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*The Crystal Report on Executive Compensation*



## **Exporting High Pay to America**

**by Graef Crystal**

**June 1, 2009**

Time was when one of America's leading exports to Britain was fancy new executive pay plans and extremely high executive pay. But if what is now being proposed for Sir Martin Sorrell is any guide, the exports will shortly be going from East to West.

Sir Martin is the CEO of WPP plc, a London-based advertising giant.

The 64-year old Sir Martin has a more than passing familiarity with U.S. ways and U.S. pay levels. After graduating from the University of Cambridge, he completed an M.B.A. at the Harvard Business School.

In more recent years, his company has swallowed up some of the biggest names in U.S. advertising, including J.Walter Thompson, The Ogilvy Group, Young & Rubicam and Grey Global.

WPP has now before its shareholders a new long-term incentive plan, with the imaginative name of Renewed Leadership Equity Acquisition Plan or Renewed "LEAP". (You should expect nothing less from an advertising company!)

The new plan has been titled "Renewed", because similar plans were implemented in every year since 2004. The earliest plan rewarded for performance over a four-year period. The more recent ones, including the latest, reward performance over a five-year period.

Some descriptive material on this plan was included in the company's Form 20-F, filed with the U.S. Securities and Exchange Commission on May 12.

## **The Plan**

In architecture, the Renewed LEAP permits the executive to put up shares he already owns, up to a pre-established limit. Then, depending on how WPP's total shareholder return over the performance period compares to that of eight other worldwide advertising companies, the executive can receive as many as five free shares for every share he has put up...down to no shares.

According to articles published in *The Financial Times* and *The London Times*, Sir Martin is eligible to put up as much as \$19 million of shares he already owns.

If WPP's total return during the five-year performance period ranks it either #1 or #2 among the nine companies (including WPP itself), Sir Martin would receive five free shares for every share he pledged. The number of free shares to be paid for lesser levels of relative shareholder return are: 4 shares (for Position #3); 3 shares (for Position #4); 1.5 shares (for Position #5—the group median); and no shares (for Position #6 through Position #9, i.e., below-median performance).

The two British papers have trumpeted that if Sir Martin puts up \$19 million of his own shares and rings the bell vis a vis his comparator group, he would end up getting \$95 million of free shares in return.

This is true, but it assumes both that Sir Martin puts up the maximum in shares and that WPP's share price remains constant throughout the five-year period. As to a constant share price, that is the one scenario that is highly unlikely to happen.

## **WPP Performance**

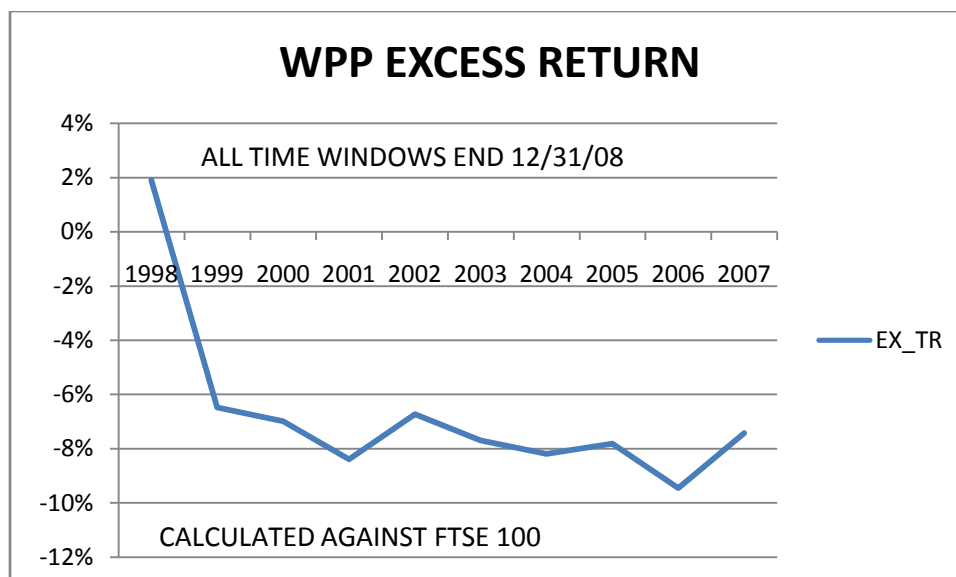
A question here is: How is WPP as a performer?

I have neither the time nor the energy to perform a detailed analysis on the eight comparators, given that we are dealing here with British Pounds, U.S. dollars, French Francs and Japanese Yen.

But I have looked into WPP's total return performance over 10 years. Here, I constructed 10 time windows, the longest of which covered the 10 years ended Dec. 31, 2008. The second window covered the nine years ended Dec. 31, 2008 – and so forth until the 10<sup>th</sup> window covered only 2008.

For each time window, I calculated WPP's "excess return", i.e., the amount by which the company's return exceeded (or was under) the return on the FTSE 100 (of which WPP is a member).

These excess returns may be seen on the following chart:



It is only in the widest time window that WPP managed to beat the FTSE 100. It lagged the index in the other nine time windows, with excess returns in a close range – from negative 6 percent to negative 9 percent.

If WPP's performance against the FTSE 100 is any indication of what its performance is likely to be against the eight major advertising companies – and it may or not be-- Sir Martin would not appear to be in any danger of adding to his already sizeable fortune.

Still, that \$95 million payout touted by the British newspapers is a eye-popping number. And this is especially the case since, in the past, a new LEAP plan has started every year. Or, to put it another way, each year contributes to five different performance cycles. From that perspective, then, the \$95 million mentioned in the British press could be seen as the rewards for just one year, but coming five years out.

Relative shareholder return plans are becoming quite common in the U.S., but I have yet to see one with that large a potential payout.

Still, Sir Martin spends a not insubstantial amount of time in the U.S. And over late-night drinks, he might just start talking about his new LEAP plan.

And then we're in for it! WPP will be a favorite addition to any American pay comparator group, whether or not the company is in advertising or merely buys some of it.

2009 marks Graef Crystal's 50<sup>th</sup> 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.