

# CSUITE

INSIGHT

## THE **BIG** PICTURE

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CEO Pay and TSR

Seymour Cash Invents the SSRUI



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# LEAD

WITH A CAPITAL "L"!

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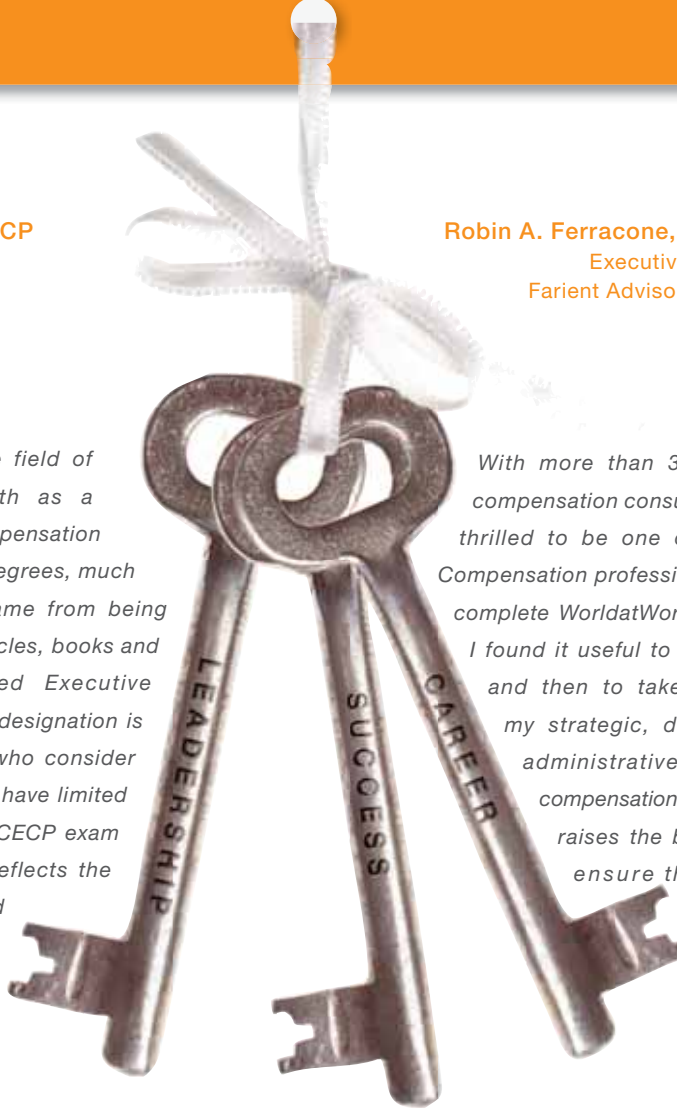
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Randy Keuch, CECP  
Vice President,  
Total Rewards  
HJ Heinz Company

I have spent over 30 years in the field of compensation and benefits, both as a practitioner and as an executive compensation consultant. Aside from my college degrees, much of my learnings in these fields came from being mentored by others and reading articles, books and technical releases. The Certified Executive Compensation Professional (CECP) designation is a perfect solution for those of us who consider ourselves "experts" in our field, but have limited time for formal courses. I took the CECP exam and now have a designation that reflects the body of knowledge that I acquired through the years. This designation is most assuredly a differentiator when considering job candidates in executive compensation.



Robin A. Ferracone, CECP  
Executive Chair  
Farient Advisors, LLC



With more than 30 years of executive compensation consulting experience, I was thrilled to be one of the first Executive Compensation professionals in the industry to complete WorldatWork's CECP designation. I found it useful to prepare for the exam, and then to take the exam to gauge my strategic, design, technical, and administrative skills in executive compensation. The CECP Certification raises the bar for our industry to ensure that those who are working in executive compensation are properly credentialed.

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## LETTER FROM THE PUBLISHER



David has led Equilar from a pure start-up since its inception in 2000 to one of the most respected and trusted names in the executive compensation industry.

## LEADERSHIP

I'D LIKE TO OFFER a warm welcome to all attendees of the Equilar 2011 Executive Compensation Summit in San Diego, where we're premiering this fifth issue of *C-Suite Insight*. I'm looking forward to a fun three days, packed with information and insights about the latest trends in executive pay.

We've put together a speaker roster that runs the gamut of compensation interests, from detailed analyses of all the key trends to the 35,000-foot-level view of the major issues facing directors, C-suite executives and HR professionals.


To complement these discussions, this issue of *C-Suite Insight* covers many of the tangible statistics that are so important to the industry. How much are C-suite executives getting paid? What are the components and what are the trends?

On the other hand, this issue addresses one of the big intangibles: leadership. What does it take to be a business leader? What separates the mediocre from the good, and the good from the great?

No matter what the economic or political climate may be, the essentials of leadership remain critical to success—not only the short-term bottom line, but also the long-term view of value creation and contribution to local communities and the world.

Over the past 18 months, I've been proud of the dialogue we've established with the numerous interviews and feature articles in *C-Suite Insight*. We've decided to extend this effort by providing a free online service, *C-Suite Daily*. If you're not receiving these quick daily summaries of what's going on in the world of business and executive compensation, please go to [www.c-suiteinsight.com](http://www.c-suiteinsight.com) and sign up!

Our annual executive compensation conference is another way for us to interact with our clients and the industry, to gather people together in a conversation, and to examine all of the major issues in detail. I'll be doing my best to stay visible throughout the Summit. If you're attending, I hope you'll come up to me, say hello, and chat a bit.

If you couldn't make it to the conference, I hope you'll still enjoy the important information in this issue of *C-Suite Insight*. As always, feel free to share your questions and comments. 

DAVID CHUN  
CEO, Equilar  
[dchun@equilar.com](mailto:dchun@equilar.com)

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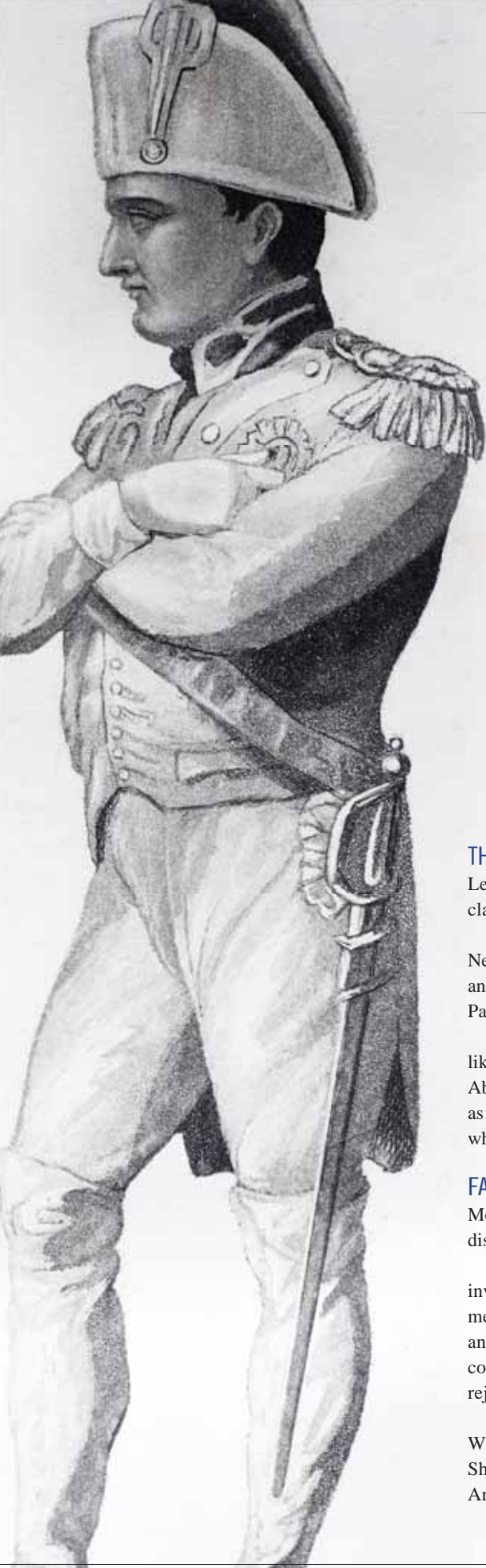
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# The Eternal Value of Leadership

BY ROGER STRUKHOFF

Leadership is the most prized commodity among, well, leaders.  
Without it, organizations and countries fail.



# Fundamentals

The word's roots are humble, coming from the Old English and German "leder," or "leather," for the leather straps with which horses are led. And that's it. Nothing profound or transcendent.

We expect our leaders to do much more than hang onto the straps. We expect them to transcend the day-to-day humdrum, to set a tone and create a vision, and to Lead with a capital L.

## THROUGH THE MILLENNIA

Leadership is something that transcends time and cultures. Every ancient civilization, classical empire, and modern-day nation has its pantheon of great leaders.

Military leaders have ranged from Alcibiades and Hannibal through Napoleon and Nelson, the generation of leaders in WWII, or today's David Petraeus. The sports world is an oft-cited source of great leadership, whether one is talking about Vince Lombardi and Paul Brown, Bill Walsh and Bill Belichick, or John Wooden and "Coach K."

In business, ancient texts such as Sun Tzu's *The Art of War* (and their modern glosses, like *Leadership Secrets of Attila the Hun*) have risen in popularity. Many have studied Abraham Lincoln in the search to identify leadership characteristics. Absolute values such as truthfulness, loyalty, courage, and tenacity have been examined among many people who've been recognized as great leaders over the millennia.

## FAST FORWARD TO TODAY

Modern-day leadership gurus, starting with Tom Peters in the late 70s, are frequently read, discussed, and imitated.

In modern-day American business, the names of a few legendary CEOs are routinely invoked in discussions of leadership: Jack Welch at GM, Lou Gerstner at IBM, several members of the Intel gang. Today, Microsoft's Gates & Ballmer, Oracle's Larry Ellison, and Apple's Steve Jobs, in particular, are lauded. Amazon's Jeff Bezos has quietly continued to enjoy corporate success, and Howard Schultz is back in the news after rejuvenating Starbucks.

Women aren't absent from the list, whether the discussion is about eBay's Meg Whitman, Mary Kay Ash and the cosmetics company she founded, Ogilvy & Mather's Shelly Lazarus, or current CEOs Ellen Kullman of DuPont, Andrea Jung of Avon, or Anne Mulcahy of Xerox.

## A PAIR OF INSIGHTS

This issue of *C-Suite Insight* is focused on leadership. To learn more, we interviewed two present-day experts in the field. Dr. Curt Crawford has served as a high-level CEO, and currently offers leadership lessons through his firm, XCEO. Korn Ferry's Joe Griesedieck has a special interest in succession planning, an area that many leaders don't like discussing because they are, after all, discussing who will replace them. A full interview with Crawford can be found on page 18; our interview with Griesedieck will appear in the next issue of the magazine.

Post-interview, we gleaned some additional comments from them on the subject of leadership. For one thing, we were interested in learning about how leaders stay cool under pressure. They may look and sound great in good times, but what does it take when things get rough?

Dr. Crawford told us, "When the ride gets bumpy, you want to make sure you're doing the fundamentals correctly."

## THE FUNDAMENTALS COME DOWN TO THREE IMPORTANT AREAS

"The first area is, How effective is the board?" he asked. "The board has to be effective in how it conducts its business, and there are ways to measure its effectiveness beyond short-term indexes like stock price."

The second challenge is to determine "the core strengths and experience of the board members," he said. "And does the board have an effective way of assessing and understanding how to maintain [its own] very high performance?"

The third aspect is to measure how the CEO is actually performing. "Leaders want to be held accountable," according to Dr. Crawford. "They expect it, and they expect to produce outstanding results." Looking at results on a monthly or quarterly basis is not an exercise in watching the stock value, per se, but in determining "whether or not the company is moving in the right direction."

Dr. Crawford also puts a premium on a will to win. "No one remembers who finished in second place," he said. "The idea here is that winning does count. People want to be associated with companies that win, and with a CEO who says, 'I win most of the time' instead of 'I win some of the time.'"

## FIND YOUR SUCCESSOR!

Does a single-minded emphasis on performance and winning put the critical issue of succession planning on the back burner? It does not, according to Griesedieck. "Maybe it did a few years ago, but not today. We've found that a lot of boards felt they didn't have a good succession plan in place. The way I translate that is that [they're referring to] a succession plan that is defensible in terms of shareholder reactions or ISS reactions."

Griesedieck says boards are asking themselves, "Are we confident that we're going through the right steps to say that we've done a thorough job in assessing both internal and external candidates?" Overall, he concludes, "I would say that succession planning is, in fact, much more on the front burner."

## BE AGILE! STAY AGILE!

What about agility? A CEO can have all the tangible and "it factor" intangibles to be a great leader, and a board can create a solid succession plan, but most companies face continuously changing markets and competitors.

effectiveness  
core strength  
& experience  
accountability  
agility

*Leadership is really about making sure that people are pushing themselves to the limits, while staying within the guidelines, of what they really want to do*

Dr. Crawford uses DuPont as an example of how to be agile. “Ellen Kullman understands that she has to compete on a global basis, and she has to compete against start-ups in Silicon Valley, as well as major industrial companies that have a history of building products similar to DuPont’s,” he said. “DuPont today is not the company it was when I joined the board about 15 years ago.”

“The company has a rich history of intellectual property, and does have a history of reinventing itself,” Crawford noted. “When it started out, dynamite was a core business. But if you look at the company today, you see DuPont’s business in Kevlar, and Tyvek, and an entire agricultural business that’s designed to help feed the world.”

Griesedieck echoes those comments: “First of all, [a leader] has to understand what the strategy of a company is—not just today, but what it’s going to look like three or five years out. And people who have done a great job in the company up until now may not be the right people to lead the future. The company may need different experiences and different competencies.”

That doesn’t necessarily mean looking outside, Griesedieck said. “[Companies] should look internally. If boards are doing their jobs, they should not only be looking at CEO succession, but also the whole C-suite and below. They need to make sure the CEO and the Head of Human Resources or Talent Development are really looking at developing talent. Because you don’t want to go outside if you don’t have to; it’s always riskier, culturally and otherwise.”

