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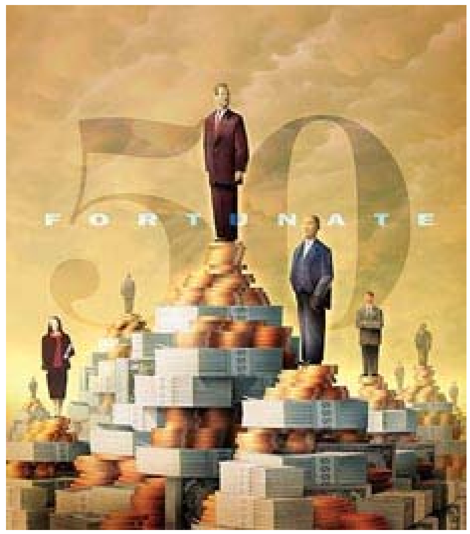
'Fortunate' executives averaged $8.7 million

2005 wasn't the best year for the highest-paid local executives, as their total compensation dropped, but they still took home an average of $8.7 million

Sunday, May 07, 2006

By Len Boselovic, Pittsburgh Post-Gazette

tr> It was a tough year for the Fortunate 50. The 50 highest-paid executives in the region saw their total compensation slip 16 percent -- to an average of $8.7 million. A 33 percent decline in gains they realized from exercising stock options was the main culprit.



The executives -- 49 men and one woman -- also saw their average salary fall 2 percent, their bonuses decline 7 percent on average and the value of their restricted stock awards drop 37 percent.

The only category that increased was "other" compensation, which includes long-term incentives, payments to deferred compensation plans, retirement plan contributions and the perks that come with the job. Average compensation in this catch-all category nearly tripled to $1.8 million.

Equitable Resources Chairman, President and Chief Executive Officer Murry S. Gerber topped the Fortunate 50, thanks to $34.3 million in stock option gains. Mr. Gerber's 2005 compensation of $54.9 million was 20 percent higher than the 2004 Fortunate 50 leader, former U.S. Steel chairman Thomas J. Usher, who collected $45.7 million.

Mr. Gerber's "other" compensation included $19.8 million in long-term incentive payments, which accounted for more than a fifth of the $90.4 million in other compensation the 50 executives received.

Despite the drop-off in the average compensation on the latest Fortunate 50 list, it took just as much to qualify as it did in 2004.

The cut-off was $3.7 million both years, which is

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what Mellon Financial Senior Vice Chairman Steven G. Elliott pulled in last year to round out the list.

Nationally, executive salaries remained flat last year at $975,000, according to a survey of 350 companies by human resources consulting firm Mercer, while the median CEO's bonus rose 8 percent to $1.4 million. Combined, Mercer says, the median CEO salary and bonus rose 7 percent last year to $2.4 million.

For the Fortunate 50, the median CEO salary and bonus was $1.6 million last year, while the average fell 5 percent to $1.8 million. By comparison, the average wage for a worker in the Pittsburgh metropolitan area was about $35,000, according to the U.S. Department of Labor.

At that rate, it would take the average worker 19 years to earn the average annual salary of a Fortunate 50 member and 249 years to earn the average total compensation of a Fortunate 50 member.

As this year's list shows, it's still for the most part a man's world when it comes to reeling in the big bucks.

The only woman to make the list was Susan P. McGalla, president of American Eagle Outfitters. Ms. McGalla, who a year ago was one of three females to make the 2004 Fortunate 50 list, last year collected $5.4 million, good enough to finish 31st.

Gone from the Fortunate 50 are U.S. Steel Chief Financial Officer Gretchen R. Haggerty, whose compensation of $3.2 million put her in 55th place. Also departed is former American Eagle Outfitters CFO Laura A. Weil, who, until last week, had moved onto greener pastures as chief operating officer of Ann Taylor Stores. The New York specialty retailer announced Thursday Ms. Weil resigned to pursue other interests.

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The Post-Gazette Fortunate 50 is based on the highest-paid executives at more than 60 publicly held companies either based in the region or with significant operations here.

Compensation is for the company's most recently completed fiscal year. It includes salary, bonus, long-term incentive payments, restricted stock awards, gains realized from exercising stock options and perquisites such as country club dues, health insurance, retirement plan contributions, financial counseling and personal use of company-owned jets. Restricted stock is valued as of the day it was awarded.

The totals do not include the projected value of unexercised stock options awarded in the most recent fiscal year.

-- Len Boselovic

For the second consecutive year, no African-Americans were among the Fortunate 50.

