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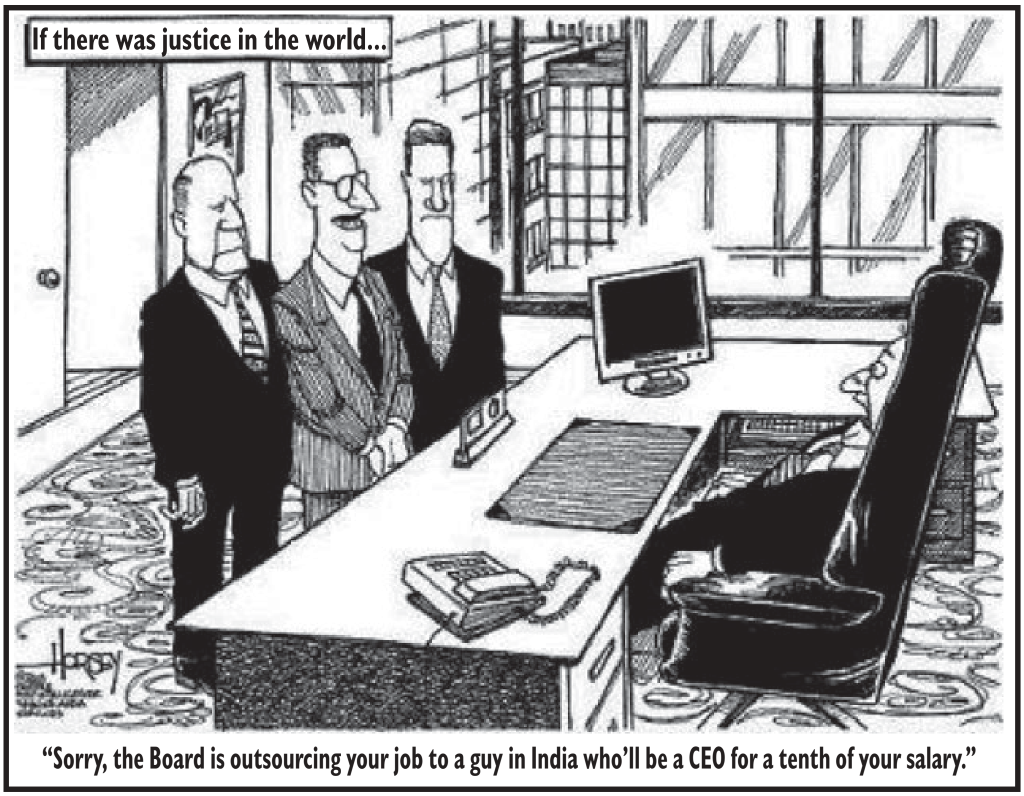
Executive Excess 2004

Campaign Contributions, Outsourcing, Unexpensed Stock Options and Rising CEO Pay

11th Annual CEO Compensation Survey



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IPS UNITED FOR A FAIR ECONOMY

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The Institute for Policy Studies is an independent center for progressive research and education founded in Washington, DC in 1963. IPS scholar-activists are dedicated to providing politicians, journalists, academics and activists with exciting policy ideas that can make real change possible.

United for a Fair Economy is a national, independent, nonpartisan, 501(c)(3) non-profit organization. UFE raises awareness that concentrated wealth and power undermine the economy, corrupt democracy, deepen the racial divide, and tear communities apart. We support and help build social movements for greater equality.

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Key Findings

Outsourcing service jobs to other countries pays off for CEOs.

Top executives at the 50 largest outsourcers of service jobs made an average of $10.4 million in 2003, 46 percent more than they as a group received the previous year and 28 percent more than the average large-company CEO. These 50 CEOs seem to be personally benefiting from a trend that has already cost hundreds of thousands of U.S. jobs and is projected to cost millions more over the next decade.

Outsourcing to developing countries has widened the chasm between U.S. CEOs and their workers. India has claimed the greatest number of outsourced service jobs, particularly for call centers and software programming work. The average pay of the leading outsourcing CEOs is 3,300 times the pay of an average Indian call center employee and 1,300 times more than the pay of an average Indian computer programmer.

Despite a growing public outcry, Congress has not done anything to stem the tide of jobs lost to outsourcing, and the Bush Administration has called the trend a “good thing.” This inaction may be connected to the political contributions of the top 50 outsourcing companies, who have so far given a combined $10.4 million in Political Action Committee (PAC) contributions to federal candidates during the 2004 election cycle. The higher-than-average CEO pay at the top 50 outsourcing companies is just one example of “political profits” – rewards gained by working the system of political contributions and cronyism rather than by building a better mousetrap.

CEOs heavily involved in political contributions have higher-than-average pay.

Taking an active role in political fundraising seems to boost CEOs’ fortunes. Currently, there are 38 CEOs who have each personally raised at least $100,000 in individual contributions from friends and business associates for one of the two major presidential candidates. These executives-slash-fundraisers averaged $15.2 million in total pay in 2003, 88 percent more than the average large-company CEO.

Sponsoring a convention doesn’t hurt, either. CEOs of the 69 companies that sponsored this summer’s political conventions averaged $9.2 million in total compensation in 2003, representing a hefty 52 percent raise over their average pay in 2002. By contrast, the average large-company CEO surveyed by *Business Week* received a raise of only 9 percent in 2003.

There is also correlation between corporate campaign contributions and high CEO pay. The top 41 corporate campaign contributors of the 2003-04 election cycle paid their CEOs an average of $17.4 million in 2003, more than twice as much as the salary received by the the average large-company CEO.

Corporate lobbyists are blocking common-sense treatment of stock options.

Under intense pressure from corporate lobbyists, members of Congress are attempting to block new rules that would require corporations to report all options grants as expenses in their financial statements. Meanwhile, corporations have claimed an estimated $3.9 billion in tax deductions related to stock options exercised by 350 leading CEOs since 1997 (the year accounting regulators first tried to require expensing). Similarly, the Securities and Exchange Commission's efforts to give shareholders greater access to nominating corporate directors has been ham-strung by corporate bullying, despite unprecedented public support.

The CEO - worker pay gap is growing.

After two years of narrowing, the gap between CEO pay and worker pay is growing again. With executive pay up 9 percent in 2003, the ratio between CEO pay and worker pay reached 301 to 1, up from 282 to 1 in 2002. If the minimum wage had increased as quickly as CEO pay has since 1990, it would today be $15.76 per hour, rather than the current $5.15 per hour.

CEOs make much more than executives in a far riskier profession: the military.

The argument that exorbitant CEO pay is justified by the executives' high level of risk and responsibility doesn't hold much water when one considers the relative pittance earned by members of the U.S. military in Iraq. For example, average CEO pay ($8.1 million, according to *Business Week*) is 56 times more than the pay for a U.S. Army general with 20 years experience ($144,932.40) and 634 times more than the pay for a starting U.S. soldier ($12,776.40).

The estimated annual compensation of the 919 soldiers killed in Iraq as of early August 2004 totaled $38 million combined. That's less than the combined pay of just *five* average American CEOs. And it's less than the amount received by each of a dozen single U.S. executives covered in the annual *Business Week* survey. Among the top 12: George David, CEO of No. 6 defense contractor United Technologies. In 2003, as his company supplied Black Hawk helicopters to the Pentagon, David made $70 million.

Investors continue to awaken to the problem of bloated CEO pay.

For the second year in a row, shareholder proposals on executive pay dominated corporate annual meetings, with more than 300 proposals filed on subjects including stock options, gold-plated executive retirement plans, and reports on wage gaps between CEOs and average workers. News of New York Stock Exchange CEO Richard Grasso's $140 million pay package ignited public anger and forced his resignation. More than 45 percent of Disney shareholders supported a no-confidence vote against CEO Michael Eisner, who remains one of America's all-time highest-paid executives despite Disney's tepid performance under his leadership. These developments are signs of growing support for actions to rein in runaway CEO pay.

Introduction

A climate of anxiety has enveloped the country over the past year. Workers are increasingly anxious about their job security and the rising cost of basics like health insurance, housing, college, and gasoline. Many military families are facing particularly difficult financial strains at home as they grapple with the dire risks to their loved ones far away. And through it all, too many corporate executives remain removed from such cares and worries. As they demand cost-cutting on the factory floor and in the back offices, costs in their own executive suites continue to soar. And as the Iraq conflict rages on, many corporate leaders are personally profiting from the suffering through war-related contracts.

We are also struck in this Presidential election year by the continued heavy corporate involvement in funding campaigns and the apparent inability of the political system to address issues like job outsourcing and the non-expensing of stock options. For many companies, "political profits" play as important a role in business success as investments in new products or enhanced customer service. Profits enhanced by investments in the political process seem to have a greater chance of finding their way into the pockets of CEOs.

At the same time, we have seen some positive signs over the past year that corporate leaders are not untouchable. Deepening public anger over excessive executive pay has prompted shareholders, workers, and even some corporate and Wall Street leaders to demand change. For example:

- New York Stock Exchange CEO Richard Grasso was forced to resign following disclosure of his $140 million pay package. The Exchange has filed suit against Grasso, seeking a return of some of his excessive pay.

- Long-time pay giant Michael Eisner, CEO of the Walt Disney Company, received a vote of "no confidence" from 45 percent of Disney shareholders. The rebuke forced Eisner to give up his role as Disney's chairman, although he remains CEO.

- For the second year in a row, shareholder proposals on executive compensation dominated corporate annual meetings, with more than 300 resolutions filed by concerned shareholders.

- Whole Foods Market set a positive example by limiting CEO John Mackey's salary to no more than 14 times the pay of the average frontline employee. In addition, all employees can qualify for stock options, and the company says that 94 percent of options go to nonexecutive staff.

Despite these developments, however, it is clear that executive pay is still out of control. Even in the post-Enron world, corporate boards are far too clubby and corporate lobbyists continue to hold far too much influence over our political system. Greater public pressure and political action will be needed to narrow the gap between executives and the legions of employees who also play an important role in creating shareholder value.

The evidence suggests that CEOs who outsource service jobs are rewarded with higher pay. Should we care?

1. Rewarding CEOs for Outsourcing Jobs

Have the CEOs who outsource thousands of service jobs to countries like India been rewarded with higher pay? The evidence detailed below suggests that they have. But should we care?

Bush Administration officials and corporate lobbyists have worked hard to convince American workers that they will benefit from the outsourcing of service sector jobs to low-wage countries. President Bush's top economic advisor, N. Gregory Mankiw, famously told members of Congress that outsourcing was a "good thing" and Treasury Secretary John Snow has expressed similar views. A new Big Business alliance, the Economic Growth and American Jobs Coalition, has launched a major PR campaign aimed at blocking bills pending in nearly 40 states that would restrict outsourcing of government contracts.