“If you’re a big company,” he says, “you should have the luxury of having multiple candidates. If you’re a smaller company, it’s harder. Even so, as boards assess internal candidates, they do a ‘talent benchmarking.’”


“This is not a search, but just a look, to ask, ‘Who would be best-in-class, according to our spec, if we were to look outside?’ By doing so, they can come back to any constituent or shareholder group and say they’ve actually done a very thorough job of not only vetting the internal candidates but looking at who would be good on the outside.”

In conclusion: “The day the CEO is appointed is the day the board should start planning for his or her succession.”

#### THE BIG PICTURE

What about industry relevance? One of the great success stories was Lou Gerstner’s time at IBM, even though he came from the food business. Griesedieck noted, “Lou had been successful in everything he did. He was successful at McKinsey; he was successful when he was in the food business. So [the IBM board] didn’t have to look so much at his industry experience. But what were the leadership skills that he brought to IBM?”

“Learning agility” is what boards should truly seek, says Griesedieck. He defines it as “the ability to adjust and adapt to new situations and find a way to succeed.”

Dr. Crawford’s own leadership company, XCEO, focuses on “the X-factor of excellence,” he said. “Leadership is really about making sure that people are pushing themselves to the limits, while staying within the guidelines, of what they really want to do. The X-factor also means achieving extraordinary levels of performance. It describes a passion and a level of energy; people really are willing to commit to doing what’s important to them, and to do it—fairly, honestly, ethically, morally, and legally.” 



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# C-SUITE INSIGHT

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GOVERNANCE  
STANDARDS

ANNUAL  
INCENTIVE  
PROGRAMS

## What Are the **BURNING ISSUES?**

At *C-Suite Insight*, we have benefited from the input of the numerous industry consultants and legal experts who read and contribute to the magazine. For this issue, we wanted to step back from the day-to-day and find out what bigger issues concern these industry leaders. Rather than ask them a specific question about, say, Dodd-Frank or new SEC regulations, we hit them with this:

**For compensation and governance professionals, what is one idea that should be questioned, reconsidered, scrutinized, or otherwise challenged?**

As expected, the answers didn't all focus on a specific area, but covered a lot of ground.

### CHALLENGING GOVERNANCE STANDARDS

David A. Hofrichter, Ph.D.  
Principal & Leader,  
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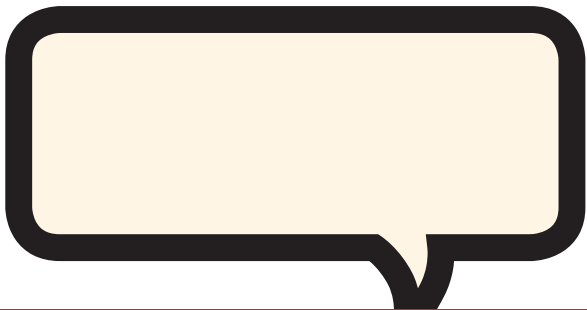


It is now commonplace to view stock ownership guidelines, clawback provisions, stock holding requirements, etc. as required pillars of any well-designed executive compensation program. Their primary intent is to rein in the perceived excesses in executive pay and better align leadership behavior with shareholders' interests.

But do they really? New Aon Hewitt research would suggest that executives' satisfaction with their compensation programs is decreasing. Some may dismiss this as just their natural reaction to being reined in and having limits imposed upon them.

But what if it is more? What if the plans of today, with all their supposed safeguards, are not impacting anything? Do we really believe that an executive with a 5x ownership requirement will do anything differently from one with a lesser requirement, or none at all? Or that the existence of a clawback provision will really reduce risk-taking behavior?

We need to challenge these "legislated solutions" and really determine what design elements truly impact value creation and positive behavior.



QUESTIONING THE ROLE OF LONG-TERM INCENTIVES

Steve Cross  
Managing Partner  
Cogent Compensation Partners  
Houston, TX



Over time, the role of long-term incentives has evolved significantly. With the advent of market volatility and risk mitigation, perhaps it is time for compensation and governance professionals to challenge their role.

The pressure to make long-term compensation strictly “performance-based” has led professionals to create ever-tighter linkages to company performance. This is not without some unintended outcomes. For example, it is more difficult to set goals and measure absolute performance, which has led to shorter measurement periods and more relative performance comparisons.

Obscured is the real linkage between absolute shareholder value creation and the executive contribution over the long term. Many performance-based LTI programs have evolved to fit the category of mid-term performance plans. While there may well be a role for such plans in total compensation, perhaps it’s time to reevaluate the definition of long-term incentive compensation.

EXAMINING PAY FOR PERFORMANCE

Peter Chingos  
Senior Partner  
Eric Hosken  
Partner  
Compensation Advisory Partners  
New York, NY



Compensation professionals focus a lot of time and effort on establishing market competitive target total compensation levels, without always ensuring that actual compensation delivered is aligned with performance results.

By and large, companies apply adequate rigor in reconciling compensation outcomes with actual performance, versus pre-established internal performance goals. However, an assessment of performance relative to the company’s internal goals may not tell the whole story.

We think that many companies could provide a more complete year-end assessment of performance by also looking at performance versus peers and versus Wall Street expectations. This kind of a year-end “back-test” of the pay-for-performance relationship from multiple perspectives allows the company to better align pay levels with performance, particularly in industries where financial goal-setting is a challenge.

Companies that consistently meet internal goals, while coming up short compared to peers or Street expectations, may need to assess whether the pay-for-performance relationship is responsible, and whether the degree of stretch supports the corresponding pay delivery.

USING DISCRETION IN ANNUAL INCENTIVE PROGRAMS

Jim Wolf  
Managing Partner  
Meridian Compensation Partners  
The Woodlands, TX



Annual bonus programs should be hands-on, rather than arm’s length. Third parties often criticize the use of board discretion in determining bonuses, especially when payments appear excessive. However, a credible evaluation of organization and individual performance requires a degree of subjective evaluation.

A board exists to exercise sound judgment. While adhering to a prescribed financial formula may appear to improve corporate governance, blindly accepting a formula output over broader observations can generate payments that are misaligned with performance. Sound governance and business judgment requires a balanced evaluation of business metrics with other observed performance.

Areas often requiring a discretionary evaluation include the treatment of extraordinary gains or losses, M&A activity, management responses to unforeseen events, strategic initiatives and environmental or safety performance.

Advisors should help boards apply discretion effectively: pose questions, challenge conclusions, and facilitate discussion.

SUBVERTING THE DOMINANT PARADIGM

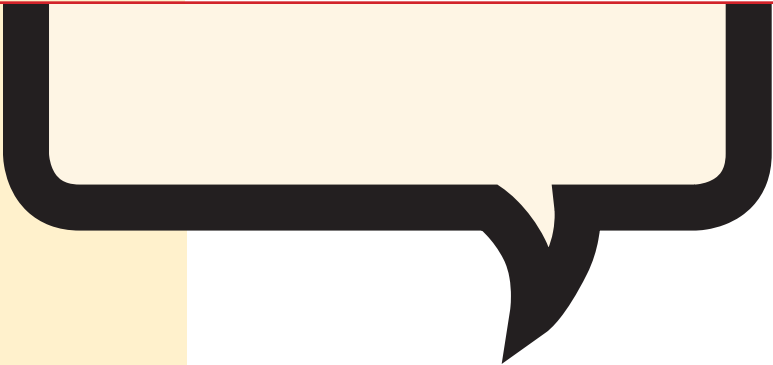
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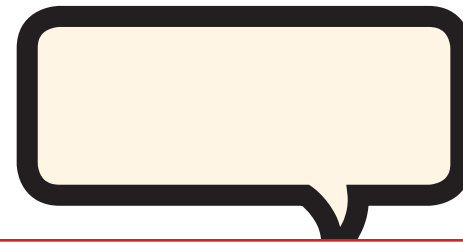


We should move away from both (a) a single dominant paradigm of how to motivate and reward executives (i.e. base salary, annual performance bonus, equity awards or other long-term incentive compensation and post-employment security benefits) to more creative and varied solutions tied to the particulars of each enterprise and of the individuals occupying the key roles, and (b) relying exclusively (or at least overwhelmingly) on compensation to motivate and reward executives.

The industry should instead apply greater psychological sophistication and insight in developing arrangements, to align the interests, objectives, and self-realization and worth of executives with the long-term success of their corporate employers.

Unfortunately, an obsessive focus on the across-the-board comparability of proxy disclosure, the adoption of say on pay, and the influence of proxy-advisory firms and their ilk are likely to push us in the opposite direction, towards greater uniformity and standardization around so-called best practices. We should resist that pressure.





**MORE COMMON SENSE,  
FEWER INFLEXIBLE FORMULAS**

Jonathan Ocker  
Chair of Compensation & Benefits,  
7 Global Corporate Secretary Groups  
Orrick, Herrington & Sutcliffe  
San Francisco, CA



It is human nature to fall prey to generalizations, rather than to consider all of the facts before making a decision. Too often, shareholders and compensation committees follow the recommendations of ISS and compensation consultants, without questioning whether the recommendations are appropriate for the specific business needs of the company.

We need a less formulaic approach, and more common sense from all constituents, when evaluating recommendations and voting on executive compensation proposals.

Among many others, ISS has a voting guideline that can result in a “no” vote on management’s say-on-pay proposals when such an outcome is not warranted.

One case in point is repricing. Stock option repricings have become poor pay practices. Yet if a company finds that it is necessary to reprice stock options as a business strategy to incentivize employees, ISS will recommend a say-on-pay “no” vote, even if executive officers are specifically ineligible to participate in the repricing.

However, say on pay is a nonbinding referendum on executive compensation, and a “no” vote recommendation on a repricing that does not involve executive officers is not warranted. There are other examples of ISS’s influence that have led to binary, non-reflective decision-making. For example, the Shareholder Value Transfer calculation and Poor Pay-for-Performance test, while helpful reference points in evaluating executive compensation, often govern decisions.

**PONDERING THE  
PORTFOLIO APPROACH**

Robbi Fox  
Senior Advisor  
Exequity  
Libertyville, IL



I believe the one idea that should be challenged is the view that a portfolio approach to long-term incentives makes sense for every company and all participants.

In the last few years, we have increasingly seen companies move to using a portfolio approach to long-term incentives, typically a mix of stock options, performance-based shares or units, and time-based restricted stock or units. The general rationale is that “all eggs should not be placed in one basket,” and a portfolio approach balances risks.

Although this may make sense for many companies, it’s not necessarily the most appropriate approach for everyone. In the case of a high-growth company, does it make sense to use restricted stock?

The typical arguments for the use of restricted stock are that executives can build stock ownership, and that the stock is needed for retention purposes. Can stock ownership be developed with performance plans, or even paying a portion of the annual bonus in stock? Is there even a retention issue? What message is the company sending to the market (with respect to its confidence in the company’s potential) if restricted stock is used?

There has been a decline in the use of stock options, even though stock options reflect an alignment of executive compensation with ultimate shareholder value creation. Challenging the portfolio approach to long-term incentives is actually one issue within a larger arena, which is that compensation-design practices are starting to all look alike, even though there are clearly very significant differences among industries, companies, life-cycles, and business objectives.

Our profession needs to challenge itself to look beyond the latest “flavor of the month” and what everyone else is doing.

# VIEWS

## INTERVIEWS

This issue of *C-Suite Insight* takes a big-picture view of executive compensation and the issues surrounding it. Our collection of four interviews follows that theme.

We start with XCEO’s Dr. Curt Crawford, who shares his insights on leadership, a quality everyone agrees is essential, but can be hard to define and implement.

No organization boasts a more extensive vision than CalPERS when it comes to seeing the big picture from an investor’s point of view. Famous for its scope and size, this organization’s leadership is always willing to speak up about corporate governance. Anne Simpson of CalPERS lets us know her current thoughts.

We then turn to Professor Kevin Murphy of USC, who offers pointed views on how politicians in Washington, D.C. have tried to upend Wall Street culture, and tells us what the real big-picture issues are to him. Professor Murphy also contributes a brief look at the history of CEO pay.

Finally, well-done surveys are a great way to get a valid big-picture view of business. So we end this series by interviewing WorldatWork’s Ryan Johnson, who tells us how his organization aims to bring consistency to conflicting information in executive compensation surveys. He also fills us in on some new developments.



**Dr. Curtis J. Crawford**  
Founder, President and Chief Executive Officer  
XCEO, Inc.



**Anne Simpson**  
Sr. Portfolio Mgr., Head of Corporate Governance  
CalPERS



**Dr. Kevin J. Murphy**  
Professor, Marshall School of Business  
University of Southern California



**Ryan Johnson, CCP**  
Vice President, Publishing & Community  
WorldatWork

INTERVIEW WITH **CURTIS J. CRAWFORD**

**L**eadership is essential, if sometimes difficult to define. But no company will be successful without great leadership in the C-Suite and on the board.

To dig into the details of what makes a great leader, *C-Suite Insight* recently interviewed Dr. Curtis J. Crawford, Founder, President and Chief Executive Officer of XCEO, Inc. He is the author of several books, including *The Manager's Guide to Mentoring*.

Prior to founding XCEO, Dr. Crawford was President and Chief Executive Officer of Onix Microsystems, and also served as Chairman of ON Semiconductor Corporation. He's also served in C-Suite positions at Zilog, AT&T Microelectronics, and in the Microelectronics Group of Lucent. He began his business career as an IBM systems engineer.

Dr. Crawford received a B.A. and M.A. from Governors State University, an M.B.A. from DePaul University, and a Ph.D. from Capella University. Today, he sits on the Board of Directors at both DuPont and ON Semiconductor.

**"LEADERSHIP IS ONE OF THE LAST FRONTIERS FOR CORPORATIONS TODAY."**

**C-Suite Insight:** What's the first thing you would say about leadership and business today?

**Curt Crawford:** Leadership is one of the last frontiers for corporations today. By this, I mean, you cannot outsource leadership. It has to be done by the organization itself.

The same thing holds true for individuals. An individual has to take responsibility for his or her own development, and seek out ways to leverage the support they get from others.

**CSI:** But leadership is also focused on competition, I would think.

**CC:** Of course. And in my view, it is the difference-maker between those who merely compete and those who win consistently.

You know, the difference between winning and losing, or coming in first and coming in second, is typically not a large margin. But the difficulty in winning continues to increase because competition gets more and more fierce.

