, that advisory say-on-pay can promote shareholder welfare, under certain conditions. Moreover, some recent reforms in the compensation area also aim at benefiting other stakeholders or also society at large (for example, by limiting potential external effects such as excessive risk-taking due to poorly designed compensation systems).

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<sup>13)</sup> The updated study is available at [http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=1793089](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1793089)

<sup>14)</sup> This calculation factors out other reasons for a firm’s stock price movement around the announcement day

In 27 of the 48 SMI and SMIM companies in Switzerland, shareholders already had a non-binding consultative vote on the compensation report for the year 2010. All reports were approved, whereby the majority of companies achieved a positive or very positive result.

### **5.3 Six principles**

Despite – or because of – the market fluctuations we have seen over the past years and the many new regulatory challenges companies face, we continue recommending that executive compensation is designed with six simple principles in mind.

1. Only a strong board can implement an effective total compensation system.
2. The incentive system must be designed as a “best fit” with company strategy – and it needs to be communicated as such.
3. Compensation should be linked to a few key performance indicators (KPIs), but not exclusively to easily controllable factors.
4. Limits to pay are counter-productive.
5. An effective compensation system establishes entrepreneurial incentives.
6. An effective compensation system focuses on value created for the long term.

# Appendix

## Companies surveyed *(in alphabetical order)*

### **SMI companies**

ABB  
Actelion  
Adecco  
Credit Suisse  
Holcim  
Julius Bär  
Lonza  
Nestlé  
Novartis  
Richemont  
Roche  
SGS  
Swatch  
Swiss Re  
Swisscom  
Syngenta  
Synthes  
Transocean  
UBS  
ZFS

### **SMIM companies**

Arzyta  
Baloise  
Barry Callebaut  
Clariant  
Galenica  
GAM  
Geberit  
Georg Fischer  
Givaudan  
Helvetia  
Kühne & Nagel  
Lindt  
Logitech  
Meyer Burger  
Nobel Biocare  
Panalpina  
Pargesa  
Petroplus  
PSP  
Schindler  
Sika  
Sonova  
Straumann  
Sulzer  
Swiss Life  
Swiss Prime Site  
Temenos  
Valiant



# **PwC**

## **Human Resource Services**

For further information about this survey or our services in the field of compensation planning for executives and applicable governance, disclosure and accounting requirements, please contact:



**Dr. Robert W. Kuipers**  
Partner, HRS Consulting  
PricewaterhouseCoopers  
Phone: +41 58 792 45 30  
Email: robert.kuipers@ch.pwc.com



**Remo Schmid**  
Partner, HRS Consulting  
PricewaterhouseCoopers  
Phone: +41 58 792 46 08  
Email: remo.schmid@ch.pwc.com



**Prof. Alexander F. Wagner, PhD\***  
Independent Counsel, HRS Consulting  
Swiss Finance Institute, University of Zurich  
Phone: +41 44 634 39 63  
Email: alexander.wagner@bf.uzh.ch

### **Other recent PwC publications on the subject of executive compensation and disclosure:**

- The psychology of incentives: If executive pay is broken, making it more complex is not the answer, 2011
- Breaking the mould: Risk and governance will change the structure of reward, 2011
- Global Equity Incentives Survey 2011

[www.pwc.ch/reward](http://www.pwc.ch/reward)

If you would like further copies of this survey or of the above publications, please contact:

**Heidi Fässler**  
HRS Consulting  
PricewaterhouseCoopers  
Birchstrasse 160  
8050 Zurich  
Switzerland

Phone: +41 58 792 45 31  
Email: heidi.faessler@ch.pwc.com

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Chairman	SMI				SMI Changes		SMIM				SMIM Changes	
	2007	2008	2009	2010	09/10	07/10	2007	2008	2009	2010	09/10	07/10
Upper Quartile	2,568,379	2,388,785	3,070,609	3,734,814	+21.63%	+45.42%	906,043	932,560	751,464	697,994	-7.12%	-22.96%
Median	1,200,000	844,723	1,330,867	1,288,694	-3.17%	+7.39%	430,500	581,876	560,591	603,100	+7.58%	+40.09%
Lower Quartile	520,869	397,564	670,599	675,175	+0.68%	+29.62%	278,750	261,000	305,640	376,250	+23.10%	+34.98%
Highest	14,624,000	15,228,951	15,116,196	10,599,302	-29.88%	-27.52%	10,625,656	7,418,000	7,418,000	7,418,000	0.00%	-30.19%
Average	2,328,611	2,424,636	2,954,167	2,851,841	-3.46%	+22.47%	1,231,812	906,415	862,602	930,107	+7.83%	-24.49%
Lowest	0	0	256,570	331,275	+29.12%	n/a	0	0	144,000	141,000	-2.08%	n/a

Board of Directors	SMI				SMI Changes		SMIM				SMIM Changes	
	2007	2008	2009	2010	09/10	07/10	2007	2008	2009	2010	09/10	07/10
Upper Quartile	400,000	375,053	400,034	427,975	+6.98%	+6.99%	221,000	218,217	223,975	231,823	+3.50%	+4.90%
Median	296,030	279,869	317,407	328,694	+3.56%	+11.03%	169,000	154,500	158,423	172,555	+8.92%	+2.10%
Lower Quartile	176,265	170,000	192,799	219,440	+13.82%	+24.49%	105,919	106,250	105,050	117,000	+11.38%	+10.46%
Highest	5,027,381	2,901,796	5,274,667	6,034,881	+14.41%	+20.04%	3,255,621	4,107,000	4,107,000	4,107,000	0.00%	+26.15%
Average	377,953	363,552	400,572	415,027	+3.61%	+9.81%	248,103	239,510	230,052	235,286	+2.28%	-5.17%
Lowest	0	0	0	0	0.00%	0.00%	0	0	0	0	0.00%	0.00%

CEO	SMI				SMI Changes		SMIM				SMIM Changes	
	2007	2008	2009	2010	09/10	07/10	2007	2008	2009	2010	09/10	07/10
Upper Quartile	12,618,250	8,185,720	12,518,763	8,687,749	-30.60%	-31.15%	4,058,039	3,469,390	3,664,328	3,547,000	-3.20%	-12.59%
Median	7,727,944	5,351,799	5,861,461	7,473,618	+27.50%	-3.29%	2,750,174	2,520,853	2,178,500	2,515,000	+15.45%	-8.55%
Lower Quartile	4,792,787	3,770,484	3,935,927	5,615,828	+42.68%	+17.17%	1,788,900	1,581,127	1,383,553	1,853,605	+33.97%	+3.62%
Highest	22,280,000	20,544,032	20,471,929	12,760,000	-37.67%	-42.73%	12,024,884	7,062,808	7,840,619	6,999,000	-10.73%	-41.80%
Average	9,326,781	6,943,456	8,191,353	7,166,879	-12.51%	-23.16%	3,814,715	2,939,052	2,948,413	2,761,837	-6.33%	-27.60%
Lowest	1,704,000	1,814,702	1,819,000	1,560,206	-14.23%	-8.44%	1,012,836	930,824	710,000	5,000	-99.30%	-99.51%

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