Rich Rewards for the Regions Corporate Elite

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It pays, more than ever, to be at the top.

The median total compensation for the 100 highest-paid executives in The Washington Post's annual survey of executive pay was $5.25 million in 2004, up slightly from $5.13 million the year before.

Last year, 294 executives of area companies received packages worth $1 million or more, compared with 270 executives in 2003 and 190 in 2000, according to The Post's study of top-level compensation at 157 local companies that publicly report pay and benefits.

The median total compensation -- which includes salary and bonus, long-term benefits, perks and the projected value of option grants -- for all executives in the 2004 survey was $704,713, compared with $668,049 in 2003. The median is the midpoint of the survey, with half below and half above. The survey covered 764 executives in 2004 compared with 728 in 2003.

Dale B. Wolf, 50, president and chief executive of Coventry Health Care Inc. of Bethesda, had the richest compensation package of any Washington area executive in 2004. His salary, bonus, perks and stock options put his total compensation at $32.3 million. The biggest portion of Wolf's pay was stock options, which The Post valued at $30.6 million, assuming an annual stock price increase of 5 percent over the life of the options.

Richard D. Fairbank, chief executive of Capitol One Financial Corp. of McLean, was second in total compensation, at $29.5 million. Fairbank received no salary or bonus. Nearly all his compensation package was options.

Of the executives who took home the most cash in 2004, the top four were the senior executives of Friedman, Billings, Ramsey Group Inc., an investment bank based in Arlington County. At the top of the list for cash, co-chief executives Eric F. Billings and Emanuel J. Friedman each pulled down $10.7 million in 2004, $9.4 million of that in the form of a cash bonus. Friedman, who was forced to resign this spring from the firm he co-founded, is being investigated by the Securities and Exchange Commission.

In general, raises for chief executives at area companies tracked increases in shareholder value. Of the 117 local chief executives in place at least two years on Dec. 31, the average cash pay increase last year was 17 percent, and the average total return to shareholders was 20 percent.

But there were exceptions -- 21 chief executives at companies whose shareholders lost money in 2004 received cash pay increases, and 10 of those received double-digit cash pay increases.

Of the 100 highest-compensated executives, 97 were men. The highest-paid woman at a public company in the Washington area was Joan M. Sweeney, chief operating officer of Allied Capital Corp., a Washington corporate finance company. Sweeney was paid $8.5 million, including $1.5 million in cash and options worth an estimated $5.5 million.

Rewards and Incentives

Companies with executives at the top of the lists for total compensation or total cash argued that the rewards were earned as pay for performance.

At Coventry Health Care, Wolf was promoted from chief financial officer to chief executive in January, one of the career turning points when boards of directors often award senior executives with a super-size increase in compensation.

The board of the Bethesda health insurer awarded options to Wolf in June on 1 million shares of company stock "as a performance-based stock incentive to retain and incent Mr. Wolf to continue the success of the company and in anticipation of Mr. Wolf's becoming the chief executive officer," according to the company's filing with the SEC. Wolf and other company officials did not return phone calls seeking comment.

Wolf and former chief executive Allen F. Wise, who is now chairman, took over a troubled managed health care company in 1995. Coventry has built its business buying mid-size, often under-performing health plans in a number of states and turning them around, said Joseph D. France, who follows Coventry at Banc of America Securities.

"They are by far the best performer in managed care in recent years," France said. "They are very entrepreneurial. In terms of return that shareholders have enjoyed, their compensation stacks up well."

Coventry's shareholders have had a 174 percent return in the two years ended Dec. 31, according to Bloomberg News.

At Capitol One, Fairbank has been compensated almost wholly through options for a number of years, on the grounds that if the stock price declines and shareholders lose money, he won't receive a dime. So far, however, this strategy has worked to his benefit. Last year alone, he cashed in options with a net value to him of $56.5 million. All the options he exercised last year were about to expire; he had held on to them for nearly the life of their terms. A $1,000 investment in the credit card company's stock 10 years ago would be worth more than $10,000 today.