Chart 1.1: Average CEO Pay Increase from 2002 to 2003

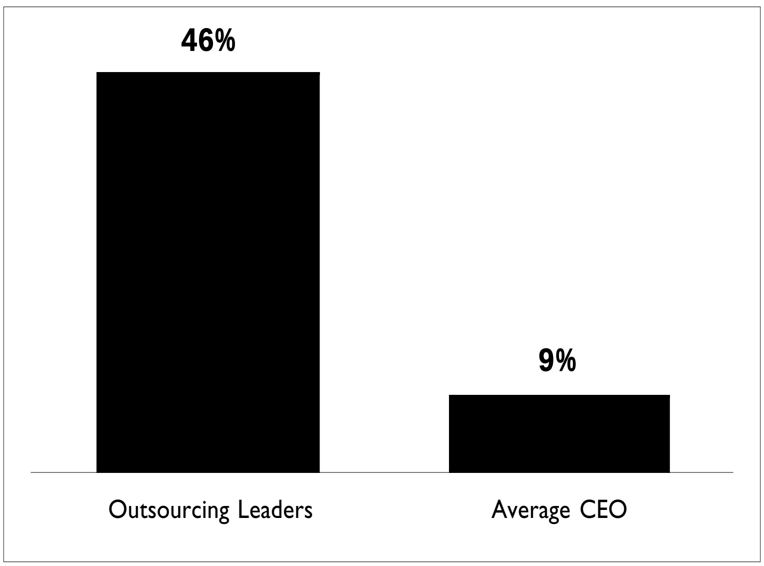
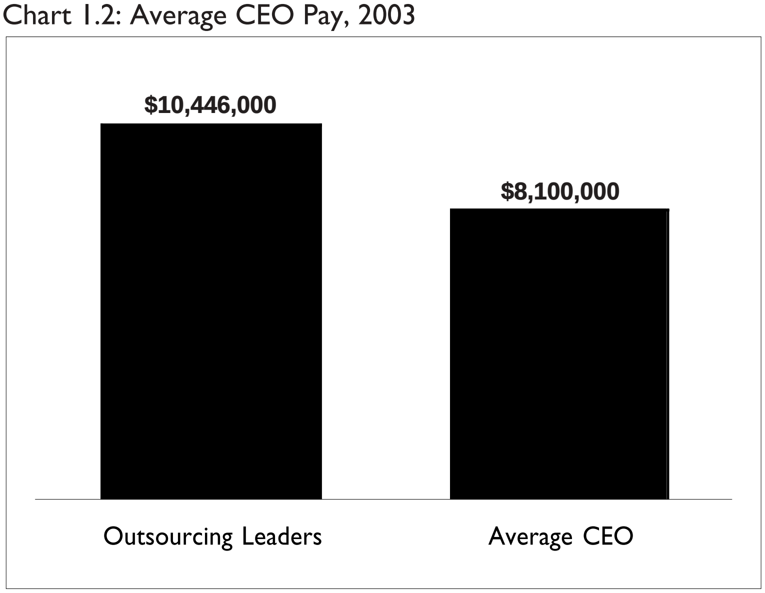


Chart 1.2: Average CEO Pay, 2003



Their argument is this: foreign outsourcing boosts efficiency that generates increased profits that will be used to support jobs in the United States.

Outsourcing does indeed increase profits by lowering labor costs. But there is no evidence that this is translating into more and better American jobs. To the contrary. U.S. software-related jobs — which are among those most vulnerable to outsourcing —have been in steady decline, dropping 16 percent between 2001 and 2004.[1]

Firms appear to be channeling their outsourcing profits not into U.S. jobs, but rather into the pockets of chief executives. This study examined 50 leading services outsourcing firms and found that their CEOs received, on average, a 46 percent increase in total compensation in 2003, compared to only a 9 percent pay raise for the average CEO as measured by *Business Week*. The top outsourcers earned an average of $10.4 million in 2003, up from

Table 1.1: 2003 CEO Pay at the 50 Leading Services-Outsourcing Companies

Company	CEO	CEO Pay (in thousands)	Change from 2002
Accenture	Joe W. Forehand	$ 2,206	+2%
Affiliated Computer Services	Jeff A. Rich	10,242	-25%
Agere Systems	John T. Dickson	1,852	+136%
Agilent Technologies	Edward W. Barnholt	1,922	+108%
American Express	Kenneth I. Chenault	11,546	-37%
AT&T Wireless	John D. Zeglis	4,173	+49%
Avaya Inc.	Donald K. Peterson	2,512	+60%
Bank of America	Kenneth D. Lewis	37,940	+108%
Bank of New York	Thomas A. Renyi	14,598	+148%
BellSouth	F.D. Ackerman	11,094	+107%
Boeing	Phil Condit	3,811	-8%
Capital One Financial	Richard D. Fairbank	61	-37%
Cisco Systems	John T. Chambers	0	+0%
Citigroup	Sanford Weill	54,060	+305%
CNA Financial	Stephen W. Lilienthal	2,887	+35%
Cognizant Technology Solutions	Wijeyaraj (Kumar) Mahadeva	27,000	+79%
Computer Sciences Corp.	Van B.Honeycutt	7,936	+29%
Conseco	William J. Shea	16,595	* +746%
Convergys	James F. Orr	1,968	-81%
Covansys	Martin C. Clague	650	+36%
Dell	Michael S. Dell	3,002	-12%
Delta Airlines	Leo F. Mullin	1,122	-77%
Earthlink	Charles G. Betty	968	+18%
EDS	Michael H. Jordan	3,728	* +149%
eFunds	Paul F. Walsh	826	+9%
FedEx	Frederick W. Smith	2,665	-3%
First Data Corporation	Charles T. Fote	4,377	-89%
Fluor Corporation	Alan L. Boeckmann	4,814	+13%
Ford Motor	William Clay Ford, Jr.	1,677	+662%
General Electric	Jeffrey R. Immelt	11,580	-23%
General Motors	G. R. Wagoner, Jr.	8,432	-30%
Hewlett-Packard	Carly S. Fiorina	3,426	-17%
Honeywell International	David M. Cote	6,487	-80%
IBM	Samuel J. Palmisano	7,730	+13%
Intel	Craig R. Barrett	9,124	-53%
Intuit	Stephen M. Bennett	22,301	+425%
JP Morgan Chase	William B. Harrison, Jr.	16,554	+45%
Keane, Inc.	Brian T. Keane	1,439	+97%
Mattel	Robert A. Eckert	1,884	-84%
MCI	Michael D. Capellas	3,000	+44%
Morgan Stanley	Philip J. Purcell	23,307	-2%
Motorola	C. B. Galvin	6,829	+103%
Oracle	Lawrence J. Ellison	40,589	+103,974%
Quantum	Richard Belluzzo	1,432	* -62%
Sabre Holdings	W.J. Hannigan	2,498	+106%
SBC Communications	Edward E. Whitacre, Jr.	18,308	+117%
Sprint FON Group	Gary D. Forsee	16,446	+650%
Time Warner	Richard D. Parsons	11,874	+907%
Unisys	Lawrence A. Weinbach	2,361	-12%
United Technologies	George David	70,452	+629%
	Total	**522,285**	
	Average	**10,446**	**+46%**
	***Business Week* Average**	**8,100**	**+9%**

* New CEO in 2003.

Sources: WashTech Offshore Tracker, *Business Week,* April 19, 2004, April 21, 2003, and April 15, 2002, and corporate proxy statements filed with the Securities and Exchange Commission. CEO Pay includes salary, bonus, "other annual compensation," restricted stock awards, long-term incentive payouts, and the value of stock options exercised. Percentage change based on the average total compensation for all CEOs for each year.

The profit potential of outsourcing is huge. Fourteen million U.S. service jobs are considered vulnerable to being shipped overseas.

an average of $7.1 million in 2002. The average total compensation of the top outsourcers was more than 28 percent higher than the $8.1 million earned by the average U.S. CEO in 2003. Over the three-year period 2001 to 2003, the 50 top outsourcing CEOs pulled down more than $2.2 billion combined, while offshoring or announcing plans to offshore an estimated 200,000 jobs. (See the next section for details on the top 15 earners among the Outsourcing Leaders.)

Some might assume that the outsourcers made more money than average CEOs because they run larger-than-average companies. In fact, the 50 top outsourcers include firms that range substantially in size. Fifteen are not on the Fortune 100 list of largest U.S. companies, while an additional 11 failed to make the top 500.

A Perverse Reward System

The fact that leading outsourcers make more money than average CEOs is one more reflection of a perverse system that rewards executives for making decisions that may improve their bottom line while hurting workers and communities. The McKinsey & Company consulting firm estimates that outsourcing to low-wage countries can result in cost cuts of 45 to 55 percent (after accounting for higher infrastructure and other costs).[3] Given that an estimated 14 million U.S. service jobs are considered vulnerable to being shipped overseas, the profit potential of outsourcing is huge.[4]

But service outsourcing also comes with tremendous costs for U.S. workers and communities. Although the number of jobs outsourced thus far may appear small relative to the total U.S. workforce, layoffs related to outsourcing have a huge impact on the affected communities. And American workers are justifiably concerned about a trend that is expected to accelerate rapidly in coming years. According to Forrester Research, about 3.4 million service jobs will move offshore by 2015.[5] Perhaps even more significant is the increased power of highly mobile firms to bargain down U.S. service sector wages by threatening to move jobs elsewhere. Once primarily a concern for manufacturing workers, this pressure now also affects service workers, including even highly-skilled software engineers and medical professionals.

About the Outsourcer List

As outsourcing has become a highly sensitive issue with the American public, companies have tended to guard information about their outsourcing activities as if they were state secrets. Forcing overseas service vendors to sign nondisclosure agreements is common. Based on media accounts, the Washington Alliance of Technology Workers (WashTech), an affiliate of the Communications Workers of America, has compiled a database of corporations that have reportedly created or announced plans to create a significant number of service jobs overseas.[2] Given the difficulties of information collection, the database is not comprehensive. However, it does offer the best available picture of the companies that are on the forefront of the outsourcing trend. This study focuses on the 50 companies that WashTech had estimated (as of July 9, 2004) as having the largest number of offshored jobs since 2001 and for which executive compensation data were available. It does not attempt to calculate the exact number of U.S. jobs affected.

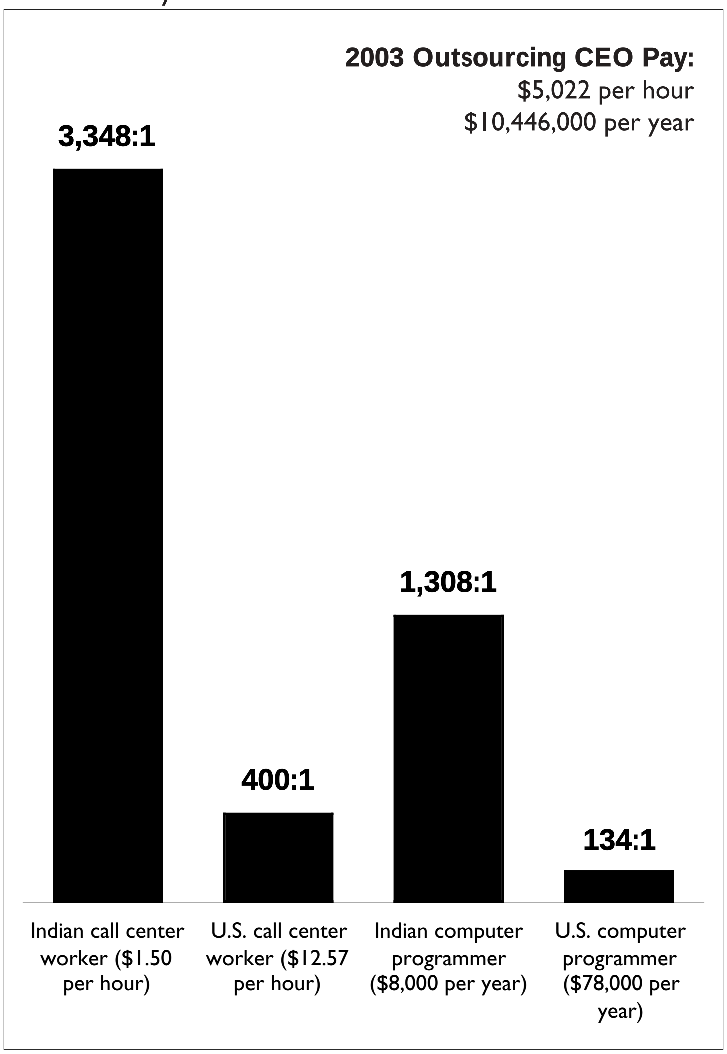
Do Developing Country Workers Share in the Rewards of Outsourcing?

