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**Missed Opportunity to Reform Executive
Compensation**

**CEO Publication
B 11-13 (601)**

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September 2011

Missed Opportunity to Reform Executive Compensation

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All is well in the land of executive pay. It looks like 2010 was a very good year for executives. After two so-so years in 2008 and 2009, executive pay in the United States reached an all time high in 2010. Salary survey data from Hay and Equilar show that in 2010 the average pay package for the head of a large U.S. company was 9 million dollars, an increase of about 25% over 2009. The new normal with respect to executive compensation appears to be very similar to the old pre-recession normal.

Executives were showered with pay of all types – salaries, bonuses, stock options and stock grants. The biggest gain came in cash bonuses. The only decrease came in club membership and other perquisites. Needless to say, most employees of large organizations did not experience the sizable pay gains that executives did in 2010. Indeed layoffs continued and most corporations tightened their budgets in 2010.

The pay difference between the top and the bottom in large corporations has expanded tremendously since the early 1980's, roughly speaking it has gone from 100 to 1 to 500 to 1. Some steps have been taken by the government to limit executive pay, most notably mandated shareholder votes on pay packages. However, so far most companies have not reduced the amount of compensation that their executives receive.

Numerous critics of executive compensation have raised the issue of how sustainable organizations and indeed societies are when there is a large difference between the best and the least well paid members of an organization. The drop in executive pay that occurred in 2008 and 2009 offered the opportunity for corporations to reduce the pay difference between the top and

the bottom. All they had to do was show some restraint in the degree to which they rewarded their executives for the improved corporate performance that took place in 2010. By giving smaller bonuses and less stock, they could have reduced the pay distance between the top and bottom of the organization – opportunity missed.

The rise in executive compensation that took place in 2010 was largely due to incentive compensation plans that were created or changed to account for the recession. One thing did not change; they continued to be based almost exclusively on the financial performance of firms. Organizations missed the opportunity to make an important change in the basis for executive incentive payments. They did not introduce a triple bottom line performance as a determinant of the incentives that were given in 2010.

Instead of basing the incentive payments strictly on financial performance they could have based them on environmental performance and social performance. This would have had two positive effects. It would have focused executives more on a balanced set of performance results and as a result improved the sustainable performance of organizations. It also most likely would have reduced the amount of pay that individual executives got: a win/win.

Although financial performance increased dramatically in 2010, there is little reason to believe that the social and environmental performance of organizations improved at the same rate or at all. Thus if they were considered to be a part of executive performance, bonuses would have been lower in 2010 and total compensation for executives would not have made such a dramatic upward movement. In addition it would have brought home to executives the importance of the social and environmental performance of their firms.

What about the future? It looks like 2011 is going to be another good year for executive compensation, if you are an executive. Maybe not quite as good as 2010, but executive compensation is likely to rise significantly given the positive performance of the stock market so far and the continued improvement of corporate earnings.

Thus it is likely that in 2012 we will look back at the executive pay levels in 2011 and see that the distance between executives and the rest of the organization has gotten greater. In addition, we will once again see that executive performance was focused on financial performance. Not a positive picture for those who believe that sustainable organizational performance requires financial, social and environmental performance and that a large pay gap between the top and bottom of an organization is dysfunctional.