

Analysis of compensation policies for executives and directors of bio-pharmaceutical companies in the context of the global spread of COVID-19

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Abstract. This paper analyzes the AbbVie, Pfizer and Johnson&Johnson biopharmaceutical industry companies in the context of the spread of COVID-19. There have been articles using 3P1M to study compensation patterns in other industries and it is necessary to use 3P1M to analyze compensation policies of biopharmaceutical companies in order to motivate employees or directors as COVID-19 affects people's health around the world. Firstly, this paper using the quantitative analysis method compared the three companies' differences of executive compensation about 3P1M and summarized the similarities of them. They have similar philosophies of their compensation policies in three aspects. And the executives of these three companies receive retainer but the components of their cash compensation are different. Among 3P1M, the most different part of 3p1M is their compensation incentive policy that related to executives' performance. Secondly, this part analysis and compared the similarities and differences of the components of director compensation policy by aspects of the retainer that paid to different board members, incentive grants, stock ownership guidelines.

Keywords: Compensation policy; Bio-pharmaceutical companies.

1. Introduce

Over the past two years, the financial market, which is the most direct reference of the market economy, has experienced drastic fluctuations due to the spread of COVID-19 worldwide. For example, during the period of the outbreak of the epidemic in 2020, the US stock market was "circuit breaker" for four times, and the stock markets around the world experienced a sharp decline. Meanwhile, some components of the stock prices of the medical and biological industry even rose more than the market, which is enough to prove that biopharmaceutical companies are receiving more and more attention. Especially in the COVID-19 outbreak, the production efficiency and innovation capacity of biopharmaceutical companies to a certain extent determine the efficiency of people's prevention and control. The productivity and innovation ability of enterprises are also highly correlated with salary policies, except that they are affected by uncontrollable external factors.

Prior to this, there have been a lot of studies on the benefit growth of biopharmaceutical companies, such as incentive policies for employees. For example, Li Hao published a research on eva-based performance evaluation of a biopharmaceutical company. He stated that EVA (economic value added) can be used to evaluate the performance of enterprises to better understand the perfor

Mance indicators and promote the value improvement of enterprises. This paper describes the relationship between performance measurement and performance improvement in a biopharmaceutical firm. The evaluation of performance indicators is a part of the compensation policy. In addition, Liu Yun has researched the importance of improving the employee compensation system and specific optimization methods in the article "BY Salary System Optimization research of Biopharmaceutical Company"[1]. This article pointed out in detail BY the company employees pay policy currently existing problems and gives good suggestions.

However, I think the research on one company is not representative enough. Before pointing out the problems, comparing and summarizing the similarities and differences of compensation policies of several top biomedical companies will be more conducive to the subsequent discussion of existing problems. For biological pharmaceutical companies, for example, if give employees and directors

incentive wages accounted for the proportion of total wages is too large, they may focus on the company's short-term benefits rather than its long-term development. However, if this proportion is too low, there may not be enough incentive for employees and directors and it is harmful to the biopharmaceutical enterprises. Moreover, the proportion of incentive salary to total salary is only a part of the compensation policy for employees and directors. There are many other factors that will affect the production efficiency of biopharmaceutical enterprises.

Therefore, in the background of the spread of COVID-19, this essay will compare and analyze in depth the correlation between the compensation policies of employees and directors of several top biopharmaceutical companies and the production efficiency of enterprises. Through these comparison and analysis, it can be found that the existing problems of the current salary policy can also provide a reference for all biopharmaceutical enterprises in other markets to formulate a salary policy.

2. Data and Method

2.1 Method

Based on the sales volume, turnover and stock price data of AbbVie, Pfizer and Johnson & Johnson biopharmaceutical companies, this paper analyzed the compensation policies of employees and non-employees directors of these companies using case study, quantitative analysis and literature research method [2]. It is generally believed that the common ground of three or more companies in the same industry can be regarded as a common rule of this industry to some extent, which is worth studying. Therefore, this paper chooses to study AbbVie, Pfizer and Johnson & Johnson, three of the world's top biopharmaceutical companies [3]. This paper analyzes the rationality of the compensation model of the three companies in combination with 3P1M modern compensation payment model in four aspects, they are employee position, performance, person and market. This text reveals the similarities and differences between the salaries of ordinary employees, senior executives and non-employee directors of the three companies through the mutual comparison of quantitative analysis method, and considers their respective positions in the overall project.