The benefits of outsourcing are also questionable for workers and communities in the developing world. By far the leading developing country destination for U.S. service sector outsourcing is India. U.S. firms account for more than two-thirds of the country's $12.5 billion annual business in international software and business support services. Analysts predict that the market could quadruple by 2008.[6] Given a lack of other economic opportunities, Indian workers are understandably often eager to secure new jobs catering to the U.S. market. However, in a largely unregulated global economy, these workers must face the nagging fear that their jobs could quickly evaporate as soon as firms can find lower costs elsewhere.

There are strong concerns that the outsourcing trend is not a panacea for the developing world.

China, of course, looms on the horizon. It is already the second-biggest developing-country draw for service work, offering rock-bottom wages and an official ban on basic union rights. While it lacks India's English-speaking advantage, this may not be the case forever, as the government is heavily promoting English-language education. Mexico's current competition with China for manufacturing jobs could foreshadow what is in store for service jobs. Although employment in Mexico's border export zone more than doubled after the initiation of the North American Free Trade Agreement in 1994, the country has in recent years lost several hundred thousand of these jobs, partly because of flight to lower-wage China. And in fact, India has also already lost some manufacturing jobs to China.

Chart 1.3: Ratio between Average Pay for Outsourcing CEOs and Pay for Workers in India and the U.S.[7]



While a relative handful of Indian workers are undoubtedly benefiting from outsourcing (at least in the short term), the recent election in that country revealed widespread resentment among the Indian poor who feel they have not benefited from the global service sector. Impoverished peasants turned out in droves, for example, to bring about a surprise upset for the governor of Andhra Pradesh, known as the architect of the country's high-tech foreign investment strategy and nicknamed the "CEO" of his state. Thus, while U.S. workers are facing increased job anxiety as a result of outsourcing, there are also strong concerns that the outsourcing trend is not a panacea for the developing world.

The Growing Gulf Between Service Sector Workers and Their Bosses

One clear impact of the outsourcing trend is that as U.S. corporations globalize their service workforces, the pay gap between workers and

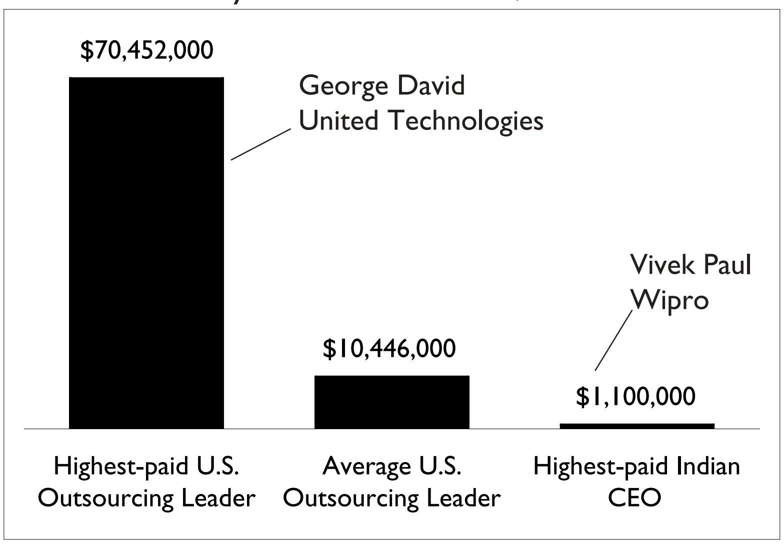
If lower labor costs and increased efficiency are their ultimate goal, U.S. executives might consider outsourcing themselves.

their bosses has grown even larger. If there is a chasm between pay levels for U.S. and Indian workers, the gap between compensation for U.S. Outsourcing CEOs and Indian workers is on the scale of the Grand Canyon (see Chart 1.3).

Should American *CEOs* be Outsourced?

If lower labor costs and increased efficiency are their ultimate goal, U.S. executives might consider outsourcing themselves. While their foreign counterparts are also seeing their pay levels expand (following the American model), U.S. executives still make far more than CEOs in every other country. In India, the highest-paid CEO is Vivek Paul, named one of the best managers in the world by *Business Week*. Paul leads Wipro, India's largest information technology services company, which provides consulting, systems integration, and maintenance services, including outsourcing services for international firms. The company had 2003 revenues of nearly $1 billion, profits of $171 million, and 23,300 employees. And yet Paul was able to get by on only $1.1 million, 11 percent of the average pay for the leading American outsourcing CEOs (see Chart 1.4).

Chart 1.4: CEO Pay in the U.S. and India, 2003



A Closer Look at 15 Top Service Outsourcers

The range of economic sectors involved in services outsourcing is remarkable.

The Institute for Policy Studies and United for a Fair Economy have undertaken a detailed look at 50 U.S. firms that have each outsourced (or announced plans to outsource) more than 800 service jobs over the past three years. The range of economic sectors involved in services outsourcing is remarkable. Leading outsourcers of service jobs include industrial powerhouses such as IBM and General Electric; leading military contractors such as United Technologies; management consulting firms like Accenture; conglomerates like Fluor; entertainment giants such as Time Warner; financial leaders such as Citigroup, Morgan Stanley, and J.P. Morgan Chase; insurance powers like Conseco; telecommunications companies like Sprint and SBC Communications; as well as prominent information technology firms like Oracle and Cognizant.

Here are some more details on the outsourcing activities of the 15 leading outsourcers with the highest-paid CEOs.

1. United Technologies
The Top Outsourcing Leader in terms of 2003 pay was George David of United Technologies. David made $70.4 million, up 629 percent over his 2002 compensation of $9.7 million. In 2001, David decreed that the company, an industrial conglomerate and military contractor, would be cutting $500 million out of its annual procurement budget of about $3.5 billion. As a result, the firm began rapidly replacing U.S. labor with less expensive Indian workers. The firm has software development centers in Pune and Bangalore, as well as outsourcing contracts with five Indian vendors. David's goal is to send 80 percent of the firm's software application development and support to India.[8]
2003 CEO Pay: $70.4 million

2. Citigroup
This year Citigroup became the sole owner of e-Serve International, an Indian IT service company that provides call center, transaction processing and data management services for Citibank. The Mumbai, India-based company employs 4,500 people.[9] Outgoing Citigroup CEO Sanford Weill made more than $54 million in 2003 – seven times the average for his CEO peers.
2003 CEO Pay: $54 million

3. Oracle
Software giant Oracle has announced plans to double the size of its two research centers in India, one in Hyderabad and the other in Bangalore, bringing its Indian workforce to more than 6,000 employees. The company also has several hundred employees in research and development operations in Shenzhen and Beijing, China. Oracle CEO Lawrence Ellison is one of the highest-paid CEOs in history. He made $40.6 million in 2003, up from 2002, but lower than his staggering earnings of more than $700 million in 2001.
2003 CEO Pay: $40.6 million

Employees who lose their jobs at Bank of America are given severance pay on the condition that they help train their lower-wage replacements.

BofA CEO Kenneth Lewis made $37.9 million in 2003, more than double his 2002 pay.

4. Bank of America

Bank of America (BofA) has slashed nearly 5,000 U.S. jobs while outsourcing up to 1,100 jobs to India.[10] In July 2004, the firm announced that it will cut an additional 12,500 U.S. jobs in the next two years.[11] As at several other firms, BofA's American employees are given severance pay on the condition that they help train their replacements.[12] Meanwhile, the firm is set to open a new facility in the Indian city of Hyderabad that will handle support and transactions for most of the bank's major divisions, including consumer and corporate accounts.[13] In the midst of the job cuts and outsourcing, Bank of America CEO Kenneth Lewis received $37.9 million in compensation in 2003, nearly 110 percent more than in 2002.

2003 CEO Pay: $37.9 million

5. Cognizant Technology Solutions

CEO Wijeyaraj (Kumar) Mahadeva was one of the top paid executives in the world in 2003, while leading a firm that has 70 percent of its workforce in low-wage India.[14] Mahadeva received more than $27 million in executive compensation, an 80 percent increase over his 2002 earnings. The New Jersey-based IT firm already employs nearly 12,000 workers in India and has ambitious expansion plans.[15] Now primarily based in Chennai, India's up-and-coming IT city, Cognizant announced plans in March to invest $42 million to expand their Pune facility, build a second facility in Chennai, set up an office in Bangalore, as well as hire at least 4,000 new IT professionals this year.[16] Cognizant is also recruiting and training workers for a new software development center in China. The company plans to have 100 people employed at this facility, located near Shanghai, within a year.[17]

2003 CEO Pay: $27.0 million

6. Morgan Stanley

As early as 2002, Morgan Stanley outsourced a significant portion of its IT work to foreign countries, hiring over 1,000 workers in India, the Philippines and other locations.[18] Morgan Stanley analysts also advise investors to favor companies that bust unions. According to company documents released in November 2002, researchers advised clients to "Look for the union label – and run the other way – Rigidity in labour costs, while perhaps beneficial to employees, may prove toxic to shareholders."[19] On the day these documents were made public, the bank announced cuts of 2,000 staff.[20] These cuts, combined with outsourcing, have helped line the pockets of CEO Philip J. Purcell, who has earned over $67 million over the last three years.

2003 CEO Pay: $23.3 million

7. Intuit

CEO Stephen M. Bennett got a 425 percent pay hike in 2003 to $22.3 million, while he shifted call center jobs to India. Intuit sells personal finance software, including Quicken and TurboTax. The firm's outsourcing has rattled the community of Tucson, Arizona, where call-center jobs make up 5 percent of the local workforce. Intuit's 1,300 workers make the company the third largest call-center employer in the city.[21] But while employees worry about the future of their jobs, Intuit saw a 145 percent increase in profits last year.[22]

2003 CEO Pay: $22.3 million

8. SBC Communications

SBC, a telecom company that purchased Pacific Bell in 1997, has outsourced an estimated 3,000 jobs to India and the Philippines. In May 2004, SBC workers went on a four-day strike, partly in protest over outsourcing. The company eventually agreed to try to bring jobs back to the United States and negotiated a new contract.[23] After receiving total compensation of more than $18 million in 2003, it was probably difficult for CEO Edward Whitacre, Jr. to argue that U.S. workers are too expensive.