So we, as corporations or as individuals, need to find every competitive advantage that we can, in order for us to increase the odds of winning. Developing leadership skills is the way to do this.

**CSI:** I was thinking a lot of these people make it on their own skills, and it might be difficult to approach such

## AN INDIVIDUAL HAS TO TAKE RESPONSIBILITY FOR HIS OR HER OWN DEVELOPMENT.

strong-minded individuals to say they may need help. It sounds like you focus on the question, "Well, do you want to win the gold, or will you settle for the silver?"

**CC:** Yes, you've captured the essence of my point. Those who win are typically those who get help.

If you look at any major activity, whether it is in sports or politics or in business, the ones who typically win are those who are at a point where they understand and value help as a differentiator for them.

I was mentoring one of my friends in Atlanta a couple of years ago. I said, "Mentoring is a very powerful difference maker." And he said, "Well, I don't think I need a mentor."

I simply replied, "I understand that," which prompted him to ask, "Well, what do you understand?" I said I don't need one."

I told him, "Well, because you're not going for the gold. The only people who need mentors are those who are convinced and willing that they want to win. And those who do, they get help."

**CSI:** You worked for many years as a top executive. When did the light bulb go on that you could teach to others what you had learned as an executive?

**CC:** There was a very specific point in my career where I had somewhat of an epiphany, where I thought that I needed to capture what I'm thinking in a succinct way, then try to deliver it so that it would be consistent to an entire organization.

This was in 1995. At the time, I had maybe 30,000 to 40,000 people working for me. I remember preparing for a meeting and being concerned about two things: that we were performing exceptionally well, and that even so, maybe we weren't performing as well as we could.

**CSI:** How did you put these thoughts into writing?

**CC:** Well, I didn't know how to measure what I was thinking, so I decided to write this speech about it. I sent copies of that speech to the Chairman and President of AT&T, and also to Jack Welch, who

was Chairman of GE at the time. I received great notes back from each of them, suggesting that not only was my message on target, but I should find a way to share that on a much broader platform.

**CSI:** How does what you teach apply to organizations of different sizes? Is your message effective running the gamut from entrepreneurial start-ups, through small to medium businesses, to very large corporations?

**CC:** Leadership is done one-on-one. That's how it happens. Leadership is not the charismatic person speaking in an auditorium to 60,000 people. So if I have an organization of 20,000 people working for me, it generally happens in one-on-one situations, or one-on-three, one-on-ten.

**CSI:** As a leader, you're trying to inspire your company's leaders...

**CC:** The responsibility of the leader, as I view it, has always been to create an environment—in very selective words—that inspires each person to perform at the highest levels of his or her capability. That's my aspiration.

**CSI:** Consistently.

**CC:** Every day I come to work and try to create an environment in which my colleagues are inspired—not required, but inspired—to perform the best they know how. If I find that their aspirations are insufficient to get us to the level that we need to get to, then I need to get the people who work with me that do have the aspirations that are properly aligned with our business goals.

You have to create the environment that people come into every day, and in which they want to kick the door down to get here, rather than wait in the parking lot until one minute before they're required to show up to work.

**CSI:** Then how do you set an example of leadership as a board member?

**CC:** The boardroom is an ideal place to demonstrate leadership, and to test whether or not you can be effective at doing so.

You're with a group of equals in responsibility, and generally so based on their experiences as well. The particular collection of individuals that have been selected and approved by the shareholders are considered to be very, very successful people.

**CSI:** So how do you add value in this high-achiever environment?

**CC:** The way I go about doing that is making sure that I am prepared as best as I can be. Then I look for opportunities where, based on my experiences and my interests, I can add value.

I don't just go to a board meeting and participate, I go to a board meeting anticipating opportunities where I can add value to my colleagues. I also look to see where I can add value to the CEO in helping him or her create shareholder value. I make this effort, and I encourage other directors to make this effort to find out your sweet spot—the place where you can bring something to the boardroom table that helps all of us perform better.

**CSI:** But unlike the case with employees, these board members aren't working for you. How do you influence them? How do you really get through to them?

**CC:** You have to earn the opportunity to make an impact. You do that by being prepared; you do that by being passionate; you do that by being effective at what you do. So therefore, being prepared, being knowledgeable, understanding how to be effective, is critical in a boardroom. ■

YOU HAVE TO EARN THE OPPORTUNITY TO MAKE AN IMPACT.

## INTERVIEW WITH ANNE SIMPSON



**D**escribed as “one of the world's most influential investor activists,” Anne Simpson serves as Senior Portfolio Manager and head of Corporate Governance at the California Public Employees' Retirement System (CalPERS), which is the largest public pension fund in the United States.

With more than \$235 billion in market assets, CalPERS provides retirement and health benefits to more than 1.6 million public employees, retirees and their families.

Prior to joining CalPERS in mid-2009, Anne served as Executive Director of the International Corporate Governance Network (ICGN), an organization that represents investors responsible for \$15 trillion in global assets—roughly the value of the entire U.S. or EU economy.

Anne has authored two books on corporate governance, and also serves as a Senior Faculty Fellow and Lecturer in Yale University's School of Management. She is a graduate of Oxford University, and was a Slater Fellow at Wellesley College.

*C-Suite Insight* conducted a wide-ranging interview with the London native, now based out of CalPERS' headquarters in Sacramento, California.

Our interview with Anne will appear in two parts, with the conclusion in the next issue of *C-Suite Insight*. In the first part of the interview, we started with say on pay, but quickly expanded to discuss the bigger picture, on this issue and others.

“SOCIETIES NEED BIG SHAREHOLDERS TO ENGAGE BECAUSE THE QUESTION TO US IS, ‘IF NOT YOU, THEN WHO?’”

## SAY ON PAY

**C-Suite Insight:** Say on pay is a big issue these days, of course, so let's start there.

**Anne Simpson:** Sure. CalPERS has long been a supporter of say on pay, for the simple reason that shareholders bankroll this [corporate] expense. We think it's only polite to ask the opinion of those who are providing the funding.

**CSI:** Well, it is shareholders' money, after all.

**AS:** Yes, but the serious reason is to ensure alignment of interest over the long term. We want boards to pay attention to the owners, who are paying for all of this. Yet the invention of say on pay means very little, unless we also have directors standing for election.

**CSI:** It's been described as a blunt instrument...

**AS:** More like a feather duster. Because let's say you put your proposal on pay to the vote, and you lose. The question becomes, "Then what?" The board can simply say, "You didn't like what we did, see you in court; or, sell your shares."

I would say that say on pay is very welcome, because pay is just wildly out of control in too many places in the United States. It needs to be brought back under control. It's a waste of money

if you're not deploying your capital productively, and the expansion in pay in the C-suite has not always been accompanied by commensurate performance.

**CSI:** So what are you and your army doing about it?

**AS:** We have made a priority this year of going company-by-company, board-by-board, and negotiating the introduction of majority voting. Because ultimately, regardless of this popularity vote on pay, which is fine and a good thing, the real issue is being able to hold board members accountable, including the people who sit on the compensation committee.

You know they're there to do a job. If they don't do the job properly, then they should step aside and let others come forward. So majority voting is really important.

## GOVERNANCE AND RESPONSIBILITY

**AS:** You know, way back in the 70s, Peter Drucker wrote a book called *Pension Fund Socialism*, in which he took the view that as ordinary people's money was pouring into pension savings, these would therefore become the dominant shareholders.

**CSI:** And?

**AS:** Well, dream on, Peter Drucker, and God rest you wherever you may be, but the

reverse has happened. The money has poured in without any updating of the mechanisms for oversight. So now we have a 21st-century capital market with a 19th-century governance structure. We've got a lot of work to do.

**CSI:** You mean that working-class individuals are major investors today, but within a system that was set up for the Gilded Age...

**AS:** We've known for a while that companies do not make money in a vacuum. Companies are about people and communities, and markets are about communities and societies. Reputation is vital. At CalPERS we understand that sustainability is fundamental to the risk and return equation.

**CSI:** Let's pursue this a bit. CalPERS was out in front of the movement to disinvest from South Africa when it was an apartheid nation. Today, the focus may not be so much on states but on companies' working conditions: Nike has come under fire, factory suicides in China have been related to Apple, people are concerned about where Starbucks gets its coffee...

**AS:** Absolutely right. The international push for disinvestment from South Africa was seen as a critical part of putting pressure on the apartheid regime. These

days, can you financially isolate a regime in what have become global markets? I think the answer is no.

The second part of your question is more interesting, because globalization means that you have a community of owners across borders. They could and should be ensuring that proper standards are met.

There are questions about how they conduct themselves ethically and socially, their commitment to human rights, the labor standards and quality, consumer safety, and whether anyone would want to have tainted goods.

The global village that we create through modern media means that there is a much stronger sense of community. People think, "Well, you can see there's child labor in Pakistan or Indonesia," or wherever it might be. There is an immediate sense that these are kids—as opposed to the thinking of a bygone era that I was brought up in, where people often thought, "Well, these are foreigners, grateful for the work."

The whole framework of international standards emanating from the United Nations has been very important, and the dissolving of borders [when it comes to] trade and capital flows is a very positive thing. The result is that corporate responsibility is an investment issue.

## THE GLOBAL VILLAGE THAT WE CREATE THROUGH MODERN MEDIA MEANS THAT THERE IS A MUCH STRONGER SENSE OF COMMUNITY.

## GLOBAL REACH

**CSI:** This global supply chain affects stock markets outside of the U.S. in a big way. CalPERS, which is just one example of a major fund, has investments in more than 40 different countries.

**AS:** Yes, we're actually in 47 global markets now. Equity investment funds want to find a way to expose our portfolios to economic growth, and the fast-growing economies of the future are, I'm afraid, not going to be either the U.K. or the U.S. They're going to be emerging markets.

**CSI:** How do you get a handle on these markets?

**AS:** We have something called "emerging markets principles," which is a screening service that identifies issues. We flag companies on a range of social, environmental, and ethical issues.

**CSI:** Where and how can you draw the line?

**AS:** Generally, we've found that many issues can be

solved, whether it's companies doing business in Sudan or Iran or any trouble spots around the world, or dealing with particular issues like health and safety.

CalPERS is just too big; there's nowhere for us to go and hide. We need markets to work—that's essential for us to fulfill our fiduciary duty, which is to pursue prudent risk adjusted returns to pay long term benefits like pensions.

**CSI:** Meaning?

**AS:** There's nowhere for us to go and find a pure and perfect corner of the stock market. There's no land of milk and honey; it doesn't exist. But societies need big shareholders to engage, because the question to us is, "If not you, then who?"

We're not going to be able to fix this with government alone. Regulation matters, but governments are at the national level, and under pressure with stretched resources. But we need to intervene as owners to try to effect change, the positive direction of change. There's no excuse for not doing that. ■

INTERVIEW WITH **KEVIN J. MURPHY**

**K**evin J. Murphy is the Kenneth L. Trefftz Chair in Finance and Professor of Finance and Business Economics at the USC Marshall School of Business. He also serves as Professor of Business and Law at the USC Gould School of Law. He earned his MA and Ph.D. at the University of Chicago, with a B.A. from UCLA.

Executive compensation is one of his areas of expertise; he worked as a consultant with TARP Special Master Kenneth Feinberg's office, and has also testified before Congress about executive compensation issues.

Speaking over the phone, Murphy discussed what's transpired since the onset of the Great Recession, and the roles of government and academia in the business world.

“CONGRESS DIDN'T WANT TO FIX COMPENSATION. THEY WANTED TO DESTROY IT.”

**C-Suite Insight:** You've written that you really thought the U.S. Congress was more interested in punishing Wall Street, and upending its bonus-based culture, than in serving taxpayer interests. You've also contrasted that with what you saw as a more moderate position taken by the Obama administration. What are your thoughts today?

**Kevin Murphy:** Without question, many influential members of Congress were obsessed with putting an end to the Wall Street bonus culture. Their motives were driven, in part, by a belief that the culture is what drove us off the cliff and caused the crisis, and the only solution was to destroy the current system and start over from scratch.

A larger part of Congressional motives, however, were driven by raw anger over bankers, bonuses, and bailouts. The anger erupted when Merrill Lynch paid big bonuses just before the BofA merger, and exploded after AIG announced bonuses for its financial unit. Congress needed someone to punish, and the Wall Street bonus culture was an easy and obvious target.

**CSI:** What in particular struck you as an overreaction?

**KM:** Congress didn't want to fix compensation. They wanted to destroy it. They prohibited TARP recipients from paying any kind of incen-

tive bonuses, stock options, signing bonuses, severance bonuses, golden parachutes to their top 25 employees—allowing only base salaries and relatively small amounts of restricted stock.

Effectively, Congress took away the most effective tools banks have to provide incentives. It imposed a huge competitive disadvantage on TARP recipients trying to compete with non-TARP firms for managerial talent.

**CSI:** Yet this negative-incentive view did, ironically, work in some cases to get companies out of TARP quickly.

**KM:** All governmental attempts to regulate pay have unintended consequences, and it's very rare for those unintended consequences to be positive.

But, in this case, the TARP restrictions were sufficiently draconian that the banks paid back the money a lot faster than anybody dreamed they would pay it back. Of course they had to have government permission in order to pay it back, which is why it took some of the banks so long to do it. The government wasn't particularly happy about the early repayment. Remember that TARP was created because banks didn't have enough capital on their balance sheets.

**CSI:** What were your thoughts when things first hit the fan in late 2008?

**KM:** Like a lot of us, I became obsessed with the financial crisis and learning about its roots. But it didn't take very long for me to conclude that the crisis had very little, if anything, to do with top executive compensation in the banks.

**CSI:** How so?

**KM:** Compensation can promote excessive risk-taking when executives are rewarded for success but not penalized for failure. Historically, banks pay low base salaries coupled with high bonus opportunities, and those bonus opportunities are often paid in stocks and options that have relatively long vesting or transferability restrictions. The executives receive large rewards for success but also face large penalties for failure.

**CSI:** So this hardly encouraged excessive risk.

**KM:** In fact, the top-executive pay practices at the biggest banks serve as role models for compensation best practices, and a prescription for reducing risk-taking activities. It's important to stress that this conclusion only pertains to the top-level executives, and not traders or mortgage brokers where a lot of the risk was actually being taken. But if you look at the TARP restrictions, they were focused on the top 25 executives in each bank, not traders or brokers.