2.2 DATA

AbbVie, Pfizer and Johnson & Johnson are among the world's top biopharmaceutical companies. Johnson & Johnson was among the top ten most enviable firms in the United States and placed 20th globally in Fortune and Business Week's 1997 market value index rankings [4]. Pfizer Inc. was established in 1849 and has a long history. Pfizer, a biopharmaceutical firm with its corporate headquarters in New York, is a science-based, patient-focused business. And ABBVIE ranked 247th on the 2021 Fortune Global 500 list in 2021. As a global research-based biopharmaceutical company, it has nearly 30,000 employees worldwide and it sells its products to more than 170 nations and regions.

3. Result and discussion

This part will focus on three main points, the similarities and differences of executive compensation in 4 different views, them of directors and compensation policy of biopharmaceutical companies.

3.1 The similarities and differences of executive compensation of the three companies and the reasons are analyzed from the aspect of 3P1M.

First of all, the three companies formulated compensation policy for their executives based on similar philosophies in the following aspects.

Provides the compensation and incentives necessary to recruit, motivate, and retain important leaders who are essential to a company's long-term success. Aligns each executive's compensation with the short- and long-term performance of the company.

We are driven to achieve near-term preferred benchmark compensation in comparison to our pharmaceutical peers and general industry comparison groups in order to determine compensation target levels and determine the value and level of incentive opportunities. This is done by taking into account the company's market capital and complexity (through revenue, product range, international operations, and other factors). This will be discussed in more detail in the Market section pf 3P1M [5].

Position: Because the positions discussed in this part are all executives, this part only analyzes the executive cash compensation of these three companies, which is the fixed part that can be obtained as an executive and the benefits that provide to all executives with reasonable limited rules.

The compensation committee of these three companies believe that it is a suitable base wage amount to ensure their companies can draw and keep a leadership group. In the same time, it is important in sustaining long-term profitable growth for our stockholders in some extent. Base salary at Johnson Johnson and Abbvie accounts for an average of just 14% of total revenue and it's of Pfizer is 18% in their 2020 Proxy Statement. As these data, compared with Abbvie inc and Johnson& Johnson inc, Pfizer inc believes the appropriate percentage of cash is larger, it can ensure that our program structure has an acceptable balance to reduce compensation-related.

The benefits of all three companies include pension plans and Supplemental Pension Plan that, an unqualified supplementary pension plan. However, the details of them vary from company to company. For Abbvie inc, the primary qualifying defined benefit plan of the company is its pension plan.

The majority of AbbVie employees working in the United States who are age 21 or older are covered by the broad-based Pension Plan of AbbVie, which offers participants a life annuity benefit at normal retirement equal to 1.10 percent of 5-year final average earnings times years of benefit service after 2003 plus other factors. A maximum of 35 years of benefit service is allowed, and the final average earnings of AbbVie are based on the average of the employee's 60 highest-paid consecutive calendar months of pay (salary and non-equity incentive plan compensation). Up to the IRS's covered compensation limit, Johnson & Johnson's Salaried Pension Plan uses the U.S. pension formula to calculate payments. In 2021, the cap was \$290,000. Out of the last 120 pay periods, the highest 60 consecutive months make up the final average earnings. Because the base salary and annual incentive payments are included in earnings, the average of it is less than AbbVie inc. Pfizer's pension earnings are the highest yearly bonus and salary average for the previous five calendar years.

Performance: The majority of three companies' executives' pay is performance-based, it includes long-term incentives pay and short-term incentives pay. The percentage of incentives pay of AbbVie, Pfizer and Johnson Johnson are 74%, 86% and 82% respectively [6].

