

Pay-for-Performance Methodology Overview

Executive pay is closely examined by institutional investors to ensure company practices are aligned with long-term shareholder interest. For this reason, Glass Lewis is committed to providing consistent, data-driven pay assessments that enable our clients to understand how remuneration packages are linked to company performance outcomes. Our proprietary Pay-for-Performance methodology, which serves as the foundation for the Benchmark Policy remuneration analysis, was developed based on our ongoing dialogue with institutional investors, issuers and other market participants to more comprehensively evaluate pay alignment.

This quantitative analysis provides a consistent framework for our clients to determine how well companies link executive pay to relative performance over three to five years. We use this analysis to inform the Benchmark Policy voting recommendations on report proposals. While companies that demonstrate a weaker link (an overall rating of “Severe Concern” or “High Concern”) may be more likely to receive a negative recommendation, other qualitative factors are considered in developing the recommendations. The Benchmark Policy reviews each company on a case-by-case basis and may identify elements that mitigate concerns to a certain extent. These additional factors include, but are not limited to, overall incentive structure, significant forthcoming changes, reasonable short- and long-term payout levels and the operational, economic and business context for the year in review.

Many of the factors that affect a given company’s performance will also affect the rest of the industry. Therefore, executive remuneration should be closely tied to a company’s track record of performance relative to its peers. That is, management should be especially rewarded for directing the company in a manner that outperforms its peers. As such, the majority of the tests in the methodology review company performance against peers.

In determining the peer groups used by the Pay-for-Performance model, Glass Lewis utilises a proprietary methodology that considers both market and industry peers. Each component is considered on a weighted basis and is subject to size-based ranking and screening. Since the peer group used is based on an independent, proprietary technique, it will often differ from the one used by the company which, in turn, will affect the resulting analyses.

[Our pay-for-performance model takes a scorecard-based approach using six tests. Brief descriptions of the tests are as follows:](#)

- Total Vested CEO Pay vs. TSR
 - Relative compared to Glass Lewis peers
 - Five-year weighted average measurement period (three years minimum)
- Total Vested CEO Pay vs. Financial Performance
 - Relative compared to Glass Lewis peers
 - Five-year weighted average measurement period (three years minimum)
 - See below for a breakdown of financial metrics
- CEO STI Payouts vs. TSR
 - STI payout in percentage of maximum opportunity
 - Relative to regional benchmarks
 - Measured over five one-year periods and averaged
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- CEO LTI Payout vs. TSR
 - LTI payout in percentage of maximum opportunity
 - Relative to regional benchmarks
 - Measured over five three-year periods and averaged (three years minimum)
- Alternative Test to Tests 3 and 4 - Multiple of Median
 - Total vested CEO pay vs. company size (market cap, revenues, total assets)
 - Relative to regional peers
 - Alternative may be needed due to sample size and disclosure limitations
 - Are incentives unlimited or are limits not disclosed?
 - Is maximum LTIP payout potential excessive?
 - Is there a short vesting period for LTIs?
 - Are any performance goals not disclosed for awards granted in the year?
 - Are payouts disclosed for the latest year under review?
- Qualitative Test
 - Any one-off awards granted?
 - Any upward discretion exercised?
 - Is fixed pay greater than variable pay?
 - Are incentives unlimited or are limits not disclosed?
 - Is maximum LTIP payout potential excessive?
 - Is there a short vesting period for LTIs?
 - Are any performance goals not disclosed for awards granted in the year?
 - Are payouts disclosed for the latest year under review?

Frequently Asked Questions

Coverage

For which markets do Glass Lewis produce Pay-for-Performance scores?

The Glass Lewis Pay-for-Performance universe comprises companies listed in certain stock indices for each supported region. This universe is reviewed and rebalanced by our research team twice a year.

Country

United Kingdom
Austria
Belgium
Denmark
Finland
France
Germany
Ireland
Italy
Netherlands
Norway
Portugal
Spain
Sweden
Switzerland

Indices

FTSE 350
ATX
BEL 20, BEL MID
OMX Nordic 120
OMX Nordic 120
CAC 40, Euronext 100, Euronext 150
DAX, MDAX
ISEQ 20
FTSE MIB, Euronext 150
AEX, AMX
Euronext 100, Euronext 150
PSI-20
IBEX 35, IBEX MidCap
OMX Nordic 120
SMI, SMIM

Glass Lewis typically does not calculate Pay-for-Performance scores for externally managed companies given that they do not directly compensate their executives. This includes:

- Closed-end funds
- Investment trusts
- Alternative investment funds

Further, companies may be excluded from the Pay-for-Performance universe during the rebalancing process if they:

- Fall out of one of the coverage indices due to:
 - A drop in market capitalization
 - Insufficient liquidity
 - Regulatory non-compliance
 - Financial performance
- Undergo Corporate Actions:
 - Go private
 - Are part of a merger or acquisition
 - Are part of a spin-off
- Voluntarily delist from the relevant index.