**CSI:** When you talk about taxpayers' interests, in your opinion, how well did TARP work? And have you considered the option of a government just doing nothing? What do you think would have happened had the government just let the chips fall where they may?

**KM:** Even before TARP, the Federal Reserve was doing things to provide much-needed liquidity to some of the banks, and I believe that played an important role in stabilizing the system. We don't know that TARP itself played a major role in getting through the crisis. We know now that the cost of TARP was a lot less than we thought it would be. Its payback has been phenomenally successful. Then again, some of the recipients were AIG, General Motors, and Chrysler, going far beyond the original intention of the TARP legislation.

Although it's hard to play the "what if" game, even now I would have liked to see AIG go under to see if it really would have hurt the overall economy, or who it would have hurt.

**CSI:** You live in Los Angeles. So I hope you watched the Oscar broadcast earlier this year, and noticed that Charles Ferguson's "Inside Job" won the award for Best Documentary. (The film was focused on the financial-services industry's role in precipitating the Great Recession.)

**KM:** Yes, I saw the segment and heard his speech.

**CSI:** So you noticed he decried the fact that no one had gone to jail over this. What's your opinion?

**KM:** If we're handing out arrest warrants, perhaps we should start with Barney Frank and Chris Dodd for their role in facilitating and prolonging the crisis.

More seriously, I think the documentary made some points that were worthwhile. But it was entirely too easy on the government's role in creating the crisis, including the Fed's monetary policy and the U.S. government's housing policy, which provided incentives for everybody to own a house or two, regardless of whether they could afford it. Rep. Frank was featured in the documentary as a voice of reason, and yet he has been among the strongest supporters of loose housing policies for decades. Since the prevailing view is that the crisis was triggered by too many people owning homes they couldn't afford, we need to consider the role that Mr. Frank and others in Congress played in setting the stage for the crisis.

**CSI:** What's your view on the debate over consultant independence, and the strictures of Dodd-Frank?

**KM:** The attack on consultants is, in large part, an attempt to find somebody to

blame for what is perceived to be excessive levels of pay. Several politicians were targeting consultants long before there was any evidence whatsoever about whether or not—or to what extent—consultants are complicit in what are viewed as excesses.

**CSI:** What has your research found on this topic?

**KM:** In my research with my colleague Tatiana Sandino, we found that CEOs get paid slightly more when consultants offer additional services beyond just compensation consulting. But we also found that CEOs get paid more when the compensation consultant works exclusively for the Board of Directors.

**CSI:** So what's your take on Dodd-Frank and how it's going to be implemented by the SEC?

**KM:** Even before Dodd-Frank, the SEC implemented rules in December 2009 that I believed will actually end up helping consulting firms.

Everyone was expecting that the new SEC rules would require companies to not only identify their consultant, but also identify any other work the consultant does for the company and what the relative fees are for the executive pay and non-pay services. As a last-minute adjustment, the SEC created a safe harbor that allows companies to avoid disclosing these other services, or

the fees for these services, if the company also retains a consultant that works exclusively for the Board, and provides no other services beyond executive pay.

In effect, the SEC rule is a Full-Employment Act for both boutique firms working only for the board, and for the large integrated firms who can keep providing undisclosed services as long as the board hires their own boutique consultant. The rule has also given rise to recent quasi-independent spinoffs, such as Towers Watson's PayGovernance, Hewitt's Meridian, and Mercer's Compensation Advisory Partners. These spinoffs are "independent" but retain close connections and data-sharing arrangements with their parent companies. The Board, for example, can retain Meridian while management retains Hewitt, and the services Hewitt provides beyond executive pay are not disclosed.

**CSI:** What effect does this have on overall executive compensation? It sounds like acrobatics to get back to the same place.

**KM:** The spinoffs may help keep the large integrated firms under the radar, but I don't think it's going to have a major effect on compensation. While it is easy for Congress to be suspicious of consultants when complaining that pay levels are too high, let's not forget that compen-

KEVIN MURPHY'S BOOK ON CEO PAY WON'T BE OUT UNTIL 2012, BUT HE WAS KIND ENOUGH TO SHARE AN ADVANCE EXCERPT WITH *C-SUITE INSIGHT*. HIS THOUGHTS ON EXECUTIVE COMPENSATION'S PAST AND FUTURE APPEAR ON THE NEXT PAGE.

sation consultants provide an extremely valuable service to companies, by designing incentive plans, providing critical benchmarking data, and helping companies navigate through the increasingly complicated rules and regulations affecting pay.

**CSI:** Let's talk about the book you're working on, *CEO Pay and What to Do About It*. What will its overall message be? [The book will be published by Harvard Business Press in 2012; its co-authors are Harvard Professor Emeritus Michael Jensen and Econalytics Founder Eric G. Wruck.]

**KM:** The general theme of the book is to discuss the current state of CEO pay, what the problems are, and how to fix them. We also provide rich background data on the evolution of pay over the past century, focusing on the regulatory and economic factors that have led us to where we are.

A primary focus of the book is designing both equity-based and non-equity-based incentives. We'll discuss, for example, three

dimensions of any incentive plan: (1) performance measures (that is, equity-based, accounting-based, or non-financial), (2) performance standards (that is, whether the bonus is based on beating budgets, prior-year performance, or industry peers), and (3) how pay varies with performance (that is, are there caps or floors, and how does this change over time). As the saying goes, the devil is usually in the details, which means that the solutions are also in the details.

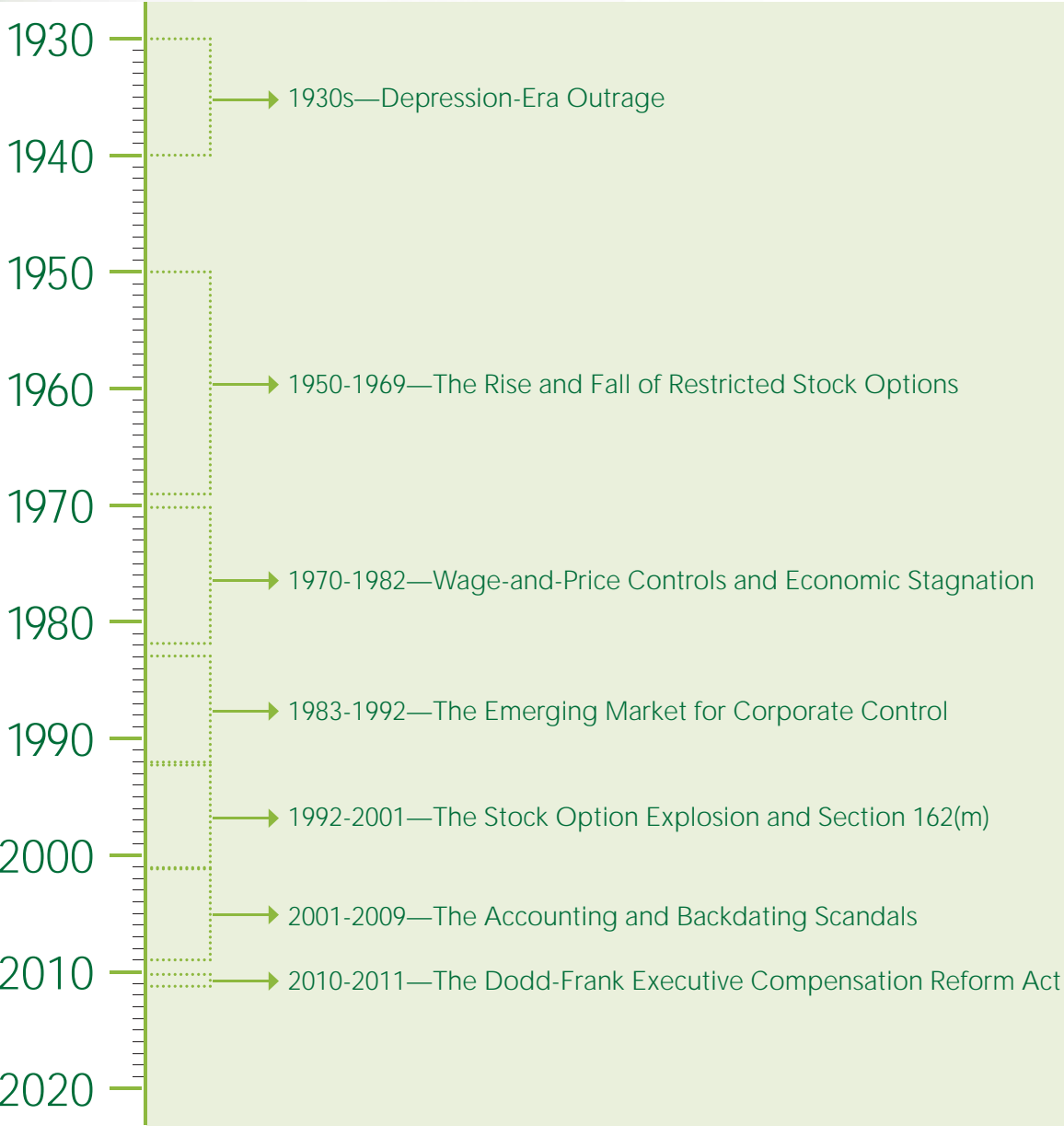
**CSI:** Generally speaking, how well are people listening to all the academic research that you and others conduct?

**KM:** Well, I'll tell you that Mike Jensen and I routinely get blamed for the run-up in stock options in the '90s based on our 1990 Harvard Business Review article, "CEO Incentives: It's Not How Much You Pay, But How." It's flattering, in a way, but I'm also worried that we encouraged firms to grant too many options to too many people, with little regard for their cost. ■

# A BRIEF HISTORY OF CEO PAY

USC Marshall School of Business Professor Kevin Murphy (interviewed in this issue of *C-Suite Insight*) has authored a book-length analysis of CEO pay in the United States through the decades.

Below, we present very brief excerpts from his original work. Those interested in seeing more of it can contact Professor Murphy at [kjmurphy@usc.edu](mailto:kjmurphy@usc.edu).



## 1930s

### Depression-Era Outrage

Franklin D. Roosevelt’s appointment to the American presidency in 1933 ended three terms of Republican government and ushered the New Deal into a country recovering from the Great Depression.

In the April prior to the 1932 election—in the face of proposed bailout loans from the governments Reconstruction Finance Corporation (RFC)—the Interstate Commerce Commission demanded that all railroads disclose executives making more than \$10,000 per year.

The disclosed pay levels outraged the new administration, and in May 1933, the RFC required railroad companies receiving government assistance to reduce executive pay by up to 60%. Ultimately, the U.S. Senate authorized the Federal Coordinator of Transportation to impose an informal (but uniformly complied with) cap of \$60,000 per year for all railroad presidents.

## 1950-1969

### The Rise and Fall of Restricted Stock Options

By 1950, the tax issue surrounding stock options was a big deal: the highest marginal tax rate on ordinary income had swelled to 91% (from 25% in 1928), compared to a capital gains rate of 25%.

Moreover, while the Supreme Court required taxes to be paid immediately upon exercise, the 1934 Securities Act required executives to hold shares acquired through option exercises for at least six months before they could sell.

A business-friendly Congress enacted the Revenue Act of 1950, creating the restricted stock option which would not be taxable upon exercise, only as a capital gain when the shares were ultimately sold.

The 1964 tax law reduced the top marginal tax rate on ordinary income from 91% to 70%, which significantly reduced the attractiveness of restricted options over cash compensation.

The popularity of qualified stock options thereby fell, then collapsed following the Tax Reform Act of 1969, which reduced the top marginal tax rate to 50% and defined gains from exercising restricted or qualified options as a tax preference item subject to a new Alternative Minimum Tax (AMT) on high wage earners.

## 1970-1982

### Wage-and-Price Controls and Economic Stagnation

In August 1971, in an ultimately unsuccessful attempt to control inflation, President Nixon imposed a 90-day freeze on commodity prices and wages (including executive pay).

The Nixon wage and price controls were not the first instances of legislation that explicitly limited executive compensation, but they were the first imposed in a peacetime economy.

Companies could petition to adopt new incentive plans as long as they were directly related to increased productivity. As a result, scores of companies introduced performance-based bonus plans tied to accounting data or revenues, or converted their existing plans into plans exempt from the limits.

While cash compensation escalated (at least in nominal terms) during the 1970s, the use of stock options was relatively stagnant. The prolonged stagnation in the stock market drove much of this, in turn driven in part by the oil-price shocks of 1973 and 1977.

While executives continued to receive periodic option grants during this time, many of the grants replaced options that expired worthless or options that were canceled and reissued with a lower exercise price.

The void in compensation created by worthless stock options was quickly filled by a plethora of new plans designed to provide more predictable payouts, including: book-value plans (where executives receive dividends plus the appreciation in book values); long-term performance plans (with payouts based on long-term earnings growth targets); and guaranteed bonuses (with payouts guaranteed independent of performance).

An attack on perquisites escalated in 1977 as President Carter famously rallied against companies taking deductions for the three-martini lunch, yachts and hunting lodges maintained to entertain business associates, first-class air travel, and fees paid to social and athletic clubs and money spent on sports and theater tickets.

Congress resisted implementing most of Carter’s reforms as part the Revenue Act of 1978 (in large part because it would potentially affect their own consumption of perquisites), but agreed to eliminate deductions for entertainment facilities.

CONGRESS CREATED A NEW TYPE OF STOCK OPTIONS.

## 1983-1992

### The Emerging Market for Corporate Control

By the early 1980s, CEOs and boards were subject to increasing pressure and incentives from the market for corporate control. Companies with excess cash became targets of hostile takeovers.

An important pay-related development in the takeover market of the 1980s was the evolution of golden parachute agreements that awarded payments to incumbent executives following a change in control.

Change-in-control arrangements became controversial following a \$4.1 million payment to William Agee, the CEO of Bendix. In 1982, Bendix launched a hostile takeover bid for Martin Marietta, which in turn made a hostile takeover bid for Bendix. Bendix ultimately found a white knight and was acquired by Allied Corp., but only paying CEO Agee his golden parachute.