2003 CEO Pay: $18.3 Million

9. Conseco

Beginning in 2000, financially troubled insurance firm Conseco Inc. slashed several thousand U.S. jobs while sending 2,000 jobs to India, mostly for claims processing.[24] Despite these cuts, the firm filed for bankruptcy in 2002, re-emerging in September 2003. In contrast to the company's employees and creditors, Conseco's executives made out like bandits. Gary Wendt, who was hired in 2000 and led the outsourcing process, got a $45 million signing bonus. He also reaped $1.6 million in stock profits when Conseco, under his management, bought ExlService, an Indian office service company that Wendt had helped found. (Conseco sold ExlService in November 2002.[25]) Wendt received a generous golden parachute when he stepped down in 2002. He was replaced by William J. Shea, who earned over $16.6 million in 2003, twice the level for average CEOs.

2003 CEO Pay: $16.6 Million

10. JP Morgan Chase

CEO William B. Harrison, Jr. enjoyed a 45 percent pay raise in 2003 to $16.5 million, more than twice the total compensation of the average CEO. Harrison's generous reward came in large part because of JP Morgan's merger with Bank One, which is expected to result in 10,000 job cuts. Meanwhile, the firm received taxpayer-funded government contracts and then turned around and offshored the work to Mexico and India. JP Morgan's Electronic Financial Services division coordinates call centers related to foods stamp and welfare programs for more than 30 states. Because the work has been offshored, when New York residents call to inquire about their food stamp benefits, for example, they are connected to an operator in Pune or Bangalore, India if they are English speakers and to one in Tijuana if they are Spanish-speaking. The company's investment banking arm also employs researchers in Mumbai.

2003 CEO Pay: $16.5 million

11. Sprint

CEO Gary Forsee earned $16.5 million in 2003 at a time when the company was reeling from 21,000 jobs cuts made between late 2001 and late 2003.[26] Sprint's outsourcing activities have been difficult to track. While Forsee told journalists in August 2003 that the firm's plans to offshore would likely affect only "several hundred" jobs, a company memo to potential vendors that was leaked to the press indicated that Sprint was planning to outsource work done by more than 3,000 of its existing employees and contractors.[27] In February of this year, CNN reported that Sprint was outsourcing 5,000 to 6,000 jobs to

JP Morgan Chase received taxpayer-funded government contracts from the State of New York and then turned around and offshored the work to Mexico and India.

Meanwhile, CEO William B. Harrison, Jr. enjoyed a 45 percent pay raise in 2003 to $16.5 million.

American Express has laid off thousands of U.S. workers in recent years, while transferring jobs to India and the Philippines.

AmEx CEO Kenneth Chenault has earned a combined total of over $33 million over the last three years.

IBM.[28] Since IBM had just acquired Daksh eServices, India's third-largest call center, it was widely assumed that the Sprint jobs would be going to India.[29]
2003 CEO Pay: $16.4 million

12. Bank of New York
CEO Thomas Renyi made $14.6 million in 2003 while overseeing a process of outsourcing jobs to India and the Philippines. In March, the firm announced that it was sending an additional 250 computer software jobs to Mumbai, where it already employed 670 workers.[30] The firm also announced plans in 2003 to open a software development center in the Philippines.[31]
2003 CEO Pay: $14.6 million

13. Time Warner
Time Warner CEO Richard Parsons made $11.9 million in 2003, while shifting software engineering jobs from California to Bangalore, India. America Online (AOL), a part of the Time Warner media empire, already operated a call center in Bangalore, India that employs about 1,600 people, although some sources have said the AOL space may accommodate up to 3,000 workers.[32] The center handles some 10 million calls per year, including inquiries from AOL customers in the United States. Then in December 2003, the news leaked that the company was also setting up a software development center in Bangalore. Earlier that same month, the company had laid off 450 workers, mostly software engineers, from its California headquarters.[33] The exact number of workers to be employed at the Bangalore center is unknown. AOL also outsources an unspecified number of bilingual customer service jobs to Monterrey, Mexico.[34]
2003 CEO Pay: $11.9 million

14. General Electric
General Electric is widely recognized as one of the founders of India's business process outsourcing industry. The company employs 12,000 people in the country who perform a variety of tasks, including answering calls about consumer credit cards, giving IT technical assistance, and handling network security.[35] GE CEO Jeffrey Immelt made $11.6 million in 2003, 43 percent more than the average U.S. CEO.
2003 CEO Pay: $11.6 million

15. American Express
American Express has laid off thousands of U.S. workers in recent years, while transferring jobs to India and the Philippines. In 2002, the firm opened a 137,000-square-foot global service call center in Gurgaon, India."[36] By early 2004, American Express was ranked by an Indian publication as the seventh-largest business process outsourcing firm in the country, with an estimated 3,500 employees.[37] In addition, the Philippines' government announced in July of this year that the company had been approved for an expansion of its operations there, with the opening of a new call center.[38] CEO Kenneth I. Chenault has earned a combined total of over $33 million over the last three years.
2003 CEO Pay: $11.5 million

2. (Political) Partying Pays

CEOs at the 30 companies that sponsored the Democratic National Convention saw their average pay jump 96 percent from 2002 to 2003.

This summer's political conventions give new meaning to the term "political party." Four days each in Boston and New York costing nearly a quarter of a billion dollars, paid for increasingly by taxpayers and by corporate sponsors. In these days when strategic political investments can be as important to business success as sound research and development decisions were in days gone by, CEOs of those firms most heavily engaged in financing political conventions and presidential campaigns have been richly rewarded in their paychecks.

We examined CEO pay packages at the 69 publicly-traded U.S.-based corporations that were listed as financial or in-kind sponsors of the two major political party conventions (see Table 2.1 for a complete list). The CEOs of these firms enjoyed a 52 percent increase in average pay in 2003, compared to just a 9 percent raise for the average CEO. The convention-sponsoring CEOs received, on average, $9.2 million in total compensation in 2003, 13 percent more than the average CEO in the *Business Week* survey.

Chart 2.1: Average CEO Pay Increase from 2002 to 2003

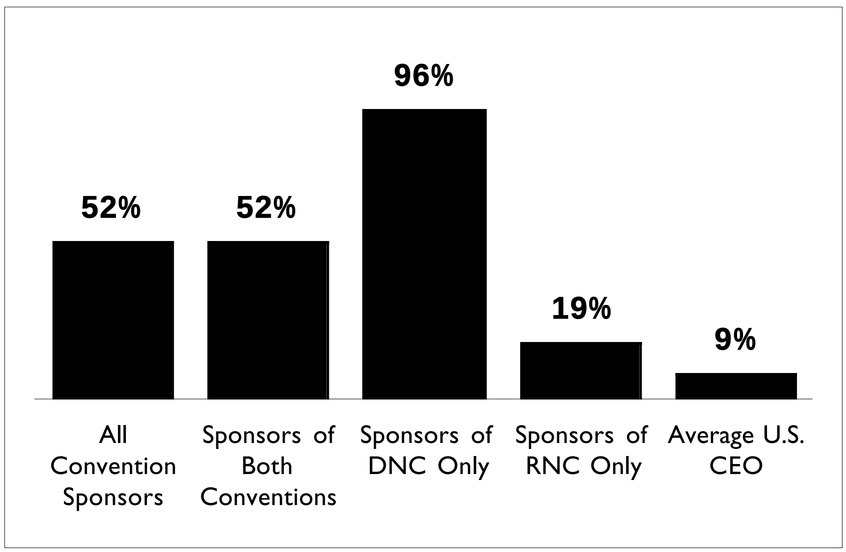
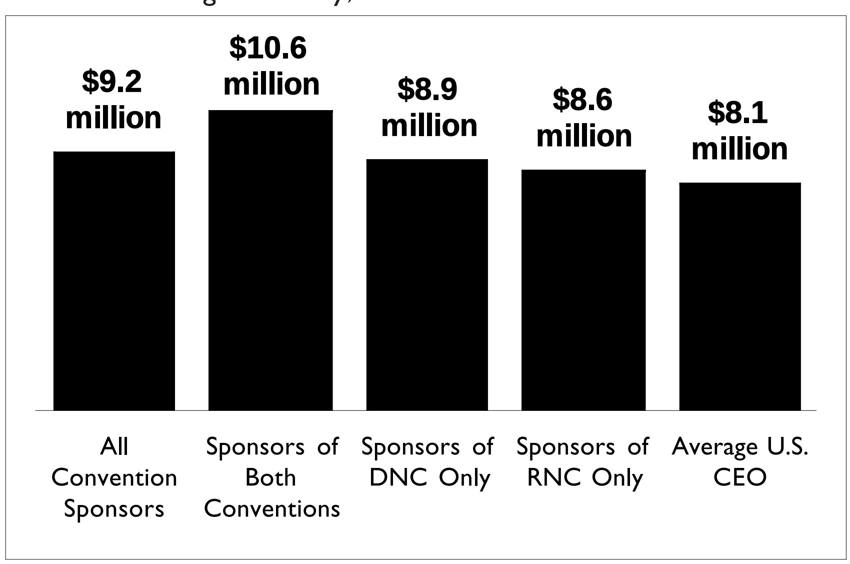


Chart 2.2: Average CEO Pay, 2003



Grouping the convention sponsors according to which convention they sponsored yields some interesting results. Of the 69 convention sponsors, 29 sponsored the Democratic convention only, 24 sponsored the Republican convention only, and 16 companies chose to hedge their bets by sponsoring both conventions. CEOs of these 16 "two-timing" companies had the highest average 2003 pay at $10.6 million, followed by the Democratic underwriters, who averaged $8.9 million, and the Republican sponsors, whose average pay clocked in at $8.6 million.

CEOs at the Democratic-only sponsors saw the biggest pay jump from 2002 to 2003. These 29 companies saw their average CEO pay rise 96 percent in 2003. CEO pay at the 16 companies that sponsored both conventions rose 52 percent, while CEO pay at the GOP-sponsoring companies rose 19 percent.