In addition, European companies within the coverage universe must generally meet the following criteria:

- They must have three consecutive years of comparable remuneration data available.
- They must have three consecutive years of comparable financial data available, covering a minimum of four financial metrics, including TSR plus three metrics from among ROE, ROA, EPS, revenue, OCF, TBV, and FFO.
- They must have at least ten peer companies (as selected by Glass Lewis) that fulfill the same remuneration and financial data requirements.

Moreover, the following ineligibility conditions apply:

- The company has changed its financial year-end recently; eligibility for a score will resume after three full years of reporting for the new fiscal year-end.

Methodology

Which executive officers' total remuneration is taken into account?

The highest paid executive, who is generally the chief executive officer ("CEO"). However, in some instances the remuneration of an executive chair may exceed that of the CEO, or an executive chair may hold a position that serves in lieu of a traditional CEO role. In such cases, the executive chair's remuneration is used for the analysis.

How is total remuneration defined?

The highest paid executive, who is generally the chief executive officer ("CEO"). However, in some instances the remuneration of an executive chair may exceed that of the CEO, or an executive chair may hold a position that serves in lieu of a traditional CEO role. In such cases, the executive chair's remuneration is used for the analysis.

Why is the Pay-for-Performance analysis focused predominantly on the CEO's pay?

The focus on CEO remuneration stems from several key factors, including prevailing market norms, consistent investor feedback, and extensive industry discussions. Further, the CEO is generally the highest paid executive and typically serves as a proxy for the company's overall pay-for-performance alignment. This position inherently places CEO pay under considerable scrutiny. In many cases, the remuneration outcomes for other executives within a company are tied to similar performance criteria as those applied to the CEO.

Why does the Pay-for-Performance model primarily use vested pay in its European methodology rather than granted pay as in the United States and Canada?

The approach in Europe uses vested long-term incentives (LTIs) to ensure a more meaningful analysis of incentive plan outcomes in direct relation to actual performance results within the relevant period. LTI values are recorded at their vesting date or at the end of the performance period, depending on specific disclosure and applicability of the awards.

This approach aligns with prevailing market norms and expectations in the region, largely influenced by the historical availability of specific disclosure types and the dominant structure of incentive systems in these markets.

Nonetheless, granted pay is still considered when assessing the overall balance and composition of executive pay mix.

How is vested pay captured when this is not disclosed?

In instances where the value of vested long-term awards is not consistently disclosed, such as for many companies based in Switzerland and some in France and the Netherlands, for example, an estimation process is undertaken. This estimation is based on all available information, including the value of the grant, the number of equity instruments granted, the grant date, the disclosed vesting percentage, and/or the level of target achievement upon vesting.

Should a company not disclose sufficient and timely information to conduct a meaningful estimate, it would be considered ineligible for Pay-for-Performance scoring.

How are equity awards valued?

The model conducts its own valuations for both granted stock and option awards.

Time-based and performance-based full value grants are valued by multiplying the number of shares granted by the closing stock price on the grant date. If the grant date does not fall on a trading day, the closing price from the preceding trading day is used.

Within the EMEA region, disclosure practices for performance-based awards can vary, with companies disclosing awards granted based on either target or maximum opportunity. The methodology accounts for these discrepancies where appropriate to ensure a consistent and equitable assessment.

Stock options and stock appreciation rights are valued using the Black-Scholes-Merton model, applying standard assumptions. Please note that the specific underlying assumptions used in these valuations are not publicly disclosed.

How are multiple CEOs in a given fiscal year accounted for?

When a company changes its CEO during a fiscal year, the remuneration paid to both the outgoing and incoming executives is aggregated. Specifically, cash-based payments are pro-rated based on the duration each individual served as CEO, while equity remuneration intended for the CEO role is aggregated in full.

In cases involving co-CEO structures, the total remuneration attributed to the CEO role is captured. This means that the total pay for each co-CEO is aggregated.

How is the remuneration of CEOs who have been in position for fewer than three years treated?

The model utilises the total amounts granted and vested for the CEO for each year under review. Therefore, in cases of a CEO change, the aggregated CEO remuneration will represent a combination of all individuals who served in that role during the specified timeframe, pro-rated for time served.

It is important to note that any vested pay that was originally granted to the current CEO during a period when they were not holding the CEO position is explicitly excluded from this calculation.

Whose pay is used when the CEO is not a member of the board of directors?

The analysis is based on the CEO's pay, irrespective of their board membership status. In a two-tier governance structure – common in some EMEA markets - CEOs would not typically be a member of the supervisory board.

