

Shareholders One Step Closer to Having a “Say on Pay”

The US House of Representatives votes to give shareholders an advisory non-binding vote on executive compensation.

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Executives at top companies command huge salaries, millions of dollars a year with perks and stock options. People might agree or disagree whether some of these CEOs, CFOs and COOs earn their huge paychecks, but no one can say \$1 million a year (or more) is a small amount of money. A Bloomberg poll from March 2006 found that more than 80% of Americans polled—divided evenly between the well off and those making under \$10,000 a year—agreed that CEOs are paid “too much.”

According to Harvard Professor [Lucian Bebchuk](#), who recently testified before the [House Financial Services Committee](#), over the past 15 years the salaries of Fortune 500 CEOs have risen from 140 times what an average worker makes, to over 500 times an average worker’s pay. Businesses are required to post the minimum wage in a visible location—currently \$5.15 an hour. These same businesses certainly don’t post what their maximum wage earners are making.

In this environment, many US shareholders concerned about rising executive compensation are working to make their voices heard. On April 20th they got one step closer, as the US House of Representatives passed “The Shareholder Vote on Executive Compensation Act” (HR 1257) by a vote of 269-134.

Democratic Representative Barney Frank of Massachusetts, Chairman of the Financial Services Committee, sponsored the bill. The bill requires that companies give shareholders a yearly non-binding advisory vote on their executive compensation packages. It also requires companies to offer an additional non-binding vote if the company offers a new gold parachute package as they simultaneously negotiate the purchase or sale of the company.

The bill had little Republican support and survived a number of Republican attempts to amend, including an amendment that would have taken away the shareholder’s advisory vote if the company was within 10% of the average of like companies. The White House came out against the bill and, in an April 17 Statement of Administration Policy, said that with the recent changes in the Securities and Exchange Commission’s (SEC) disclosure rules on executive pay, shareholders are receiving comprehensive information on executive pay. With the White House’s stance against the bill as it stands now, it is unknown if the President will veto the bill if it makes it out of the Senate. Currently, the bill has been referred to the Senate Committee on Banking, Housing, and Urban Affairs.

In 2006, the SEC changed its disclosure laws on executive pay, requiring companies to disclose to shareholders their executive compensation practices. HR 1257 sponsors think that HR 1257 adds to the SEC’s new rules by giving shareholders a way to voice their concerns.

The Corporate Library ([TCL](#)), a governance analysis firm that provides information on corporate issues including corporate pay issues, supports a non-binding vote on executive compensation at publicly listed companies. Paul Hodgson, a Senior Research Associate for TCL, told Socialfunds.com “If the Executive Compensation Bill is signed into law, it will require investors to have a greater understanding of compensation policy in order to be able to make informed, intelligent voting decisions.”

“It will also require institutional investors actually to think about compensation and its implications for value growth and investment and not simply vote with management as happens too often,” Hodgson said.

United for a Fair Economy ([UFE](#)), a non-profit, nonpartisan organization that works for greater economic equality and to build awareness that concentrated wealth undermines democracy, has written an annual Executive Excess report for the past ten years.

“It used to be a big deal when one of the major papers or magazines would write about CEO pay,” said Mike Lapham, project director of the Responsible Wealth project at UFE. “Now it’s part of the mainstream public conversation. People are starting to realize that most of the economic gains of the past two decades have gone to those at the top, and CEO pay is one of the most egregious examples of this. When people see \$50 million pay packages for executives while their wages are relatively flat, they get mad.”

People concerned about the discrepancy of earnings between CEOs and other workers have long called for companies to be transparent around how they award top wages. Shareholders, pension and mutual funds, including the California State Teachers’ retirement System (CalPERS) and the Interfaith Center on Corporate Responsibility (ICCR), have been working for years to have a say on how executives are compensated. England, The Netherlands, Sweden and Australia already have laws requiring companies to give shareholders a voice in deciding executive pay.

Recent shareholder proposal votes have showed great support for a non-binding advisory vote for shareholders on executive pay. For example, 49.2% of votes cast at Merck’s annual meeting were for the proposal to give shareholders a non-binding advisory vote on executive pay. The ISS reports that executive pay votes have averaged 39.7% at six shareholder meetings this year. It should be remembered that the percentage of votes cast in favor of such resolutions at companies is not a measure of how many stockholders actually would vote against compensation at the company, but an indication of how many wish to be able to voice their opinion on executive compensation.

As a result of a dialogue and shareholder proposal led by [Boston Common Asset Management](#), Aflac Insurance in February became the first US Company to commit to adopting an advisory vote. Boston Common filed a shareholder proposal at Aflac, which led to dialogue between management, the board, and Boston Common.

“We learned more about Aflac’s compensation philosophy and persuaded management to view the proposal as a valuable corporate governance reform rather than an attack on the company’s pay practices,” said Dawn Wolfe, Social Research Analyst at Boston Common. “In the end, we

were able to find middle ground. Boston Common withdrew the proposal and Aflac committed to adopting an advisory vote on executive compensation practices in 2009.”

The bill does not set limits on the size or nature of an executive’s pay and the annual advisory vote is non-binding. “This is a key component of the bill,” Wolfe stated. “Shareowners will not suddenly be given authority to micro-manage dollar amounts or restrain the board from doing its job. The advisory vote will simply give investors an opportunity to state if we believe a compensation package is reasonable.”

The role that the Federal government should play in helping decide executive pay is debatable. However, Lapham of UFE told Socialfunds.com, “The reality is that government already has a big role in CEO pay through tax policy. Individual taxpayers and small businesses are subsidizing excessive CEO pay. When companies write off executive salaries as a ‘reasonable business expense’ on their tax returns, the rest of us pick up the tab.” There is a 1993 provision in the tax code, Section 162(m), that limits the tax deduction of pay for the five highest-paid executives at public companies to \$1 million, unless the pay is “performance based.” Most companies skirt this \$1 million limit by setting easy goals for executives to reach, and, therefore, write off the entire payment made to top earners.