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Who Moved My Bonus? Executive Pay Makes a U-Turn

By **KATHRYN JONES**

BIG corporations, buffeted by widespread economic pain and heightened scrutiny of lush compensation packages, appear to be paying attention to a longstanding complaint from shareholders: When it comes to [executive pay](#), greed — even the appearance of it — is not good.

Executive compensation for the highest-paid chief executives at public companies fell in 2008, the first such downturn in five years. And the bottom dropped out of the bonus pool, the incentive that angered investors after the controversial bonus payouts at the [American International Group](#).

“We could begin to see a fundamental sea change in the compensation of executives,” says Charles M. Elson, director of the John L. Weinberg Center for Corporate Governance at the [University of Delaware](#).

“The idea should be that compensation is related to the overall value of the company,” he adds. “If shareholder value has fallen, so should the value of the executive pay package. Pay should reflect company performance and align with shareholder interests.”

For some time now, “should” has been the operative word for investors and corporate governance groups pressing for closer links among executive pay, performance and shareholder value.

But the recent public outrage over A.I.G., [Merrill Lynch](#) and other struggling or taxpayer-supported companies that paid big bonuses — as well as continuing business woes and the fear of possible shareholder revolts — has spurred some corporate compensation committees to rein in executive pay and cut or even do away with bonuses. (At A.I.G., 15 of the largest 20 bonuses, totaling about \$30 million, have been returned.)

“We’re seeing at long last that boards are linking pay closer to performance,” says Stephen M. Davis, senior fellow at the Millstein Center for Corporate Governance and Performance at the Yale School of Management. “The challenge is whether they see this as a one-off episode to address public anger over out-of-control pay or if this is something that will be more permanent.

“These are green shoots,” he says of the lower pay figures. “To use a spring analogy, it remains to be seen whether these are annuals or perennials.”

The compensation research firm [Equilar](#) (equilar.com) recently compiled data for The New York Times reflecting pay for 200 chief executives at 198 public companies that filed their annual proxies by March 27 and had revenue of at least \$6.3 billion. (Two companies, [Motorola](#) and Synnex, had co-C.E.O.’s.)

The data supports Mr. Elson’s and Mr. Davis’s observations. It shows that as shareholder values and financial

performance have fallen, so have average and median compensation numbers for chief executives — although not by the same margins. And some C.E.O.'s continue to receive lavish pay packages even though many employees and shareholders have suffered hardships like layoffs, pay cuts and deep losses in [401\(k\)'s](#) and other investments.

Equilar found that median total compensation — the midpoint at which half the values are lower and half are higher — was down 9.4 percent last year, to \$8.4 million. Average total compensation fell 5.1 percent, to \$10.8 million. The totals are for C.E.O.'s who have held their jobs for at least two complete years.

The last time Equilar recorded a big decline in C.E.O. pay was after the tech bubble burst, from 2001 to 2002. During that period, compensation for chief executives at companies in the Standard & Poor's 500-stock index declined 9.9 percent, falling to a median of \$7.06 million in 2002 from \$7.84 million in 2001. From 2002 to 2003, S.& P. 500 executive pay was essentially flat. After that, it increased each year until last year.

The big slide in bonuses was largely responsible for dragging down executive pay in 2008. For C.E.O.'s in place at least two years, median cash bonuses plummeted 21.6 percent, with the average cash payout down 16 percent. The median cash bonus in 2008 was about \$1.57 million, compared with more than \$2 million in 2007. The average bonus was \$2.42 million, down from \$2.88 million a year earlier.

Stock and option awards remain huge pieces of C.E.O. pay. But their values are based on the dates when they were granted, so there is no guarantee that executives will actually realize these amounts; in many cases, the values have declined with the market.

The executive on the list who earned the most last year, Sanjay K. Jha of Motorola, was paid almost entirely in such stock and option grants. He earned \$104.4 million in total compensation, \$103.6 million of that in grants when he was hired away from [Qualcomm](#) in August.

Following him on the list were [Lawrence J. Ellison](#) of Oracle, with \$84.6 million; [Robert A. Iger](#) of [Walt Disney](#), \$51.1 million; [Kenneth I. Chenault](#) of [American Express](#), \$42.8 million; and [Vikram S. Pandit](#) of [Citigroup](#), \$38.2 million.

