



***Compensation & Reward
Management
MBHR6002***

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Index-Session 39

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Session Objectives

***Compensation of Special
Groups***

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Report: Workers Want Vastly Different Rewards

- More than half of those surveyed agree that quality of Co's recognition efforts affects how they perform their job, w/ only 10% completely satisfied w/ their Co's rewards program
 - 70% receive verbal praise, but only 49% want it
 - 40% who want written praise receive it
 - 30% who want to be singled out thru special event are recognized that way
 - 29% who want cash bonus as recognition for their work receive it
 - 27% who want incentives such as award merchandise, gift cards, or trips receive them
 - 27% who want award such as trophy or plaque receive it
- “This study shows CEO are motivated in vastly different ways and Cos still have a long way to go to ensure their CEO feel valued”
 - 64% said their Co should offer greater choice of workplace rewards when it comes to recognizing efforts

Report: Workers Want Vastly Different Rewards

- Reducing Employee turnover and becoming an Employee of choice are two of most pressing concerns Cos have today
- Compared to Ees unsatisfied w/ their Ee recognition program, Ees who are completely satisfied with it are:
 - 11% as likely to be satisfied w/ job
 - 7 % as likely to spend careers w/ Co
 - 7 % as likely to recommend their org to others
 - 6 % as likely to invest \$ in their Company if they could
 - 5 % as likely to feel highly valued at work
- One way to add freshness and enthusiasm is by forming advisory panel of people from different job levels and parts of Co

Issues: Supervisory Pay

- Major *challenge* in paying supervisors
 - *Equity*
- Provide *incentives* to entice non exempt employees to accept challenges of being a supervisor

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Strategies: Supervisory Pay

◎ Pay strategies

- > Key base salaries of supervisors to an amount exceeding highest paid employee
- > Pay supervisors for scheduled overtime

◎ Trend in supervisory compensation

- > Increased variable pay
 - More than half of all companies have a variable pay component for supervisors

Explanations for CEO Compensation

- ◎ Social comparisons
 - > Executive salaries bear a consistent relative relationship to pay of lower-level employees
- ◎ Economic approach
 - > Value of CEO should correspond to some measure of organizational success
- ◎ Agency theory
 - > Incorporates political motivations
 - > CEO compensation should be designed to ensure executives focus on best interests of firm and stockholders

Components of an Executive Compensation Package

- Base salary
- Short-term (annual) incentives or bonuses
- Long-term incentives and capital appreciation plans
- Executive benefits
- Perquisites

Breakdown of Executive Compensation Components

EXHIBIT 14.4 Breakdown of Executive Compensation Components

Compensation Component	1970s	1980s	1990s	Today
Base salary	60%	40%	33%	16%
Benefits	*	15	*	*
Perks	*	5	*	*
Short-term incentives	25	20	27	16
Long-term incentives	15	20	40	68

*Unreported.

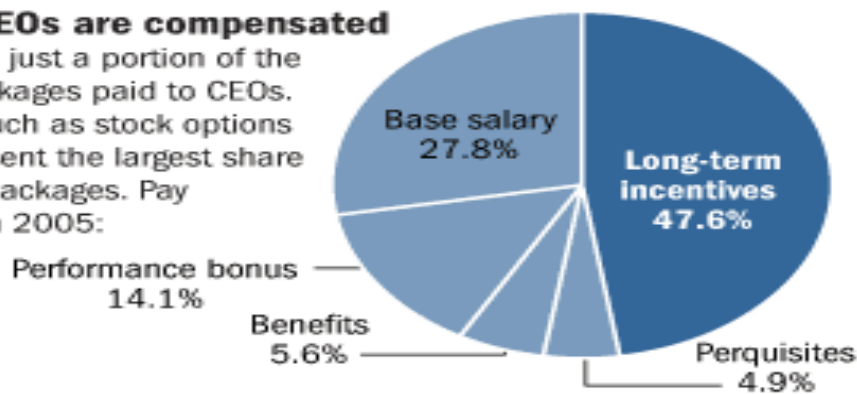
Sources: IOMA, *Pay for Performance Report*, May 1998, p. 11, and June 2003, p. 12; various issues of the *Wall Street Journal*; Data from Towers, Perrin, Wyatt Co.; M. Bishko, "Compensating Your Overseas Executive, Part 1: Strategies for the 1990s," *Compensation and Benefits Review*, May–June 1990, pp. 22–30.

Executive Compensation

- ◎ Two factors contributed to pay scales that now have CEOs earning more than 300x pay of average American worker
 - > Advent of giant stock option grants, form of compensation made more attractive by 1993 change to tax law that maintained corporate tax deductions for executive pay over \$1m if pay was tied to performance
 - > Widespread practice of linking pay to levels at companies of similar size
 - Has effect to raise average that everyone will use as baseline

How the nation's CEOs are compensated

Base salaries constitute just a portion of the total compensation packages paid to CEOs. Long-term incentives, such as stock options and stock grants, represent the largest share of total compensation packages. Pay components for CEOs in 2005:



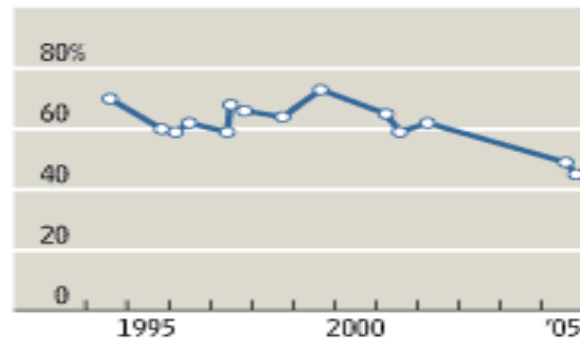
Pay vs. the market

Cumulative percentage change in CEO compensation, employee compensation and the S&P 500, annual data¹



