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2019 CEO and CFO Compensation Practices: Trends in the Energy Industry

The energy industry sectors continued to struggle in 2018 and 2019 while adapting to internal and external conditions. Sudden economic shifts, including M&A activity, market volatility, low oil prices, declining capital access, and tax changes, impacted energy companies at every level, including generating significant challenges in attracting and retaining top-tier talent at the board level and in the C-suite.

For board directors, the amount of time required to understand and absorb the constantly evolving governance landscape on top of corporate oversight has roughly doubled in the last five years. Challenges have included:

- Attraction and retention of highly qualified directors and executives who are willing to fully commit to the tasks and invest the time needed to ensure successful outcomes.
- Changing Securities and Exchange Commission (SEC) guidance, which weighs heavily on the middle-market energy industry sectors.
- Financial interest from private equity and other investors and activists created an environment that challenges boards and management.

As a result, energy companies need to evolve their current compensation structures to keep up with the demand for competent executives.

BOARD OF DIRECTORS

The **BDO 600 – 2019 Study of Board Compensation Practices**—which examines the board compensation practices of middle-market energy companies—revealed that the median director retainer has increased by roughly 15% since 2014. However, from 2017 to 2018, energy industry board members experienced an increase in board retainers and fees of only 1%, which was offset by a 20% decrease in committee retainers and fees and a decrease in total equity pay of 6%. These decreases resulted in an overall 3% drop in pay. The mix of pay remained consistent year-over-year—roughly 52% cash and 48% equity for directors. Nonetheless, the overall trend was that full-value stock awards continued to outpace stock options. Stock awards increased 4% over the prior year, whereas stock options decreased 12% and total equity pay increased 2%.

CEO AND CFO POSITIONS

CEO and CFO positions are by far the most vulnerable to turnover in down or volatile markets. A CEO or CFO resignation can send shock waves through a company and can take a considerable amount of time to remedy. Reducing a company's exposure to these potentially catastrophic events greatly depends on sound compensation philosophy accompanied by performance-laden compensation structures and pay deliveries. This is where incentive compensation becomes an integral part of the total direct compensation packages in mid-market public companies. To understand total direct compensation and pay practices in the energy sectors, the **BDO 600 – 2019 Study of CEO/CFO Compensation Practices** examines the total compensation packages of CEO and CFO positions.

The study showed that since 2014, moderate increases in cash year-over-year and full-value equity awards have dominated the compensation packages of both CEO and CFO positions. Overall, the mix has held steady in the last two years with roughly 60% equity-to-cash rewards, which have significant performance hurdles. CFOs realized 41% of total pay compared with CEOs' total pay. Historically, the energy industry CFOs reported the highest average compensation among all industries included in this study. However, in recent years, the energy industry's CEO compensation levels have fallen behind the healthcare, real estate, and technology industries'. In 2018, the energy industry's CEOs experienced a 16% decrease in pay from the prior year, primarily because of highly volatile oil and gas markets and reduced stock prices. This delicate balance can make CEOs and CFOs highly vulnerable targets to competitors. Options such as long-term incentive plans may be under water, which may be why full-value shares with a proper line-of-sight can keep key executives in their seats through a correction or unrealized negative market activity.

With uncertainty dominating the sector, increasing and balancing directors' and executives' compensation is important to maintain stability. **The BDO 600 – 2019 Study of Board Compensation Practices** and **The BDO 600 — 2019 Study of CEO/CFO Compensation Practices** illustrate the need for tailored compensation philosophies, strategic alignment, and long-range objectives in the C-suite.

Contact Us

If you have any questions, comments or suggestions, please contact our Compensation Consulting practice by emailing us at compensation@bdo.com or by calling your local BDO office.

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