



# EUROPE

## Evaluating Pay for Performance Alignment Implementing a P4P Model

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## Executive Summary

In 2016, ISS introduced for the first time a quantitative pay-for-performance (P4P) assessment for the largest European companies and (more recently) [Australia](#). We have sought to leverage the common features of the ISS pay-for-performance models implemented in the [US](#), and [Canada](#), where appropriate. The approach has been adapted as necessary to fit the European context, notably in relation to the construction of peer groups and the pay calculation methodology.

ISS differentiated the European peer group approach from our US and Canadian models in one key way: by adopting a banded approach to market pay levels for the European model. With the 2016 introduction of the European P4P, the European approach solely used ISS-selected peers. Based on feedback from both investors and issuers, as of 2017, the European model also uses company-selected peers as part of the peer group construction process. Additionally, the pay methodology is based on realised pay, while the US, Canadian, and Australian models use granted pay. The rationale for these differences is explained in more detail later in this document.

For ISS benchmark voting guidelines, assessment of remuneration for European (including UK & Irish) companies follows the ISS Global Principles on Executive and Director Compensation as detailed below:

1. Provide shareholders with clear, comprehensive compensation disclosures;
2. Maintain appropriate pay-for-performance alignment with emphasis on long-term shareholder value;
3. Avoid arrangements that risk “pay for failure;”
4. Maintain an independent and effective compensation committee;
5. Avoid inappropriate pay to non-executive directors.

The ISS European pay-for-performance model provides quantitative elements, which consider both relative P4P alignment compared with peer groups and absolute P4P alignment. The methodology is described in this paper, and, like our P4P methodology for US and Canada, it incorporates models for RDA (Relative Degree of Alignment) MOM (Multiple of Median), and PTA (Pay-TSR Alignment). In 2020, ISS added a supplemental evaluation of Economic Value Added (EVA) performance of companies versus peers – the methodology for this test is also described in this paper.

It is important to emphasise that the inclusion of the European pay-for-performance model to ISS benchmark research reports is additive and is intended to provide additional data points for comparability. Therefore, while the P4P model is based on realised pay, the additional qualitative review by ISS research analysts will continue to take into account both the granted and realised elements of remuneration during the year under review. The qualitative factors that ISS also considers in its holistic analysis of pay in each specific market or region are discussed in the separate ISS European and United Kingdom & Ireland benchmark policies.

The European P4P coverage universe began with the STOXX Europe 600 and was expanded in 2017 to include 600 additional companies from the main European local market indices including the UK FTSE All-Share (ex-investment trusts). In 2021, the coverage was expanded again to include roughly 400 additional “widely-held” companies in certain covered countries primarily in the Nordic and Germanic regions. Overall, with the addition of companies added to coverage over time as part of the above index groups, as of to date this represents roughly 1,800 European publicly-traded companies covered under the P4P model.

Further information is available by contacting ISS through the [ISS Help Center](https://issgovernance.service-now.com/csp) (<https://issgovernance.service-now.com/csp>).

## Introduction

The current ISS pay-for-performance (P4P) model for the US was launched in 2012 and was implemented for Canada in 2013. Feedback from institutional investors identified significant interest in a quantitative pay-for-performance model for Europe. The 2014 ISS Policy Survey noted that 83 percent of investors who responded indicated that they supported the development of a European pay for performance quantitative methodology, including the use of peer group comparisons. Considering this feedback, ISS embarked on launching a standardized P4P model for the European market.

However, ISS recognises that remuneration disclosures across the various European markets are more diverse than in the single markets of US and Canada, and that there are certain local market practices which mean that elements of the US and Canadian quantitative methodologies need to be adapted to be appropriate for the European context. Two particular challenges within the European context are (1) most pay disclosure practices are market-specific, and (2) there has been significant evolution of different and often varying market practices in recent years. These challenges have been addressed as part of the development of the model.

The purpose of ISS' pay-for-performance evaluation is to measure the alignment between pay and performance over a sustained period. ISS' P4P quantitative assessment is designed to measure such alignments, based on both relative and absolute pay-performance evaluations.

## The ISS P4P methodology delivers a common, global approach

The quantitative methodology utilises two components:

- **A relative evaluation** – rankings of CEO pay and performance relative to peer companies.
- **An absolute evaluation** – CEO pay relative to shareholder return for the subject company.

Both are considered from an investor's perspective in evaluating the efficacy of top executive pay packages over time. For the relative evaluation, peer groups are designed not for pay benchmarking or stock-picking but rather to compare pay and company performance within a group of companies that are reasonably similar in terms of industry profile and size.

The evaluation focuses on the realised pay for the lead executive, typically the CEO, for the period under consideration, although it is important to note that the three different models measure pay over three different time periods (typically one, three, and five years for the MOM, RDA, and PTA models respectively). To keep things simple, for the rest of the document, we will refer to this as total CEO pay, as this is what has been analysed in the vast majority of cases.

## What We Measure -- Pay

All figures in the European P4P model are based on realised (i.e. vested) not granted pay. The CEO's total remuneration includes the cash and benefit values actually paid, and the value of any amounts "realised" (i.e. exercised or earned due to satisfaction of performance goals) from incentive grants made during a specified measurement period, based on their value at the end of the measurement period.

This is one area where the European implementation differs from our US and Canadian approach, which uses a granted pay definition. During the development of the model, the ISS European research team reviewed how pay is typically disclosed in each market and the outcome was that a model based on realised pay was determined to fit better with the general direction of pan-European market practice; this conclusion was subsequently tested and verified with a number of our institutional investor clients during the model development phase.

One example of the trend towards looking at realised pay rather than granted pay, is the Deutscher Corporate Governance Kodex, the German Corporate Governance Code, which in its 2013 version added a recommendation that listed companies disclose management board pay both on a realised basis and on a granted basis (previously pay disclosure was generally recommended without specific guidelines, leading the majority of companies to disclose granted pay data only). Another example is the introduction of the UK Single Total Figure table, which was brought in for large and medium-sized companies in 2013, and, per updated guidance released in 2016, requires the following disclosure<sup>1</sup>:

*The annual remuneration report must include a table showing the single total figure of remuneration for each director for the reported year and the financial year before that. The company may disclose the information for executive and non-executive directors in separate tables.*

*The table must include, for each of the two years, a total figure and show the breakdown of that figure by disclosing figures for distinct components including: base salary; taxable benefits; short-term incentives (including any deferred component); long-term incentives vested in the year; pension related benefits; any other items in the nature of remuneration and any sum recovered or withheld during the year in respect of amounts paid in earlier years. The table may also include such other information as the directors determine.*

*In relation to short-term and long-term incentives, there must be disclosed after the table details of the performance measures used, the performance targets set at the beginning of the performance period and details of actual performance achieved.*

*Where any discretion has been exercised in respect of a short-term or long-term incentive that vested in the reported year, details of how the discretion was exercised and how the level of award was determined must be given.*

It is important to note that the qualitative review undertaken by ISS research analysts in ISS proxy voting reports will continue to take into account both granted pay and realised pay. Both views of remuneration practices are valuable to institutional investors, as they answer fundamentally different questions which are forward-looking (granted) and retrospective (realised) in nature.

### Calculating a European single total pay figure

The European P4P model calculates a single total figure based on the CEO's realised pay for the year under review.

Where a suitable single realised pay figure is not available from the current company disclosures, ISS has created a model single total figure based on knowledge of local market practices. In certain markets where the standard is still to report only granted pay values, the local ISS Research teams are involved in identifying consistent handling rules to create consistent realised pay figures for the year under review. Where company disclosure is considered too limited to permit this, a company may be excluded from the model for poor disclosure.

If a company wishes to see how its total pay figure was calculated, it can request this information through the [ISS Help Center](https://issgovernance.service-now.com/csp) (<https://issgovernance.service-now.com/csp>).

<sup>1</sup> As referred to on Page 9 of the GC100 and Investor Group Directors' Remuneration Reporting Guidance 2016

In the markets covered by ISS European policy<sup>2</sup> the pay components which contribute towards the overall single figure for total CEO remuneration are listed in the table below, with a discussion of how each item is interpreted.

**Figure 1. Elements of Pay in the Continental Markets**

Item	Commentary
Base salary	The annual base salary received for the last financial year, as reported in the emoluments table (or equivalent) in the financial statements.
Perquisites	The cost or estimated value of other benefits, for example, private health insurance.
Pension	The 'pension costs' for the last financial year, as reported in the emoluments table (or equivalent).
All other compensation	All other compensation is a category which can be used for payments that do not fit into any other category, for example, severance pay.
Cash bonus	Bonus earned for the last financial year as reported in the emoluments table (or equivalent) in the financial statements, or otherwise disclosed.
Deferred/share bonus	The portion of the annual bonus that has been earned and will be deferred, assuming that the deferred portion is not subject to any further performance conditions, other than continued employment. In addition, payments from previous bonus deferrals should be included, in case these have been subject to performance conditions.
Non-equity incentives	Non-equity incentives refer to cash-settled LTIPs.
Restricted stock	Share-based payments should reflect the value of share awards vesting over the prior year (so "realised" or take-home equity-based pay). If it concerns non-performance-based stock awards, the value at grant date will be used.
Options	This includes both take-home pay from non-performance-based as well as performance-based stock options vesting during the year (or potentially exercised). Options will be valued using intrinsic value (exercise price minus market price) because changes in the fair value of the award after vesting generally reflect investment decisions made by the executive rather than remuneration decisions made by the company.

For the UK, the figure for total CEO remuneration uses the single total figure disclosed by the company, and many of the largest Irish and Jersey companies tend to use the UK single total figure disclosure format. For the small number of companies who do not, a "synthetic" single total figure has been calculated from the individual remuneration elements as in the European example.

### Exclusions for poor disclosure practices

All subject companies underwent a data quality review after the data available had been collected by ISS from the company materials, to ensure that the overall pay figure could be calculated in a consistent fashion for all companies in a market. For the European P4P model to produce a valid and relevant output, the model requires at least three years of pay disclosure. As part of this review, a minority of subject companies were found to have such poor disclosure practices that they could not be included in the model. The companies which were excluded were

<sup>2</sup> Austria, Belgium, Denmark, France, Finland, Germany, Greece, Italy, Luxembourg, the Netherlands, Norway, Portugal, Spain, Sweden, and Switzerland.

from a variety of markets and sectors, and the review concluded that these exclusions were largely due to company-specific inadequate disclosure practice rather than such poor disclosure being typical of a specific market or sector.

## What We Measure -- Performance

**Total Shareholder Return (TSR).** There are, of course, myriad ways to measure corporate performance, and key metrics may vary considerably from industry to industry and from company to company depending on their particular business strategy at any given time. Investors expect that incentive plan metrics will stem from that strategy and be designed to motivate the behavior and executive decisions that will lead to its successful execution, but the one key common measure for investors in the context of a long-term pay-for-performance evaluation is total shareholder return (TSR).

We would note that this does not imply that ISS advocates for companies using TSR as the single metric underlying their incentive programs; many companies and shareholders may prefer that incentive awards be tied to the company's business goals more broadly than TSR. However, if a company's business strategy is sound and well executed, the expectation is that it will create value for shareowners over time, and this will generally be reflected in long-term total shareholder returns. TSR is therefore the primary measure used in ISS' quantitative pay-for-performance alignment models. Various other financial and operational metrics are also considered when company practices and remuneration decisions are analysed as part of the qualitative review undertaken for ISS proxy research reports.

In 2018, ISS changed the way in which TSR is calculated for the purposes of the P4P model by switching from a point-to-point calculation, where TSR is determined by the closing price (adjusted for dividends) at the beginning and end of the measurement period, to a calculation that takes the monthly *average* closing price at the beginning and end of the measurement period (with the closing prices also adjusted for dividends). The purpose of this change to using monthly averages was to limit the impact of sudden and short-term daily fluctuations in stock price and better reflect the true movement in the asset value over the period. The TSR data used in the European pay-for-performance model is provided by the same data vendor (S&P/Compustat XpressFeed).

**Economic Value Added (EVA).** Investors have indicated to ISS that TSR should be the primary consideration when evaluating performance in the pay-for-performance context. However, investors have also indicated that it is appropriate to supplement TSR with other financial metrics to assess long-term performance. Accordingly, in addition to TSR, ISS is exploring the potential for future use of Economic Value Added (EVA) measures to add additional insight into a company's financial performance. To that end, EVA measures are displayed in European ISS research reports, although not as part of the pay-for-performance screen – i.e., they are for display-only and are not currently used as a scoring element.

The four EVA metrics displayed are: EVA Margin, EVA Spread, EVA Momentum vs. Sales, and EVA Momentum vs. Capital. EVA Metrics are calculated by ISS EVA and are based on audited financial data reported in public filings. The selection and display of these metrics should not be interpreted as ISS' suggestion that EVA metrics or other particular metrics should be used to form a company's compensation program. Rather, the metrics add supplemental view of company performance and pay alignment from a shareholder value perspective.

For more information on the EVA methodology and metrics, please see the [Appendix](#). You may also visit the ISS EVA Resource Center, at: <https://www.issgovernance.com/solutions/iss-analytics/iss-eva-resource-center/>.

