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The Crystal Report on Executive Compensation



Equilar Releases Two New Studies

by Graef Crystal

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Equilar Inc., in my opinion the leading provider of executive pay data, has released two new studies.

Hiring from the Outside

The first of these concentrates on the pay of CEOs hired from the outside versus CEOs who made their way up their company's management ladder.

Although most lay people would tell you that there is a positive correlation between tenure and pay, they are wrong.

Early in my career, I changed jobs a number of times. One of my compensation colleagues averred that changing jobs was foolish because "you'll end up in the same place anyway". But, I countered: "That may be true, but I'm going to get to that same place a lot faster!"

You always have your best shot at getting a big leap in pay when you are on the outside, and when the other company is lusting after your talents. On top of that, if you're high up enough, you can hire your own compensation attorney to drive an even tougher bargain, and his or her billings will likely be paid by your new employer.

Some other facts revealed by this paper include:

- The likelihood of your coming in from the outside to be CEO is higher for smaller companies than for larger companies.
- But the pay premium paid for an outsider is wildly higher for the largest companies. CEOs in those companies who were hired from outside earned \$13.5 million versus only about \$7.5 million for inside promotees.

- Among CEOs with two or more years of tenure, there was little drop in total pay in 2008 compared to 2007 -- \$7.7 million in 2008 versus \$8 million in 2007.
- Not surprisingly, there is a connection between low shareholder returns and the hiring of a new CEO from the outside. That's something that regular compensation studies rarely pick up. One way to pay for non-performance is to lower pay. But perhaps the more potent weapon is to show someone the door.

Long-Term Incentives

In a second paper, Equilar notes that there is the beginnings of a resurgence in the practice of granting only stock options as the sole form of long-term incentive compensation.

In my long experience, I have seen CEOs become quite opportunistic when it comes to long-term incentive grants. When times are good or are thought about to become good, the usage of stock options starts to rise. When times are bad and not expected to recover soon, then option usage becomes depressed, and plans with soft creamy centers, like free shares, come to the fore.

Of course, CEOs, though better than outsiders at predicting their company's near-term future, are far from perfect.

But they can take advantage of knowing what "the herd" (i.e., other companies) are doing. Companies constantly survey one another, so if one type of long-term incentive looks to be gaining in usage, it isn't long before other companies jump on board, too.

Equilar's report, not surprisingly, shows that the number of shares comprising option and free share grants has risen sharply. That is simply an effect of lower stock prices.

But its report also discloses that the grant date fair values of options and free shares have fallen between the first half of 2008 and the first half of 2009 – 19 percent in the case of options and 22 percent in the case of free share awards.

Both of these reports may be found by clicking on the below link;

http://www.equilar.com/Executive_Compensation_Newsletter.php

2009 marks Graef Crystal's 50th anniversary in the executive compensation field. He has been a director of compensation for General Dynamics and Pfizer, worked as a consultant for Booz, Allen & Hamilton, served as worldwide practice director at Towers Perrin for 18 years, was a professor at the University of California at Berkeley's Haas School of Business for 10 years and

a syndicated columnist for Bloomberg News for almost nine years. He has written six books and more than 1,600 articles on executive pay.