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The Crystal Report on Executive Compensation

RICHARD FULD – TWO WORDS MEANING TOTAL FAILURE

by Graef Crystal

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Seemingly almost single-handedly, Richard Fuld, the chief executive officer of Lehman Brothers Holdings Inc., has destroyed a company that managed to last 158 years.

In the process, he also destroyed the bulk of his own fortune.

According to a filing made on March 5, 2008, Mr. Fuld was the owner (as of Jan. 31, 2008) of 10,851,890 shares of Lehman stock, including both vested and unvested restricted stock units.. At its all-time high close price of $85.80 on Feb. 2, 2007, those shares would have been worth $942 million.

At the close price of $0.215 on Sept. 19, his shares are now worth $2.3 million. His loss, therefore, has been $931 million.

But that's not all Mr. Fuld has lost. His 2.5 million unexercised option shares are worthless. They have strike prices ranging from $35.70 to $63.83. Had they been exercised on Feb. 2, 2007, they would have brought gains of $99 million.

Compared to what might have been on Feb. 2, 2007, Mr. Fuld personally lost approximately $1 billion.

Oh, and that figure doesn't include some $16 million lump-sum value in a non-qualified supplemental executive retirement plan. He will probably have to say "bye, bye" to that amount, too.

But to paraphrase the famous song from "Evita", "Don't Cry for Me, Fuldatina". For Dick Fuld received enormous rewards before his company collapsed.

From the fiscal year ended Nov. 30, 1994 (the company went public on May 2, 1994) through the fiscal year ended Nov. 2007, here is what Mr. Fuld carted away:

- Aggregate base salaries of $10.5 million.

- Aggregate cash bonuses of $69.1 million.

- Aggregate restricted stock awards of $108 million at the time of grant (but this figure excludes $41 million of additional free shares granted to him on Dec. 7, 2007 for his performance during FY2007.)

- Aggregate stock option gains of $363 million.

- Aggregate payouts from a third long-term incentive plan of $21 million.

Counting all of the above, including the free share award made on Dec. 7, 2007 and some $560,000 of miscellaneous compensation, the grand total pay tab for the 14-year period comes to $614 million, or $44 million a year.

During this span of time, Mr. Fuld was granted about 6-7 million free shares (a rough, but, I think, not uneducated, guess, given that Lehman did not disclose grant dates in its proxy statements for many years), and he exercised stock options covering another 13 million shares.

Looking at the progression of his actual shareholdings over time, it is apparent that though he may have held on to some of those 19-20 million shares, or their after-tax equivalent, he seems to have sold the great bulk of them. He may have lost big in this last year, but being an investment banker, it's hard to believe he did not diversify himself in earlier years by investing much of his after-tax free share proceeds and option proceeds in safer investments, not to mention a goodly portion of his huge cash bonuses.

So there would appear to be no need to book Carnegie Hall for a benefit concert for poor old Dick Fuld. Besides, it's hard to figure who would attend, anyway.

So what did shareholders get for that $614 million ride?

Well, until nearly the end, they did pretty well.

I first looked at his performance in narrowing time windows. The first time window began on May 2, 1994, when Lehman went public, and ended on Nov. 30, 2007. The second began on Nov. 30, 2005 and ended Nov. 30, 2007. Thereafter, each succeeding time window began one year later, and all ended on Nov. 30, 2007. The last of the 13 time windows was the single-year ended Nov. 30, 2007.

Here are the results:

TOTAL RETURN PERFORMANCE IN NARROWING TIME WINDOWS

FROM	TO	LEHMAN AMNUAL TOTAL RETURN	S&P 500 ANNUAL TOTAL RETURN	EXCESS RETURN
5/2/1994	11/30/2007	21.5%	11.1%	10.4%
11/30/1995	11/30/2007	23.0%	9.5%	13.4%
11/30/1996	11/30/2007	22.4%	8.0%	14.4%
11/30/1997	11/30/2007	18.1%	6.2%	12.0%
11/30/1998	11/30/2007	20.4%	4.4%	16.0%
11/30/1999	11/30/2007	16.8%	2.5%	14.3%
11/30/2000	11/30/2007	15.0%	3.5%	11.5%
11/30/2001	11/30/2007	12.1%	6.3%	5.7%
11/30/2002	11/30/2007	16.2%	11.6%	4.6%
11/30/2003	11/30/2007	15.7%	10.8%	4.9%
11/30/2004	11/30/2007	15.2%	10.1%	5.2%
11/30/2005	11/30/2007	0.5%	10.9%	-10.4%
11/30/2006	11/30/2007	-14.2%	7.7%	-22.0%

During those 13 narrowing time windows of performance, Lehman beat the Standard & Poor's 500 Index in 11 time windows – indeed in every time window, except the two narrowest ones, i.e., the two-year window ended Nov. 30, 2007 and the single-year window also ended Nov. 30, 2007.

I also looked at Lehman's performance in 13 single-year time windows of performance:

TOTAL RETURN PERFORMANCE IN SINGLE TIME WINDOWS

		LEHMAN AMNUAL TOTAL RETURN	S&P 500 ANNUAL TOTAL RETURN	EXCESS RETURN
11/30/1994	11/30/1995	53.6%	37.0%	16.6%
11/30/1995	11/30/1996	29.7%	27.8%	1.9%
11/30/1996	11/30/1997	74.7%	28.5%	46.2%
11/30/1997	11/30/1998	-0.6%	23.7%	-24.2%
11/30/1998	11/30/1999	53.7%	20.9%	32.8%
11/30/1999	11/30/2000	30.3%	-4.2%	34.5%
11/30/2000	11/30/2001	34.0%	-12.2%	46.2%
11/30/2001	11/30/2002	-6.6%	-16.5%	9.9%
11/30/2002	11/30/2003	18.5%	15.1%	3.4%
11/30/2003	11/30/2004	16.9%	12.8%	4.1%
11/30/2004	11/30/2005	51.6%	8.4%	43.1%
11/30/2005	11/30/2006	17.7%	14.2%	3.5%
11/30/2006	11/30/2007	-14.2%	7.7%	-22.0%

Once again, Lehman did quite well, beating the S&P 500 in 11 of the single-year time windows. It fell behind the S&P 500 for the single years ended Nov. 30, 1998 and Nov. 30, 2007.

But of course all of the above time windows ended on Nov. 30, 2007, i.e., before the Lehman plane hurtled into the ground.

Investment bankers earn millions in fees for doing so-called "Due Diligence". But where was the due diligence at Lehman as it invested enormously in shaky securities?

I suppose you could say that the system worked, that for his failure, Dick Fuld paid an enormous price.

But to my way of thinking, it didn't work as well as it should have, because before that enormous price was paid, Mr. Fuld carted away hundreds of millions, scores of which he would not have earned had someone at Lehman done due diligence and avoided those doggy investments.

Certain of the compensation data for this article were obtained from Equilar, Inc., a leading provider of executive pay data (www.equilar.com) .

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. In the Spring of 2009, he will be teaching a course in executive compensation at the University of California at Berkeley's Boalt School of Law.