## What We Measure -- Relative and Absolute Alignment Over Time

In 2011, a substantial majority of institutional investor respondents to ISS' policy survey confirmed two factors as important in determining pay-for-performance alignment: pay relative to peers (considered very relevant by 62

percent of investor respondents), and pay increases that are disproportionate to the company's performance trend (considered very relevant by 88 percent of investor respondents). A majority of company (issuer) respondents also indicated these factors as at least somewhat relevant to a pay-for-performance evaluation.

In light of this and similar feedback from roundtables and other discussions forums, ISS incorporated both perspectives into the quantitative component of its pay-for-performance analysis when developing the US pay-for-performance approach which was launched in 2012. This ensures a balanced evaluation from both relative and absolute pay-for-performance perspectives.

## ISS' Evaluation of Pay-for-Performance Alignment

### Measures of Pay-for-Performance Alignment

At the core of the methodology are three measures: two *relative* measures where a company's CEO pay magnitude and the degree of pay-for-performance alignment are evaluated in reference to a group of comparable companies, and one *absolute* measure, where alignment between executive pay and company performance is evaluated independently of other companies' performance.

The three measures are:

- **Relative Degree of Alignment.** This relative measure compares the percentile ranks of a company's CEO pay and TSR performance, relative to an industry-and-size derived comparison group, over a three-year period.
- **Multiple of Median.** This relative measure expresses the prior year's CEO pay as a multiple of the median pay of its comparison group for the most recently available annual period.
- **Pay-TSR Alignment.** This absolute measure compares the trends of the CEO's annual pay and the value of an investment in the company over (typically) the prior five-year period.

### Measures of Relative Alignment

#### Relative Degree of Alignment (RDA)

This measure addresses the question: Is the pay the CEO has received for the period under review commensurate with the performance achieved by the company in the same period, relative to a comparable group? The measure compares the percentile ranks of a company's CEO pay and TSR performance, relative to a comparison group of 12-24 companies selected by ISS on the basis of size and industry over a three-year period.

To determine this measure, the subject company's percentile ranks for pay and performance are calculated for the three-year period. Because of the sensitivity of TSR to overall market performance, annualised TSR performance for all companies will be measured for the same period.

Combined percentile ranks for pay and for performance are calculated, and the Relative Degree of Alignment is equal to the difference between the ranks: the combined performance rank minus the **combined pay rank**.

**Figure 2. Example of Calculating RDA Score**

	Performance %ile Rank	Pay %ile Rank	Difference
3-Year	32	59	-27



Values for the Relative Degree of Alignment measure range between -100 and +100, with -100 representing the high pay for low performance (i.e., 100<sup>th</sup> percentile pay combined with 0<sup>th</sup> percentile performance), zero representing a high degree of alignment (the pay rank is equal to the performance rank), and positive values representing high performance for low pay.

If a subject company does not have 3 years' worth of data, then RDA will be run in either 2 or 1-year scope, depending on the number of years of data the subject company has available and the trading history of the company. For companies with a trading history of three years or more, a minimum of three years of pay data is required for the company to be included in the model.

### **Multiple of Median (MOM)**

This measure addresses the question: Was the CEO paid significantly more in the last year than his or her peers in the comparison group? To calculate this measure, the company's one-year CEO pay is divided by the median pay for the comparison group.

## **Measure of Absolute Alignment**

The absolute alignment test is intended to compare pay and TSR trends to determine whether shareholders' and executives' experiences are directionally aligned.

### **Pay-TSR Alignment (PTA)**

PTA is a long-term measure of directional alignment. It is important to note that it is not designed to measure the sensitivity of CEO pay to performance – i.e. whether pay and performance go up and down together on a year-over-year basis.

The measure is calculated as the difference between the slopes of weighted linear regressions for pay and for shareholder returns over a five-year period. This difference indicates the degree to which CEO pay has changed more or less rapidly than shareholder returns over that period.

The regressions that calculate Pay and TSR trends are weighted least-squares regressions of pay and TSR against the independent (x) variable time. Because the timing of the measurements for pay and for TSR is different, however, the regressions are handled differently. The indexed TSR values represent “fence posts” – fiscal year-end markers – that connect the “fence rails” of pay delivered between those markers.

- For the pay regression, five values are measured, at times (years) 1, 2, 3, 4, and 5. The dependent (y) values for the pay regression are the total CEO compensation values for the five most recent fiscal years.
- For the TSR regression, six values are measured, at times (years) 0, 1, 2, 3, 4, and 5. The dependent (y) values for the TSR regression are determined by hypothetically “investing” EUR 100 in the company on the day five years prior to the most recent fiscal year end, and measuring the value of that EUR 100 investment on each of the subsequent five fiscal year end dates, for a total of six indexed TSR values.

The following table traces a hypothetical company's Pay and Indexed TSR values for the five-year period in question. The TSR % change column indicates the percentage return over the one-year period in question, for reference.

Year (X)	Pay	Indexed TSR	TSR % change
2016 (0)	-	100	-
2017 (1)	1,231	109	9.0%
2018 (2)	2,553	118	8.3%
2019 (3)	1,821	91	-22.9%
2020 (4)	1,789	99	8.8%
2021 (5)	2,226	104	5.1%

The regressions are weighted to place slightly more emphasis on recent experience. Because there are a different number of data points for the two regressions, pay and TSR each have their own weights calculated.

The indexed TSR calculation depends on a continuous series of TSR data. If TSR data for only the first period is missing, PTA will be calculated on the basis of four years of data, otherwise PTA will not be calculated. If pay data are missing for any one period, then that period carries zero weight for both pay and TSR in the calculation.

The slope of the weighted least-squares regression is calculated as follows, if  $P_i$  represents the pay or performance value for period  $i$ ,  $W_i$  represents the corresponding weight for period  $i$ , and  $X_i$  is simply  $i$ :

$$slope = \frac{\sum W_i \sum W_i X_i P_i - \sum W_i X_i \sum W_i P_i}{\sum W_i \sum W_i X_i^2 - (\sum W_i X_i)^2}$$

In order that the two slopes are comparable to one another, each must be normalized by dividing by their respective weighted-average values:

$$norm. factor = \frac{W_i P_i}{\sum W_i}$$

The normalized slopes are therefore analogous to a 5-year “trend rate” for pay and performance, weighted to reflect recent history. The final Pay-TSR Alignment measure is simply equal to the difference: performance slope minus the pay slope. Potential values for PTA are theoretically unbounded, but in practice they range from just over -100 percent to just over 100 percent.

## The European Approach to Peer Group Construction

The peer groups approach for the European pay-for-performance model differs from that used in the ISS US and Canadian models by adopting a banded approach to market pay levels for the European model. In 2017 ISS also introduced the [company-selected peer methodology](#) to European peer group construction.

ISS' methodology for selecting peers maintains a focus on identifying companies that are reasonably similar to the subject company in terms of industry profile, size, and market capitalization, taking into account a company's self-selected peers to guide industry selections.

### Number of peers

As in the US model, the European model typically has a minimum of 12 peers and a maximum of 24 peers.

### Remuneration data and Industry classification

ISS' remuneration data sample covers about 1,800 European companies' total remuneration in the past 3 to 5 years. All monetary amounts are in or converted to million euros. The industry classification used is the GICS<sup>3</sup> code, which is a four-tiered, hierarchical industry classification system currently consisting of 11 sectors (GICS 2), 24 industry groups (GICS 4), 69 industries (GICS 6) and 158 sub-industries (GICS 8). Each company has a GICS 8 code based on its principal line of business activity.

Peer group constructions from June 1, 2023, will take into account that S&P and MSCI will be making adjustments to their GICS classification on March 17th, 2023. The revision is a result of consultation with market participants. Changes and can be reviewed here. The new GICS structure will consist of 11 Sectors, 25 Industry Groups, 74 Industries and 163 Sub-Industries. The new GICS code 40201050 (Commercial & Residential Mortgage Finance) is fully derived from the discontinued 40102010 (Thriffs & Mortgage Finance); and therefore, will be added the group of asset-based companies for the purpose of peer group construction. Because the new GICS code 40201060 (Transaction & Payment Processing Services) is largely derived from 45102020 (Data Processing & Outsourced Services), this group will use revenues to compare for company size. How size is calculated

The European P4P model shares the current methodology taken from the US model as described in the US Pay-for-Performance white paper. The majority of industry sectors use revenues as an indicator of size. However, certain industry sectors use market capitalization (market cap) or assets on the balance sheet. The decision tree within the algorithm has been implemented as follows:

- **Revenues:** If subject company is not in the GICS codes below, use revenues to compare for company size
- **Assets:** If subject company is in the GICS codes below, then qualify all peers within these asset-based GICS using assets, but qualify all peers outside the asset-based GICS using revenues
  - 40101010 Diversified Banks
  - 40101015 Regional Banks
- 40102010 Thrifts & Mortgage Finance
  - 40202010 Consumer Finance
- 40201020 Diversified Financial Services
- 40201050 Commercial & Residential Mortgage Finance
- **Market cap:** If subject company is in the GICS codes below, only the market cap test is used to qualify a peer

<sup>3</sup> <https://www.msci.com/gics>

- 10102010 Integrated Oil & Gas
- 10102020 Oil & Gas Exploration & Production
- 10102030 Oil & Gas Refining & Marketing
- 10102040 Oil & Gas Storage & Transportation
- 10102050 Coal & Consumable Fuels

Both subject and potential peer must be in the asset-based GICS groups listed above in order to be compared on the basis of assets. In cases where a subject company is in one of the asset-based GICS groups and a potential peer is not, revenues will be used for size comparisons. This principle applies to the size comparisons made to qualify a peer for potential inclusion as a peer, to the size rankings made to maintain the subject company near the median size of the peer group, and to the size prioritisation of peers.

If a company wishes to understand how its size was calculated, it can request this information through the [ISS Help Center](https://issgovernance.service-now.com/csp) (<https://issgovernance.service-now.com/csp>).

### Peer group construction

The ISS US methodology benchmarks "similar" companies by the two important explanatory factors of executive remuneration in the US: size and industry, which has been confirmed by empirical data, using common regression analysis.

The European situation is similar to US but adds a new dimension: "country," where empirical remuneration data concludes that size, country, and industry are the three significant explanatory factors. This means that, in the European context, the ISS methodology extends the view of benchmarking similar companies from "size/industry" to "size/industry and countries of similar pay level".

If a company does not agree with the peers which have been allocated by the model, or considers they have been wrongly allocated, it can provide this feedback through the [ISS Help Center](https://issgovernance.service-now.com/csp) (<https://issgovernance.service-now.com/csp>).

### Country bands

ISS incorporates the view of "countries of similar pay level" through the concept of "bands" and by grouping into the same band countries that show similar country-level remuneration, after controlling for size and industry. The inclusion of this additional consideration, "band", allows the methodology to remove as far as possible the undesirable biases that can occur when companies from very different band(s) are used for benchmarking purposes.

More precisely, the ISS European P4P methodology incorporates "band" consideration to remove such undesirable bias at two stages:

- **Stage 1:** The methodology benchmarks a subject company to peers from the same/similar band(s) whenever possible.
- **Stage 2:** The methodology further compares a subject company's P4P result to all subject companies' P4P outcomes in the same band to eliminate systematic band-specific bias not removed in the prior step.

In other words, stage 1 is reflected in the ISS peer selection methodology. Stage 2 is reflected in ISS' view of P4P outcome = "LOW/MEDIUM/HIGH" concern, which is set up at a per-band basis in the European context.

When grouping countries into bands, ISS considers the following:

- Views from the regression-adjusted analyses of ISS' European remuneration data that present country-level remuneration (by median and average, and by other versions of regression analyses commonly adopted).
- Views from feedback from institutional investors.

The constituents of the country bands are shown below.

**Figure 3. Constituents of country bands**

Band	A	B	C	D
<b>Constituents</b>	UK Ireland Jersey	Germany Switzerland	Belgium Denmark France Italy Netherlands Sweden Spain	Austria Finland Greece Luxembourg Norway Portugal

The country bands were originally constructed based on the testing of the data used by the model to identify country groupings around quantum of total CEO pay, adjusted for average company size. They were also discussed with a number of institutional investor clients during the model development phase to check that the company placings were in line with expectations. The membership of each band is reviewed annually to reflect changes in market practice over time. Based on this review and pay level trends in Europe, Denmark's pay levels are closer to that of the levels of band C countries; it was therefore decided to move Denmark from band D to C as of 2019.

### Company-disclosed peers

In the US and Canada, companies include their chosen peers for benchmarking purposes in their disclosed meeting materials. In Europe, it is still very rare to see companies systematically including self-selected peers in the annual report or other materials, with the exception of some larger companies in certain markets.

As this is not a widespread practice in all European markets, the decision was made for 2016 season to only use ISS-selected peers in the European pay-for-performance model. Following market feedback from both institutional investors as well as corporate issuers, in 2017 ISS introduced the company-selected peer methodology to the European P4P. Although the disclosure of peers remains limited (i.e., the level of disclosure is approximately 24% of the 2024 coverage universe), an increasing share of companies are disclosing peers and it is encouraged as a best-practice.