One slot below Ms. McGalla is former Mellon Financial Chairman Martin G. McGuinn, who received $5.4 million last year. That is dwarfed by the estimated $46.3 million Mr. McGuinn will receive as the result of leaving the company with two years left on his contract. His payout will be even greater if his successor, former Wachovia executive Robert Kelly, is able to energize Mellon shares. That would make the options and restricted shares Mr. McGuinn holds more valuable.

Over the five years ended Dec. 31, Mellon shareholders have lost 5 percent annually on their investment.

Despite mounting pressure to more closely align executive compensation with a company's long-term performance, examples of excess pay for poor performance remain plentiful, nationally as well as in the region.

The Corporate Library recently highlighted 11 large companies that paid their CEOs in excess of $15 million over the last two years even though stockholders of these companies lost money over the last five years. Among the companies on the corporate watchdog's list: Verizon Communications, AT&T, Home Depot and Lucent Technologies.

Locally, the Fortunate 50 includes three executives from companies where shareholders have suffered double-digit annual losses over the last five years.

They are Ariba CEO Robert M. Calderoni, Ariba executive vice president Kevin S. Costello and Black Box CEO Fred C. Young. Ariba shares have generated annualized returns of negative 63 percent over the company's five last fiscal years, while Black Box shares fell an average of 11 percent annually.

Conversely, the Fortunate 50 doesn't include any executives from the five regional companies that have generated the biggest annualized gains for shareholders over the past five years.

Ansys President and CEO James E. Cashman III, whose software concern has produced 50 percent annualized gains over the period, finished 51st, $89,000 out of the running. MSA Chairman and CEO John T. Ryan III finished 53rd, with compensation of $3.3 million. Despite a 28 percent slide last year, the O'Hara safety products company has generated annualized returns of 38 percent over the last five years.

Although some observers believe executive pay increases have moderated, there's still plenty of critics. Their targets include companies that have amply awarded shareholders.

Take UnitedHealth Group, a Minnetonka, Minn., insurer headed by Chairman and CEO William W. McGuire. By the company's math, an investor who purchased $100 worth of UnitedHealth stock at the beginning of 2000 and reinvested the dividends had shares valued at $938 at the end of last year.

Critics aren't griping about the $10.7 million Mr. McGuire was paid last year. What they are outraged at is the $1.6 billion in gains he can realize by exercising stock options that were part of his pay package. He's holding another $174.9 million in options that can't currently be exercised. The Securities and Exchange Commission is investigating how some of the options were granted.

No matter what the outcome of the probe, it raises questions about how carefully compensation committees -- board members who develop pay plans with the advice of consultants -- as well as the entire board, weigh the possible outcomes of their decisions.

"Very few compensation committees would say $1.6 billion is OK," says Stephen Mader, vice chairman of Christian & Timbers, which advises companies on executive pay. "He [Mr. McGuire] is representative of a compensation committee that did not model out the possibilities."

Says consultant Ralph Ward, publisher of Boardroom Insider: "Boards and their compensation committees have a real myopia about the cumulative effect of their individual pay choices."

Perception also may have something to do with executive pay. Studies have shown that CEOs who are perceived to be charismatic get higher compensation than those who are not. But Bradley R. Angle, who teaches business administration at the University of Pittsburgh, says a study he and three other professors conducted concluded a CEO's perceived charisma has no bearing on a company's future performance.

"It would suggest that if CEOs are getting paid more for charisma, that's not justified," he says.

Past criticism over large options payouts has prompted many companies to move away from stock options and toward restricted stock.

"I think it's a good idea," says Tim Pollock, who teaches management Penn State University.

Options provide the right to purchase stock, typically over the next 10 years, at the price the stock was trading at when the option was granted. If the stock price doesn't go up before the option expires, the executive hasn't lost anything.

Here's the rationale for using options as motivators. An executive gets options to purchase 1,000 shares for $10 each. Because of his hard work, the stock rises to $20 over the next two years, giving him a $10,000 gain (the $10 increase in stock price times 1,000 shares).

The bull market of the late 1990s and the bubble that followed made clear what critics knew all along: investor hysteria, fraudulent accounting, and other factors often have more of an impact on stock prices than the actions of executives. Moreover, once companies were ordered to start expensing options directly on their income statements, the attraction of options faded.

So more companies are switching to restricted stock, shares given to executives that vest over a period of several years. Unlike options, where there was no loss, the value of restricted shares can decline. Mr. Pollock believes executives will behave better knowing there's the potential for a loss.

One problem critics have with restricted stock is that executives typically get the shares no matter how well their company performs. That's why it's facetiously referred to as "pay for pulse." Where companies do impose a requirement, restricted shares "vaporize if you don't hit the objective," Mr. Mader says.

Because of continuing demands to more closely link executive pay with performance, more companies may start linking restricted stock grants to performance goals, he adds.

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Back