Court decisions and legislation in the late 1980s (coupled with the October 1987 stock market crash) brought the hostile takeover market in the U.S. to a virtual halt. The high-yield debt market was crippled by the indictment and subsequent guilty pleas of Michael Milken and Drexel Burnham Lambert, by restrictions on high-yield debt holdings, and by major punitive changes in the U.S. bankruptcy law that made it uneconomic to reorganize troubled firms outside of bankruptcy.

The CEO pay debate achieved international prominence in the early 1990s. The controversy heightened with the November 1991 release of Graef Crystal's exposé on CEO pay, *In Search of Excess*, and exploded following President George H. W. Bush's January 1992 pilgrimage to Japan with an entourage of highly paid U.S. executives. An intended plea for Japanese trade concessions that U.S. competitiveness was hindered by its excessive executive compensation practices as attention focused on the huge pay disparities between top executives in the two countries.

In response to growing outrage, legislation was introduced in the House of Representatives disallowing deductions for compensation exceeding 25 times the lowest-paid worker, and the Corporate Pay Responsibility Act was introduced in the Senate to give shareholders more rights to propose compensation-related policies.

The SEC preempted the pending Senate bill in February 1992 by requiring companies to include non-binding shareholder resolutions about CEO pay in company proxy statements, and announced sweeping new rules in October 1992 affecting the disclosure of top executive compensation in the annual proxy statement.

## AN IMPORTANT PAY-RELATED DEVELOPMENT IN THE TAKEOVER MARKET OF THE 1980s WAS THE EVOLUTION OF THE GOLDEN PARACHUTE.

## 1992-2001

### The Stock Option Explosion and Section 162(m)

The use of stock options caused CEO pay in the U.S. to explode in the early 1990s. Stock options soon became the primary component of executive pay—and the most controversial.

In April 1992, FASB voted 7-0 to endorse an accounting charge for options, and issued a formal proposal in 1993. The proposal created a storm of criticism among business executives, high-tech companies, accountants, compensation consultants, the Secretary of the Treasury, and shareholder groups.

Even President Clinton, usually a critic of high executive pay, waded into the debate in December, expressing that it would be unfortunate if FASB's proposal inadvertently undermined the competitiveness of some of America's most promising high-tech companies. FASB ultimately relented, recommending but not requiring companies to take an accounting charge for options.

By February 1993, President Clinton had backtracked on his earlier idea of making all compensation above \$1 million unreasonable and therefore non-deductible, suggesting that only pay unrelated to the productivity of the enterprise was unreasonable.

Then, as proposed by the Treasury Department and eventually approved by Congress as part of the Omnibus Budget Reconciliation Act of 1993, Section 162(m) of the tax code was applied only to public firms and not to privately held firms, and applied only to compensation paid to the CEO and the four highest-paid executive officers as disclosed in annual proxy statements. Compensation for all other employees in a firm would be fully deductible, even if it was in excess of the million-dollar limit.

## 2001-2009

### The Accounting and Backdating Scandals

Accounting scandals erupted across corporate America during the early 2000s. In the midst of these scandals, Congress quickly passed the sweeping Sarbanes-Oxley Act in July 2002, setting or expanding standards for accounting firms, auditors, and boards of directors of publicly-traded companies.

The Act was primarily focused on accounting irregularities and not on compensation. However, Congress could not resist the temptation to use the new law to further regulate executive pay.

In 2005, academic research by University of Iowa professor Erik Lie and subsequent investigations by the *Wall Street Journal* unearthed a practice that became known as option backdating. This unsavory practice violates federal disclosure rules, accounting and tax laws, and often the company's own stock-option policies. By 2010, the SEC's investigations and prosecutions of backdating had wound down.

The first decade of the new century also brought several important changes in the level and composition of CEO pay, including a significant drop in the use of stock options.

One obvious explanation for the drop in stock options and the rise in restricted stock since the early 2000s is the stock market crash associated with the burst of the Internet Bubble in 2000 and exacerbated by the terrorist attacks on the World Trade Center in 2001. The sharp market-wide decline in stock prices in the early 2000s left many outstanding options underwater and lowered executive expectations for the future increases in their company's stock prices.

Perhaps more importantly, FASB (finally) mandated expensing for stock options; companies reacted by jettisoning their broad-based option programs and shifting to (now relatively less expensive) restricted stock.

Moving forward to February 2009, in the midst of the Great Recession, Congress attempted to destroy the "Wall Street Bonus Culture" by imposing severe restrictions on executive pay for firms participating in Treasury's Troubled Asset Relief Program (TARP). For example, TARP recipients could pay only base salaries and small amounts of restricted stock, and were prohibited from offering stock options, incentive bonuses, or severance pay.

The most draconian restrictions were imposed on seven firms requiring "exceptional assistance" by the government (including AIG, Bank of America, Citigroup, General Motors, and Chrysler). Every dollar paid to the top 25 executives in these firms had to be

specifically approved by the newly christened Special Master of Executive Compensation (a.k.a. the Pay Czar).

Since taxpayers had become the major stakeholder in the seven special assistance firms, the government arguably had a legitimate interest in the firms' compensation policies.

One could imagine, for example, embracing an objective of maximizing shareholder value while protecting taxpayers, or perhaps maximizing taxpayer return on investment. However, the U.S. Treasury instructed the Special Master to make pay determinations using the "public interest standard," an ill-defined concept that allows too much discretion and destroys accountability for those exercising the discretion.

Ultimately, the Special Master catered to prevailing political and public sentiment, and severely penalized the executives in firms viewed as responsible for the meltdown by drastically reducing their cash compensation.

## 2010-2011

### The Dodd-Frank Executive Compensation Reform Act

In July 2010, President Obama signed into law the Dodd-Frank Wall Street Reform and Consumer Protection Act, or Dodd-Frank Act. While ostensibly focused on regulating firms in the financial services industry, the authors of the Dodd-Frank Act seized the opportunity to pass a sweeping reform of executive compensation and corporate governance imposed on all large publicly traded U.S. firms across all industries.

The Dodd-Frank Act has the potential to destroy much of Corporate America. Fortunately, detached and impartial opinion seems to be prevailing as U.S. regulators create rules to implement the Act's provisions. ■

INTERVIEW WITH **RYAN JOHNSON**

**T**he complexities of corporate compensation, in the C-Suite and throughout an organization, seem to increase by the day. Addressing these challenges, WorldatWork ([www.worldatwork.org](http://www.worldatwork.org)) is a not-for-profit organization that provides education, research, and conferences that are focused on compensation, benefits, and what it calls “integrated total rewards” that “attract, motivate, and retain” talent.

In the educational realm, WorldatWork offers numerous certifications, including the newly developed Certified Executive Compensation Professional (CECP) certification. C-Suite Insight recently interviewed Ryan Johnson, WorldatWork’s Vice President, Publishing and Community.

Ryan spent seven years at Arizona State University’s Morrison Institute for Public Policy; has served as a Congressional staff member in Washington, D.C.; and also worked as a consultant in the pharmaceutical and health-care industry before joining WorldatWork.

“THE ATTRACT/MOTIVATE/RETAIN EQUATION FOR EMPLOYEES AND EMPLOYERS IS OBVIOUSLY ABOUT MORE THAN JUST PAY.”

**C-Suite Insight:** Let’s start by talking about surveys a bit. You have an ongoing effort to clear up some of the confusion among the various surveys, correct?

**Ryan Johnson:** Yes. We know from our membership that many of them are struggling with the comparability of long-term incentive or LTI data among surveys. Specifically, there are proprietary methodologies that don’t lend themselves to an apples-to-apples comparison.

Our members approached WorldatWork and GEO concurrently. Non-profit organizations like us can play a unique role as neutral third parties in a situation like this. We’ve been working on this challenge for about three years.

**CSI:** How proprietary are some of these surveys? Is it like comparing apples to oranges, or apples to lawn chairs?

**RJ:** It’s not as severe as apples to lawn chairs. But we teach at WorldatWork that if you are, for example, completing an LTI data analysis for an upcoming board meeting, you really should triangulate the data with multiple sources in order to find a good decision point.

We’ve been teaching that you need to use multiple sources, and practitioners would find values that were off by a factor of 20%—

maybe even more in some instances. In other instances, it may be 5%.

**CSI:** Still statistically significant...

**RJ:** Well, it’s enough to make you scratch your head. Or it’s enough to make members of your board scratch their heads and say “Why is this data so different?”

And, of course, the person who’s pulling the data out of these surveys really isn’t usually privy to the methodology, or if the methodology is the same, they wouldn’t know the specifics in a particular survey’s assumptions that were used. So when this question is posed in a board meeting, the practitioner is put on his or her heels to say, “Well, they use different methodologies.”

And that’s really the basic problem we’ve been working on with GEO.

**CSI:** Is this problem limited to LTI?

**RJ:** It can be an issue in job descriptions, too, but it isn’t as problematic as the LTI issue. Let’s say, for example, you’re going to price a job for an “Accountant.” One of the survey providers may list the job as “Accountant III,” with a description about what an Accountant III job requirements and duties are. Another survey may list that job as “Senior Accountant.” So there’s not a perfect crosswalk among

some of these job titles and job descriptions, which again could pose challenges in terms of comparability.

**CSI:** So how can survey vendors square that circle—being more open and consistent, yet still offering what they would consider to be unique services?

**RJ:** I’ve talked with most, if not all, of the major players in this space, and I’m sympathetic to the notion that they have a business and they want to differentiate and create a unique offering. On the other hand, I also think businesses need to be attuned to their customers’ needs. I have to believe there is a survey business model out there that can accomplish both, but right now, it would seem that the practitioners—the customers in this relationship—aren’t being listened to in a way that satisfies them. If they were, WorldatWork and GEO wouldn’t be involved in this.

**CSI:** You mentioned triangulation of survey results as a best practice for executive compensation professionals. What other sorts of best practices are you seeing?

**RJ:** Of course, one of the older and more fundamental compensation precepts that WorldatWork teaches in its certification courses is that you do need to use multiple

## THE EXCHANGE RELATIONSHIP BETWEEN EMPLOYER AND EMPLOYEE IS ABOUT MORE THAN JUST MONEY.

sources when pricing jobs. Don't just rely on one source or even just two sources; that's a foundational rule, and it's not rocket science. In our executive rewards courses, for example, we teach things like how to think about selecting a peer group of companies,

how to align executive rewards properly with business goals, and how to think about the risk orientation of executive rewards. There isn't always "best practice" per se in these areas, but there are some philosophical questions that practitioners really need to think hard on.

**CSI:** What are you seeing from your members, in terms of how many surveys they are using?

**RJ:** A member survey that we released in 2008 indicated that 80% of practitioners use two or three surveys, and another 10% use four to six. So not only is it a best practice to use multiple surveys, as we teach, it's also the prevailing practice.

**CSI:** What about the situation today, the sort of elephant in the room relating to the economic meltdown in late 2008, TARP, and the Dodd-Frank legislation? Generally speaking, we're in a new era of transparency and defending what you're doing...

**RJ:** Without a doubt, the spotlight is shining brighter than ever on compensation professionals, on executive compensation, on compensation decisions that are made up and down the organization, all the way up to the comp committee and the board. There's no question that there is greater transparency, more visibility on these decisions, more scrutiny on these decisions.

**CSI:** Within this context, in which direction are benefits headed for C-Suite executives and board members?

**RJ:** Our perspective is one of total rewards, throughout the organization. The attract/motivate/retain equation for employees and employers is obviously about more than just pay. It involves every lever that an employer can use to attract, motivate, and retain. Of course, there is pay in that equation, but there are also benefits and things like flexibility and mentoring at the employee level. At the executive level, there are different wants like new opportunities and challenges and long-term stock awards for increasing shareholder value,

but in the end, we believe that the exchange relationship between employer and employee—even those in the C-suite—is about more than just money. That's why we evangelize total rewards.

**CSI:** How has this discussion evolved during your 10 years at WorldatWork?

**RJ:** For most of the past decade, we've had salary-increase budgets in our 37-year old annual survey bopping along basically at the rate of inflation: 3%, 4%, 5%. Suddenly, in 2008, the equities market plunged and the economy plunged along with it. One stark reality of the Great Recession was that employers were suddenly looking at zero-increase budgets.

In 2009, we saw the highest number of zero-increase budgets ever recorded in our survey, with almost a third of the employers in our survey reporting this. A lot of incentive budgets went to zero as well.

In that kind of environment you have employers and managers looking around and saying, "Well, if we don't have any money, what is it that we can do to motivate and engage our employees?"

**CSI:** How did they answer that question?

**RJ:** In that kind of environment, it's natural for these questions to pop up: "Can we give them increased flex-

ibility in their schedules? Can we do things like formalize the mentorship program? What can we do with career opportunities throughout the organization?"

That's when this idea of total rewards blossomed and we realized the true value of that concept.

**CSI:** What good examples have you seen of this concept in action?

**RJ:** The examples that get cited frequently for flexibility with time off are Best Buy Corporation—with their famous Results Only Work Environment program—and Netflix. But there are a lot of companies adopting total rewards concept. Places like Aflac, Mattel, General Mills.

At Aflac, the premise is pretty simple: involving the employees and asking them what they'd like helps to keep them loyal. So they've done employee surveys for a long time. A few years ago, employees said they'd like more day-to-day recognition and daycare. The CEO delivered both. Employee turnover there is ridiculously low.

General Mills recently expanded its infant care center, so they're now accommodating 60 infants right there at HQ. Can you imagine the employee engagement and loyalty that generates? And Mattel, the toy company, really tries to inject some fun and camaraderie through things like volunteering days and milk and cookie socials.

**CSI:** And Netflix?

**RJ:** Well, Netflix, which is in Silicon Valley, did something very interesting by creating sick-leave and vacation policies that are determined by employees.

**CSI:** You're kidding...

**RJ:** The policy is: "We're going to trust our employees. We want you to take whatever vacation you feel you need and take whatever sick leave you feel like you need. If you feel like you need to spend a week in Hawaii with your spouse, have at it. If you're going to be sick this week, please stay at home and be sick."

**CSI:** The idea must be that your peers determine things rather than having things determined through the traditional, top-down command structure. If you're slacking in that environment, everyone that you work with is going to pick up on it, and probably not like you very much.

**RJ:** Yes. If someone is slacking, everyone else is going to know. It's been delegated down from the C-suite and HR, and is a peer-to-peer situation now.

