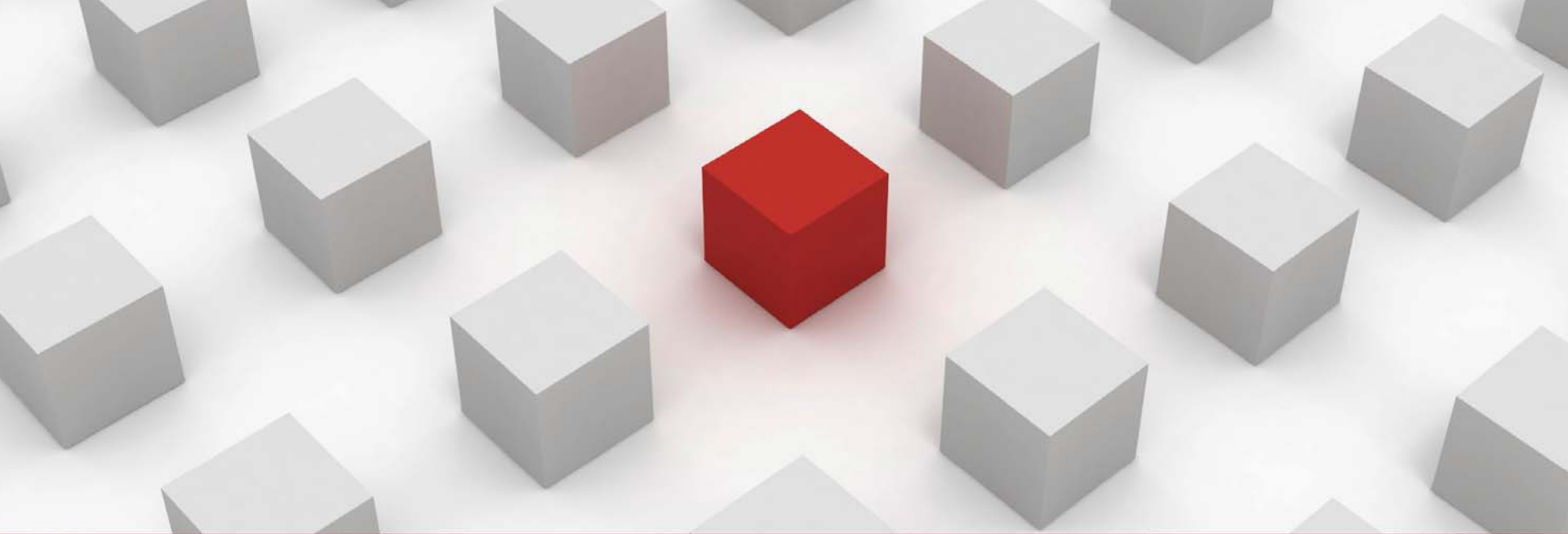


Compensation Management in Difficult Times

**PCI Human Resources Conference
Savannah, GA**

April 7, 2009



The Current Landscape

Key Stress Factors

- Economic Uncertainty
- Job Security
- Current Administration
- Change in Standard of Living
- Fluctuating Stock Prices

Change in Mindset

- Short-range thinking expected
- The need to “keep a steady course”
- “Hunker Down” mentality
- What will best practices be?
 - Bailout and effect on executive compensation
 - Difficulty in predicting market values of pay
 - Composition of total compensation package
 - Increasing importance of annual incentives
- Expect irrational, ambiguous and impractical regulations

Areas of Concern

- **Employees**
 - Keeping their jobs
 - Maintaining 401(k) value
 - Managing with less pay in current market
 - Understanding how their company is doing
- **Human Resources**
 - Retention and workforce reductions
 - Working with smaller budgets
 - Communicating value of benefits
 - Keeping employees informed
 - Working as a strategic partner with Sr. Mgmt.

2008 Annual Salary Budget Planning Survey – Q1 2009 Update

- National survey of 350+ companies
- Industries:
 - Healthcare = 15.6%
 - Financial/Insurance = 15.0%
 - Soc. Service/Foundation = 12.4%
 - Manufacturing/Production = 11.1%
 - Business Services, High-Tech, Retail, Utilities
- Revenues:
 - 26% >\$1 billion
 - 26% \$100 - \$999 million
 - 27% \$10 - \$99 million
 - 21% <\$10 million

What's Happening Now?