Peers selected or disclosed by the company are taken into account for the purpose of guiding the industry selection. The GICS-codes assigned to the company-selected peers guide the selection process to more company-alike peers. However, while the methodology does place a priority on the company's own peer selections, there are a number of reasons why a company-selected peer may not appear in the final ISS list, even if it meets the relevant size (revenue or assets and market capitalization) parameters. As noted above, the methodology also places priority on other factors as it builds the peer group:

- The company's own 8-digit GICS category
- Maintaining the subject company size at or near the median of its peer group
- Maintaining the approximate distribution of GICS industry codes as reflected in the company's self-selected peer group

At times, including a company's self-selected peer may push the subject company away from the median, or lead to an overrepresentation of that industry within the final peer group. In these cases, the company's self-selected peer may not be included. In addition, if a company's self-selected peer is the only peer company in its 6- and 8-digit GICS category, that industry grouping is not utilized in the peer selection process (since the company may have selected that peer solely due to geographic proximity, for example).

In case multiple seed peers qualify for the same group, priority in the selection process is given to the seed peers the subject has chosen in its own peer group and the distance in size (by the appropriate revenue or asset size comparison) between the subject and seed peer. Because the disclosure of company selected peers remains limited in Europe and is concentrated in a few markets, the selection process does not look at counter references (i.e. whether the seed peer has chosen the subject company as a peer or the number of peer selections among the seed peer and the subject company's peers and the companies that have chosen the subject as a peer) in order to avoid significant bias.

ISS uses the company-selected peers that are used for CEO pay benchmarking purposes.

In November 2024 ISS provides companies a "[peer update](#)" opportunity to communicate changes made to their benchmarking peer groups following their most recent proxy disclosures. During the update process, companies can inform ISS of updates to the peer groups they used to benchmark executive compensation that will be reported in their upcoming proxy statements (not to benchmark the upcoming year's pay). Companies that do not participate in the ISS peer update process will have their most recently disclosed compensation peers used in the ISS peer group construction process for the following year's ISS benchmark research analysis.

## Notes on Implementation

It is important to emphasise the inclusion of the European pay-for-performance model to the ISS benchmark research reports is additive and is intended to provide our clients with additional data points for comparability. Also, while the model is based on realised pay, the qualitative reviews by ISS research analysts take into account both the granted and realised elements of remuneration during the year under review, as appropriate.

The rest of this section discusses how the pay-for-performance charts are presented in the ISS benchmark research reports, and how frequently the model is updated.

### Presentation within the research reports

The relevant ISS European proxy research reports for the companies included in the European P4P model include the pay-for-performance graphs for the three tests RDA, MOM, and PTA. The peers used in the model are identified, as is the overall level of concern.

Within the ISS research reports:

- **The Relative Alignment (RDA)** chart compares the performance and pay rankings of the subject company and its peers over (typically) three years.
- **The Magnitude of Pay (MOM)** chart shows the CEO pay for the most recent year compared with that of its peers.
- **The Absolute Alignment (PTA)** chart compares the subject company's CEO pay with indexed TSR over (typically) five years.
- **The Pay-For-Performance Quantitative Screen** summarises the overall level of concern.

In addition to the pay-for-performance graphs, will be included:

- **The Economic Value Added (EVA) Performance** evaluation compares the EVA performance and pay rankings of the subject company and its peers over (typically) three years. *Note: the EVA analysis is shown for informational purposes-only and does not impact the P4P screen.*

Executive remuneration in the research reports includes three main sections of content.

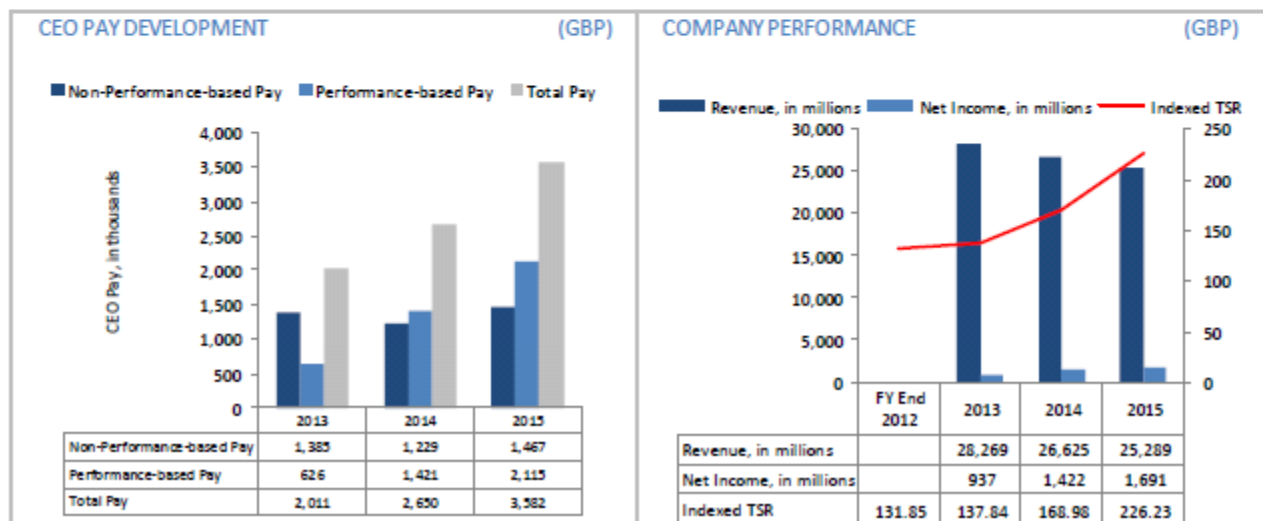
**Components of Pay Table.** The first section includes the components of pay table. This table, which contains realised pay, is included to illustrate how the total pay number was reached. The bar chart under the table to the left shows the split between variable and fixed pay for the CEO the most recent three financial years. The second bar chart displays company performance over the same period measured in revenue, net income, and indexed TSR.

Figure 4. Remuneration Profile – Components of Pay

## Remuneration Profile

COMPONENTS OF PAY				
GBP in thousands				
	CEO			CEO Peer Median
	Cooper, Alison			
	2015	Change	2014	2013
Base salary	965	+4.9%	920	920
Perquisites	16	-	16	16
Pension	480	+63.8%	293	449
All other compensation	6	-	-	-
Cash Bonus	772	-39.2%	1,270	626
Deferred Bonus	772	-	-	-
Total short-term incentives	1,544	+21.6%	1,270	626
Non-equity incentives	-	-	-	-
Restricted stock	571	+278.1%	151	0
Options	-	-	-	-
Total long-term incentives	571	+278.1%	151	0
Total	3,582	+35.2%	2,650	2,011
% of Net Income	0.21%		0.19%	0.21%
% of Revenue	0.01%		0.01%	0.01%

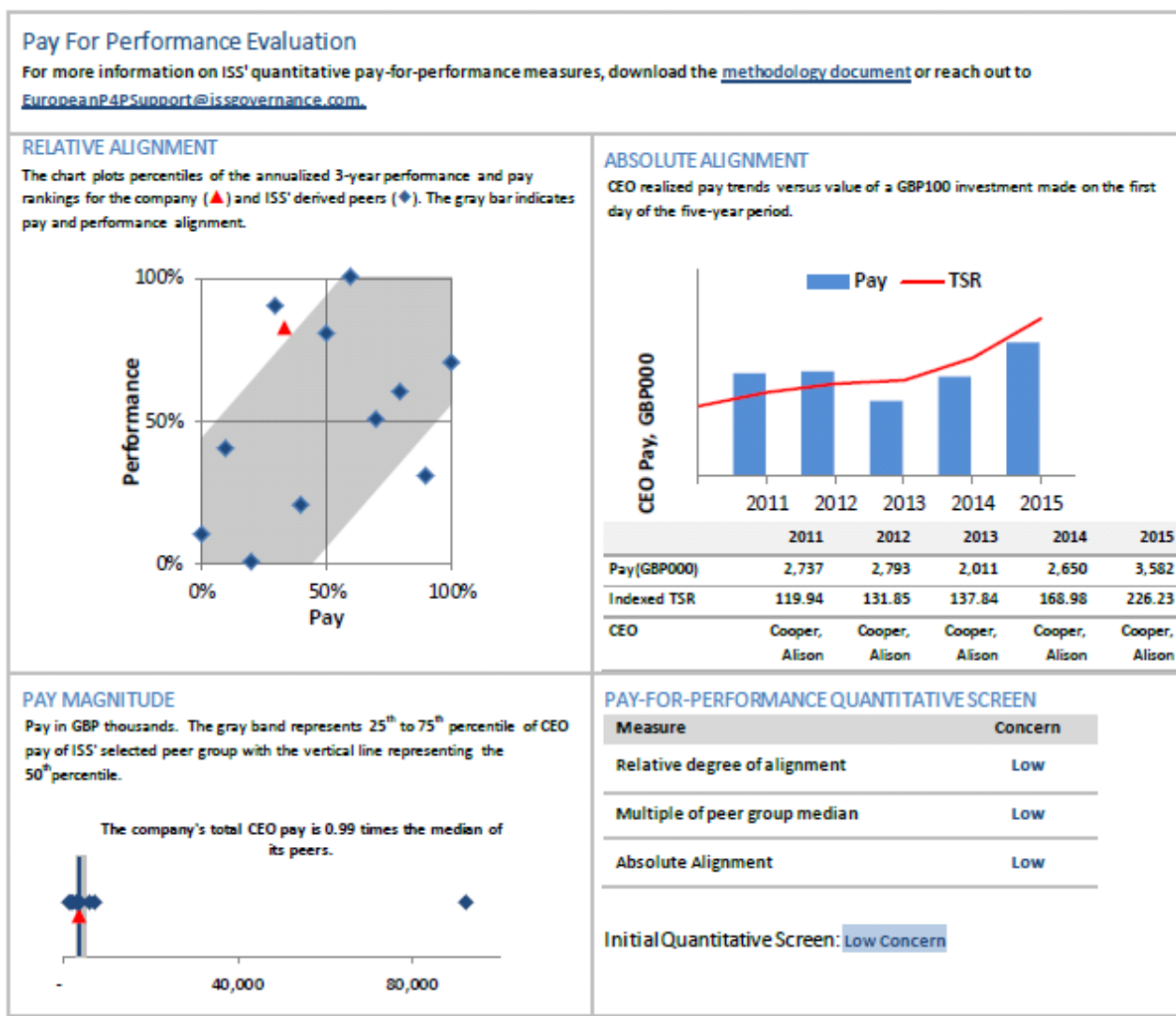
Figures above refer to realized pay and may significantly differ from issuer-reported figures.





**Pay for Performance Evaluation.** The second section is the Pay for Performance Evaluation, which includes the charts and the list of peers. The quantitative screen details the overall level of concern for each of the three models, and the initial Quantitative Screen displays the overall level of concern.







Figure 5. Pay for Performance Evaluation



For information purpose, the supplemental EVA performance evaluation is displayed after the quantitative screen and before the peer group summary.

### EVA PERFORMANCE

The below EVA performance information is provided for informational purposes. It does not affect the pay-for-performance quantitative screens.

Measure	Quartile Ranking vs. Peers	Metrics	Long-Term Performance	Quartile Ranking vs. Peers
Pay		EVA Margin	1.28	
EVA Performance		EVA Spread	2.31	
<b>Result 62.95</b>		EVA Momentum (Sales)	1.09	
<b>Result equals EVA performance rank minus CEO pay rank. A negative result indicates that the CEO pay rank is greater than the EVA performance rank.</b>		EVA Momentum (Capital)	1.78	

EVA Metrics are calculated by ISS EVA, and are based on audited financial data reported in public filings. For more information on the EVA methodology and metrics, visit <https://www.issgovernance.com/solutions/iss-analytics/iss-eva-resource-center/>

Similar as in the US, the European research reports also contain the relevant table and graph on peers disclosed by the company. The table provides information on the names of the peers selected by the ISS model, the peers selected by the company, and any overlap that exists. The graph on the right provides further details on the size of the peers selected by the ISS model and the company, and provides the relative size (the subject indexed at 100%) of the peers.

### Peer Groups

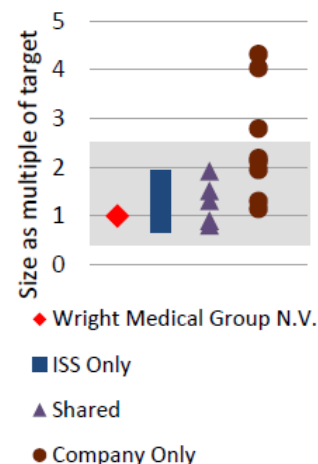
#### ISS AND COMPANY DISCLOSED PEER GROUPS

ISS-Selected Peers (7)	Accuray Incorporated AngioDynamics, Inc. CONMED Corporation Orthofix International N.V.	Analogic Corporation Cantel Medical Corp. DexCom, Inc.
Shared Peers (5)	Globus Medical, Inc. Masimo Corporation NxStage Medical, Inc.	Greatbatch, Inc. Natus Medical Incorporated
Company-Disclosed Peers (13)	Globus Medical, Inc. Haemonetics Corporation Masimo Corporation Natus Medical Incorporated NxStage Medical, Inc. Sirona Dental Systems, Inc. Thoratec Corporation	Greatbatch, Inc. Integra LifeSciences Holdings Corporation Merit Medical Systems, Inc. NuVasive, Inc. ResMed Inc. The Cooper Companies, Inc.

