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Performance-Based Equity:
Shifting Viewpoints?





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Performance-based equity has been a key element in aligning executive pay with business goals and shareholder interests, and historically viewed favorably by shareholders. While we expect that to continue, shareholders and shareholder advisory firms (e.g., ISS) are beginning to apply greater scrutiny on award designs, particularly when they are overly complex and difficult to evaluate.

Given this, how should companies assess performance awards going forward? This article will explore:

- What's driving the increased scrutiny on performance awards
- Best practices to designing performance awards to mitigate potential external scrutiny
- Market outlook and expectations

What's Driving This Change?

Both ISS and certain shareholders have signaled increased focus on performance award structures:

ISS Concerns Over Performance-Based Equity Design

In 2025, ISS emphasized the following in its qualitative assessment of performance awards:

- Non-Disclosure of Forward-Looking Goals: Failing to disclose performance targets upfront reduces transparency and accountability
 - Note: Companies must delicately balance concerns with competitive harm vs. investor needs to assess the rigor and alignment of incentive plans with shareholder interests
- Unclear Vesting Outcomes: Poor disclosure prevents assessment of plan effectiveness and payouts
- Unexplained Metric Changes: Adjusting metrics and/or targets mid-cycle without clear justification raises concerns about goalpost shifting
- Excessive Pay Opportunities: Large maximum payouts may encourage excessive risk-taking rather than long-term growth
- Weak Performance Goals: Goals that are too easily achievable undermine shareholder value creation
- Overly Complex Structures: Lack of clarity on award design can reduce investor confidence

ISS' Evolving Views on Time-Based Equity

The 2026 policy updates also clarify that an equity program composed solely of time-based awards will not raise significant concern, provided the awards have a sufficiently long-term vesting horizon. That said, ISS continues to view performance-based equity as an effective tool for aligning pay and performance.

Example of Shareholder Scrutiny: Norway's sovereign wealth fund, the world's largest, explicitly favors time-based equity over performance-based awards, citing complexity and misalignment concerns. It has opposed multiple high-profile pay packages, arguing that performance-based equity structures often fail to deliver clear, shareholder-aligned incentives.



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Potential Practices to Mitigate Scrutiny

If your company grants or plans to grant performance-based equity, provided below are a few tools to ensure awards are designed in a way that's aligned with business and shareholder interests, while also minimizing or avoiding potential external scrutiny.

✓ Use Simple, Clear, Business-Relevant Metrics *(that are understood by employees/shareholders)*

- Tie performance directly to clearly-defined, straightforward metrics that are aligned with the company's long-term business plan and strategy
- Clearly disclose how selected metrics support long-term value creation

✓ Set Rigorous, Quantifiable Goals

- Use performance targets that are challenging but achievable, tied to the budget or long-range plan shared with investors
- In setting goals, also consider aligning with any external guidance previously provided

✓ Evaluate in Light of Uncertainty

- Simplify program design to improve clarity and goal-setting during periods of volatility
- Given ISS's updated feedback on long-term time-based equity, assess whether heavy reliance on performance-based equity is necessary or if a balanced mix is more effective
- Evaluate how performance is measured (i.e., shifting from a single multi-year performance period to multiple one-year performance periods)

✓ Strengthen Proxy Disclosure

- Clearly define goals, payout structures, and rationale in annual Proxy statement
- Justify any mid-cycle adjustments to prevent concerns about goalpost shifting

Market Outlook and Expectations

Despite the increased focus on performance award design, we are not expecting a significant shift away from performance awards, as these awards can be effective tools in aligning executive and shareholder interests (recognizing a minority of companies may shift a greater portion of equity to time-based awards with longer-term vesting).

With that said, going forward, companies should consider the following:

- Re-evaluating whether performance-based equity structures truly drive shareholder value as designed or have been granted to simply "check-the-box"
- Avoiding unnecessary complexity that raises investor concerns
- Relying on thorough disclosure to ensure performance awards are transparent and well-understood



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