- 2008 Projections

- 3.8% Merit Increase
- Salary Reduction--2%
- Salary Freeze--4%
- Layoffs in 2009--6.5%

- 2009 Actual

- 3.2% Merit Increase
- Salary Reduction--4.2%
- Salary Freeze--37.2%
- Layoffs in 2009--35.1%

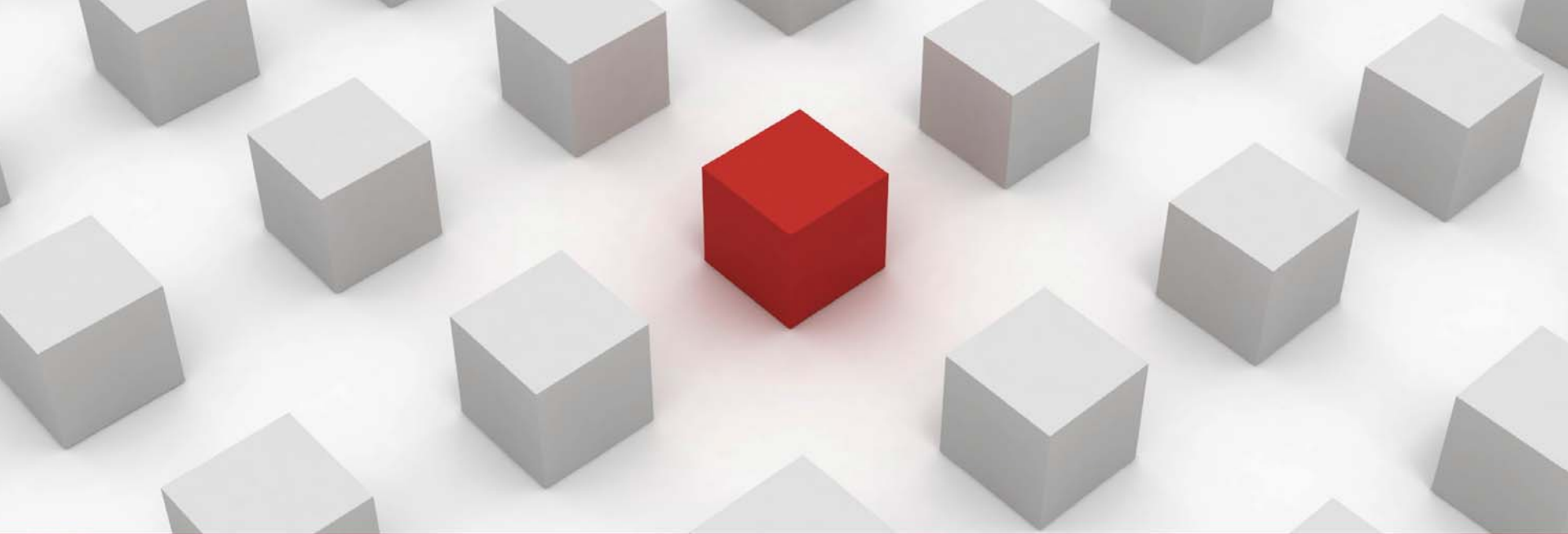
Other Responses to Cost Pressures*

October 2008 to February 2009

- Restrictions on company travel
 - 34% to 69%
- Reduction of training programs
 - 10% to 35%
- Increase communication regarding pay
 - 18% to 28%
- Increase communication regarding benefits
 - 35% to 31%
- Reduce employer match to 401(k)/403(b)
 - 2% to 12%