Next were [Mark V. Hurd](#) of [Hewlett-Packard](#), \$34 million; Jack A. Fusco of Calpine, \$32.7 million; and [Rupert Murdoch](#) of the [News Corporation](#), \$30.1 million.

[Warren E. Buffett](#) of [Berkshire Hathaway](#) remained the C.E.O. with the most accumulated wealth; his stock holdings were worth about \$40.3 billion as of Dec. 31.

Most of Mr. Hurd's total compensation came from his \$23.9 million cash bonus — the largest of anyone in the Equilar survey. Last year, Hewlett-Packard reported a 13 percent uptick in revenue on a 15 percent gain in earnings. Shareholder returns, however, fell 25 percent.

Other executives receiving the largest cash bonuses — which include those based on performance as well as discretionary ones — were Mr. Murdoch, with \$17.5 million; Mr. Ellison, \$10.8 million; and Mr. Iger, \$13.9 million.

CERTAINLY, some of the highest-paid chief executives presided over companies that did very well. Those

included Mr. Ellison; [Alan G. Lafley](#) of [Procter & Gamble](#); Joseph W. Saunders of Visa, who last year helped guide it through the biggest I.P.O. in history; and [Nicholas D. Chabreja](#) of [General Dynamics](#).

But in other cases, it was harder to see a connection between high pay and performance. That was especially true in the beleaguered financial services industry.

Citigroup, of course, was one of the most closely watched and most deeply troubled companies last year. Its stock price plunged amid concerns among investors and the public about its viability, which led the federal government to give it bailout money.

Amid those woes, Mr. Pandit earned a base salary of \$958,333 and no bonus. But his stock awards were valued at \$28.8 million and his option awards at \$8.4 million. (A large chunk of his equity awards were incentives from his appointment as C.E.O.)

In a March 20 memo to Citigroup employees, Mr. Pandit addressed what he called the “tide of negative sentiment rising in Washington” about executive pay.

“Of course, some of it is warranted,” he wrote. “But I take exception when there is a discussion about spreading the blame to each and every employee in the financial services industry. At our company, we removed the people responsible for Citi’s financial distress and acted fast to strengthen and streamline the business, and install new risk processes and new risk personnel.”

Not surprisingly, the largest declines in executive pay in 2008 came in financial services, which in past years produced some of the highest-paid executives. Total pay last year in the sector nose-dived 40.1 percent.

For example, [John J. Mack](#), who took the helm of [Morgan Stanley](#) in 2005 and started an aggressive move into high-growth but risky areas like mortgages and leveraged loans, last year saw his pay fall 97 percent. He received \$800,000 in base salary, no bonus, \$435,097 in perks and no stock or option awards. Morgan Stanley’s shareholder returns fell 70 percent last year, and the company lost more than \$2 billion in the fourth quarter.

The roster of the highest-paid executives is also notable for the names that aren’t on it. The most obvious is [John A. Thain](#), the Wall Street whiz and former chief of the [New York Stock Exchange](#). In 2007, he took over Merrill Lynch after the ouster of [E. Stanley O’Neal](#), who presided over the firm’s disastrous push into mortgage investments.

Mr. Thain was the highest-paid executive that year, with a compensation package of almost \$83.8 million thanks in large part to a hefty sign-on bonus. He dropped off the Equilar survey because of Merrill Lynch’s acquisition by [Bank of America](#). This January, three weeks after Merrill Lynch was sold and lost billions of dollars, Mr. Thain was forced out.

Also off the list is [Lloyd C. Blankfein](#), chief executive of [Goldman Sachs](#), one of the nine largest financial firms receiving money from the federal government’s [Troubled Asset Relief Program](#), or TARP.

Goldman had not yet filed a definitive proxy statement by March 27 and therefore isn’t included in the Equilar survey. Other financial companies missing from the list are [Lehman Brothers](#), which filed for

bankruptcy and sold off its assets; [Washington Mutual](#), which was seized by federal regulators in the largest bank failure in American history; and Wachovia, acquired by its rival [Wells Fargo](#). In all, 41 companies that appeared in the 2007 survey fell off last year and were replaced.