The shaded area represents the overlap group of companies that are in both ISS' comparison group and the company's disclosed CEO compensation benchmarking peer group. Excludes company peers for which financial data is not available. For more information on the ISS peer group methodology, visit [www.issgovernance.com/policy/USCompensation](http://www.issgovernance.com/policy/USCompensation)

### PEER GROUP SIZE ANALYSIS

Size (by revenue) of the ISS, company and overlap peer groups. Gray indicates 0.4- 2.5 times the company's revenue.



## Model updates

The coverage universe for the model in 2016 was the STOXX Europe 600, which was expanded in 2017 to STOXX Europe 600 and local main indices. In 2021, the coverage was expanded again to include roughly 400 additional “widely-held” companies in certain covered countries primarily in the Nordic and Germanic regions. Overall, with the addition of companies added to coverage over time as part of the applicable index groups, as of to date this represents roughly 1,800 European publicly-traded companies covered under the P4P model. The coverage universe is set and updated once per year based on the companies forming part of the index groups outlined below. The coverage currently mirrors ISS' Governance QualityScore Universe.

Country	Index
European	STOXX Europe 600, EURO STOXX 50
United Kingdom	FTSE All-Share (ex-investment trusts)
Ireland	ISEQ 20
France	Widely-held companies within the CAC All tradable, SBF 120
Belgium	BEL 20
Netherlands	AEX25, AMX25
Luxembourg	LuxX
Denmark	OMX Copenhagen 20, Nasdaq Nordic Large Cap
Norway	OBX; Nasdaq Nordic Large Cap
Sweden	OMX Stockholm 30, Widely-held companies
Finland	OMX Helsinki 25, Nasdaq Nordic Large Cap
Italy	FTSE MIB, FTSE Italia Midcap
Spain	IBEX 35
Portugal	PSI 20
Greece	FTSE ATHEX Large Cap Index 25
Germany	DAX30/MDAX50/SDAX 50/TecDAX
Switzerland	SMI 20, SMIM 30
Austria	ATX 20

## Use in ISS QualityScore

In the 2017 policy year, pay-for-performance factors were added to the Remuneration Pillar in ISS QualityScore, referencing the pay-for-performance results from the Relative Degree of Alignment (RDA), Multiple of Median (MOM), and Pay-TSR Alignment (PTA) tests that can be viewed on each company's research report. Since the 2018 policy year, these factors are weighted/scored within the QualityScore model. For details on the QualityScore methodology, please refer to <https://www.issgovernance.com/esg/rankings/>.

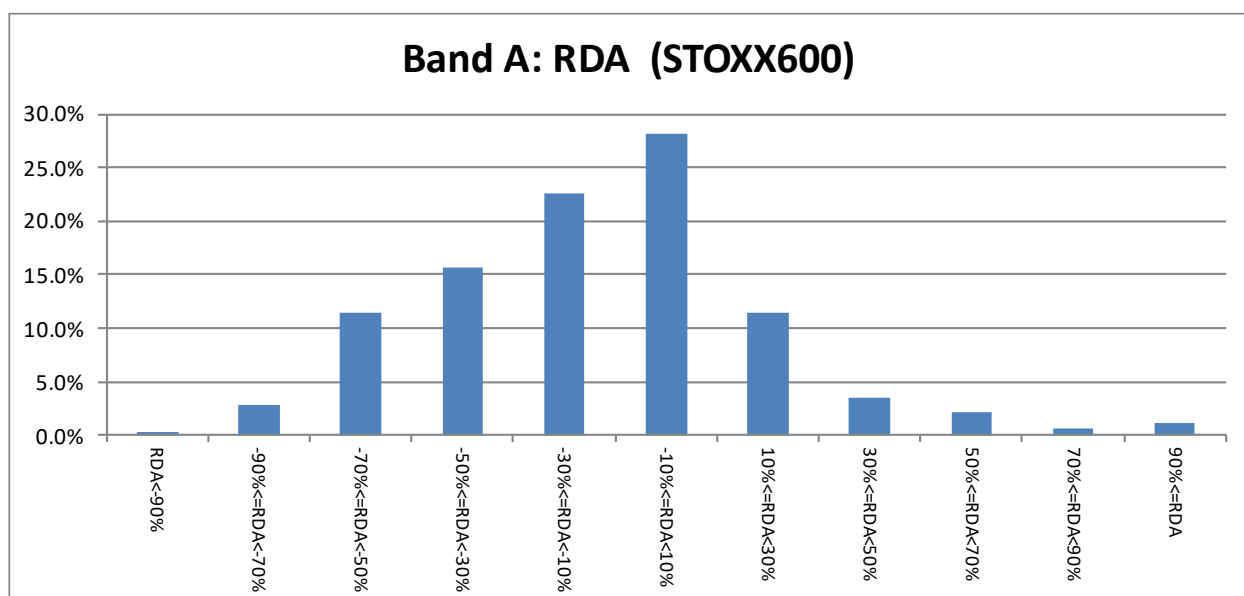
For newly covered companies, the pay-for-performance questions in QualityScore only apply after the next research report is published for these companies and where a pay-for-performance analysis is included.

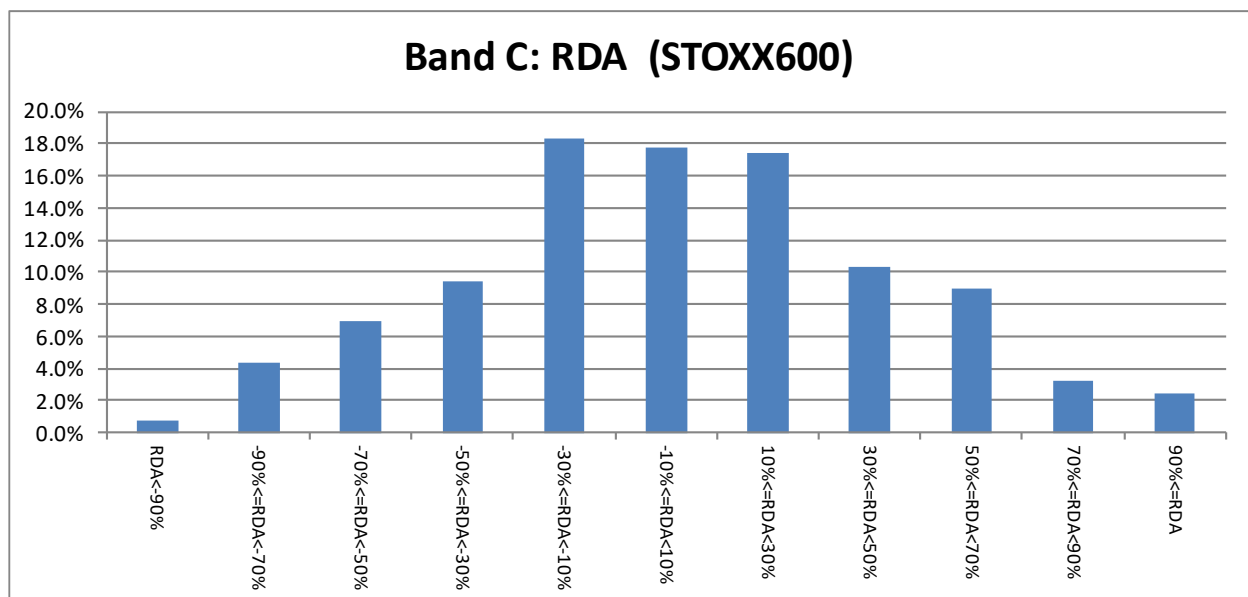
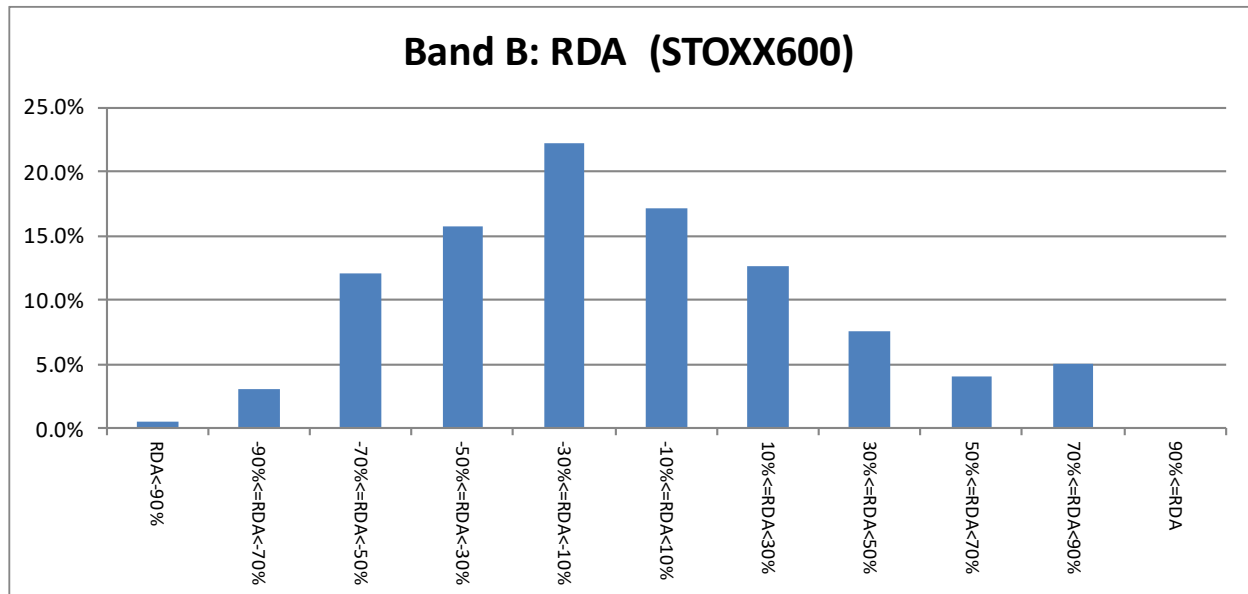
## Appendix: Back-Testing the Model