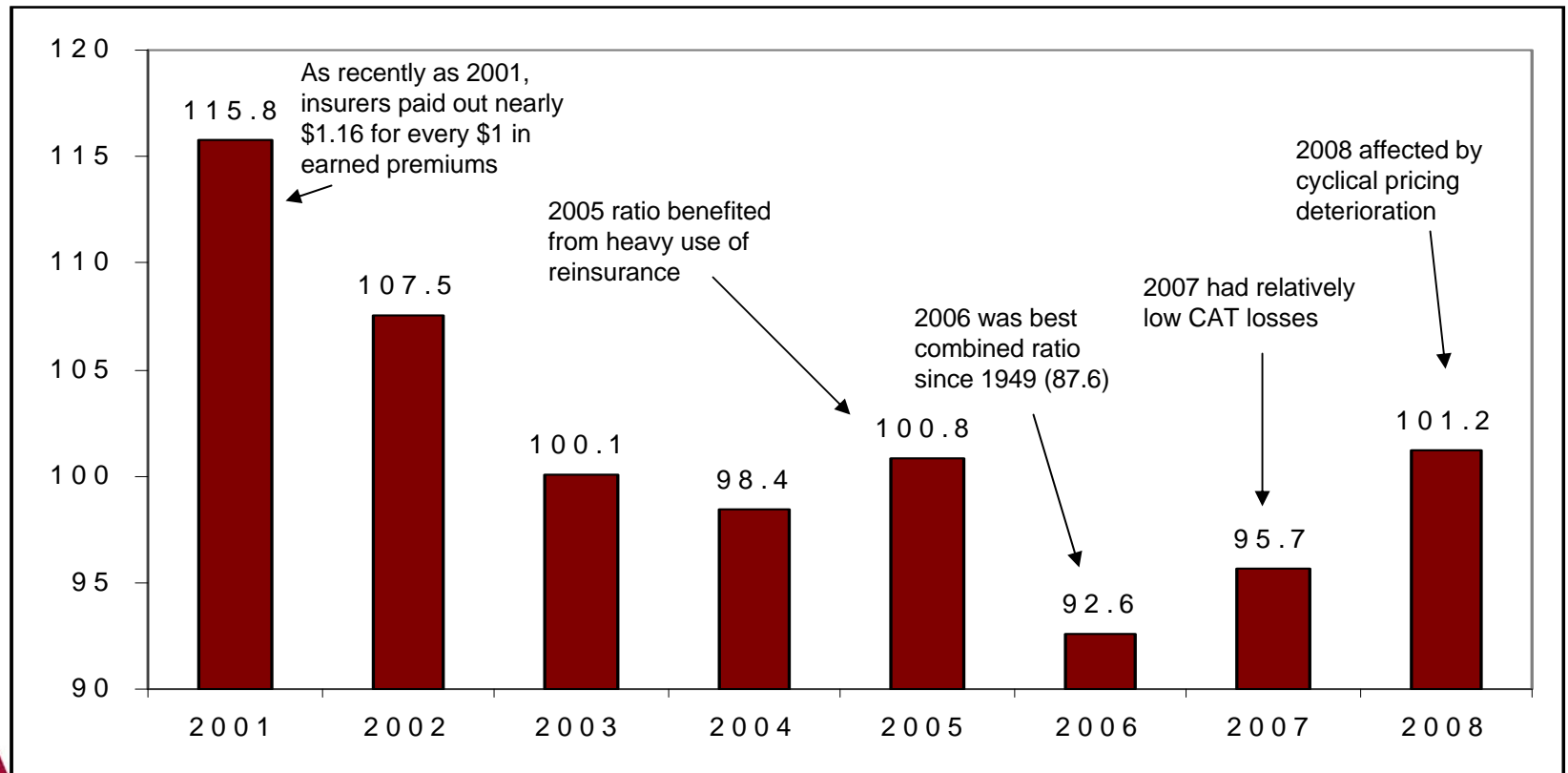
Watson Wyatt survey, March 2009





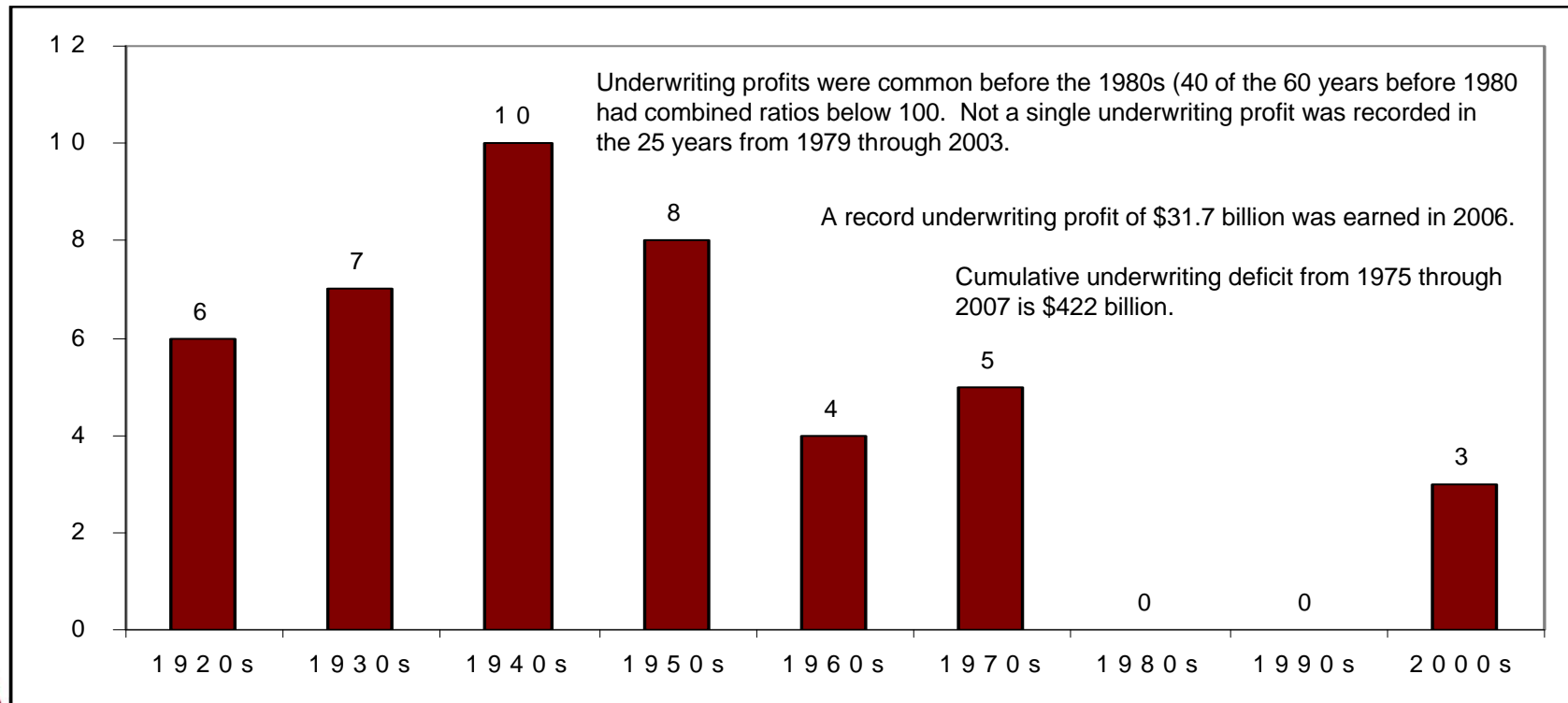
The P&C Insurance Industry in Crisis

P/C Industry Combined Ratio 2001-2008



Sources: A.M. Best, ISO, III

Number of Years with Underwriting Profits by Decade*

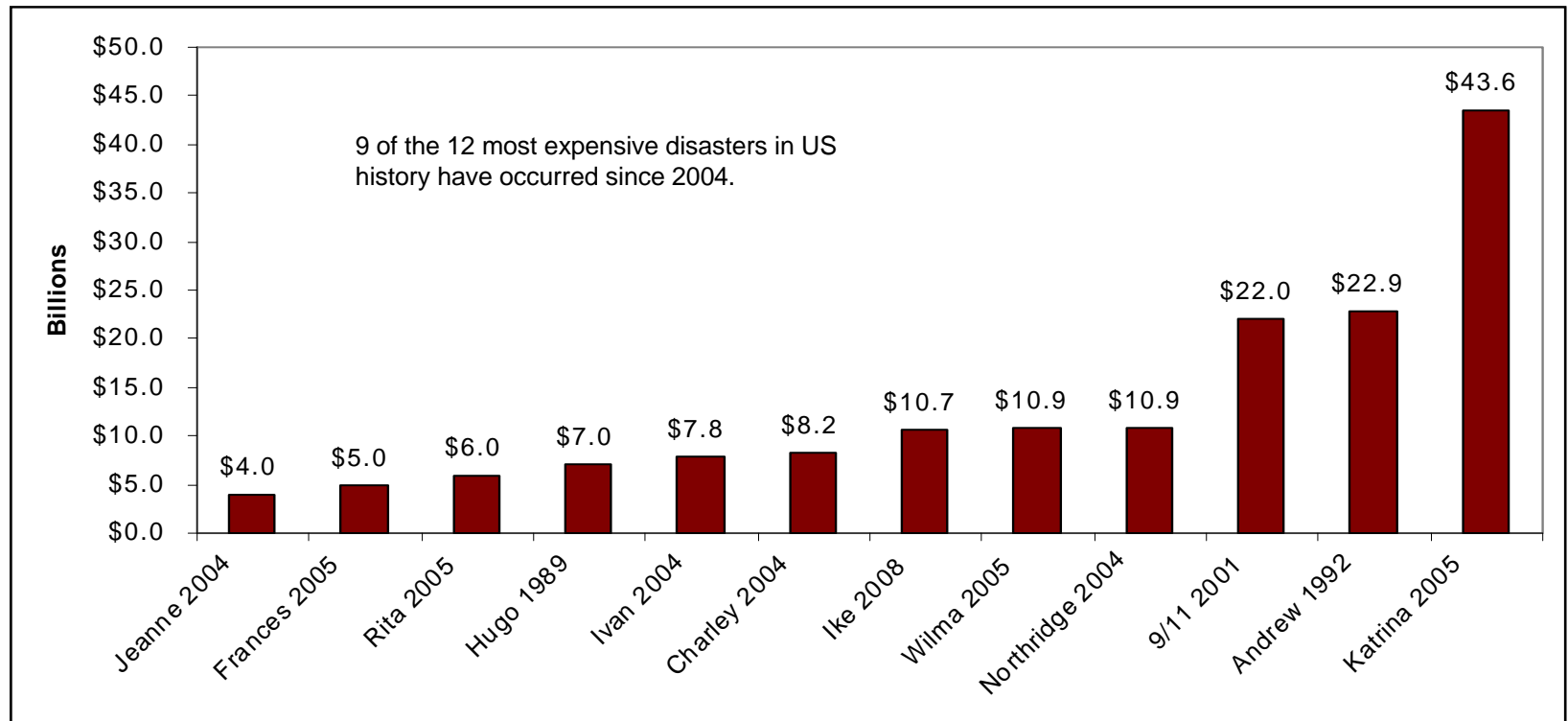


*Based on stock companies only

Source: Insurance Information Institute



12 Most Costly Disasters in US History



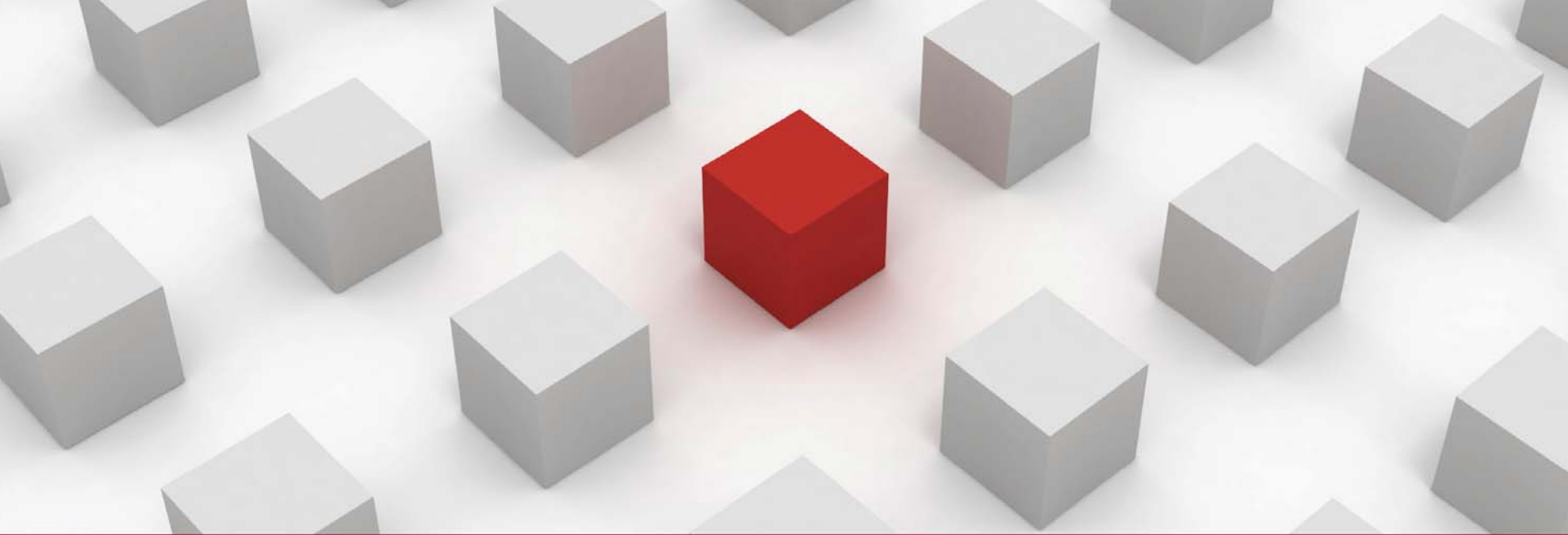
Source: Insurance Information Institute



Why P/C Insurers are NOT Like Banks

- Superior risk management
 - Insurers approach to risk focuses on underwriting discipline – avoid adverse selection
 - Banks sought volume at all costs
- Low leverage
 - Insurers do not rely on borrowed money to underwrite or pay claims
- Conservative investment philosophy
 - Typically high-quality portfolio = less volatile
- Strong relationship between underwriting and risk
 - Insurers maintain “skin in the game”