Table 2.1: 2003 CEO Pay at the 69 Companies That Sponsored One or Both Political Conventions

SPONSORED BOTH (16 Companies)

Company	CEO	CEO Pay (in thousands)	Change from 2002
Altria Group	L.C. Camilleri	$ 27,875	+657%
American International Group	M.R. Greenberg	15,345	-18%
Amgen	K.W. Sharer	9,149	-30%
AT&T	D.W. Dorman	11,562	+224%
Bank of America	K.D. Lewis	37,940	+108%
Bristol-Myers Squibb	P.R. Dolan	5,869	+434%
Clear Channel Communications	L.L. Mays	2,928	-2%
Coca-Cola	D.N. Daft	6,372	+12%
EMC	J.M. Tucci	7,059	+321%
IBM	S.J. Palmisano	7,730	+13%
Marriott International	J.W. Marriott Jr.	2,224	* -44%
Metropolitan Life	R.H. Benmosche	7,466	-6%
Microsoft	S.A. Ballmer	865	+15%
Pfizer	H.A. McKinnell	9,457	-8%
State Street Bank	D.A. Spina	7,105	+10%
Verizon	I.G. Seidenberg	11,180	+68%
	Total	**170,126**	
	Average	**10,633**	**+52%**
	Business Week Average	**8,100**	**+9%**

SPONSORED DEMOCRATIC NATIONAL CONVENTION ONLY (29 Companies)

Company	CEO	CEO Pay (in thousands)	Change from 2002
AFLAC	D.P. Amos	$ 19,195	+20%
Biogen Idec	W.H. Rastetter	1,157	-90%
Boston Properties	E.H. Linde	3,089	+106%
Boston Scientific	J.R. Tobin	2,012	-13%
Cabot Corp.	K.F. Burnes	3,611	+8%
Citizens Financial	D.R. Wells	2	0%
Equity Office Properties Trust	R.D. Kincaid	4,198	* +602%
Cendant (Howard Johnson Hotels)	H.R. Silverman	54,418	+377%
Genzyme	H.A. Termeer	19,037	+1192%
Goldman Sachs	H.M. Paulson Jr.	21,354	+126%
Hasbro	A.G. Hassenfeld	3,430	+57%
Hilton Hotels	S.F. Bollenbach	23,447	+1008%
Hewlett-Packard	C.S. Fiorina	3,426	-17%
Ikon Office Solutions	M.J. Espe	2,119	-32%
John Hancock	D.F. D'Alessandro	16,852	-22%
Keyspan	R.B. Catell	2,027	+22%
Merck	R.V. Gilmartin	2,958	-1%
Millennium Pharmaceuticals	M.J. Levin	750	+56%
Nextel	T.M. Donahue	21,598	+646%
Pitney-Bowes	M.J. Critelli	5,466	+80%
Raytheon	W.H. Swanson	6336	* -29%
Reebok	P.B. Fireman	2,756	-12%
Sepracor	T.J. Barberich	684	+21%
Sovereign Bank	J.S. Sidhu	5,648	+209%
Staples	R.L. Sargent	17,644	+444%
Starwood Hotels	B.S. Sternlicht	5,026	-3%
Gillette	J.M. Kilts	4,398	+45%
United Parcel Service	M.L. Eskew	3,028	+56%
Washington Group International	S.G. Hanks	3,166	+53%
	Total	**258,832**	
	Average	**8,925**	**+96%**
	Business Week Average	**8,100**	**+9%**

Table 2.1: 2003 CEO Pay at the 69 Companies That Sponsored One or Both Political Conventions

SPONSORED REPUBLICAN NATIONAL CONVENTION ONLY (24 Companies)

Company	CEO	CEO Pay (in thousands)	Change from 2002
ACS	J.A. Rich	10,220	-25%
American Express	K.I. Chenault	11,546	-37%
Bank of New York	T.A. Renyi	14,598	148%
Cisco Systems	J.T. Chambers	0	0%
Citigroup	S.I. Weill	54,060	305%
ConEdison	E.R. McGrath	3,199	-48%
Delta Air Lines	L.F. Mullin	1,112	-77%
Disney	M.D. Eisner	7,314	22%
Federal Express	F.W. Smith	2,665	-3%
General Electric	J.R. Immelt	11,580	-23%
General Motors	G.R. Wagoner Jr.	8,432	-30%
IDT	J.A. Courter	869	-29%
International Paper	J.T. Dillon	2,545	-70%
JP Morgan Chase	W.B. Harrison Jr.	16,554	45%
Loews	J.S. Tisch	1,392	-33%
Merrill Lynch	E.S. O'Neal	25,331	* +103%
Monster Worldwide	A.J. McKelvey	5,400	28%
New York Times	R.T. Lewis	1,770	-72%
Schering-Plough	F. Hassan	4,881	* -73%
Time Warner	R.D. Parsons	11,874	907%
Univision Communications	A.J. Perenchio	0	0%
UST	V.A. Gierer Jr.	2,786	37%
Waste Management	A.M. Myers	2,098	+14%
Xerox	A.M. Mulcahy	5,026	-2%
	Total	**205,252**	
	Average	**8,552**	**+19%**
	Business Week Average	**8,100**	**+9%**
	GRAND TOTAL (69 Companies)	**634,210**	
	Average (69 Companies)	**9,191**	**+52%**
	Business Week Average	**8,100**	**+9%**

* New CEO in 2003.

Sources: Democratic National Convention website: www.boston04.com/about_your_hosts/sponsors.asp; Republican National Convention website: www.nyc2004.org/SpecialThanks.aspx; *Business Week,* April 19, 2004 and April 21, 2003; and corporate proxy statements filed with the Securities and Exchange Commission. CEO Pay includes salary, bonus, "other annual compensation," restricted stock awards, long-term incentive payouts, and the value of stock options exercised. Percentage change based on the average of total compensation for all CEOs for each year.

Table 2.2: 2003 Pay for the 38 CEOs Who Have Each Raised at Least $100,000 for the 2004 Bush or Kerry Campaigns

CEO	Company	Candidate	CEO Pay (in thousands)	Change from 2002
R.A. Kotick	Activision	Bush	$ 483	-97%
C.H. Lindner	American Financial Group	Bush	1,498	-24%
M.R. Greenberg	American International Group	Bush	15,345	-18%
J.L. McWaters	Amerigroup	Bush	1,837	-4%
R.S. Ziman	Arden Realty	Kerry	3,583	+56%
T.A. Renyi	Bank of New York	Bush	14,598	+148%
J.E. Cayne	Bear Stearns	Bush	33,925	+87%
M.K. Rose	Burlington Northern Santa Fe	Bush	3,108	+3%
D.M. McClanahan	Centerpoint Energy	Bush	1,812	+48%
J.E. Rogers	Cinergy	Bush	12,214	+27%
W.W. O'Dell	Diebold	Bush	2,926	+95%
F.W. Smith	FedEx	Bush	2,665	-3%
H.M. Paulson Jr.	Goldman Sachs	Bush	21,354	+126%
J.A. Courter	IDT	Bush	869	-29%
A.M. Mixon III	Invacare	Bush	3,704	+32%
D.F. D'Alessandro	John Hancock	Kerry	16,852	-22%
C.M. Cawley	MBNA	Bush	34,857	-28%
E.S. O'Neal	Merrill Lynch	Bush	25,331	* +103%
P.J. Purcell	Morgan Stanley	Bush	23,307	-2%
D.C. Schar	NVR	Bush	58,094	-38%
I.F. Engelhardt	Peabody Energy	Bush	3,975	+290%
H.A. McKinnell	Pfizer	Bush	9,457	-8%
S.A. Burd	Safeway	Bush	14,041	+28%
E.G. Atsinger III	Salem Communications	Bush	700	0%
E.E. Whitacre Jr.	SBC Communications	Bush	18,308	+117%
J.P. Ward	Servicemaster	Bush	1,663	-4%
S.L. Green	SL Green Realty	Kerry	7,256	+327%
B.G. Hartley	Southside Bancshares	Bush	772	+112%
P.S. Rummell	St. Joe	Bush	39,509	+149%
M.D. Medina	Terremark Worldwide	Bush	350	0%
G.K. Thompson	Timken	Bush	9,570	+24%
R.K. Davidson	Union Pacific	Bush	15,021	+5%
G. David	United Technologies	Bush	70,452	+629%
W.W. McGuire	UnitedHealth Group	Bush	91,958	+1147%
A.J. Perenchio	Univision Communications	Bush	0	0%
I.G. Seidenberg	Verizon	Bush	11,180	+68%
S.G. Hanks	Washington Group International	Bush	3,166	+53%
A.M.. Myers	Waste Management	Bush	2,098	+14%
	Total		**577,838**	
	Average		**15,206**	**+44%**
	Business Week Average		**8,100**	**+9%**

* New CEO in 2003.

Sources: Public Citizen / Texans for Public Justice database of Bush Pioneers and Rangers identified by the Bush for President Campaign, available online at WhiteHouseForSale.org; Public Citizen database of Kerry Co-chairs identified by the Kerry for President Campaign, available online at WhiteHouseForSale.org; *Business Week,* April 19, 2004 and April 21, 2003; and corporate proxy statements filed with the Securities and Exchange Commission. CEO Pay includes salary, bonus, "other annual compensation," restricted stock awards, long-term incentive payouts, and the value of stock options exercised. Percentage change for the group as a whole based on the average total compensation for all CEOs in the group for each year. The campaigns do not reveal the total amount raised by each CEO.

Dialing for Dollars . . . and Access?

With individual contributions to Presidential campaigns limited to $2,000 per person, the Bush and Kerry campaigns have put together networks of elite fundraisers who solicit their friends and business associates for donations. The ranks of elite Bush and Kerry fundraisers include more than three dozen CEOs, many of whom sit atop corporations that routinely have important business before the federal government (see Table 2.2).

So far, there are 38 CEOs who have personally "bundled" at least $100,000 in individual contributions to one of the two major presidential campaigns. If their candidate is successful, these CEOs can presumably count on a special level of access to the President, if not a plum ambassadorship or advisory council post. Perhaps not coincidentally, these political rainmakers as a group are also extremely well-paid. In 2003, the 38 CEOs in the $100,000 club averaged $15.2 million in total pay, 88 percent more than the average large-company CEO.

All but three of the 38 top fundraising CEOs are raising money for the Bush campaign. The highest-paid Bush bundler is William W. McGuire of UnitedHealth Group, recipient of $92.0 million in total compensation in 2003. The highest-paid Kerry money man is David F. D'Allesandro, who was paid $16.6 million in 2003 as CEO of Massachusetts-based John Hancock Financial Services.

There are 38 CEOs who have each raised at least $100,000 for the Bush or Kerry campaigns.

These CEOs also happen to make, on average, 88 percent more than the average U.S. CEO.

Bundle Up!

Deploying an army of well-connected private citizens to raise large "bundles" of individual contributions is nothing new. But the technique was raised to a new level of sophistication by the 2000 Bush for President campaign, which assigned each fundraiser a unique tracking number and instructed donors to write that number on their check so that the proper "bundler" could be credited. A fundraiser who bundles together $100,000 for the Bush campaign receives the title of "Pioneer." Amassing at least $200,000 in donations moves you up to "Ranger" status. Over at the Kerry campaign, those who raise at least $100,000 are given the comparatively bland moniker of "Co-chair."

CEOs at the Biggest Corporate Contributors Cash In

There is also a correlation between overall corporate campaign contributions and high CEO pay. The 41 corporations with the most contributions to federal candidates in the 2004 election cycle paid their CEOs an average of $17.4million in 2003, more than twice as much as the typical large-company CEO (see Table 2.3).