Short-term incentive pay: Short-term incentive pay play a vital role in Motivating attainment of companies near-term priorities. Besides, to achieve our purpose, financial objectives, and leadership behaviors, executives' interests should be directly aligned with AbbVie's yearly operating strategies. The percentage of Short-term incentive pay of AbbVie, Pfizer and Johnson Johnson are 29%, 17%, 16%. It is clear that AbbVie inc occupied the highest percentage of it [7]. Through AbbVie's Performance Incentive Plan, executives receive annual monetary incentives (PIP). AbbVie sets its executive target incentive amounts at a proportion of base pay. The first step in calculating performance is to compare performance to weighted financial and leadership goals. The compensation committee then decides on final awards based on a qualitative evaluation of overall performance.

Long-term incentive pay: Through AbbVie's Performance Incentive Plan, executives receive annual monetary incentives (PIP). AbbVie sets its executive target incentive amounts at a proportion of base pay. The first step in calculating performance is to compare performance to weighted financial and leadership goals. The compensation committee then decides on final awards based on a qualitative evaluation of overall performance. These three companies' long-term incentive pay includes performance shares and the AbbVie, Pfizer and Johnson& Johnson accounts for 29%, 17%, and 16% of the total long-term pay in 2021. All of these companies' vesting period are 3 years but

there are some differences among them. The formula of Performance Share Awards percentage earned and delivered in cash of Pfizer is average of the three annual net income Performance Factors $\% + 1.5 \times$ the first 20 percentage point differential between Pfizer's TSR % and DRG Index TSR % $+ 2.0 \times$ the differential over 20 percentage points. In the same time, it is also worth to notice that half of Performance Share Awards is earning per shares, it is 3-year Cumulative Adjusted Operational EPS. And another half of it is relative total shareholder return, it is the Competitor Composite Peer Group's 3-year Compound Annual Growth Rate. In addition to the same part, AbbVie and Johnson & Johnson both have non-Qualified stock options, the percentage of them occupied 20% and 10%. However, their vesting way and period are different. As for AbbVie inc, depending on whether the recipient stays employed by the company, these awards could vest in thirds on each of the first three anniversaries of the grant date. On the grant date, the option exercise price is set at or above fair market value. For Johnson & Johnson, these share units will 100% vested 3 years after grant [8].

Person: Some objectives, such as leadership and progress toward long-term and strategic goals, are challenging to gauge using formulaic or numerical criteria. Therefore, in order to make sure that the overall evaluation of performance and pay decisions are in line with the company's actual performance over time, the compensation committee also performs a qualitative review of individual performance.

The similarities of three companies' compensation policy about personal circumstance is they all have Clawback Policy.

The committee doesn't believe there will ever be situations in which there is a restatement of results upon which any incentive plan award determinations were based or in which an executive officer violates the AbbVie Code of Business Conduct in a way that is material. However, the committee has wide latitude to take any measures required to defend the interests of stockholders, up to and including measures to reclaim incentive payments, when assessing such circumstances. The Board of these three companies can recoup all or part of any compensation paid to an executive officer in these following situations. Firstly, when executive Officer was paid based on the original financial statements even though it appeared he or she had not met financial performance goals according to the restatement. Secondly, the accountability of any executive officer whose acts or omissions, where such actions or omissions constituted misconduct, were accountable, in whole or in part, for the events leading to the restatement.

Market: The similarities of three companies' compensation policies about market is their executives' pay based on survey and open data on our peer companies in the pharmaceutical industry and the general industry comparator groups. However, the lists of other companies they compare to and the projects they focus are different. The committee of AbbVie focuses on the Health Care Peer Group because its members are AbbVie's main competitors for executive talent and because its members share critical traits with AbbVie. This committee use the pay levels of AbbVie's Health Care Peer Group to analysis their executives' compensation practice. Additionally, the Pfizer inc focus on both General Industry Comparators and Pharmaceutical Peers (a diverse range of pharmaceutical enterprises) (broad mix of large, non-pharmaceutical, multi-national companies of similar size and complexity). Using the median compensation values of their comparator groups, Pfizer Inc. develops a competitive pay framework to help determine the ideal pay mix of base pay, annual short- and long-term incentive targets and the peer data is used to analysis annual benchmark and source for potential talent. Besides, Johnson & Johnson set lists of Executive Peer Group and Competitor Composite Peer Group, in order to evaluate the executive officers' compensation for competitiveness and evaluate the relative performance of company respectively.