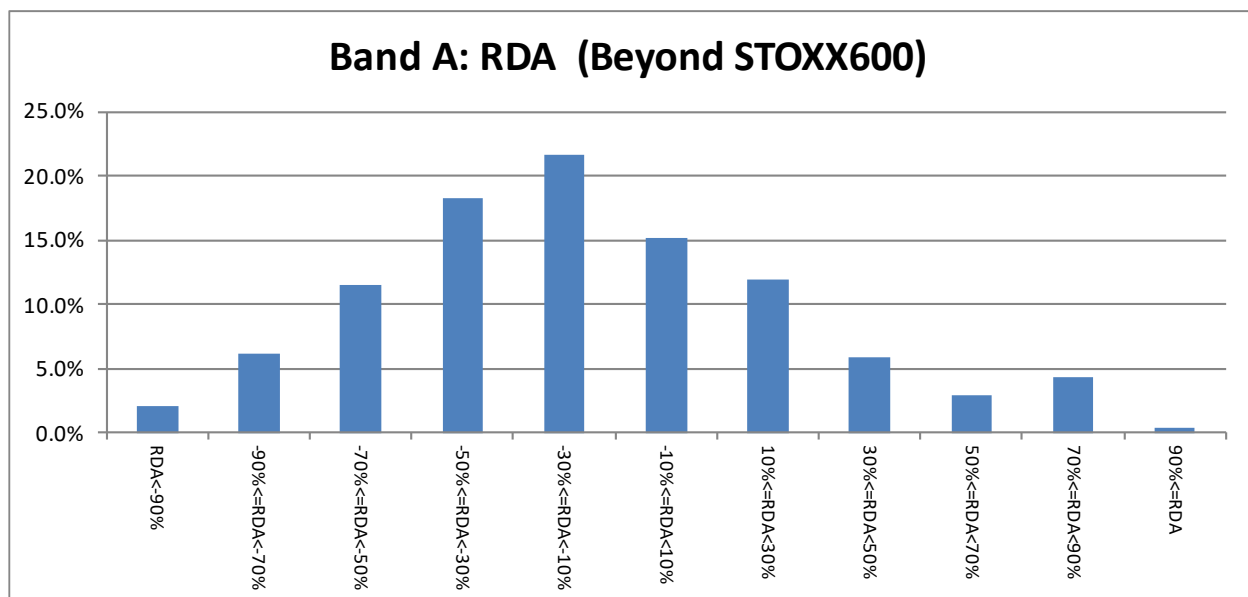
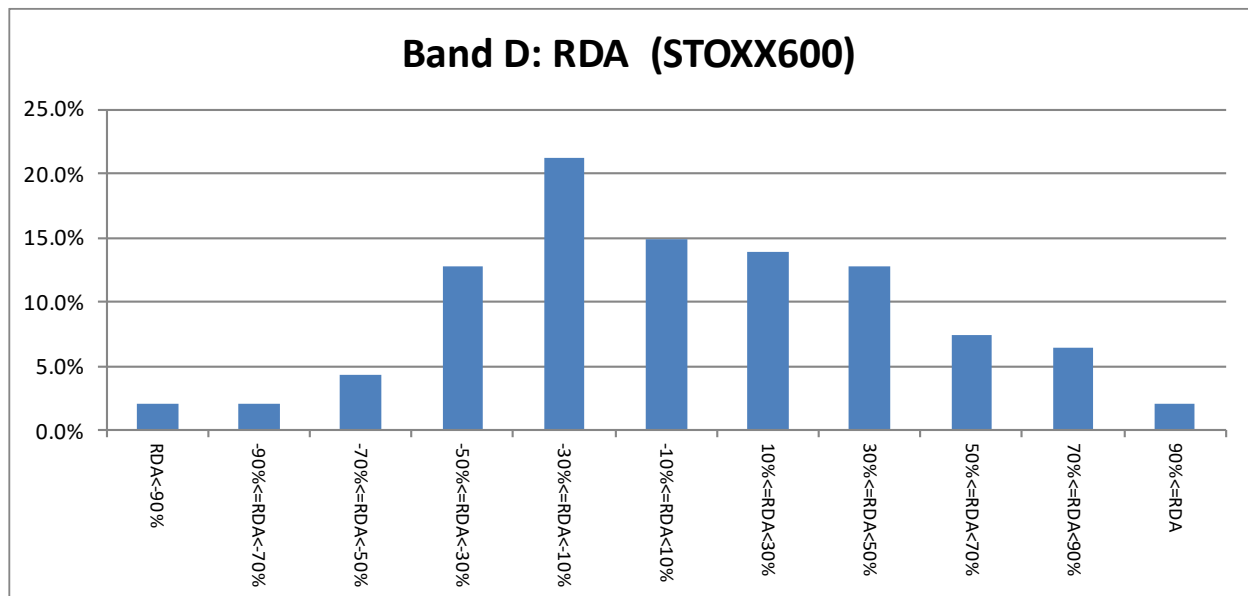
The distribution of scores has been tested for the three models, RDA, MOM, and PTA, by band and was broadly in line with that seen for the North American models, although due to the smaller sample size in the European model, the slope of the distribution was less smooth. Following the expansion of the coverage universe to companies on local main indices but not included in the STOXX600 index, the distributions of the model scores were substantially different. We have therefore separated the distribution of scores between companies that are included in the STOXX600 index and companies that are not included in the STOXX600 index but are included in the expanded European P4P coverage.

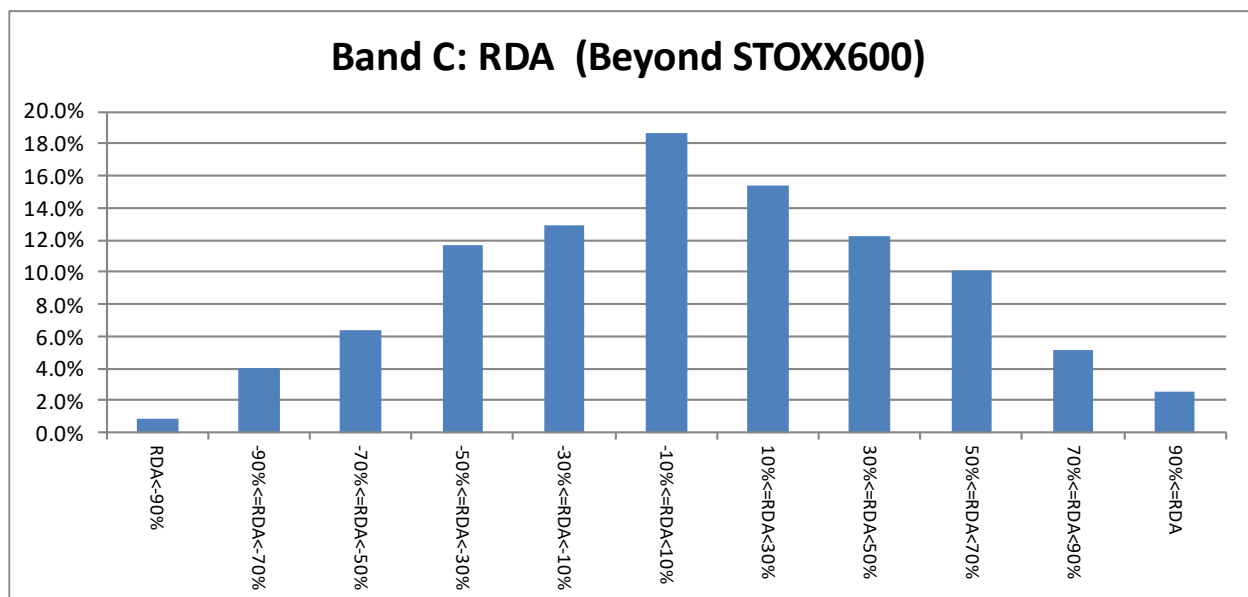
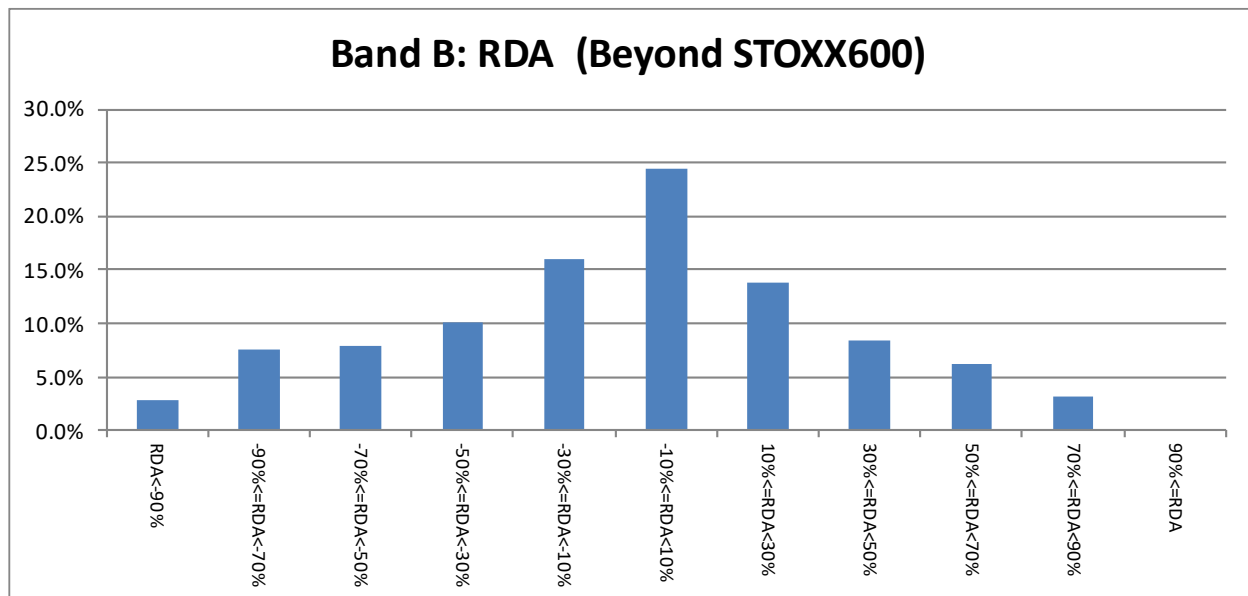
### Relative Degree of Alignment

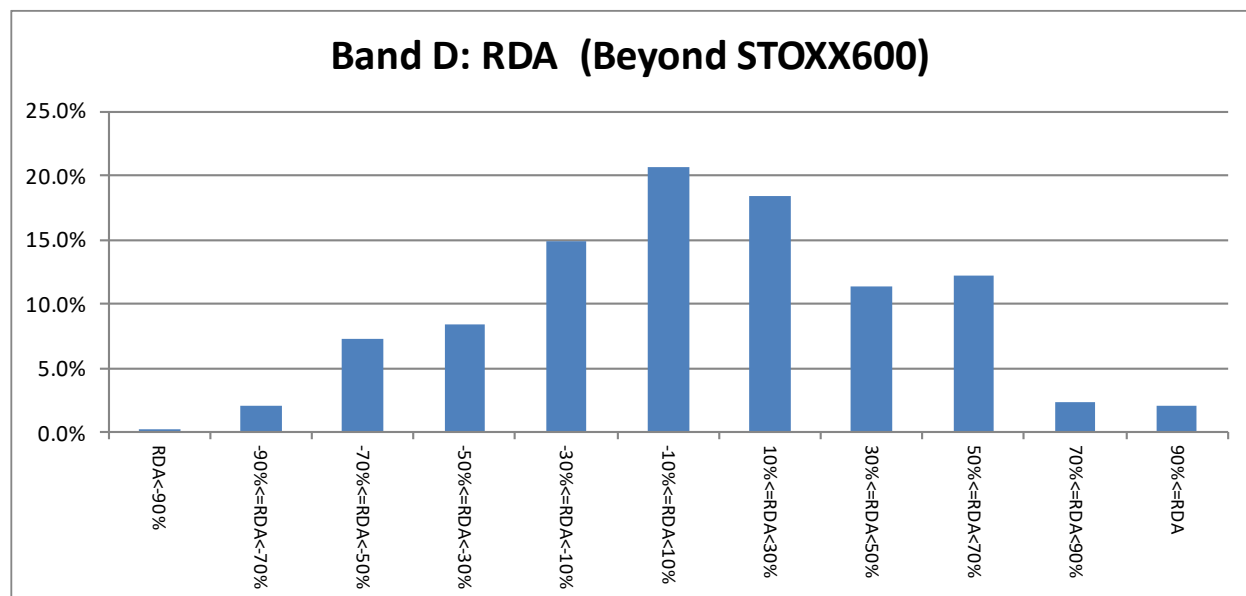
Figure 6a-h. Distribution of RDA scores for each country band.







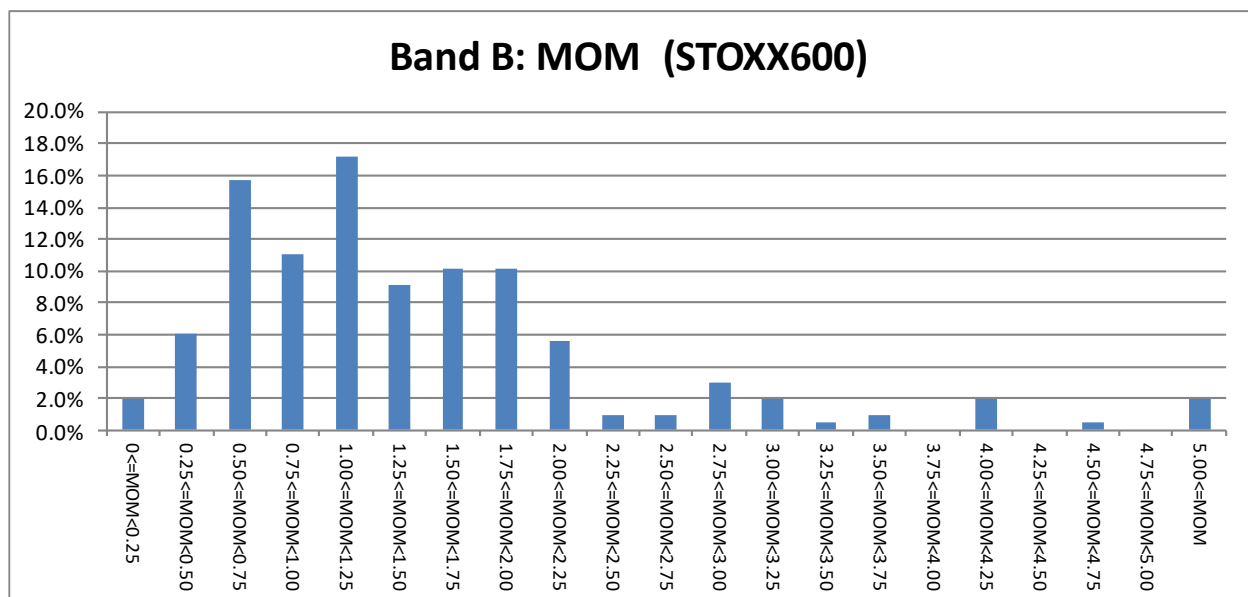
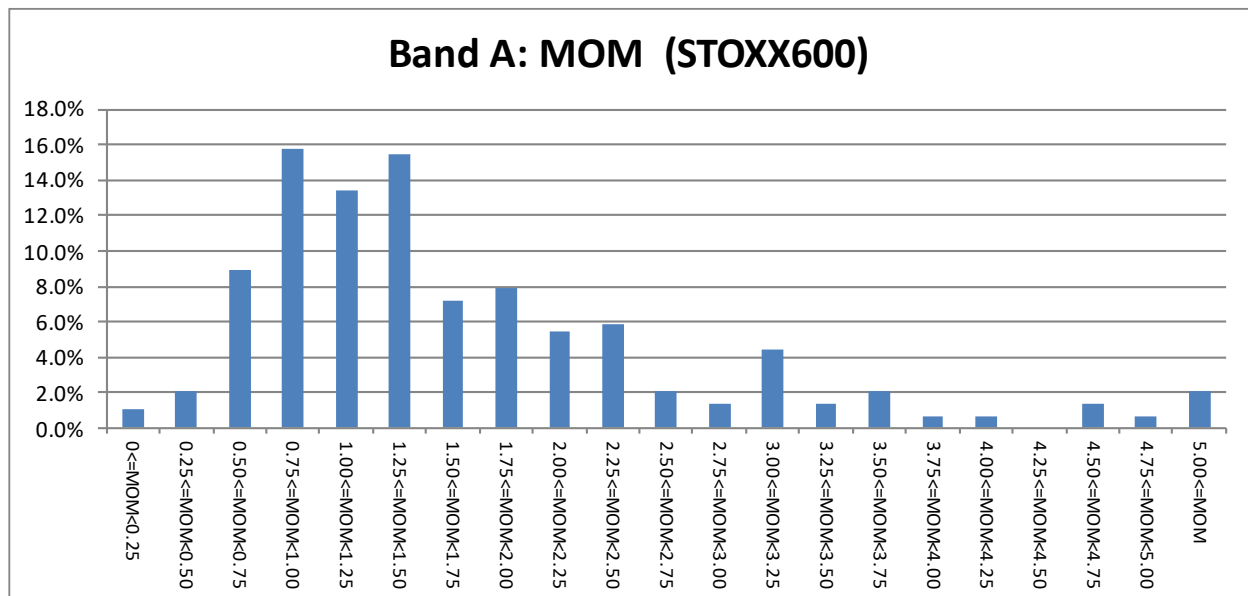