But three financial firms that received TARP money remain on the list.

In addition to Mr. Pandit of Citigroup, [Kenneth D. Lewis](#) of Bank of America last year received a base salary of \$1.5 million, but no bonus. He also got \$275,125 worth of perks and stock and option awards that brought his total pay package to more than \$9 million, down 56 percent from 2007. Last year, his bank's revenue fell 2 percent and net income slid 83 percent. Shareholder returns were down 60 percent.

Under Mr. Lewis's direction, Bank of America acquired two troubled giants, Merrill Lynch and [Countrywide Financial](#). The Merrill deal, especially, hurt Bank of America: the brokerage suffered outside losses even before the acquisition closed.

The third C.E.O. on the list whose company received TARP money is [Richard D. Fairbank](#) of [Capital One Financial](#), who last year took home one of the lowest total compensation packages. His pay fell nearly 100 percent. For 2008, Mr. Fairbank did not draw a base salary or bonus, but he received perks valued at \$68,344.

SALARY is often a tiny fraction of C.E.O. pay, eclipsed by bonuses, stock and options grants. The 200 executives included in the survey received an aggregate of \$447.8 million in cash bonus payouts in 2008. Of this amount, \$54.2 million, or 12.1 percent, came in discretionary payments and \$393.6 million, or 87.9 percent, was from performance-based payments.

Among tenured chief executives, the aggregate value of cash bonus payouts dropped \$74.9 million, or 16 percent, from 2007 to 2008. For the 162 tenured C.E.O.'s on the list, aggregate payouts in 2008 were \$392.1 million, versus \$467 million in 2007.

Tenured executives' perks and other compensation — like use of corporate aircraft, relocation expenses, contributions to 401(k)'s and company-paid supplemental life insurance premiums — fell 5.4 percent, to a median of \$211,473 from \$223,498 in 2007.

The median level of stock awards rose slightly for C.E.O.'s in place two or more years, to \$2.68 million from \$2.57 million. But the median for option awards slid to \$1.87 million from \$1.93 million a year earlier, reflecting a trend of awarding fewer stock options. One-quarter of the executives on Equilar's list didn't receive any stock options last year.

That was true even in the technology sector, where start-ups and emerging public companies traditionally have awarded stock options in lieu of high salaries to give incentives to executives. Option awards among high-tech companies fell 47.3 percent last year, to a median \$789,375 from \$1.5 million in 2007. In comparison, median stock awards were up 86.7 percent, to \$4.4 million from \$2.4 million a year earlier.

“Stock options are still a big part of the culture in Silicon Valley and the tech sector over all, but more mature companies like [Microsoft](#) have shifted to stock awards as their stock prices become less volatile and options no longer offer the incentive kick that they once had,” says Alexander Cwirko-Godycki, a research manager at

Equilar.

Beyond the financial industry, total median compensation also fell in such sectors as basic materials and energy, 4 percent; conglomerates, 21 percent; industrials goods, 6 percent; and utilities, 17 percent. Executive pay rose in only four industries: consumer goods, 4 percent; health care, 4 percent; services, 2 percent; and technology, 10 percent. Chief executives in the health care industry last year commanded the highest median pay: \$13.8 million.

“We are witnessing a seismic shift among top corporate earners,” Mr. Cwirko-Godycki says. “Wall Street and the financial sector were once at the pinnacle of the corporate world, and their pay reflected that. Because of the current crisis, we see new pay leaders emerging, particularly in health care and technology. To some extent, that probably reflects where the future strengths in this economy lie.”

The question remains whether compensation cutbacks will be enough to placate investors — and whether they’re permanent. Shareholders get their chance to weigh in at this spring’s annual meetings, but so far they’re not claiming any victories on the pay numbers. While more companies may be starting to tie pay to performance, they are still the exception rather than the rule, shareholder and advocacy groups point out.