The highest-paid CEO among the top corporate campaign contributors is Cendant's Henry Silverman, whose $54.4 million pay package is just the tip of a very large CEO pay iceberg. He owns $1 billion worth of Cendant stock and holds options worth $287 million more. Silverman also received a million-dollar contribution to what may be the most superfluous pension plan in the history of old age, and the company paid the $4.6 million annual premium on a $100 million life insurance policy. To help him make ends meet in his golden years, for the rest of his life Silverman will receive, courtesy of Cendant shareholders, medical and welfare benefits, office and clerical support, subsidized use of corporate aircraft, a car and driver, a security force when traveling on company business and reimbursement of miscellaneous business expenses (as long as they are "properly documented.")[39]

Table 2.3: 2003 CEO Pay at the 41 Companies with the Most Contributions to Federal Candidates, 2003-04

Company	CEO	Total 2003-04 Contributions	CEO Pay (in thousands)	Change from 2002
Goldman Sachs	H.M. Paulson Jr.	$ 3,910,296	$ 21,354	+126%
Morgan Stanley	P.J. Purcell	1,882,535	23,307	-2%
Microsoft	S.A. Ballmer	1,768,446	865	+15%
Time Warner	R.D. Parsons	1,730,995	11,874	+907%
Citigroup	S.I. Weill	1,659,287	54,060	+305%
SBC Communications	E.E. Whitacre Jr.	1,632,381	18,308	+117%
Wal-Mart	H.L. Scott	1,585,410	15,098	-14%
Merrill Lynch	E.S. O'Neal	1,495,333	25,331	* +103%
United Parcel Service	M.L. Eskew	1,420,591	3,028	+56%
General Electric	J.R. Immelt	1,407,850	11,580	-23%
JP Morgan Chase	W.B. Harrison Jr.	1,276,516	16,554	+45%
Lehman Brothers	R.S. Fuld Jr.	1,265,289	52,940	+84%
MBNA	C.M. Cawley	1,139,097	34,857	* -82%
Northrop Grumman	R.D. Sugar	1,097,683	5,859	+11%
FedEx	F.W. Smith	1,050,196	2,665	-3%
AFLAC	D.P. Amos	1,038,792	19,195	+20%
Bank of America	K.D. Lewis	1,020,338	37,940	+108%
Lockheed Martin	V.D. Coffman	979,048	13,690	-46%
Bear Stearns	J.E. Cayne	978,848	33,925	+87%
Verizon	I.G. Seidenberg	973,713	11,180	+68%
Boeing Co	P.M. Condit	959,205	3,811	-8%
General Dynamics	N.B. Chabraja	932,412	9,570	-37%
BellSouth	F.D. Ackerman	897,695	11,094	+107%
Wachovia	G.K. Thompson	879,916	9,570	+24%
Pfizer	H.A. McKinnell	865,134	9,457	-8%
Interpublic Group	D.A. Bell	832,122	2,376	* -65%
Union Pacific	R.K. Davidson	820,496	15,021	+5%
Southern Co	H.A. Franklin	816,325	5,460	-6%
American International Group	M.R. Greenberg	785,974	15,345	-18%
Viacom	S.M. Redstone	783,914	19,077	-6%
Wells Fargo	R.M. Kovacevich	704,641	35,908	+349%
Metropolitan Life	R.H. Benmosche	657,879	7,466	-6%
Bank One	J. Dimon	640,984	N/A - acquired	N/A
Cendant	H.R. Silverman	639,539	54,418	+377%
Altria Group	L.C. Camilleri	635,677	27,875	+657%
General Motors	G.R. Wagoner Jr.	607,131	8,432	-30%
American Financial Group	C.H. Lindner	602,049	1,498	-24%
Omnicom	J.D. Wren	600,609	3,344	+282%
Disney	M.D. Eisner	597,385	7,314	+22%
Comcast	B.L. Roberts	583,727	30,960	-22%
Federated Investors	J.F. Donahue	579,800	2,755	0%
	Total	**44,735,258**	**694,361**	
	Average		**17,359**	**+11%**
	Business Week Average		**8,100**	**+9%**

* New CEO in 2003.

Sources: Center for Responsive Politics, opensecrets.org, "2004 Election Overview: Top Overall Donors," based on Federal Election Commission (FEC) data released July 5, 2004, includes contributions from PACs and individuals giving $200 or more to federal candidates and parties as reported to the FEC; *Business Week,* April 19, 2004 and April 21, 2003; and corporate proxy statements filed with the Securities and Exchange Commission. CEO Pay includes salary, bonus, "other annual compensation," restricted stock awards, long-term incentive payouts, and the value of stock options exercised. Percentage change for the group as a whole based on the average total compensation for all CEOs in the group for each year.

3. The Spiraling Cost of Blocking Options Expensing

In 2000 alone, Enron took a tax deduction of $1.4 billion for stock options given to top managers.

It is astounding that in this, our 11th annual report on executive compensation, we still need to include a section on the interplay between excessive CEO pay and the special accounting treatment of stock options. One year ago, it seemed inevitable that the Financial Accounting Standards Board (FASB) would finally succeed in pushing through a new rule to require that corporations report all stock options as expenses in their financial statements.

FASB had tried to adopt such a rule in 1993 but retreated when opponents in the Senate threatened to dismantle the quasi-governmental body. Then the wave of corporate scandals in 2002 and 2003 brought new scrutiny to a system which allows firms to inflate earnings by not reporting options as expenses – even when they deduct these options costs from their taxable income.

This accounting trickery was a significant factor in the explosion of CEO pay that began in the 1980s. Corporate boards could lavish massive options grants on top executives with no repercussions for their income statements. It also was a factor in the corporate accounting scandals. Testifying before the Senate in 2002, Enron executive Jeffrey Skilling admitted that the options loophole had allowed his firm to inflate profits. Enron handed out such massive grants that in 2000 alone, the firm took a tax deduction of $1.4 *billion* for stock options given to top managers. Options-related tax deductions also have helped corporations avoid paying their fair share of taxes. As a share of federal revenues, corporate taxes have dropped from 12 percent in 1996 to 8 percent in 2003.[40]

As the political tide appeared to be turning, some 500 corporations began expensing options voluntarily. When financial heavyweights — including Federal Reserve Chairman Alan Greenspan, Treasury Secretary John Snow, renowned investor Warren Buffett, Nobel economist Joseph Stiglitz, and the four largest accounting firms — continued to line up in favor of the practice, FASB's success in getting options expensed seemed assured.

And yet the power of the deep-pocketed high-tech lobby should not be underestimated — particularly in an election year. The tech titans, who rely heavily on options-based compensation, have led an ambitious drive to block the FASB plan. On July 20, they won a stunning victory. In a landslide, the U.S. House of Representatives approved a bill (H.R. 3574) that would prohibit FASB from requiring companies to report options grants as expenses in financial statements, except for the options of a company's top five executives. Small businesses with annual revenues of less than $25 million would be exempted. New public

Stock options give employees the right to buy company stock at a set price in the future. They often have an exercise period of up to ten years. If an employee has an option to buy stock for $10 a share and exercises that option when the stock is trading at $50 a share, the employee will owe the company $10 a share and can sell the stock for a $40 profit. Continuing the example, exercising 100,000 stock options would produce a $4 million gain. Top executives get repeated megagrants of stock options producing megawealth.

Powerful corporate lobbyists are on the verge of once again thwarting the mandatory expensing of stock options.

companies of any size would also get a pass for three years. As an additional delay tactic, the bill's supporters also included a requirement that the Commerce and Labor departments conduct a study on the effect of mandatory expensing on U.S. competitiveness in the global economy.[41] The bill now heads to the Senate, where supporters are threatening to overcome opposition by attaching it as an amendment to an appropriations bill.

Why the House Bill on Options Expensing is Wrong – Even on CEO Pay

Leading financial experts have thoroughly savaged the House bill for promoting misleading accounting practices. Warren Buffett called it "mathematical lunacy" to treat top executives' options differently from those held by other employees. Prominent editorial boards have also been on the attack. For example, the *Financial Times* called it "silly," while the *Washington Post* said it would be "comical if the stakes were not so serious."

In addition to endorsing accounting chicanery, the bill also represents the wrong approach to addressing runaway CEO pay.

CEOs would continue to benefit from overstated earnings

If the bill became law, it is possible and even likely that it would result in a reduction in options granted to top executives. However, by allowing firms to ignore the cost of options given to other employees, the bill would perpetuate a system that allows firms to overstate earnings. This in turn would contribute to excessive CEO pay, to the extent that executive compensation is based on earnings. Thus, even if a firm shifted the composition of their pay packages away from stock options to bonuses, restricted stock awards, and other "performance-based" forms of compensation, CEOs would continue to benefit from the accounting trickery of unexpensed options.

Previous Congressional Tactics to Block Options Expensing

The tech lobby designed the latest Congressional initiative against options expensing so that it would appear to be a fight on behalf of average workers. But the current bill to block FASB's proposal is only the latest in a string of legislative efforts to block mandatory options expensing. A brief history:

1993 A Senate bill would have blocked a new rule requiring options expensing and required that the SEC ratify every FASB decision, essentially stripping FASB's authority.

1994 The Senate nearly unanimously passed a resolution denouncing FASB for even considering the rule.

2002 To counter new options expensing proposals, Sen. Joseph Lieberman (D-CT) offered an "alternative" that would use tax breaks not to discourage options, but to encourage more equitable distribution of them.

2003 Bills were introduced in both the Senate and the House to place a three-year moratorium on new rules on options accounting.

Further Delay in Action

Let's be clear. This bill was never about reining in CEO pay while protecting the "little guy." The provision mandating expensing of the top five executives' options was a clever strategy to give a populist boost to the real goal: intimidating FASB from taking any action on options whatsoever. Eleven years ago, expensing opponents managed to scare off the regulators. This time around, there are already signs of retreat. While the new rule requiring all options to be expensed was on track to go into effect in December 2004, FASB Chairman Robert Herz indicated in June that there may be a delay. He offered the flimsy excuse that corporations are too busy implementing the 2002 corporate reform legislation to be bothered with options expensing, but his waffling no doubt had more to do with the looming showdown with Congress.

Corporate tax breaks for executive stock options are a drain on the country's economic health.

How Current Options Rules Hurt U.S. Taxpayers

In last year's report, we began calculating the total amount of options gains pocketed by the 350 leading executives included in annual surveys of the *Wall Street Journal* since 1997 (the year the original FASB proposal would have taken effect). This amount now stands at $9.7 billion dollars. These CEOs' firms received an estimated $3.9 billion in tax deductions based on the stock options exercises of their CEOs alone.

The tax deductions received by these 350 firms just from their CEOs' options earnings is particularly significant in light of the nation's current budget crisis. Already strapped by large increases in military spending and tax cuts for the wealthy, these tax deductions are a further drain on the country's economic health.