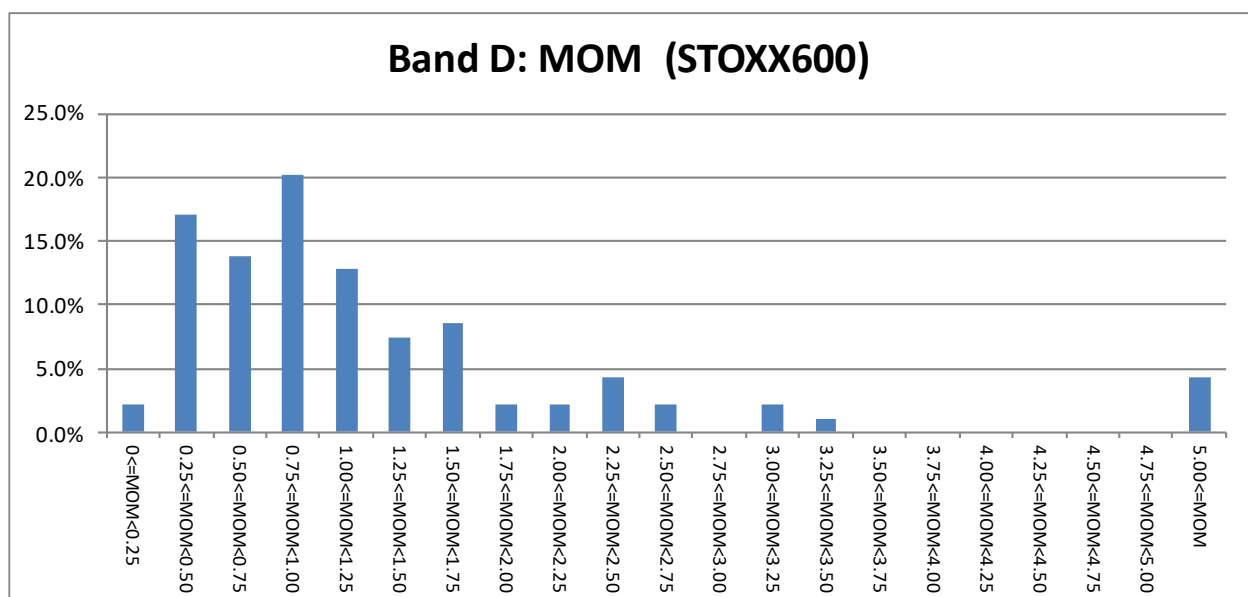
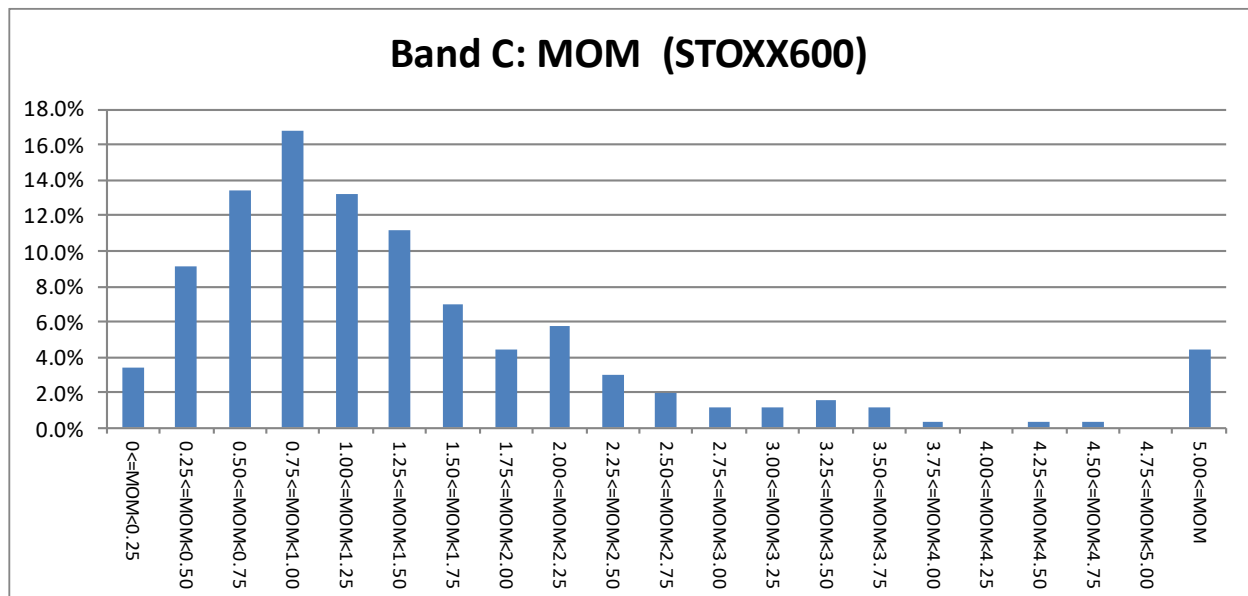


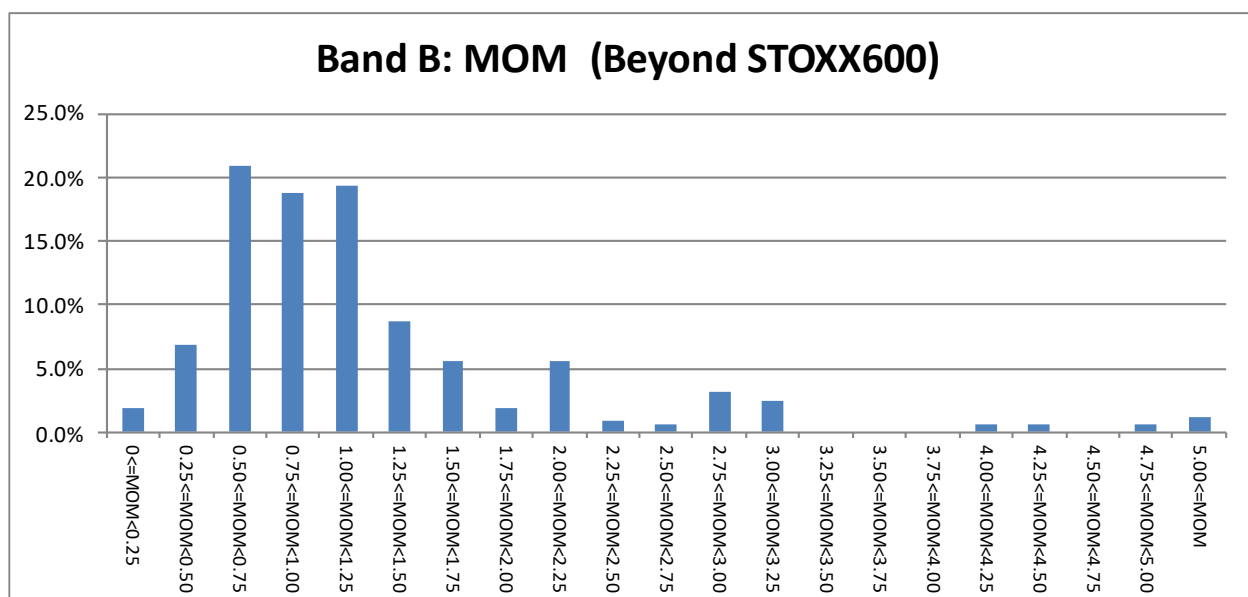
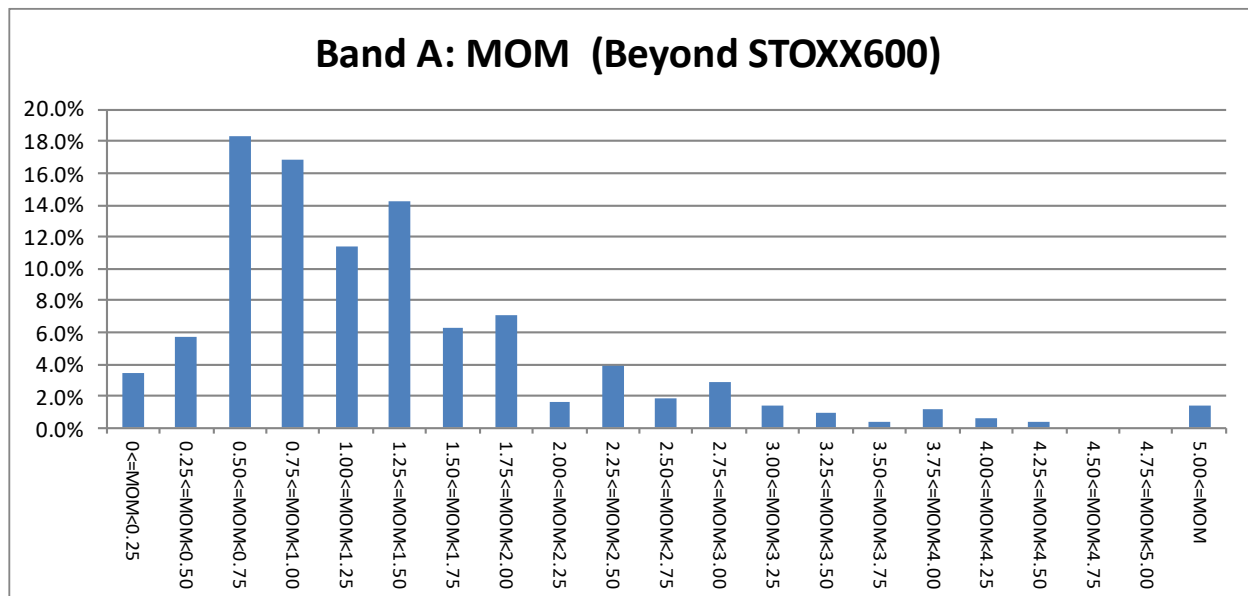
### Multiple of Median

