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Jamie Dimon's Pay Raise Sends Mixed Signals on Culture and Accountability

By: Ben W. Heineman, Jr.
February 3, 2014

The JP Morgan Chase board of directors has vexed the world with its terse announcement in a recent 8-K filing that CEO Jamie Dimon would receive a big pay raise — $20 million in total pay for 2013, up from $11.5 million for 2012, a 74 percent increase.

Not surprisingly, the news sparked strong reactions, from indignant critique to justification and support. Dimon's raise obviously has special resonance because JP Morgan's legal woes were one of the top business stories last year as it agreed to $20 billion in payments to settle a variety of cases involving the bank's conduct since 2005 when Dimon became JPM CEO. But the ultimate question that gets fuzzed-over in the filing and response is one of culture and accountability — whether a long-serving CEO is accountable for a corporate culture that has spawned major regulatory inquiries and settlements across a broad range of legal issues, even though the firm has otherwise performed well commercially.

If, as many would argue, a core CEO job is to create the company culture, the board of directors seems to ignore that bed-rock corporate principle when it increases Dimon's pay, without much explanation, after several years in which the failings of the JPM culture were on the front pages for all to see.

According to news reports, there was disagreement within the JPM board about whether Dimon should receive a large increase or have his compensation basically stay flat at the 2012 amount which reflected a substantial decrease from 2011 (about 50 percent) as a result of losses and improprieties relating to the derivative trading of the "London Whale." Similarly, commentators have been divided about whether the raise was deserved or not, citing both economic performance (2013 was about the same as 2012) and Dimon's handling of diverse legal and regulatory issues for support.

The root problem is that the board failed to clearly articulate its reasoning for this important, high-profile decision on a fundamental matter of pay for performance. The announcement made the board seem oblivious to the fact that these issues have been center stage since the beginning of the financial crisis and, in fact, are of signal importance to the whole financial services industry and, indeed, to all major corporations. Instead, the regulatory filing simply listed, in summary fashion, "factors" supporting the raise, without any analysis elsewhere: JPM's long-term performance; gains in market share and customer satisfaction; resolution of regulatory issues; improved control structures and processes; and leadership improvements. (The short phrase "regulatory issues" hardly captures the depth and breadth of major matters JPM agreed to settle in the past two years across a broad array of problems (summarized here).

A legitimate case can be made for Dimon's 2013 raise. ($18.5 of the $20 million in total comp is in restricted stock units that vest in equal increments, in two and three years even if the stock is flat). The bank earned about $18 billion, down from $21 billion the year before. But, according to analysts, without legal costs attributable to 2013 and with other adjustments, the net would have been equal to or better than the prior year. The stock price rose more than 30 percent, in line with other major financials — and the company had high rankings in such areas as fees on debt, mergers & acquisitions, syndicated loans. Dimon dealt with regulatory issues head on. He criticized the bank and himself for the Whale. He acknowledged in his annual letter to shareholders in 2013 that "we are now making our control agenda priority #1," and added 5,000 employees in control functions (for a total of 15,000). He also personally took over negotiation of major legal controversies and faced into payment of out-sized settlements to put the matters behind JPM. As well, the multiplicity of legal matters could plausibly be attributed to "piling on" by the government, not markedly poorer performance by JPM than other major financial institutions who also face a wide variety of regulatory problems.

In short, it can be argued that Dimon has positioned JPM for solid growth going forward, presumably with far fewer legal problems. By this argument, he deserved a raise that simply put him back close to where he was in 2011 before his compensation was cut for 2012 — a cut instituted because of, in the board's words, his "ultimate responsibility" for the $6 billion dollar London Whale embarrassment.

The case against the raise begins and ends with JPM's corporate culture, for which Dimon also bears ultimate responsibility. The broad array of issues for which JPM has paid settlements totaling billions all took place on Dimon's watch. Except for the inherited Washington Mutual and Bear Stearns bad practices, they all involved JPM employees. They involved core bad behavior: collusion, inadequate disclosure, money laundering, abusive behavior towards debtors, indifference to red flags of massive fraud. They arose in different parts of the bank, not just one dysfunctional unit. They substantially impacted profitability. They have seriously corroded the bank's reputation with regulators, a number of investors, and the public. JP Morgan's own report on the matters surrounding the London Whale indicates broad failings. Dimon himself, after virtually all the problems had surfaced, admitted that under his leadership the bank had failed to pay enough attention to controllership issues, and had failed to create an appropriate culture of integrity, compliance and risk management.

To be clear, the argument against the raise is not an argument against retention of Jamie Dimon as head of JP Morgan Chase (or for his removal as chairman). Despite this core failing on corporate culture, he is obviously an extremely talented CEO in many other respects. But, the board should recognize the primacy of corporate culture and determine that, in a year when that culture's weaknesses have been exposed in searing fashion, it is sending the wrong message to return Dimon's comp to its former level. Economic performance in 2013 should not be the reason since it was roughly comparable to performance in 2012.

Because the words of the 8-K on the raise were so opaque, and because the question of CEO accountability for corporate culture is so critical to business, the JPM board of directors should have articulated its reasons more carefully and completely on an issue of such importance. **If the board does indeed believe in the centrality of corporate culture and that the CEO is accountable for creating and sustaining that culture, then it should clearly make that case** — perhaps in Proxy Statement comp section. It should clearly state that Dimon's actions and words are making a difference — and why; and that a major reason for the raise is this process of candidly confronting issues and affirmatively changing resources, systems and processes — and ultimately the culture.

This may not persuade the most obdurate critics, but it would be the right argument for an increase in CEO compensation for JPM's very troubled and troubling year. Instead, obviously feeling defensive, some members of the JP Morgan board, days after the announcement, spoke on background for a *New York Times* column that indirectly sought to explain their reasoning using some of the arguments above.

Without hearing more from the board itself, however, the critics of the raise, in my view, have the stronger argument. We should not have to speculate about the pros and cons of a decision with such high visibility and symbolic importance for the corporate and financial world. The board should step up and speak up to send a clear signal.

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