The bottom line should be that “if there is no performance, there is no bonus,” says Hye-Won Choi, senior vice president and head of governance for TIAA-CREF, the big pension fund. Obviously, that wasn’t the case last year: despite the beating that equities took, only 39 executives in Equilar’s survey, or 19.5 percent, didn’t receive bonuses.

What’s also still lacking, corporate governance experts say, is active communication between boards and shareholders.

“This is my skepticism: the numbers may show the links between pay and performance are getting tighter,” Mr. Davis says. “But because the dialogue is about nonexistent between boards and shareowners, you just wonder if this is going to be a passing phase.”

Others agree.

“People get religion of sorts about ethics and corporate governance in down markets,” said James A. Allen, director of capital markets at the nonprofit CFA Institute Center for Financial Market Integrity. “When things are going well, they tend to forget about it.”

AS shareholders have watched their holdings shrink, many say they are beginning to realize that passivity can be costly.

“With the trillions of dollars that have been wiped out of pension plans and other savings, investors have come to understand they need to pay attention to the governance of corporations — from compensation to board structures,” Mr. Davis says. “If they don’t, the cost is going to come out of their pockets. They’ve got to be engaged.”

Investor and public concern played a role in bringing down executive pay in 2008, governance experts say. “The fundamental change is that boards are paying much more attention because of investor and regulatory

scrutiny,” Ms. Choi says.

Carol Bowie, head of the governance institute at the RiskMetrics Group, a financial analytics company, concurs: “If that wasn’t the case, you might have seen more discretionary bonuses and retention bonuses. Boards are very attentive to the public scrutiny.”

TIAA-CREF representatives have sat down with some boards to voice their concerns as shareholders. “It’s not a regular occurrence,” Ms. Choi says, “but our view is that it should be. Companies should want to talk to their major holders.”

“We want to level the playing field,” she says. “Boards need to pay attention to what matters to shareholders.”

What matters to big shareholders this year, Ms. Choi says, is getting a say on pay and a seat at the table for compensation and other decisions. TIAA-CREF was the first publicly traded company to give its own shareholders a say on pay. Aflac, [Verizon Communications](#), [Blockbuster](#), RiskMetrics and a handful of other companies also have agreed to adopt say on pay, and many other companies are discussing it.

Say-on-pay resolutions have been common in Britain and Australia for several years. “Bonuses need to be changed to reward for a combination of past performance and an ability to sustain performance into the future,” says Andrew Likierman, dean of the London Business School.

In the United States, Congress has proposed bills requiring all public companies to establish shareholder advisory votes on compensation. But because public companies operate under state law — more than half are incorporated in Delaware — and the votes are advisory, boards don’t have any legal obligation to abide by shareholder wishes on compensation.

Through April 1 this year, investors have filed more than 100 resolutions seeking a say on pay, RiskMetrics found. Last year, such proposals received support from an average of 44 percent of shareholder votes cast. Most of the resolutions are pending, but governance watchdogs expect that many could pass this year, given shareholders’ mood.

Disclosure remains another huge issue for investors. When the Securities and Exchange Commission passed tighter rules for corporate proxies three years ago, it required more information about the methods used to set executive pay. But instead of increasing transparency, the rules have had the unintended consequence of muddying the water with excess verbiage.

Disclosures about executive pay in proxy statements are “far too long, far too complex and don’t address the real needs of investors,” Mr. Davis says. “Too many companies are doing this as a compliance exercise. They’re missing the point.”

For example, the executive compensation portion of [I.B.M.](#)’s proxy statement runs to almost 50 pages. Apple — whose chief executive, [Steven P. Jobs](#), gets a salary of \$1 and no bonus — has a simpler document that includes compensation disclosures for the rest of the top management team as well. Even so, the pay portion in its proxy statement still covers more than 20 pages.

Some shareholders are leery that companies facing losses, lower earnings or stock prices in the tank will look

for other ways to reward executives, such as repricing or exchanging options that are now “underwater” — essentially worthless unless the share price recovers — or rewarding discretionary bonuses.

“Putting limits on executive pay is a bit like squeezing on a balloon,” says Scott A. Fenn, managing director of policy at Proxy Governance, the proxy advisory firm. “When you squeeze one place, it pops out somewhere else.”

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