 - Banks packaged, securitized and sold off the risk
- Tighter regulation and greater transparency
 - Insurers face more stringent rules than banks/hedge funds

Source: Insurance Information Institute



Managing Compensation in Crisis

Compensation Philosophy

- Key factors of a good Philosophy:
 - Define the competitive marketplace
 - Level of competitiveness
 - Mix of compensation elements
 - Degree company uses pay for performance
 - Professional growth
 - Rationale for advancement
 - Variability of pay
- Philosophy is a living document

Basic Objectives of Compensation

- **Was**
 - Attract, Retain, Motivate
- **Now**
 - **Focus** – pay for desired performance
 - **Attract** – ability to hire qualified candidates
 - **Retain** – enhance desire to stay
 - **Motivate** – “carrot & stick”

Basic Objectives of Compensation

- Importance of objectives varies for employee groups

Executives	Sales	Managers/Staff
Focus	Focus	Retain
Motivate	Motivate	Focus
Attract	Retain	Motivate
Retain	Attract	Attract

- Compensation actions should reflect priority of objectives

Total Compensation Package

1. Base Salary
2. Short-term Incentives
3. Long-term Incentives
4. Employee benefits
5. Supplemental executive benefits/perquisites

Base Salary

Before

- Automatic periodic increases
- 162(m) \$1 million cap often exceeded
- Market-driven pay

Now

- Salary freezes and cuts
- Reconsideration of excessive base pay
- Market-driven pay tied to philosophy

Short-Term Incentives

Before

- Regular bonuses expected
- Discretionary bonuses
- Vague and changing goals

Now

- Bonuses suspended or reduced
- Incentive awards tied to performance
- Clearly identified goals/objectives

Long-Term Incentives

Before

- For execs, largest portion of TDC
- Time-based vesting
- Slow shift from options (FAS123R) to other vehicles
- Shorter vesting periods

Now

- Reduced portion of TDC
- Performance-based vesting
- Increased use of RS/RSUs or Cash-based vehicles
- Premium-priced
- Longer holding period
- Clawback provisions

Compensation Outlook Managers & Staff

- Think hard about salary changes
 - Cutting salary is very dangerous
 - Look at specific groups of employees
- Rethink incentive compensation
 - Use compensation dollars judiciously
 - Avoid the “peanut butter” solution
 - What goals will drive the business forward
 - Consider non-cash rewards
- Communicate effectively
- Re-evaluate performance evaluation tools

Compensation Outlook Executive Officers

- Lower base salary to be 162(m) compliant
- Forego bonus if performance is not there
- LTI tied more closely to specific goals
- Holding requirements
- Clawback provisions
- Dual trigger Change In Control provisions
- Perquisites cut dramatically

- Measurable Pay for Performance!

Where Do We Go From Here?

- Clarify your Compensation Philosophy
- Benchmark against the Industry
- Balance compensation elements to fit your needs
- Align goals with desired performance
- Track results and tweak if necessary
- Communicate and coach up and down