3.2 The similarities and differences of the components of director compensation policy of these three companies

This part will focus on the retainer that paid to different board members, incentive grants, and stock ownership guidelines

Retainer Similarities: The similarities of three companies' compensation policy is their lead director cash compensation are \$50,000. The Audit Committee Chair Cash Retainer of Pfizer and Johnson & Johnson are \$30,000 per year, but it of AbbVie is less than others, which is \$ 25,000 per year. And it is worth to notice that the audit committee members of Pfizer and Johnson & Johnson do not earn any further compensation; only AbbVie's members received \$500 for each month they served on the committee.

Differences: All of these three companies give annual cash to their non-employees directors, the amount of cash compensation of AbbVie, Pfizer and Johnson & Johnson are \$115,000, \$142,500 and \$125,000 per year respectively. Among them, only Pfizer inc pay the cash compensation quarterly and directors have the option to defer all or part of their yearly cash salaries until they leave the Board.

Incentive grants Similarities: The Incentive Stock Program of three companies are different, but these program makes each non-employee director's benefits entirely tied to the benefits of the company as a whole, which can effectively encourage each director to prioritize company first [9]. If directors' private interests in any way interferes with the interests of company, the "conflict of interest" will exists. There is no doubt that, when each directors give priority to their own short-term benefits rather than working together, it will be detrimental to the long-term development of company.

Differences: The restricted stock units in the AbbVie Incentive Stock Program have target grant date values and vested restrictions. After rounding the award to the closest whole unit, this amounted to 1,681 restricted stock units, with a reportable value of \$194,904 in 2021. By multiplying the number of units given by the average of the high and low market values of one share of AbbVie common stock on the award grant date, AbbVie derives the grant date fair value of the awards.

Besides, based on the common stock of Pfizer's closing price on the final business day of the fiscal quarter in which the retainer is earned, the number of Pfizer stock units is determined. The value of any dividends on the common shares is used to determine how many more stock units are added to a director's account. Fee Plan for Directors of Johnson & Johnson, non-employee Directors received 1,123 DSUs each (rounded down to the nearest whole share). DSUs are immediately vested but must be postponed until the Board member's resignation.

Stock ownership guidelines Similarities: The shareholding rule of three companies all require their director hold 5 times the annual cash retention rate in the stock ownership guideline. Among them, the non-employee director of AbbVie must own AbbVie stock within five years of joining the Board or as soon as practicable after five times (5x) the annual director fee under the AbbVie Non-employee Director Fee Plan. The Pfizer and Johnson & Johnson inc give the similar stock ownership guidelines of AbbVie, it required to own Pfizer common stock and/or deferred stock units with a value of at least five times their annual cash retainer but their cash retainers are different as mentioned before.

Differences: As for the Pfizer inc, new directors are subject to milestones toward this requirement and the non-employee directors may choose to delay units issued in the immediately next year or to receive the equivalent in shares each year if they have satisfied the stock ownership criteria as of December 31 of the preceding year. And the shareholding rule of Johnson & Johnson, non-employee Directors of Johnson & Johnson have to wait five years after becoming initially subject to the rules before reaching the necessary ownership threshold [10].

4. Conclusion

Based on a large number of literature research, this paper summarizes the research status of compensation policies of three leading international biopharmaceutical companies in the context of the spread of COVID-19. Firstly, this paper have analyzed these three companies' compensation policies of their executives from 3P1M aspects. Among them, all of their positions are executives and the pension plans' benefits of these three companies are similar. However, their annual retainers and the details of their pension plans are different. The second P is performance, their executives' pay at

all three companies is mostly performance-based but the distribution ratio of short-term incentive compensation and long-term incentive compensation are varies. The third P is person ability, the similarities of this part is they all have Clawback Policies. And the M is market, they refer to the compensation policies of relevant companies in the market when formulating their own compensation policies.

Secondly, this paper have analyzed the components of director compensation policy of these three companies from their retainers, incentive grants and stock ownership guidelines.

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