Where an executive board chair is the highest paid executive, our analysis is based on the executive chair's remuneration.

How are severance payments treated?

Severance and other termination benefits that are allocated during the review year are included in the total vested remuneration.

Specifically, within the EMEA and UK markets, termination payments are typically incorporated into the assessment of the total cost of CEO remuneration for a given year. This approach is adopted even when these payments represent contractual entitlements, aligning with prevailing market expectations.

How are disclosures made in different currencies accounted for?

To ensure consistent analysis across different currencies, the model employs specific exchange rate methodologies for remuneration disclosures. The value of equity awards is normalized using the exchange rate prevalent on the grant date, provided this information is disclosed.

For cash remuneration, and in instances where the grant date exchange rate for equity awards is not disclosed, the fiscal year-end exchange rate is utilized for conversion.

This approach ensures that all remuneration figures are presented on a comparable basis within Glass Lewis' analytical framework.

What data are used for companies with shareholder meetings early in the year for whom up-to-date peer data has not yet been publicly disclosed?

For both the reference company and its peers, the most recent publicly disclosed financial and remuneration data are used. This information is generally sourced from Annual Reports and/or other relevant regulatory filings and disclosures available in a particular market.

Please note that the model does not mix remuneration and financial data from different fiscal years, as the primary objective of the Pay-for-Performance analysis is to assess how a company's executive remuneration aligns with its performance during the same period.

What financial performance metrics are used to assess company performance?

The model utilises five indicators of business performance as follows:

- All sectors: Revenue growth, return on equity, and return on assets.
- Sector-specific:
 - Banks/Financials/Mortgage REITs (excluding payment systems GICs): Annualised TBV per share and EPS growth.
 - Equity REITs and specialized REITs (excluding timber REITs and communication tower REITs): FFO growth and operating cash flow growth.
 - All other sectors: EPS growth and operating cash flow growth.

From where are companies' financial performance data sourced?

Financial performance data are provided by S&P Capital IQ.

What timeframes are company performance measures based on?

With the exception of return on assets (ROA) and return on equity (ROE), performance measures are based on a weighted average of one-year, two-year, three-year, four-year, and five-year annualised growth rates.

ROA and ROE are calculated over a single year, specifically as a weighted average of the annual ROA and ROE figures.

How are the Pay-for-Performance metrics, years, and/or tests weighted?

Glass Lewis does not publicly disclose the specific weightings applied to its Pay-for-Performance metrics, timeframes, or tests within its proprietary model.

What influence does a company's Pay-for-Performance score have on the Benchmark Policy's vote recommendations?

The Pay-for-Performance analysis provides a quantitative view of the alignment between a company's pay and performance. This information is considered alongside other qualitative and quantitative factors, including but not limited to, overall incentive structure, significant forthcoming changes, reasonable long-term payout levels and the operational, economic and business context for the year in review. In isolation, the Pay-for-Performance score will not result in a negative recommendation from the Benchmark Policy.

If a company receives a "Severe Concern" rating in the Pay-for-Performance model, will the Benchmark Policy automatically recommend against the company's say-on-pay proposal?

No. A company that receives such a rating will not automatically receive an "Against" recommendation on its say-on-pay proposal. Likewise, a company that receives a favorable rating will not automatically receive a "For" recommendation on its say-on-pay proposal. As noted above, the Benchmark Policy analysis of executive remuneration is based on both a quantitative and qualitative assessment of a company's remuneration practices.

Why are the figures in the CEO Remuneration Breakdown table different from the Summary Remuneration Table figures or the Pay-for-Performance Analysis?

In the Summary Remuneration Table included at the start of the Proxy Paper remuneration report proposal analysis, the figures are presented as disclosed by companies in the audited tables of the document shareholders are called to vote on, aside from slight variations that may be implemented to enhance comprehensibility.

The Pay-for-Performance analysis, however, is the product of a proprietary model. As such, some of the figures presented in the CEO Remuneration Breakdown may be based on internal valuations, thereby differing from the amounts disclosed by companies. Specifically, long-term incentive award valuations will typically differ for companies that disclose these awards on a grant date basis, rather than at vesting. In such cases, the proposal-level information will present granted valuations, while the Pay-for-Performance analysis will present vested valuations. Other elements that may differ typically include bonus deferrals and one-off awards.

How do mergers or acquisitions affect the model's analysis?

Glass Lewis may exclude a company's Pay-for-Performance analysis or growth rate calculation if there are M&A transactions that would impact the consistency of the financials used to calculate growth rates.

Peers

How are peer companies selected?

Peer groups are generated through a proprietary methodology that considers both industry and geographic region. For the Pay-for-Performance analysis, the model utilises the top 10 to 15 peer companies identified through this process.

When does Glass Lewis update its market peers?

Glass Lewis updates peers twice a year.



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