**CSI:** So organizations are finding creative ways to address these issues in a more complex age. In this spirit, your organization now offers a Certified Executive Compensation Professional (CECP) certification. What

does that entail? What benefits does it offer to recipients and their organizations?

**RJ:** This certification is different from the others we've offered for more than two decades now. It involves what we call a "total test," that is, a comprehensive exam of your knowledge.

Under our other certification models, you take eight courses and you pass eight exams and you get a certification. But with this one, you go and sit for the exam, and you demonstrate your knowledge in the exam and you earn the certification.

**CSI:** And it wasn't created in a vacuum...

**RJ:** Correct. We've had some great people like Randy Keuch, the Vice President for Total Rewards at Heinz, on one of our advisory boards. He's been in compensation and benefits—both as a practitioner and an executive comp consultant—for more than 30 years.

He says the CECP is a great solution for people like him, who would consider themselves experts in the field, but who have limited time to take classes. He took the exam and now has a designation that reflects both his experience and the knowledge he's acquired over the past couple of years.

Randy believes that the CECP, like our other designations, can be a differentiator in the job marketplace for many of its recipients. ■



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REPORT

## FOCUS ON RESEARCH

### COMPARING CEO PAY TO TOTAL SHAREHOLDER RETURN

#### A MULTI-YEAR ANALYSIS OF PAY FOR PERFORMANCE

**A** RECENT STUDY CONDUCTED by Equilar explores the link between total shareholder return (TSR) performance and CEO pay among S&P 1500 companies. Based on data pulled from Equilar's new TSR & CEO Pay Modeler, the study provides a benchmark for companies seeking to understand where they fall in the pay-for-performance landscape.

Changes in CEO pay were evaluated over one year (2008 – 2009) and three years (2006 – 2009), the time frames typically examined by proxy advisory firms when they evaluate CEO pay versus TSR performance for voting purposes. This article focuses on the findings from the one-year analysis.



(Note: This article is based on a report from Equilar Inc., entitled, "TSR Performance and CEO Pay Study.")

Companies with no CEO turnover were categorized into one of the following four quadrants:

- Quadrant 1  
Companies which had an increase in CEO pay and above-median TSR performance
- Quadrant 2  
Companies which had an increase in CEO pay and below-median TSR performance
- Quadrant 3  
Companies which had a decrease in CEO pay and below-median TSR performance
- Quadrant 4  
Companies which had a decrease in CEO pay and above-median TSR performance

- Key Findings**
- There was a fairly even distribution of companies into the four separate quadrants. More than 50 percent of CEOs compared in both the one-year and three-year studies saw an increase in pay.
  - Among those companies that had an increase in total CEO compensation over the one-year period, total cash compensation (including base salary and bonus) was the key driver of the increase in total compensation.
  - Over the one-year period, Retail companies were over-represented among companies that had an increase in CEO pay and above-median TSR.

- In the Lexicon**
- “Pay for performance” is a commonly used phrase in today’s business world—but its definitions vary wildly. In order to determine whether a company is “paying for performance,” several questions should be considered:
- What components of pay are under evaluation: cash pay only (including base salary and bonus), or total compensation, including the value of equity awards, perquisites, etc.?
  - What is meant by “performance”? Is it referring to individual performance, company performance, or some combination of the two? If company performance is the focus, which performance measures should be used in the evaluation—share-price measures, operational measures, or others?

One common definition of pay for performance is that of Institutional Shareholder Services (ISS), a proxy-advisory firm.

ISS evaluates “the alignment of the CEO’s pay with performance over time, focusing particularly on companies that have underperformed their peers over a sustained period. From a shareholders’ perspective, performance is predominantly gauged by the company’s stock performance over time. Even when financial or operational measures are utilized in incentive awards, the achievement related to these measures should ultimately translate into superior shareholder returns in the long-term.”

With advisory firms and regulators increasingly focusing on these two metrics, companies must continue to stay on top of how their CEO’s pay aligns with the company’s performance. Equilar’s new TSR & CEO Pay Modeler is designed to help companies see this data the way proxy-advisory firms do, heading off potential PR issues before they occur.

**The Methodology**

In order to explore the relationship between TSR performance and CEO compensation among U.S. companies, Equilar examined changes in CEO compensation at S&P 1500 companies. For the purpose of this analysis, total compensation is comprised of base salary, annual and long-term cash bonus payouts, the grant-date value of stock and option awards made during the year, changes in pension and deferred-compensation earnings, and all other compensation.

Changes in pay were evaluated over one- and three-year periods, the time frames which are typically the focus of proxy advisory firms when they evaluate “pay for performance” for voting purposes. The one-year period assessed for this study was 2008 – 2009, the most recent period for which authoritative data was available.

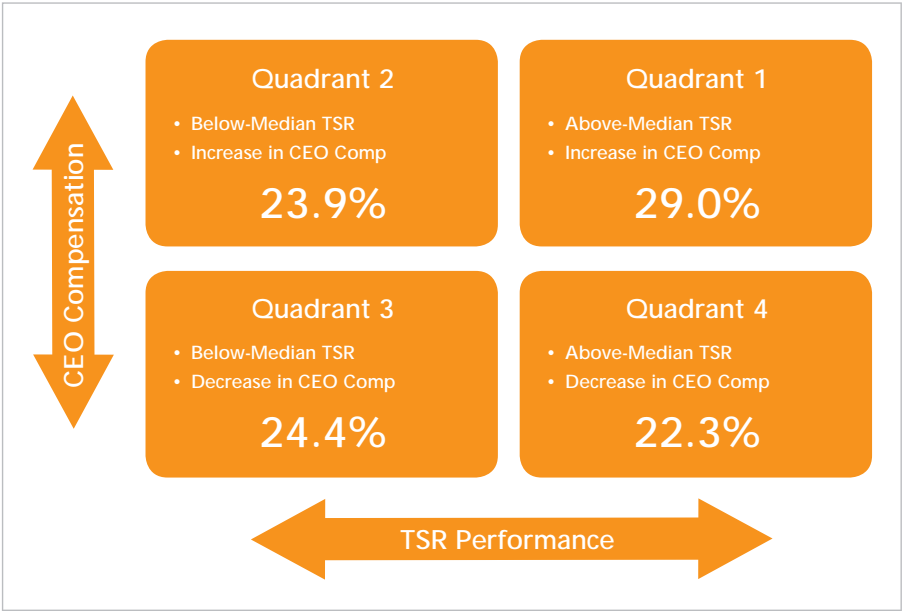
In order to focus on changes in CEO compensation that were the result of plan design and its link to firm performance, companies that underwent a change of CEO during the time period being evaluated were excluded from the study.

Given the volatile market conditions over the past several years, TSR performance among all of the companies in the S&P 1500 has changed dramatically from year to year.

Specifically, the median three-year TSR among S&P 1500 companies was 1.9 percent, the median two-year TSR was negative 4.6 percent, and the median one-year TSR was 25.9 percent. Therefore, in our analysis, below-median one-year TSR performance was considered to be below 25 percent.

**Changes in CEO Pay Levels**

Among the 1,352 companies studied in the analysis of changes in total CEO compensation over the one-year period, 715 companies, or 52.9 percent, had an increase in total CEO compensation. 631 companies, or 46.7 percent, saw a decrease in total CEO compensation. Six companies



had no change in CEO pay over the one-year period.

**TSR Performance**

Among the 715 companies that had an increase in total CEO compensation over the one-year period, 18.5 percent had a negative one-year TSR and 81.5 percent had a positive one-year TSR.

Among the 631 companies that had a decrease in total CEO compensation over the one-year period studied, 21.6 percent had negative one-year TSR and 78.4 percent had positive one-year TSR.

However, since the median one-year TSR among S&P 1500 companies was 25.9 percent, a 25-percent cutoff was used for this analysis.

The accompanying diagram above shows how many companies fell into each of the categories for the one-year timeframe. It is notable that the companies are relatively evenly distributed across the four categories.

The largest percentage, 29.0 percent, of CEOs fell into the category of receiving increases in their pay while their company experienced an above-median increase in their TSR.

The second-most-populated quadrant contained companies with decreases in CEO pay and below-median TSR, with 24.4 percent of the group fitting into that category. Interestingly, CEOs that received pay increases but saw TSR fall below the median came in third, with 23.9 percent. The diagram excludes six companies that did not have a change in CEO pay over the one-year period.

**Industry Analysis**

The companies that saw a change in CEO compensation over the one-year timeframe were studied to determine if certain industries were over-represented in a quadrant, as compared to their representation in the S&P 1500 index.

As shown in the accompanying tables, companies within the Banking and Utilities industries were over-represented in Quadrant 2, meaning those companies that exhibited an increase in CEO pay and below-median TSR, compared to peer companies within the S&P 1500.

Retail companies were over-represented in Quadrant 1, consisting of those companies which had an increase in CEO pay and above-median TSR. Insurance and Capital Goods companies were over-represented in Quadrant 3 (i.e., those companies which had a decrease in compensation and below-median TSR).

The Consumer Durables & Apparel and the Technology Hardware & Equipment industries were over-represented in Quadrant 4, the subset of companies within the S&P 1500 that exhibited above-median TSR and a decrease in compensation.

For the companies in Quadrants 1 and 2 (i.e., those companies that had an increase in total CEO compensation over the one year period), total cash compensation (including base salary and bonus) was the key driver of the increase in total compensation.

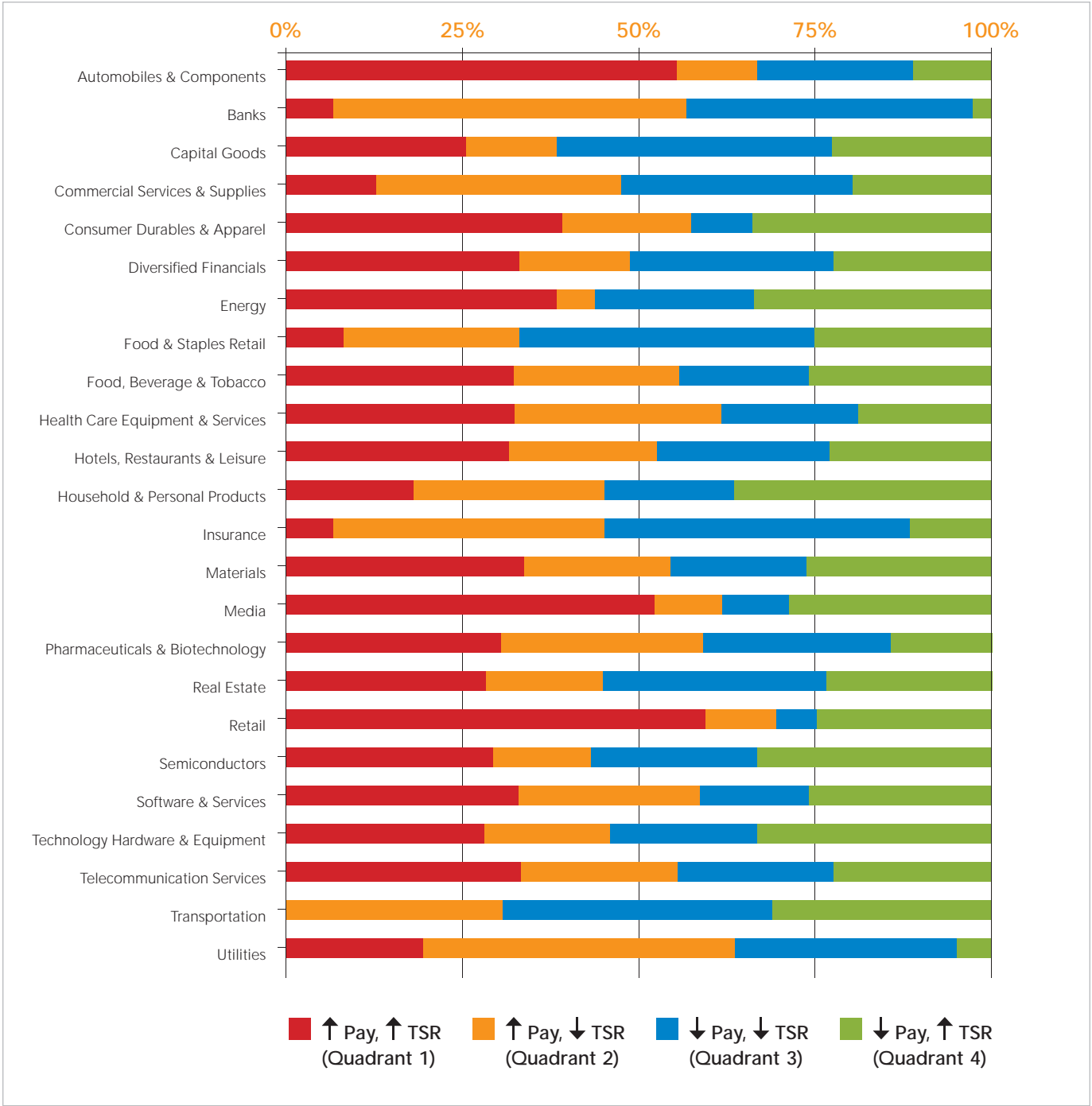
Therefore, it appears that increases in total compensation were the result of incentive-plan design and strategic compensation decisions, rather than merely an increase in the value of equity awards over the course of the year.