Options-Related Deductions in Perspective

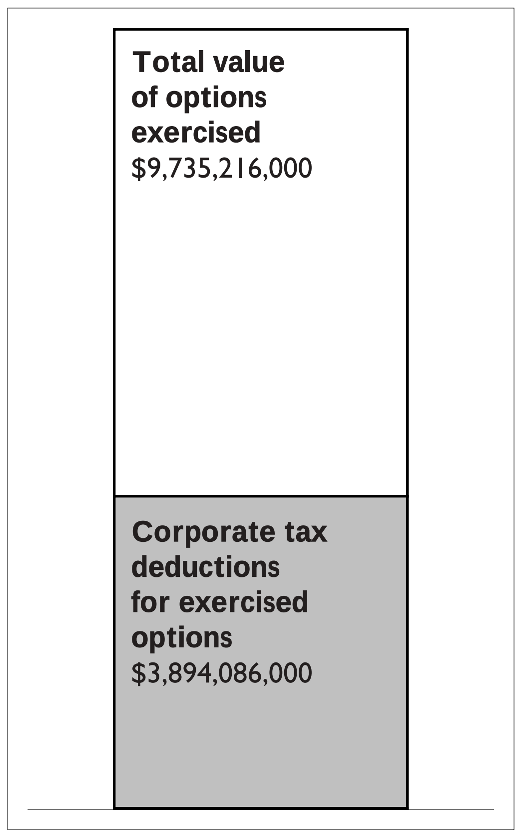
To put the cost of these options-related corporate tax deductions in perspective, consider that the $3.9 billion in deductions just from the 350 CEOs' options is:

* More than the 2005 projected budget deficits of Alaska, Colorado, Connecticut, Indiana, Iowa, Kentucky, Maine, Minnesota, Nebraska, North Carolina, Oklahoma, Rhode Island, South Carolina and West Virginia combined.[42]

* Equivalent to the combined pay of 70,000 elementary school teachers.[43]

* More than the cost of 17,000 new municipal fire trucks.[44]

Chart 3.1: Total Options Gains for 350 leading CEOs and Related Corporate Tax Deductions, 1997-2003



4. CEO Pay vs. Worker and Military Pay

After declining for the last two years, the ratio in pay between CEOs covered in Business Week's *survey and the average production worker reached 301 to 1 in 2003.*

According to *Business Week's* 54th Annual Executive Compensation Survey, which covers 365 of the largest U.S. companies, the average CEO received compensation totaling $8.1 million in 2003, up 9.1 percent from the previous year. The average production worker fared less well in 2003. Their annual pay was $26,899 in 2003, up just 2.1 percent from 2002 according to the Bureau of Labor Statistics. The average worker took home $517 in their weekly paycheck in 2003; the average large company CEO took home $155,769 in their weekly pay.

After declining for the last two years, the ratio in pay between CEOs covered in *Business Week's* survey and the average production worker reached 301 to 1 in 2003. In 2002, the ratio stood at 282 to 1. In 1982, it was just 42 to 1. In a speech before the Economic Club of Chicago, William McDonough, Chairman of the Public Company Accounting Oversight Board, said, "There is no economic theory, however far-fetched, which can justify that increase. In my frequently stated view, it is also grotesquely immoral."[45] Appointed by the Securities and Exchange Commission, McDonough is responsible for overseeing the auditors of public companies.

Chart 4.1: CEO Pay and the Minimum Wage, 1990-2003

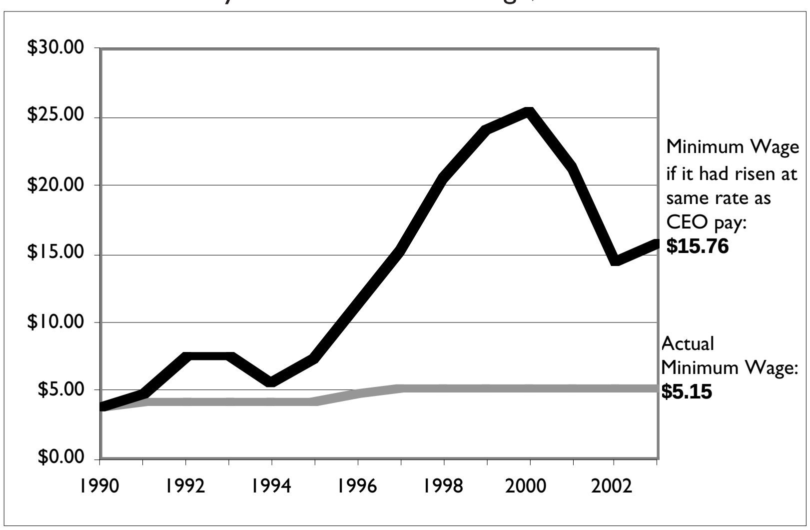
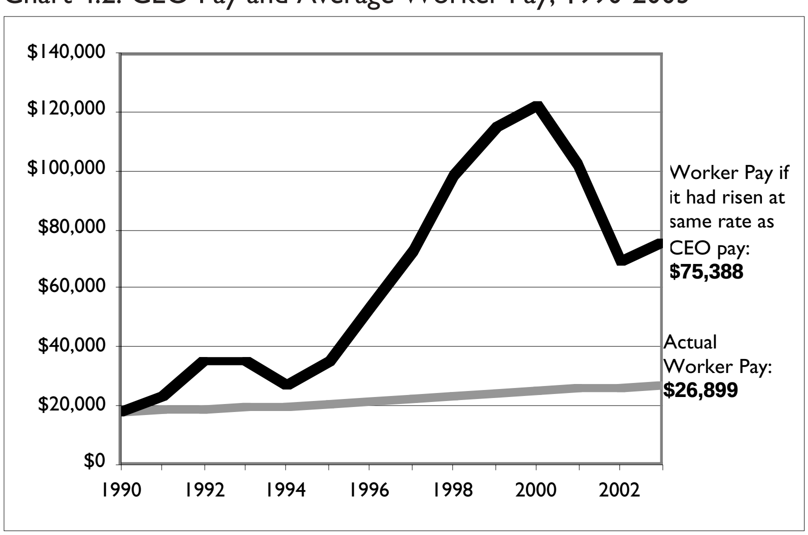
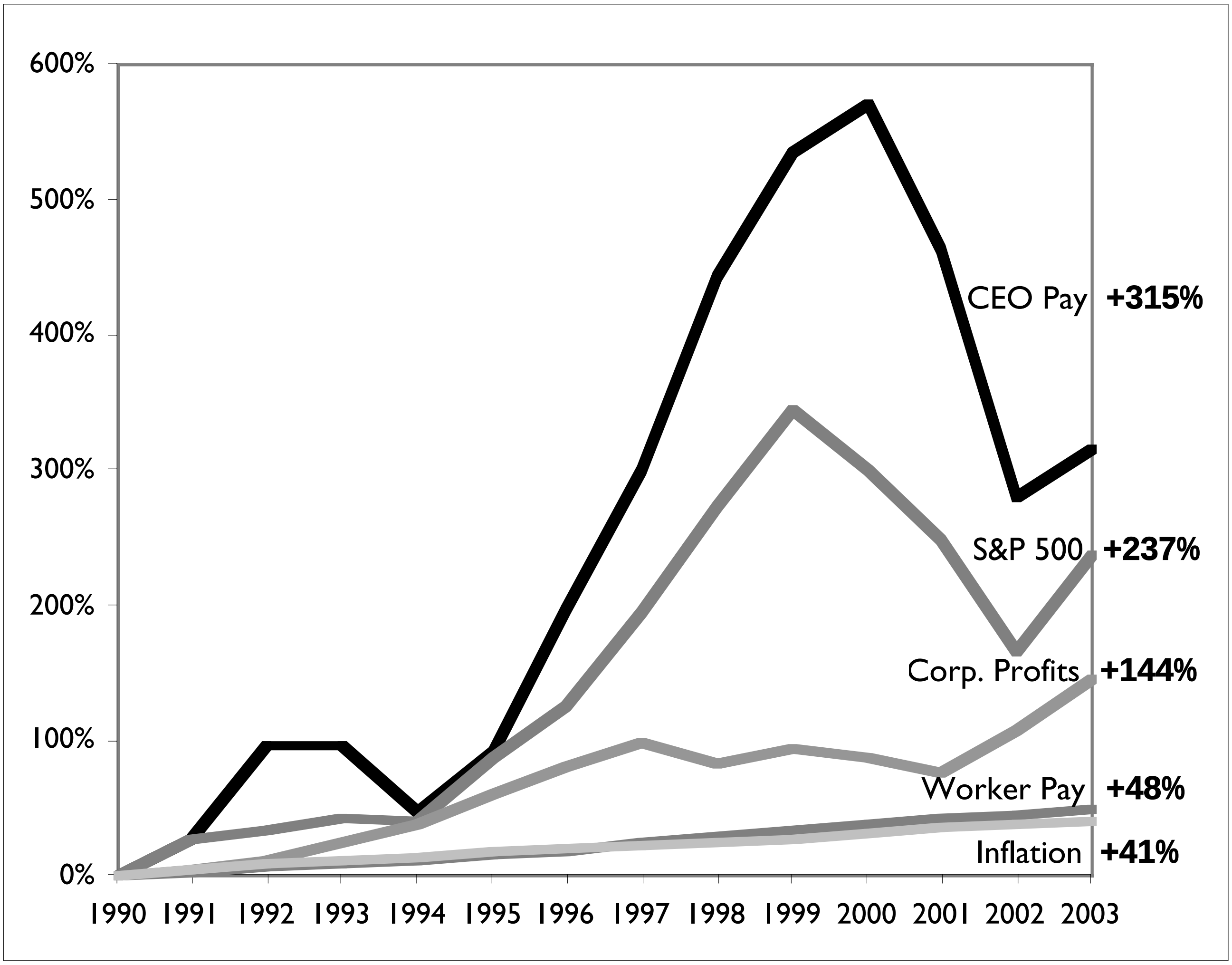


Chart 4.2: CEO Pay and Average Worker Pay, 1990-2003



Increases in CEO Pay since 1990 have far outpaced gains in worker pay. To illustrate, if the minimum wage had increased as quickly as CEO pay since 1990, it would today be $15.76 per hour, more than three times the current minimum wage of $5.15 an hour. Likewise, if the average production worker's annual pay had increased as quickly as CEO pay since 1990, it would today be $75,388 per year, nearly three times the current average of $26,899.

Chart 4.3: CEO Pay, Stock Prices, Corporate Profits, Worker Pay, and Inflation, 1990-2003



Sources: CEO Pay: *Business Week* annual executive pay surveys. **S&P 500 Index:** Standard & Poor's Corporation. Figures are year-end close. **Corporate Profits:** Bureau of Economic Analysis, National Income and Product Accounts. **Average Worker Pay:** Bureau of Labor Statistics, Average Weekly Hours of Production Workers (Series EEU00500005) and Average Hourly Earnings of Production Workers (Series EEU00500006). **Inflation:** Bureau of Labor Statistics, Consumer Price Index, All Urban Consumers.