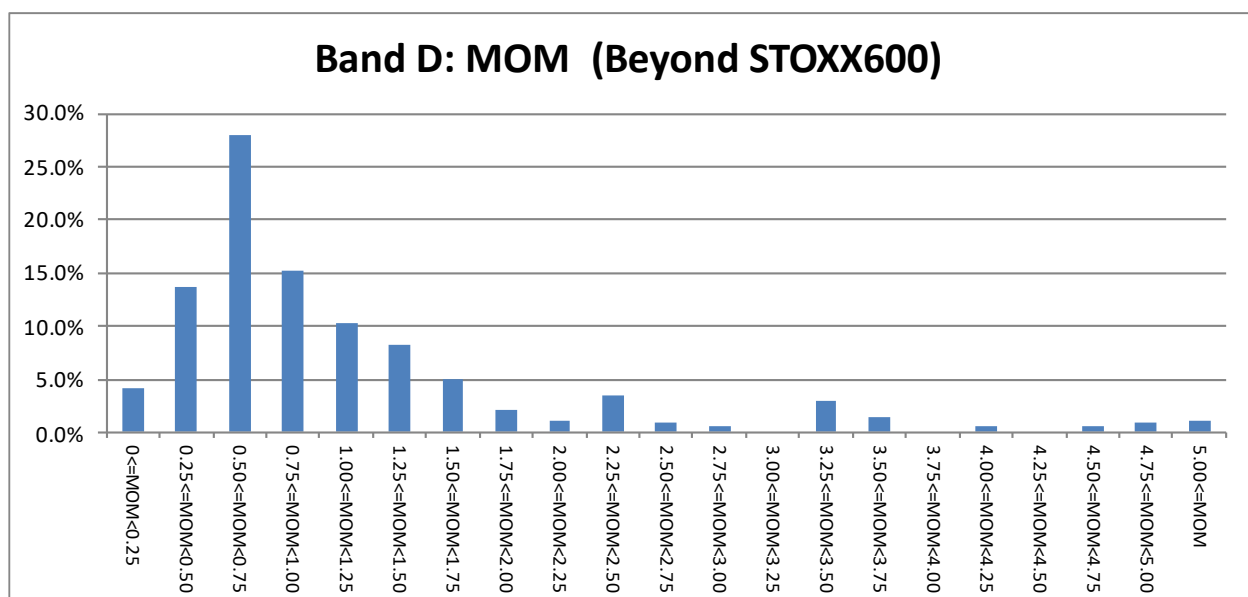
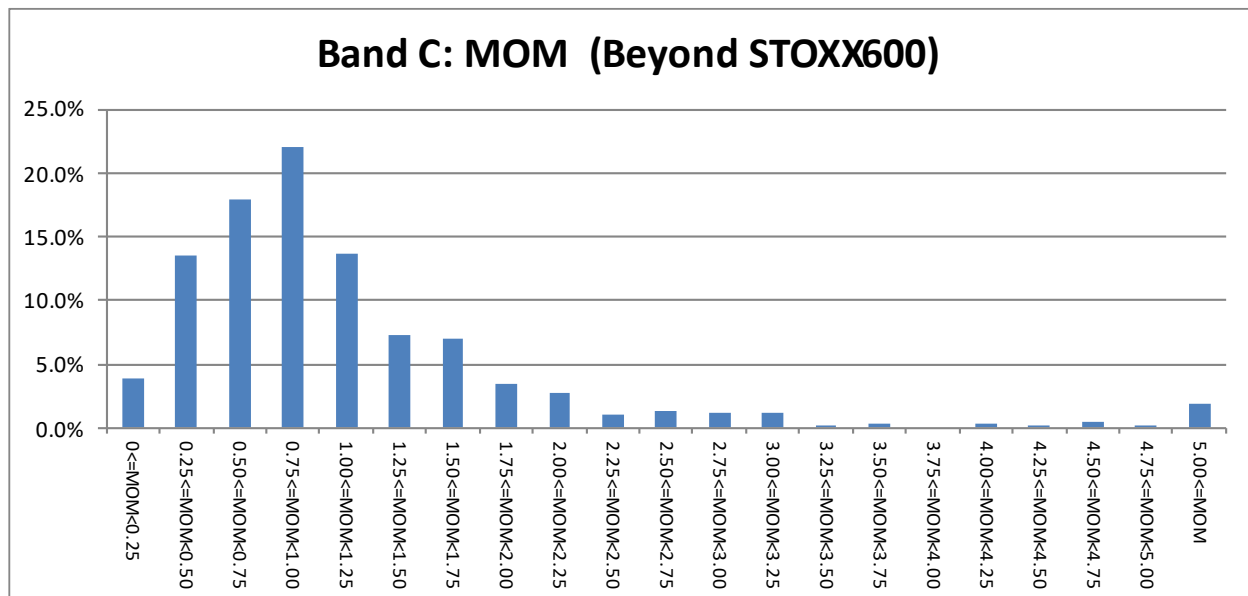
Figure 7a-h. Distribution of MOM scores for each country band.





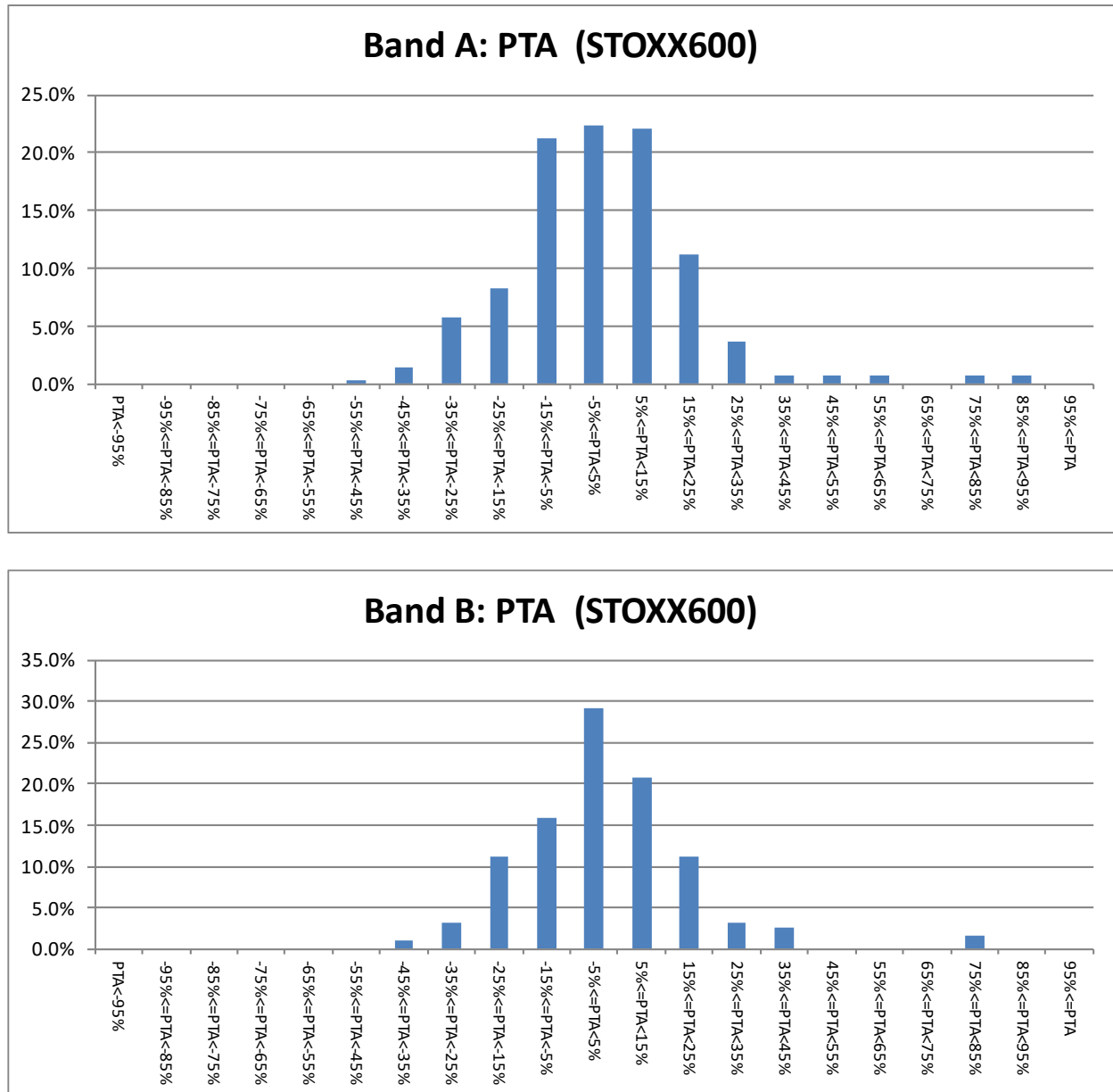


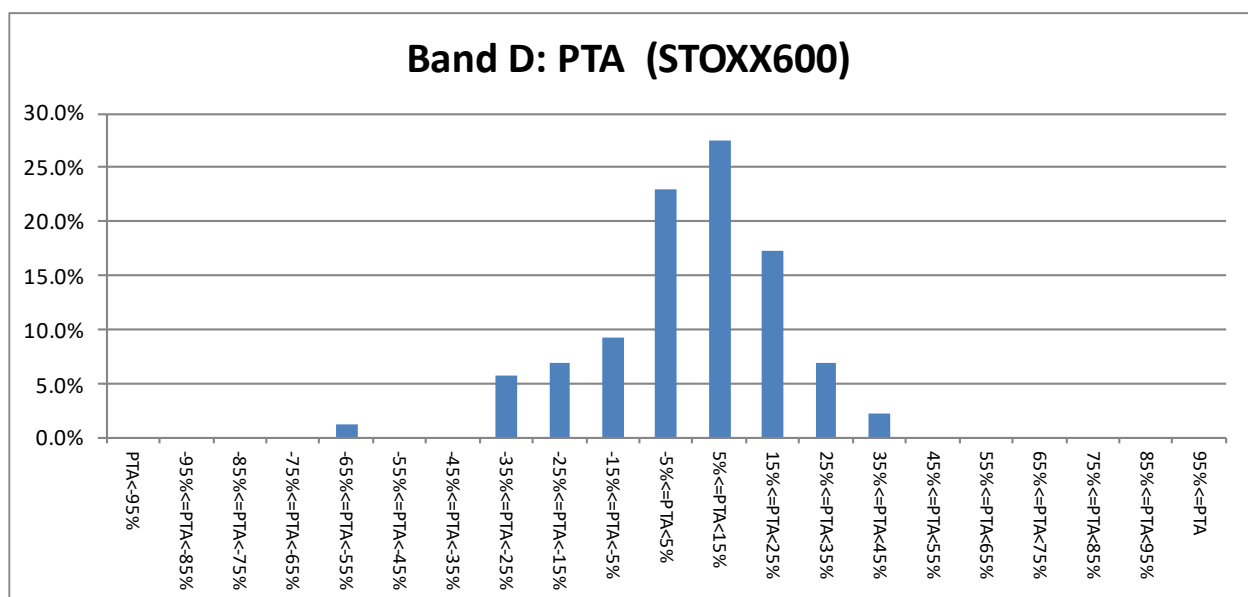
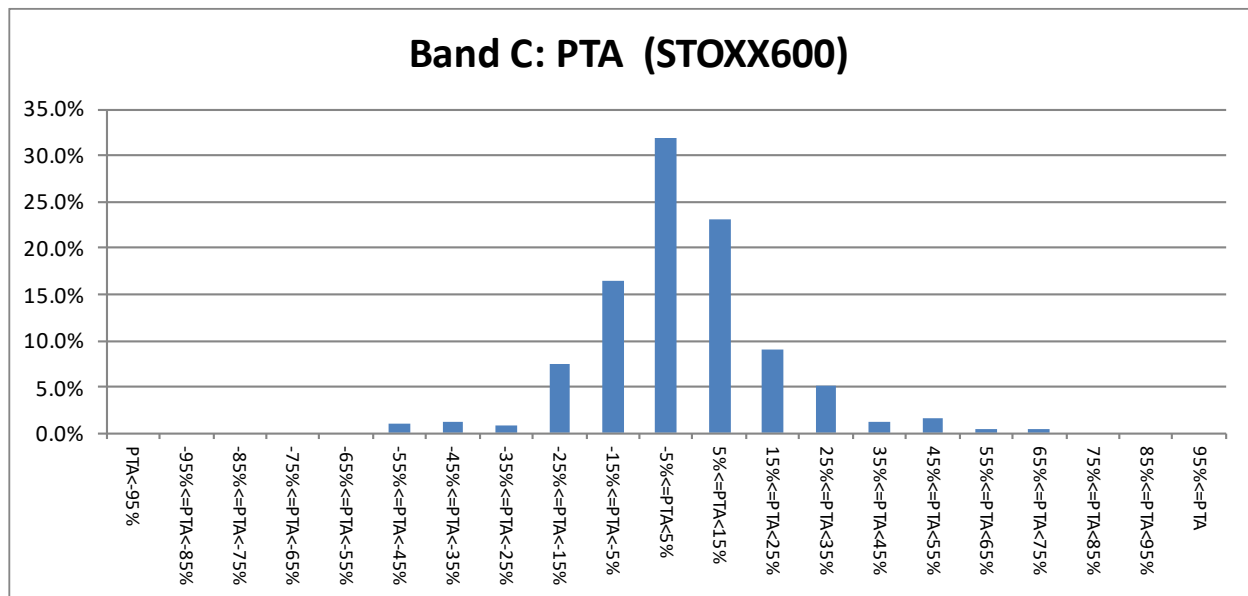