*Want to learn more? See the full report by visiting [www.equilar.com](http://www.equilar.com), calling (650) 286-4512, or e-mailing [info@equilar.com](mailto:info@equilar.com).*

Industry Prevalence within Each Quadrant vs. S&P 1500, One-Year Analysis

	% of S&P 1500	% of Quadrant 1	% of Quadrant 2	% of Quadrant 3	% of Quadrant 4
Automobiles & Components	1%	1%	0%	1%	0%
Banks	5%	1%	12%	9%	1%
Capital Goods	9%	8%	5%	15%	10%
Commercial Services & Supplies	3%	2%	5%	5%	3%
Consumer Durables & Apparel	4%	6%	3%	2%	7%
Diversified Financials	3%	4%	2%	4%	3%
Energy	6%	7%	1%	5%	8%
Food & Staples Retail	1%	0%	1%	2%	1%
Food, Beverage & Tobacco	3%	4%	3%	2%	4%
Health Care Equipment & Services	8%	8%	9%	6%	6%
Hotels, Restaurants & Leisure	4%	5%	4%	4%	4%
Household & Personal Products	1%	1%	1%	1%	1%
Insurance	3%	1%	5%	6%	2%
Materials	6%	7%	5%	5%	7%
Media	2%	3%	1%	1%	2%
Pharmaceuticals & Biotechnology	4%	4%	4%	4%	2%
Real Estate	5%	4%	3%	6%	5%
Retail	6%	13%	2%	2%	7%
Semiconductors	4%	4%	2%	4%	6%
Software & Services	7%	8%	8%	5%	8%
Technology Hardware & Equipment	6%	6%	4%	5%	9%
Telecommunication Services	1%	2%	1%	1%	1%
Transportation	2%	0%	2%	3%	3%
Utilities	5%	3%	8%	6%	1%

To further illustrate the state of each company against its peers, below is a breakout of the percentage of companies in each industry that fell into the four separate quadrants over the one year period.



# CEO PAY IN 2010: COMPARING PAY INCREASES WITH TSR



OVER THE PAST FOUR YEARS, the *New York Times* has utilized Equilar research on CEO pay at the top 200 public corporations as background information for a comprehensive report. The overarching theme of this year’s *New York Times* article was that “happy days are back” for CEOs. The article also noted that while profitability had returned for most companies, many remain sluggish in hiring employees and improving the high U.S. unemployment rate.

The *New York Times* report noted that fourth-quarter 2010 profits at U.S. corporations were up 29.2 percent, “the fastest growth in more than 60 years.”

CEO pay was up across the board as well. The median pay for the top 200 executives was \$9.6 million last year, according to the special research Equilar conducted for the *New York Times*.

This figure was a 12 percent increase over 2009, a number that trailed the median profitability increase of 17 percent and median TSR increase of 19 percent. Looking at averages, one finds that CEO pay and TSR each went up 20 percent, with profitability rising a stunning 95 percent. What can we learn from these numbers?

First, we should mention the common caveat that looking at one year’s worth of data can be a fool’s game. The year 2010 could be among the most dangerous years to do this, given the dramatic collapse in stock-market returns, profitability, and employment during the recession years of 2008 and 2009. Major improvement in recent years should be expected, and does not necessarily represent great performance.

That said, we’ve compiled a few figures that show total shareholder return (TSR) for the year, and compared it to CEO compensation. Which companies showed the strongest link between improved performance and higher CEO pay?

## LOOKING AT THE NUMBERS FOR INDIVIDUAL COMPANIES YIELDS SEVERAL “TOP 10” LISTS:

### TOP 10 PROFITABILITY INCREASES (by percentage)

Company	Increase	CEO
Autoliv	5,806%	Jan Carlson
TRW Automotive Holdings	1,449%	John C. Plant
FedEx	1,108%	Frederick W. Smith
Shaw Group	518%	J.M. Bernhard Jr.
Dow Chemical	438%	Andrew N. Liveris
PACCAR	309%	Mark C. Pigott
Arrow Electronics	288%	Michael J. Long
Ashland	286%	James J. O'Brien
Capital One Financial	209%	Richard D. Fairbank
Western Digital	194%	John F. Coyne

The major trend here: companies involved in economic fundamentals benefited the most in 2010, after suffering the most in the two previous years. The automotive industry, construction, transportation, and electronics dominate this list, though one financial services company also appears.

### TOP 10 TSR PERFORMANCE (by percentage)

Company	Increase	CEO
Cummins	142%	Theodore M. Solso
TRW Automotive Holdings	121%	John C. Plant
Autoliv	84%	Jan Carlson
Estee Lauder	72%	Fabrizio Freda
Deere	71%	Samuel L. Allen
Ford Motor	68%	Alan Mulally
Eaton	63%	Alexander M. Cutler
PACCAR	60%	Mark C. Pigott
Sunoco	57%	Lynn Laverty Elsenhans
Pantry	54%	Terrance M. Marks

**Note:** Four companies barely missed this list, coming in with TSRs of 53 percent. These companies were Marriott International, Apple, and DuPont. FedEx nearly made this list as well, with a TSR of 51 percent.

This list has a few repeats from the profitability-gains list, and also reflects economic fundamentals. The inclusion of Estee Lauder reflects some movement beyond the basics into lifestyle, as does the near-miss of Apple, which has made numerous successful attempts to transform lifestyles in a time of economic turbulence.

Our final Top 10 list shows the companies that increased their CEO pay the least relative to their increasing TSR. Again, a one-year study provides a very small picture, but it does show the CEOs who made the most for their investors last year, compared to what they made for themselves.

### TOP 10 PAY INCREASE BARGAINS (ratio of TSR increase vs. CEO pay increase)

Company	TSR	Pay Increase	Ratio (X:1)	CEO
Boeing	24%	0.46%	51.8	W. James McNerney Jr.
Hess	27%	0.98%	27.9	John B. Hess
Marsh & McLennan	27%	1.08%	25.5	Brian Duperreault
Berkshire Hathaway	21%	1.05%	20.4	Warren E. Buffett
Chubb	24%	1.35%	18.0	John D. Finnegan
Sherwin-Williams	38%	3.19%	12.0	Christopher M. Connor
Reynolds American	30%	3.76%	8.0	Susan M. Ivey
Cummins	142%	22.35%	6.3	Theodore M. Solso
Baker Hughes	43%	7.40%	5.8	Chad C. Deaton
CSX	35%	9.11%	3.9	Michael J. Ward

**Note:** An example would be a TSR increase of 100 percent, with a pay increase of 10 percent. This would yield a ratio of 10:1. A company had to exceed the average TSR, 20 percent, to make this list.

FOCUS ON RESEARCH

HOW MUCH DO TOP HR PROS MAKE?

AND HOW GOOD ARE THE PERKS?

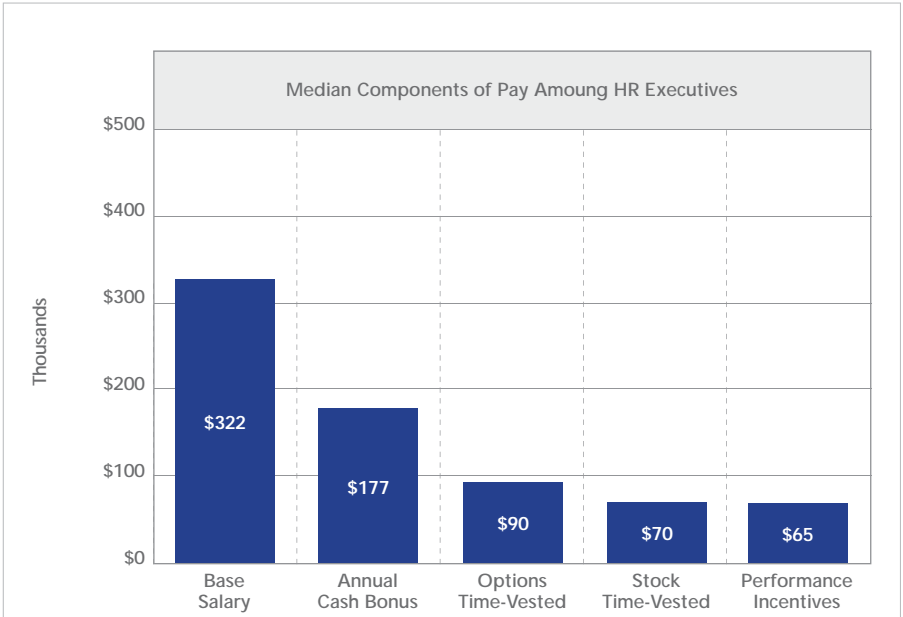
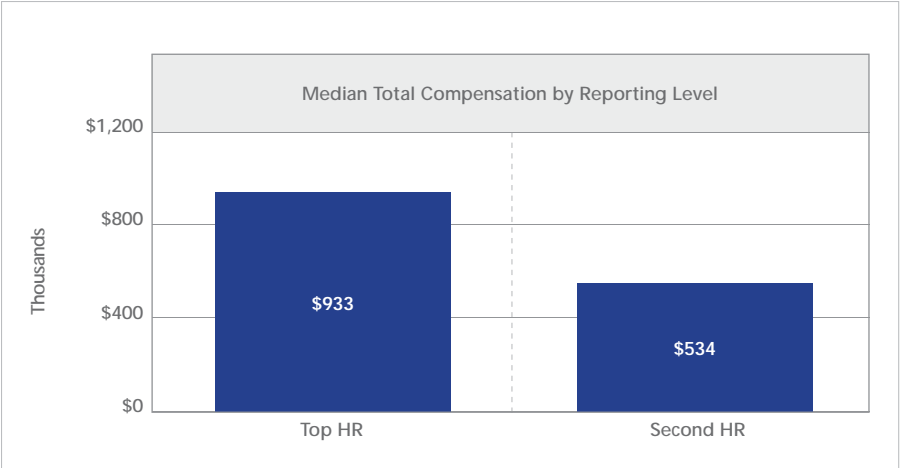
WITH NEW COMPENSATION- and governance-related SEC regulations unfolding in 2011, shareholders and institutional investors’ scrutiny of pay practices and the compensation-setting process will only continue to increase.

In this changing environment, HR executives hold a uniquely challenging position. They are often actively involved in the analysis and preparation of compensation strategies, yet they simultaneously receive pay packages commensurate with their executive status, many of which are publicly disclosed.

Equilar’s annual Top 25 Senior Officer Compensation Survey provides self-reported compensation information from participating companies. The most recent survey includes data from over 500 companies, across a representative sampling of industries. This article covers some of the report’s highlights.

Key Findings – Compensation

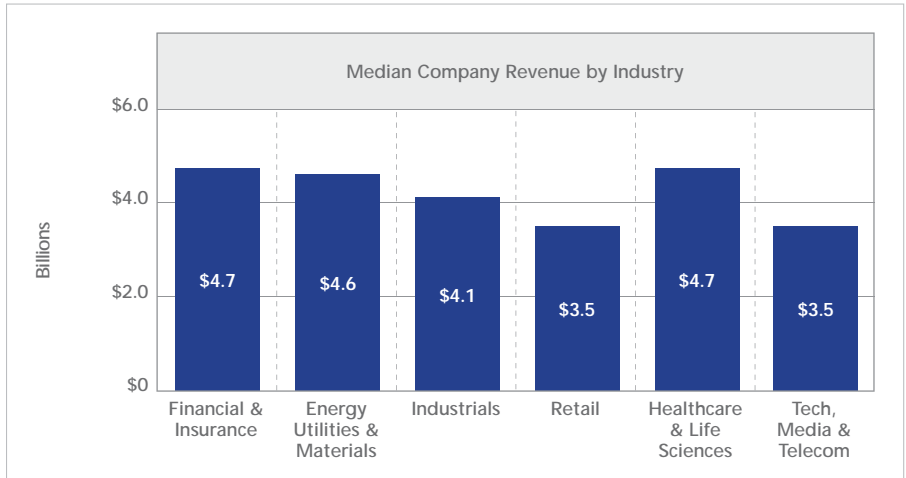
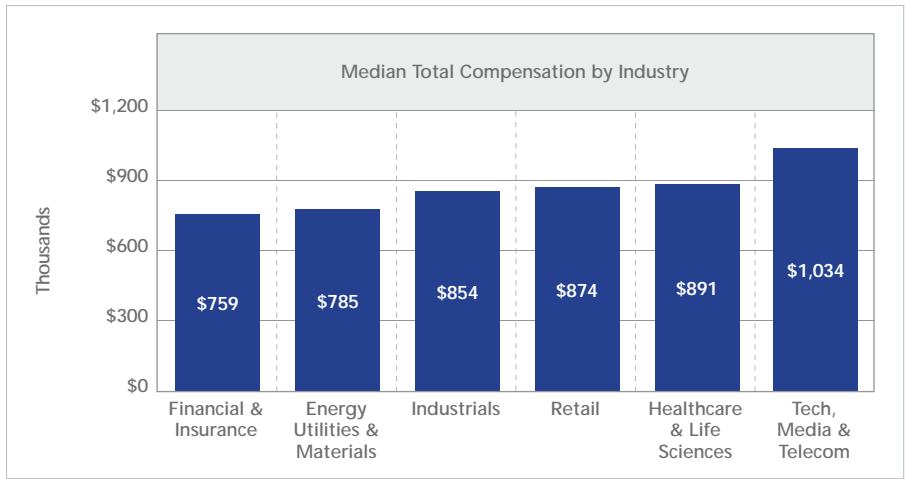
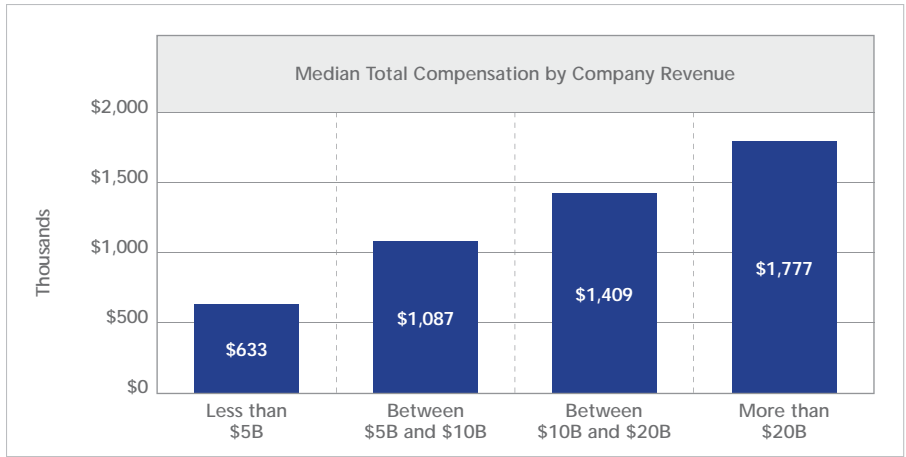
- The median total compensation for HR professionals reported in Equilar’s 2010 Top 25 Survey was \$873,149.
- Human Resources executives that were first in the HR hierarchy received a median total compensation of \$933,299, while those who were second in the HR hierarchy received a median total compensation of \$533,673.
- There is a direct relationship between the number of years an HR professional has been with a company and how much he or she gets paid. Human Resources executives with less than three years’ tenure had a median pay of \$802,411, while those with more than 10 years of tenure had a median pay of \$860,673.
- The median HR executive pay at companies with more than \$20 billion in revenue was \$1,776,887, or nearly three times the median pay at companies with less than \$5 billion in revenue.