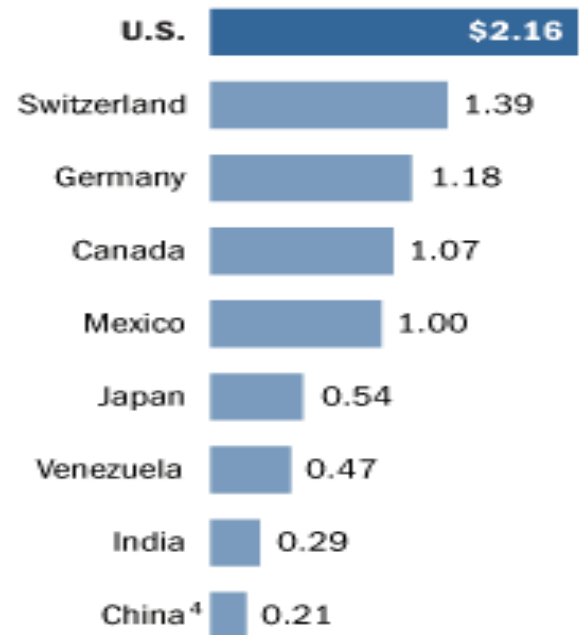
Public opinion

Percentage of survey respondents saying they hold a favorable opinion of business corporations²



International comparisons

Average total CEO compensation³ in 2005 for companies with about \$500 million in world-wide annual sales, in millions of U.S. dollars (selected countries)



¹CEO data are controlled for performance, inflation, firm's size and firm-specific attributes; employee total compensation is based on the Labor Department's Employer Cost Index ²Telephone survey of 1,003 adults; margin of error +/-3.5 percentage points ³Data are for locally headquartered companies; totals comprise basic compensation, performance bonuses, company contributions, perquisites and long-term incentives ⁴Excludes Hong Kong
Sources: Towers Perrin; Pew Research Center for People and the Press; Oxford Review of Economic Policy; WSJ Market Data Group; Bureau of Labor Statistics

Executive Compensation (Wall Street Journal study)

- ◎ Median total compensation, 2009, \$6.95m, down 0.9% from 2008 (includes salary, bonuses, value of restricted stock at time of grant, gains from options exercises, other long-term incentives)
 - > Had declined 3.4% from 2007 to 2008
 - > Long-term incentive awards declined 4.6% to median \$5m
 - > Median salaries and bonuses up 3.2%, to \$2.64m
- ◎ Companies run by best-paid CEOs generally deliver better-than-average shareholder returns
 - > But not uniformly true

Competitive Benchmarking

- Most companies historically have benchmarked executive compensation
 - Practice tends to inflate compensation
 - If all orgs seek to pay median or above, median will inevitably rise (see Business Week Commentary, “The Artificial Sweetener in CEO Pay” on website)
 - Practice tends to disregard relationship between pay and company performance
 - Some movement to tie pay to performance of peer group
 - » Source: Wall Street Journal, 4/12/04
- In 1960, CEOs earned average of 2x as much as president of U.S.; today, 30x

International Comparisons

- Median salary plus cash bonus for U.S. CEOs in office at least one year was \$2.3m in 2004, according to analysis by Boardex of London
 - U.K.: \$1.2m
 - France: \$857k
 - Sweden: \$386k
- Pay gap between U.S. and Asian CEOs even larger, according to analysis by Mercer
 - Japan: \$318k
 - Hong Kong: \$302k
 - Singapore: \$263k
 - India: \$88k
- Average CEO's salary in U.S. is 475x average ee's salary, cf. 11x in Japan, 15x in France, 20x in Canada, 22x in U.K.

Putting a Ceiling on Pay

- Growing number of shareholder activists pushing Cos to establish maximum ratios between what their executives earn and what their average- or lowest-paid workers earn
- Average CEO in U.S. earned 282x salary of average worker in 2002, cf. 42x in 1982
 - Whole Foods Market (leading organic food retailer) limits any executive's pay to no more than 14x pay of average worker (current cap is \$409k)
 - Ben & Jerry's had capped pay at 7x pay of lowest worker, but dropped policy in 1994
 - Herman Miller had capped pay at 20x, but dropped policy in 1996
- Critics argue that such practices that exclude stock options are of little value

Description of Long-Term Incentives for Executives

- ⦿ Incentive stock options
- ⦿ Non-qualified stock options
- ⦿ Phantom stock plans
- ⦿ Stock appreciation rights
- ⦿ Restricted stock plans
- ⦿ Performance share/unit plans

References

Source: Wall Street Journal, 4/1/10, based on analysis of 200 major U.S. corporations by Hay Group

Source: Wall Street Journal, 4/12/04

Source: Wall Street Journal, 1/21/06

Source: Wall Street Journal, 7/19/05, 1/21/06

Source: New York Times, 4/5/09, based on analysis of 200 large U.S. companies by Equilar

Source: Wall Street Journal, 7/19/05

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In case, you find any difficulty in understanding the concepts of lecture, please feel free to contact.

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Thanks

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