# Executive Pay

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New ideas from the regulators for disclosing managers' pay

**Outsiders' rewards**

Boards' independent directors' total compensation*
top ten 2004-05, $m

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|---|---|
| XL Capital | 8.63 |
| WellPoint | 7.86 |
| Telewest Global | 7.10 |
| Genentech | 7.05 |
| ImClone Systems | 7.00 |
| Fannie Mae | 5.71 |
| MannKind | 5.52 |
| UnitedHealth Group | 5.45 |
| Target | 5.02 |
| Kos Pharmaceuticals | 4.97 |

*Sample of 2,054 of the largest US companies (median $800,000)
Source: The Corporate Library

IT IS 14 years since America's Securities and Exchange Commission (SEC) last changed its rules on corporate disclosure of top executives' pay. In the meantime, other countries (such as Britain) have introduced more demanding standards and Americans have grown increasingly agitated by reports of Godzilla-sized pay packages that often bear little relation to a company's performance. Michael Eisner, the former boss of the Walt Disney Corporation, has become emblematic of this sort of excess. He was a genuinely outstanding manager during the first part of his more than 20 years at the top of the firm. But he was then paid $800m over a 13-year period in which his company's shares did worse than government bonds. Investors claimed they had not realised how richly Mr Eisner was being rewarded.

On January 17th the SEC's five-man board unanimously approved new proposals for increased disclosure of executive compensation. The public now has 60 days to comment on the proposals, after which they could become mandatory as early as the 2007 reporting season. The focus is on providing investors with a single number for the total remuneration of the chief executive, the chief financial officer and the three next-highest-paid executives. The information that is available today is often spread confusingly around several filed reports. In some cases, says Christopher Cox, the SEC's chairman, "disclosure obfuscates rather than illuminates the true picture of compensation." The SEC says it will require that disclosure "be provided in plain English", but refrains from saying who will be the arbiter of that.

Obfuscation is rife in three areas in particular--pensions, perks and deferred pay--and the SEC addresses all of them. The new rules will improve the disclosure of top executives' retirement benefits. Currently, it can require an academic study to work out the real figures. Research published last year by Lucian Bebchuk and Robert Jackson of Harvard University put the median value of the pension pots of a sample of top chief executives at $15m. Mr Bebchuk says that companies' "massive use of defined-benefit pension plans [for their top executives] has

been partly motivated by a desire to provide chunks of performance-insensitive pay under the radar screen."

Another way to get rewards under the radar screen is via perks. One of the most popular for American chief executives is the corporate jet. A recent study by David Yermack, a professor at New York University's Stern School of Business, found that the private use of company aircraft is "the most costly, and fastest-growing, fringe benefit enjoyed by major company CEOs." At present, companies have to disclose perks to individuals in excess of $50,000, valued on the basis of their "aggregate incremental cost" to the company. That can take an executive to far-distant golf courses many times over without showing up on shareholders' radar screens. Mr Yermack found a strong relationship between chief executives' private use of a corporate jet and golf, in particular to membership of the prestigious Augusta golf club in Georgia. On the other hand, he found an inverse relationship between the private use of company's jets and its stockmarket performance. The SEC proposes reducing the threshold for disclosing perks from $50,000 to $10,000.

Severance pay received by departing chief executives and deferred compensation schemes are other dark areas on to which the SEC promises to cast some light. Companies are currently under no obligation at all to reveal deferred compensation, which enables executives to shift their individual tax liabilities to the company.

Combining numbers of this kind into a single headline figure could provide some shocks. "The numbers in total will surprise," says Pearl Meyer, founder of an eponymous firm of compensation consultants. But they may not cause chief executives' pay to fall. On the contrary, it could rise more rapidly by pushing up the benchmarks against which pay is set.

Controls are in the hands of the non-executive board directors who appoint and decide on the remuneration packages of their top executives. For the first time, the SEC is going to require that companies reveal how much these people in aggregate are being paid. Here, however, the numbers are likely to be surprising for a different reason. A study published earlier this month by the Corporate Library, a governance watchdog, found that the median total compensation of large companies' groups of outside directors was just over $800,000, a figure that the report's author, Paul Hodgson, describes as "moderate", given that the average number of such directors is eight. Shareholders, however, may not consider it good value for money until these directors show some of the same moderation when setting the pay of their executive colleagues.