Friedman, Billings, Ramsey has earned more than $550 million in the past two years, and last year it was one of the most profitable investment banks in the nation as measured by return on equity. On Wall Street, that means big bonuses. FBR spokesman Bill Dixon said that bonus pay for senior executives is tied to earnings per share and that if FBR had lost money in 2004, the executives wouldn't have received any bonuses. FBR's chief executive salary, $480,000 last year,

is substantially below average for most Wall Street firms and less than 126 other executive salaries in this year's local survey.

The 2004 bonus for Friedman was his last. He resigned in April after the SEC began investigating insider trading allegations against him. The company has offered $7.5 million to settle the allegations on its part, but the investigations into Friedman and two other former senior FBR executives are continuing.

Friedman's 2004 pay was granted before the insider trading investigation targeted him. He received no pension or severance payments when he left the company.

Michael D. Capellas, chief executive of MCI Inc., was paid $25.2 million last year, most of it as a reward for pulling the Ashburn-based telecommunications company out of bankruptcy. He received a $5 million bonus and $18 million worth of restricted stock.

Restricted stock is given to an executive but can be sold only after a number of years.

Jeffrey J. Steiner, chief executive of Fairchild Corp. in McLean, which sells aircraft parts and sports and leisure apparel, has long been among the highest paid of local executives. He had the highest salary in the Washington area in 2004, $2.5 million, but didn't receive a bonus. As a result, his total cash payment was down significantly from $7.8 million in 2003.

Putting some of the survey numbers in perspective:

· The local companies in the 2004 survey collectively paid their 764 top executives more than $500 million in cash, perks worth $67 million, and $188 million in restricted stock and other long-term incentive payments. Assuming a stock price increase of 5 percent for all companies over the life of the option grants awarded last year, the 764 executives will take in an additional $555 million.

· The median salary and bonus for executives in the survey was $400,583, a 7.6 percent raise from 2003's median. By contrast, the median annual pay for a worker in the Washington area was $37,610 in 2004, an increase of 4 percent from 2003. Including all forms of compensation, the $704,713 median total pay received by the 764 executives in The Post survey was more than 18 times the median annual pay for the metropolitan area.

· The $40.6 million in salary and bonuses taken home collectively by the five highest-paid executives is twice the budget of the D.C. public library system.

Other Kinds of Compensation

The mix of compensation paid to executives changed in 2004, moving from stock option grants and toward more cash, perks and other forms of long-term compensation.

The median option grant for the 100 highest-compensated executives in 2004 was $2.7 million, down 6 percent from 2003. The median salary and bonus, meanwhile, rose 18 percent from 2003, to $1.5 million.

Stock options give executives the right to buy company stock at the price on the date of the grant. If the stock price goes up, the executive can profit from the difference between the market value and his exercise price. For comparison purposes, The Post used an assumed stock price annual appreciation of 5 percent over the life of the option for all the companies in the survey. Some stock may prove to be worth more, while stock options at a company whose stock price declines are rendered worthless.

The median long-term compensation grant -- usually in the form of long-term incentive plan payments or restricted stock grants -- to the 100 highest-paid executives in 2004 was $660,000, more than double what it was in 2003.

Long-term incentive plans typically grant an executive cash for meeting three- to five-year performance goals.

Lucian A. Bebchuk, a professor of law and economics at Harvard Law School who has studied the effect of corporate governance and executive compensation on shareholder value for more than a decade, said the executive numbers in the Washington area mirror national trends.

"In response to a decline in shareholder enthusiasm for options, they've channeled the growth in pay into everything but options," he said. "But it's not at all clear that this move, speaking broadly, has led to a considerable tightening of the pay-for-performance link."

Bebchuk said boards of directors continue to find new ways and new reasons to reward senior executives that have nothing to do with creating shareholder value such as increasing stock price or building market-share dominance or other objective measurements. Rewards go up when value rises, but they tend to remain high even if value falls.

"The structure is what needs reforming," Bebchuk said. "Boards hide behind boilerplate reasons" for increasing pay, such as peer group comparisons, that don't address whether the shareholders have been rewarded. In addition, a range of benefits and payouts, such as severance agreements for executives who are fired or huge pension benefits for executives, often reward executives handsomely even if they screw up.

"If a large part of an executive's career compensation comes from a pension, it decouples their pay from performance of the company," he said.