The chart and the table on the right display the individual components of total compensation.

Summary Statistic	Base Salary	Bonus	Options	Stock	Performance Incentives	Total Compensation
Median	\$321,775	\$177,110	\$89,763	\$69,620	\$65,260	\$873,149
Mean	\$343,548	\$212,867	\$192,268	\$179,936	\$196,572	\$1,125,192
10th Percentile	\$212,400	\$58,293	\$-	\$-	\$-	\$403,063
25th Percentile	\$260,000	\$106,800	\$-	\$-	\$-	\$582,541
75th Percentile	\$414,750	\$291,313	\$262,421	\$205,500	\$259,729	\$1,438,668
90th Percentile	\$492,500	\$395,260	\$503,861	\$457,350	\$518,586	\$2,060,418

(Note. This article is based on a report from Equilar Inc., entitled, “In-Depth Top HR Compensation.”)

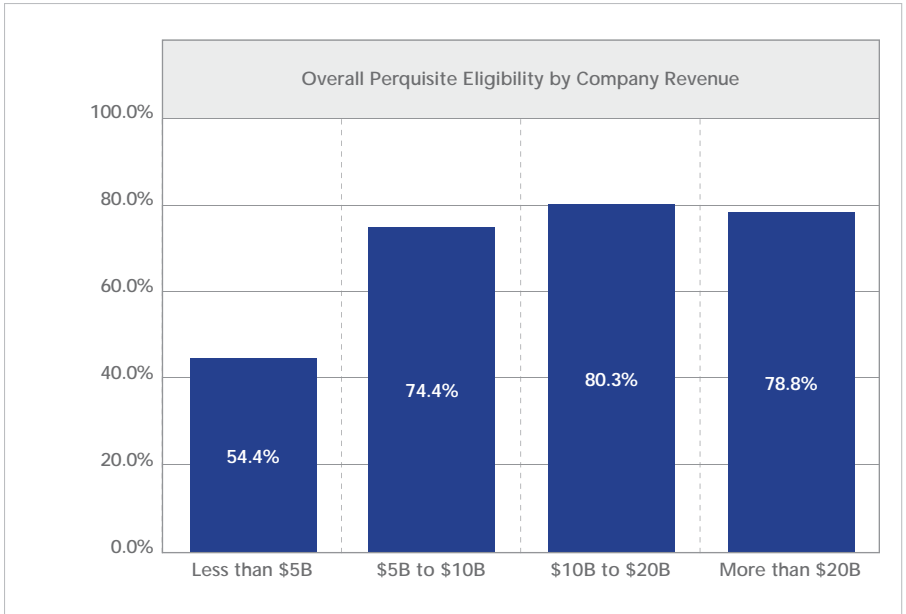
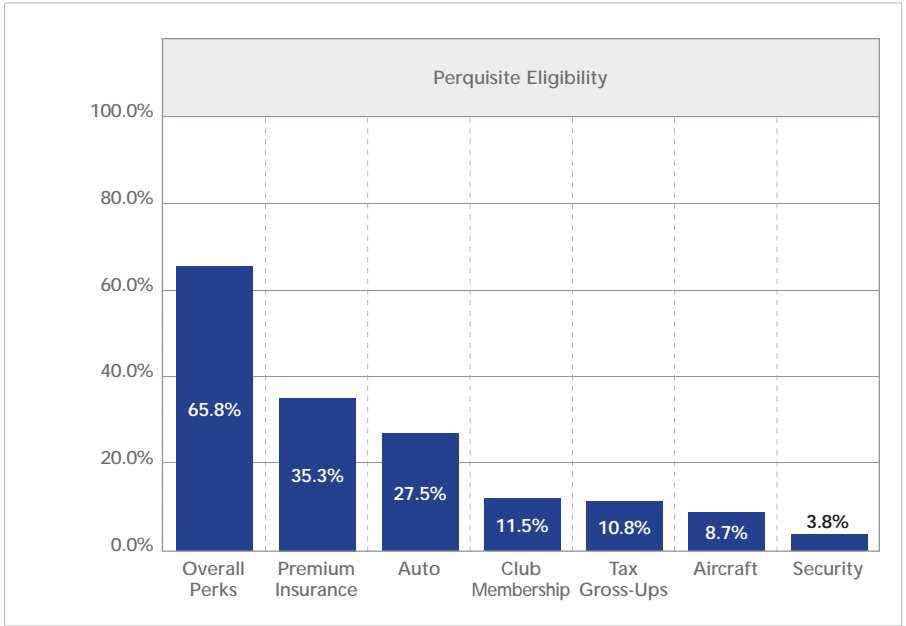


- Survey results also indicate a disparity in pay based on company location. HR executives at companies located in the Midwest or South census regions were paid less than their peers in the West or Northeast census regions.
- Despite relatively low median revenue, companies in the Technology, Media, and Telecommunications industry paid their HR executives more than any other industry. In contrast, HR executives in the Financial and Insurance industry received less pay than their peers, even though their median revenue was the second highest.
- Options were the most commonly used incentive vehicle. 60.9% of HR professionals in the survey received a time-based option award, and 58.3% received a time-based stock or unit award. Performance-based stock or unit awards came in third, at 42.1%.
- The most common incentive combination for Human Resources professionals in the survey consisted of time-based options and time-based stock awards. An overwhelming majority of time-based option awards vest in installments; three or four years are the most common vesting periods, followed by a five-year vesting period.
- The most common vesting schedule for time-based stock awards was a three-year cliff, or vesting all at once at the end of a three-year period. More than three-quarters of performance incentives granted to HR executives were equity-based. Long-term cash incentives made up 20.8% of all performance incentives granted.

**Key Findings—Perquisites**

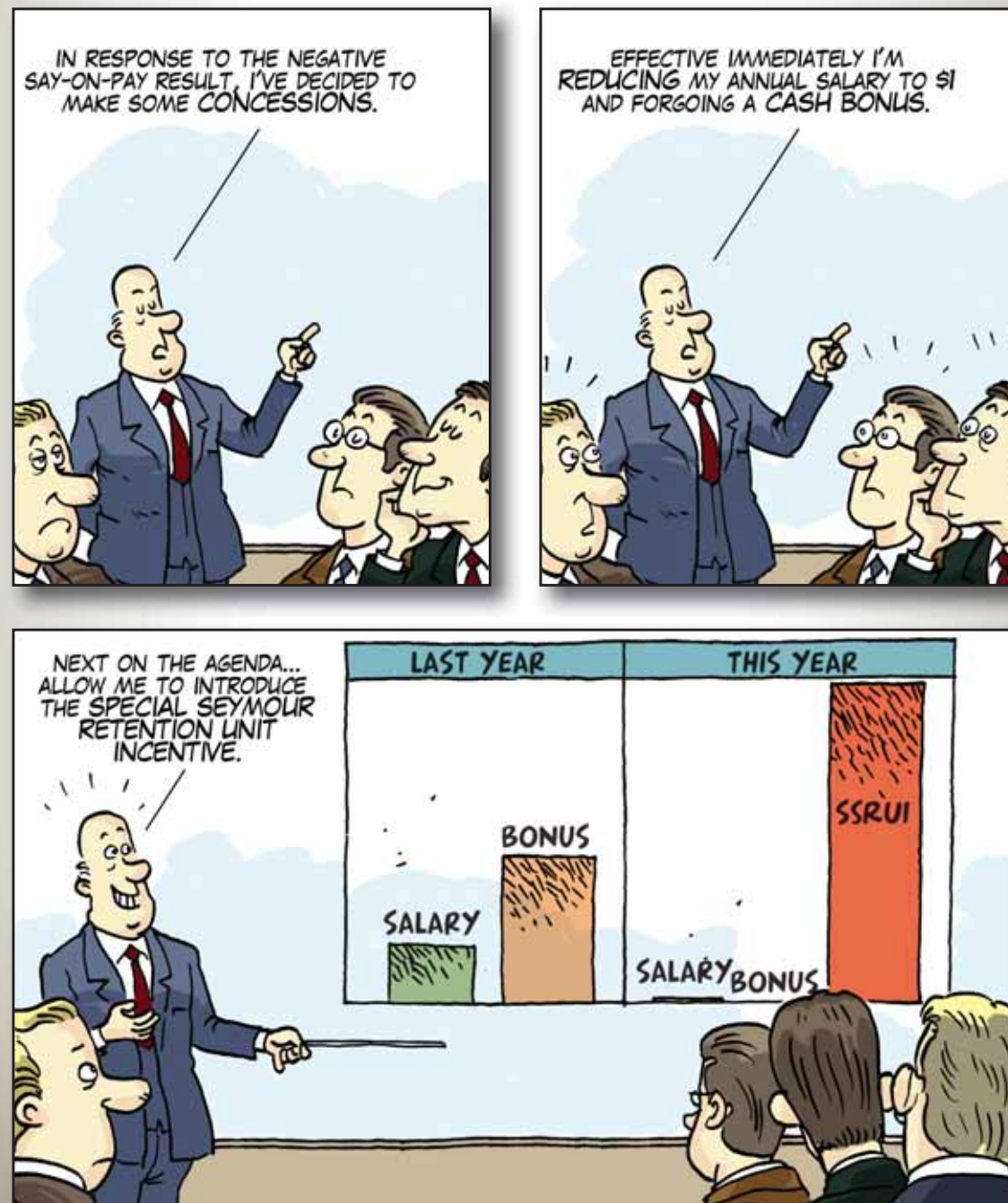
- According to Equilar’s 2010 Top 25 Survey, 65.8% of HR professionals were eligible to receive perquisites.
- Perquisite eligibility shows a direct correlation with company revenue, except at the largest companies. This is likely due to increasing public scrutiny of executive perquisites at the largest public companies.
- Though they earn the highest median pay, Human Resources executives working in Technology, Media, or Telecommunications companies are less likely than their peers in other industries to receive perquisites.
- Overall, HR professionals who do not report to the CEO are less likely to receive perquisites. As with total compensation, the number of years a Human Resources executive has been with a company also increases his or her overall perquisite eligibility.

*Want to learn more? See the full report by visiting [www.equilar.com](http://www.equilar.com), calling (650) 286-4512, or e-mailing [info@equilar.com](mailto:info@equilar.com).*



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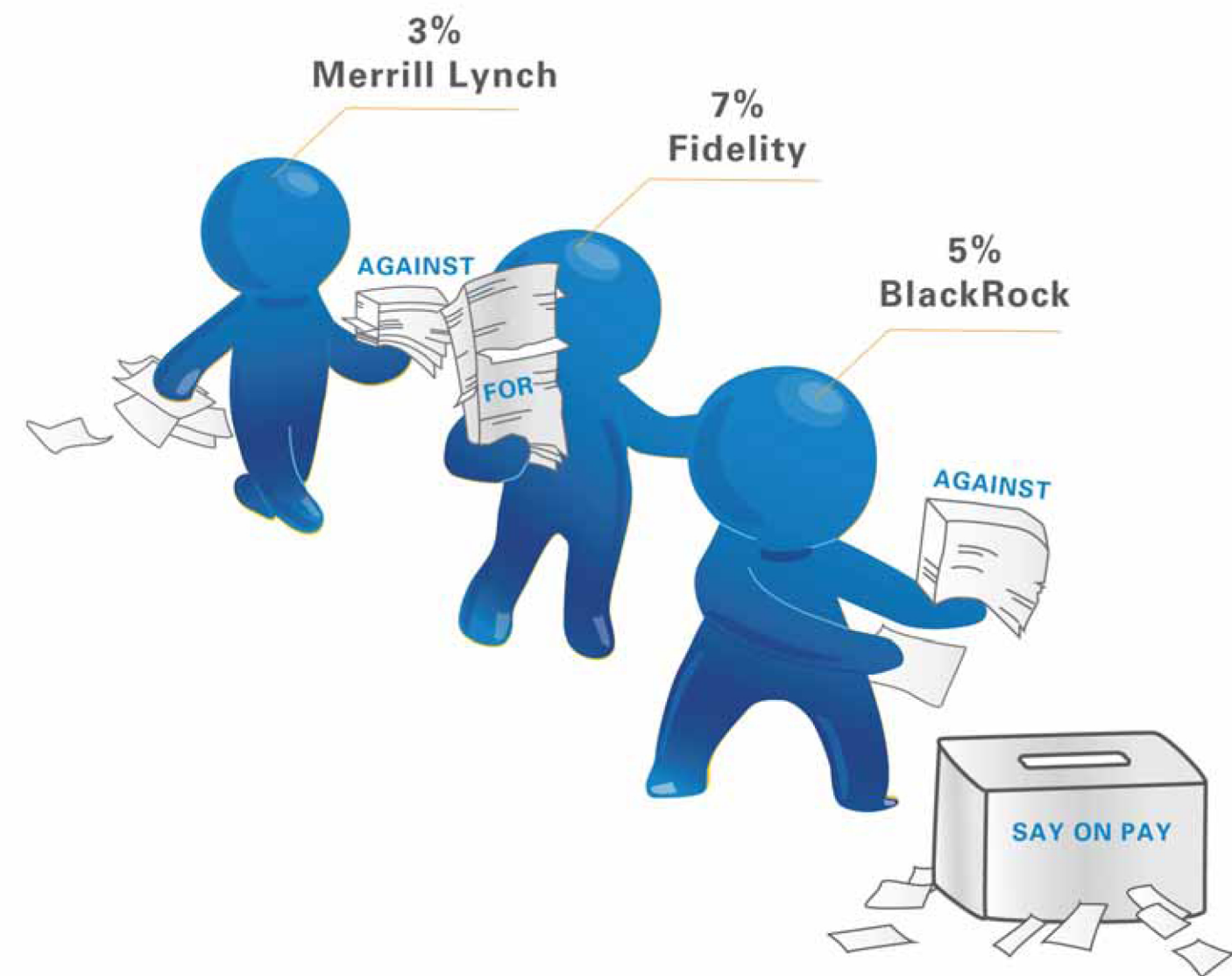
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