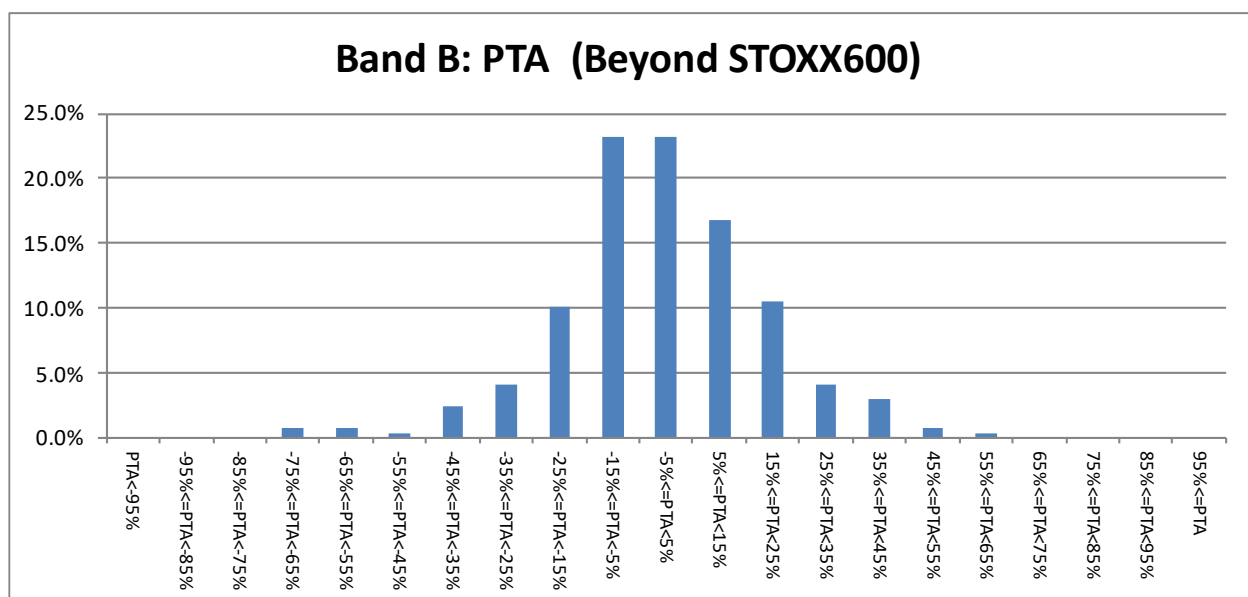
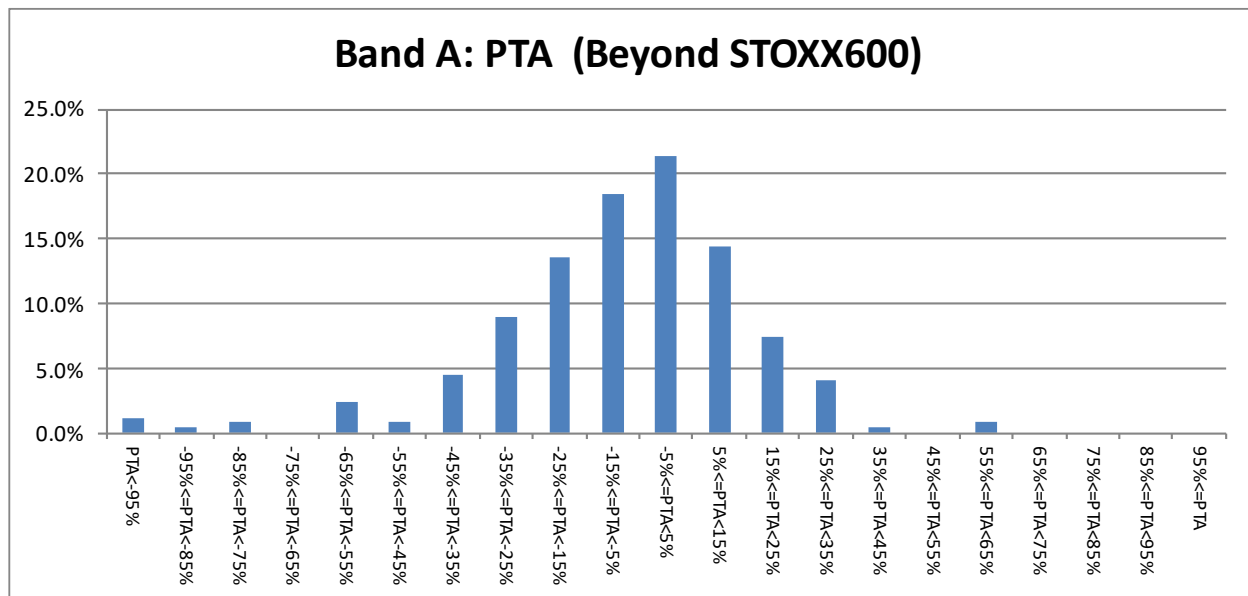


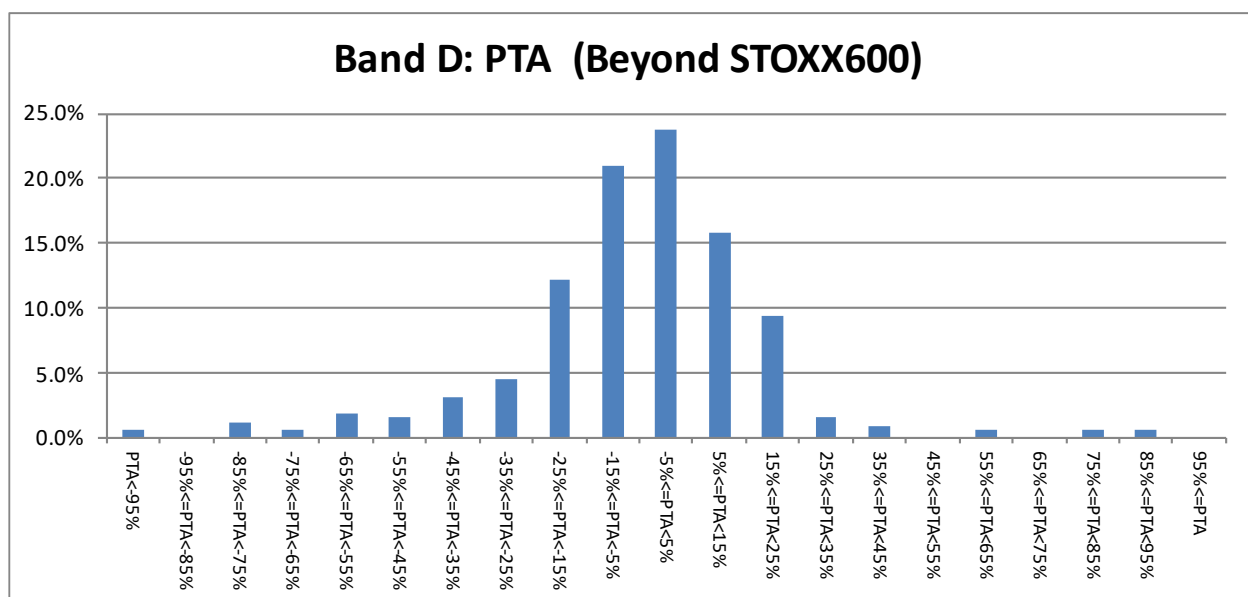
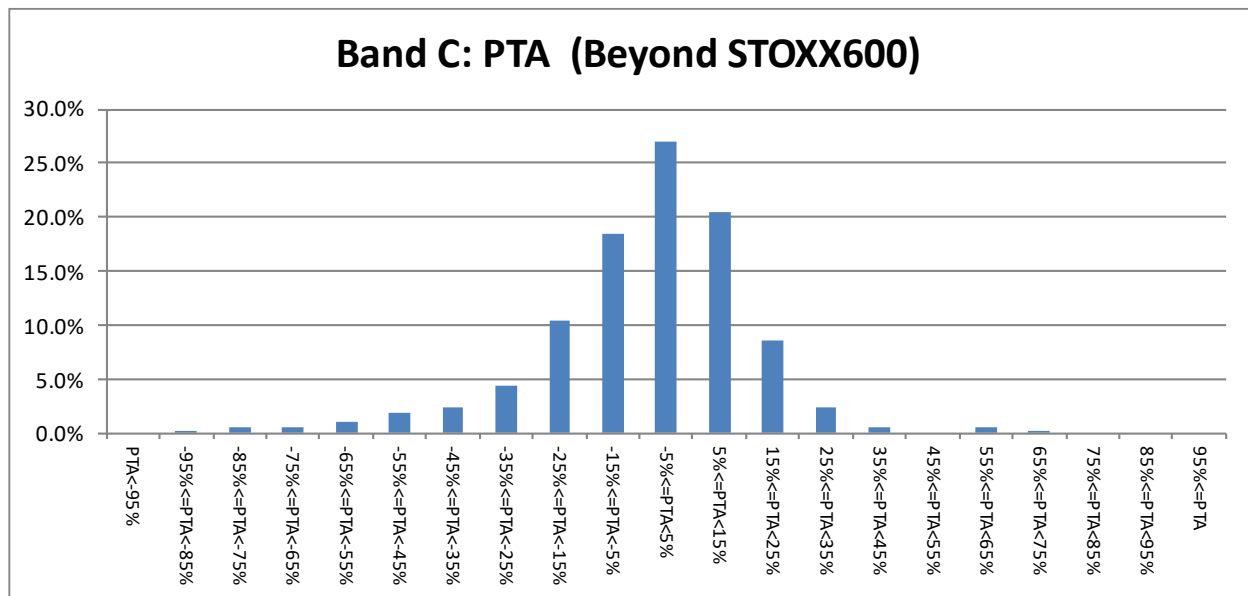
## Pay-TSR Alignment

Figure 8a-h. Distribution of PTA scores for each country band.











## Appendix: Economic Value-Added (EVA) Evaluation

In 2020, ISS introduced the display of EVA-based metrics in European ISS research reports. The EVA metrics did not form part of the pay-for-performance screen or concern levels and were displayed for informational purposes only. The information below serves as guidance for understanding the methodology behind the EVA metrics and analysis displayed in the report.

**Economic Value Added (EVA).** EVA represents the economic profit a company earns after meeting all its obligations – including the demands of capital providers. As a formula, EVA is net operating profit after taxes (NOPAT), less a capital charge computed by multiplying the firm’s capital base by its cost of capital. Unlike standard measures of profit, EVA cuts through accounting distortions and charges for the use of capital. EVA uses a rules-based method of translating accounting data into economic performance information through a consistent framework, thus making it comparable across companies, industries, and countries.

The four EVA-based metrics displayed in the report can be further understood as follows:

METRIC	DEFINITION
<b>EVA Margin</b> ( $EVA \div Sales$ )	The percent of sales remaining after covering all operating and capital costs, a combined measure of profit and loss (P&L) efficiency and balance sheet asset management.
<b>EVA Spread</b> ( $EVA \div Capital$ )	The EVA yield on capital, which equals the spread between the firm's return on capital (ROC) and its cost of capital (COC).
<b>EVA Momentum vs. Sales</b> ( $\Delta EVA \div Prior Sales$ )	The trend line annual growth rate in EVA over the past three years, scaled to Sales.
<b>EVA Momentum vs. Capital</b> ( $\Delta EVA \div Prior Capital$ )	The trend line annual growth rate in EVA over the past three years, scaled to Capital.

**Methodology.** Performance for these EVA metrics is measured across a three-year period (or a shortened two-year period depending on trading history and data availability), and the subject company is ranked against its ISS-selected peers across each of the metrics. Performance is measured using the 12 most recent trailing quarters (16 for momentum metrics) as of ISS’ quarterly data download. Data is derived from company-reported income statement, balance sheet, and footnote financial data, which is obtained from S&P Compustat. A minimum of 8 trailing quarters of valid data is required for the EVA Margin and EVA Spread metrics to be calculated, and 12 trailing quarters of valid data for EVA momentum metrics – this applies to the subject company as well as ISS-selected peers. As with the other screens, a minimum of 12 peers with valid data is required to run this evaluation.

The metric performance ranks are combined into an average performance rank, which is compared to the subject company’s CEO pay rank, in a similar fashion to the operation of the Relative Degree of Alignment (RDA) test, creating a EVA performance “Result.” This may range from -100 to +100, with -100 representing high pay for low performance. A negative result indicates that the CEO pay rank is greater than the average financial performance rank, and a positive result means that the CEO pay rank is below the average financial performance rank. The “Result” is displayed within the EVA Evaluation.

**Resources for Issuers.** All PFP-covered companies are entitled to download their EVA Profile for free. The profile provides a high-level breakdown of a company's EVA calculation and the four metrics to be displayed in the report using the most recently available Quarterly Data Download (QDD) data applicable to the company's next annual meeting. For more information on the EVA methodology, including the adjustments used to calculate EVA, and to download your company's free EVA Profile, visit the [ISS EVA Resource Center](#).

**Measurement Periods.** EVA metrics are generally measured over a three-year period (unless the subject company has only two years of data). For a three-year period, the metrics are calculated over the trailing 12 quarters (or 16 quarters for EVA momentum metrics) as of the applicable Quarterly Data Download (QDD) for each company, using quarterly financial data.

ISS downloads the financial model inputs for all companies four times per year. Downloads occur on the dates below, with the QDD used for a given analysis depending on the shareholder meeting date for the company as shown:

Shareholder Meeting Date Range		Data Download Date
From	To	
March 1	May 31	<b>December 1</b>
June 1	August 31	<b>March 1</b>
September 1	November 30	<b>June 1</b>
December 1	February 28	<b>September 1</b>

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