Table 4.1: Total Annual Compensation for 919 U.S. Troops Killed in Iraq

Rank	Number Killed	Pay Grade	Total Annual Compensation per Person	Total for Rank
Army				
Private	33	E-2	$ 27,428	$ 905,137
Private First Class	107	E-3	30,676	3,282,289
Lance Corporal	6	E-3	28,534	171,202
Specialist	206	E-4	34,780	7,164,598
Corporal	12	E-4	34,780	417,355
Sergeant	124	E-5	41,436	5,138,064
Staff Sergeant	80	E-6	47,542	3,803,328
Sergeant First Class	19	E-7	60,739	1,154,045
Master Sergeant	7	E-8	66,917	468,418
Command Sergeant Major	5	E-9	76,586	382,932
Chief Warrant Officer	28	W-5	88,279	2,471,818
Second Lieutenant	9	O-1	46,484	418,352
First Lieutenant	16	O-2	44,482	711,711
Captain	30	O-3	73,556	2,206,667
Major	4	O-4	57,870	231,481
Lieutenant Colonel	4	O-5	99,393	397,571
Unknown	5	E-4	34,780	173,898
Marines				
Private	5	E-1	25,542	127,710
Private First Class	29	E-2	27,428	795,424
Lance Corporal	62	E-3	30,676	1,901,887
Corporal	41	E-4	34,780	1,425,964
Sergeant	15	E-5	41,436	621,540
Staff Sergeant	12	E-6	47,542	570,499
Gunnery Sergeant	4	E-7	60,739	242,957
First Sergeant	1	E-8	66,917	66,917
Master Sergeant	1	E-8	66,917	66,917
Second Lieutenant	4	O-1	46,484	185,934
First Lieutenant	3	O-2	56,498	169,493
Captain	6	O-3	73,556	441,333
Major	3	O-4	85,464	256,393
Unknown	1	E-4	34,780	34,780
Navy				
Hospitalman	1	E-3	30,676	30,676
Hospitalsman 3rd class	2	E-3	30,676	61,351
Petty officer 3rd class	8	E-4	34,780	278,237
Petty officer 2nd class	8	E-5	41,436	331,488
Petty officer 1st class	1	E-6	47,542	47,542
SEAL	1	E-6	47,542	47,542
Lieutenant	4	O-3	73,556	294,222
Air Force				
Airman First Class	2	E-3	29,776	59,551
Senior Airman	1	E-4	34,060	34,060
Staff Sergeant	2	E-5	41,016	82,032
Technical Sergeant	1	E-6	47,422	47,422
Master Sergeant	2	E-7	60,919	121,838
Captain	1	O-3	72,956	72,956
Major	3	O-4	85,464	256,393
Total	**919**			**37,914,744**

Note: This list is intended as an estimate based on the best available information as of early August, 2004. When rank was unknown, we assigned a rank of E-4. For ranks with more than one pay grade (e.g. Army Private, Chief Warrant Officer), we assigned the highest possible pay grade to all personnel.

Source: Press reports, Department of Defense. “Total Compensation” includes basic pay, subsistence allowance, housing allowance, and imminent danger pay.

Risk-Based Pay?

Defenders of sky-high CEO pay often argue that such compensation levels are justified because corporate leaders bear tremendous responsibilities and risks and must oversee complicated business activities. The war in Iraq and the tremendous risks and responsibilities borne by the military put this argument in some perspective.

Military generals, who are responsible for the lives of thousands of personnel and command highly complex operations, receive only a tiny fraction of a typical CEO's pay.

Military generals, who are responsible for the lives of thousands of personnel and command highly complex operations, receive only a tiny fraction of a typical CEO's pay. A U.S. army general with 20 years experience makes \$144,932.40 per year.[46] Average CEO pay, at \$8.1 million, is 56 times as high as the earnings of these generals.

Compared with the starting base pay of a U.S. soldier (\$12,776.40), average CEO pay is even more excessive. The CEO-to-soldier pay ratio is 634-to-1.

And when put in the context of those who have paid the ultimate price of the war, current CEO pay levels are even more disturbing. The combined annual pay of the 919 soldiers killed in Iraq as of early August 2004 was \$38 million (see Table 4.1). That's less than the combined pay of just five average American CEOs. And it's less than the amount received by a dozen individual U.S. executives covered in the annual *Business Week* survey, including the \$70 million received by George David at No. 6 defense contractor United Technologies, maker of the Black Hawk helicopter.

Adding further insult to injury, many military families whose loved ones are at risk in Iraq have had to resort to welfare to put food on their tables. Army Emergency Relief has reported a several-hundred-percent increase in requests for access to food stamps and subsidized meals between 2002 and 2003.

There are several steps that could be taken to reduce taxpayer subsidies for excessive CEO pay.

Conclusion: Actions for Change

1. End the Tax Breaks for Excessive CEO Pay

The U.S. tax code provides that reasonable business expenses may be deducted on tax returns. While there are rules about what constitutes "reasonable" when it comes to things like entertainment expenses, there is no such standard when it comes to executive pay and perks. Hence, companies still get away with deducting the full amount of executive compensation from their corporate income taxes, shifting the burden onto ordinary taxpayers. There are several steps that could be taken to reduce taxpayer subsidies for excessive CEO pay:

A. Limit the deductibility of executive compensation that exceeds a certain multiple of average worker pay.

The Income Equity Act (H.R. 2888) introduced by Representative Martin Sabo (D-MN) defines "reasonable business expense" for corporate compensation as pay packages that are less than 25 times the pay of the company's lowest paid employee. The bill does not restrict corporations from paying executives and others as lavishly as they wish. Rather, it puts a cap on the amount of pay that is deductible, thus preventing the government from subsidizing and encouraging corporate pay practices that widen the economic divide between workers and executives.

B. Eliminate the deductibility of executive pension, health, insurance and other perks not broadly available to other employees.

While a growing number of corporations are reducing employee health and retirement benefits, executives of these same firms continue to enjoy gold-plated versions of these important benefits. Companies should be free to pay whatever benefits to executives they wish, but tax policy should promote the common good, and not promote giving one group significant advantages not available to others.

C. Require that options be expensed.

The issue of expensing options has been viewed primarily as a matter of accounting transparency. But, as this report has pointed out, the current lack of a requirement on options expensing also places a heavy burden on taxpayers. These rules allow corporations to deduct options grants from their taxes, even though they are not required to report them as expenses in their financial statements. Thus, ordinary taxpayers have had to make up for lost tax revenues related to exorbitant options-based compensation. Senator Carl Levin (D-MI) has highlighted the unfairness of this situation by introducing the Ending the Double Standard for Stock Options Act (S. 182). The bill would restrict tax deductibility for options to the amount expensed on company income statements prepared for shareholders. Of course, a preferred solution would be for the corporate lobbyists to back off and allow the Financial Accounting Standards Board to go ahead with their proposal to require expensing of all options at all firms.

2. Give shareholders and workers more authority and more information on executive compensation.

Changing executive pay policies will require changes to basic corporate governance structures that give shareholders, workers, and the general public a stronger role.

Controlling excessive executive compensation requires addressing the rot at the core of the system. Corporate boards continue to be heavily made up of current and retired CEOs, which leads to serious and unaddressed conflicts of interest. Sarbanes-Oxley and other corporate reforms have served to further entrench peer CEOs as directors, since they have the accounting and business management experience required by such reform policies. Changing executive pay policies will require changes to basic corporate governance structures that give shareholders, workers, and the general public a stronger role.

A. Require shareholder approval of executive severance plans that exceed more than one year salary and bonus.

Failing as a CEO is often more lucrative than succeeding. In an attempt to avoid damaging public accusations at the time of an unexpected executive "transition," companies have paid out exorbitant sums to failed executives. A growing number of shareholder proposals have called for large severance plans to be put up for a shareholder vote. These proposals have proved popular among shareholders and should be required of all corporations by SEC rule.

B. Give shareholders the right to nominate directors directly.

On October 15, 2003, the Securities and Exchange Commission issued a proposed rule that would offer shareholders the right to directly nominate candidates for corporate boards by proxy ballot. The SEC received a record response of more than 13,000 public comments, more than 90 percent of which were in favor of the rule. The business community responded to this modest reform with a barrage of behind-the-scenes lobbying and threats of lawsuits. As a result, the SEC's final rule, expected earlier this year, remains bottled up.

C. Institute European executive pay controls.

Defenders of U.S. executive pay practices point to market pressures as one of the factors behind the explosion in CEO pay. But that doesn't explain why European executives, who head equally complex companies, are paid on average a fifth of what their U.S. counterparts are paid. What does explain the difference? Large companies in both the United Kingdom and Germany are required to have employee seats on corporate boards of directors. In addition, U.K. companies are required to put executive pay up for a shareholder vote each year. While no executive pay prospect has been voted down, some have gotten large negative votes. The embarrassing prospect of a negative vote creates a natural check on excess.

There are many CEOs who have led successful companies while at the same time limiting their own pay or sharing the wealth with employees.

D. Tighten reporting requirements on executive pay.

Sunlight is the best disinfectant, the old saying goes. Executive pay disclosure was last revamped more than a decade ago. At that time, reporting requirements regarding perks such as country club memberships and use of company aircraft for personal use were strengthened. It is time for another tightening of disclosure rules. Corporations should have to provide answers to questions such as: How does the executive's pay compare to other executives in the company's peer group? What is the pay ratio between highest and lowest paid worker? How many jobs did the company create during the year? How many employees did the company lay off? What is the ratio of the company's highest-paid employee to the company's net profit and to charitable giving?

3. Voluntary Corporate Actions

A vast body of academic research, as well as common sense, indicates that narrowing the gap in pay between top executives and frontline workers can result in a more committed, stable workforce and a stronger organization. Indeed, there are many examples of companies that have figured out how to succeed while at the same time sharing the wealth. Here are a few examples.

Terry Armstrong, SAS Shoemakers

Yes, Virginia, there is a Santa Claus, and in December 2003 the employees of SAS Shoemakers received proof. In Pittsfield, Maine, when the factory employees were called to the breakroom for an announcement, many braced themselves for news of factory shutdown. "Everybody thought the factory was going to close because there aren't so many shoe shops left," worker Charlene Wyman told the Boston Globe.

The workers had no idea what they were in for. Each received a $1,000 bonus for each year he or she had worked for the company. At the same time, workers in four other plants across the country received similar Christmas bonuses. Said Marie McNichol, a former employee of SAS's founder, Terry Armstrong, "He just wants to give back. He started out with nothing."

Armstrong remains faithful to the Pittsfield factory, promising to keep the plant open as long as he's alive, because he was raised in the area. The bonus not only helped the town's income (Pittsfield is in one of Maine's poorest counties), but it also slowed the recent decline of Maine's shoe industry, which has led companies to outsource jobs and lay off thousands of workers.[47]

Charlie Butcher, Butcher Company

At a farewell barbecue in 2000, Charlie Butcher, owner of Butcher Co., a family-owned manufacturer of floor care products and cleaning supplies, hinted to his 325 employees that they were in store for a bonus. Two weeks after the barbecue, Butcher sold the company to floor wax giant S.C. Johnson & Sons for a price of $18 million. Making good on his oblique promise, he divided the money among his employees, many of whom had been loyal to the company for decades. Butcher explained his long-held belief that his employees were the key to the business's success, continuing, "I meant it, and when the opportunity came to put my money where my mouth was, that's exactly what I did."[48]

"I consider our workers an asset, not an expense."

— Malden Mills CEO Aaron Feuerstein

John Chambers, Cisco Systems

During John Chambers's stint as CEO, Cisco has increased its annual revenues from $1.2 billion in 1995 to $18.9 billion in 2003. While his public recognition doesn't come cheap, Chambers's salary does, at least when times are tough. In 2002, as Cisco was facing layoffs of 8,500 employees, Chambers opted to lower his annual salary to $1 with no bonus. He took the same $1 salary in 2003. True, Chambers is hardly scraping by. He holds stock options worth around $200 million. But his no-pay gesture is much more than the vast majority of his similarly wealthy CEO counterparts have been able to muster during periods of layoffs.[49]

Aaron Feuerstein, Malden Mills

In 1995, a fire destroyed nearly all of Malden Mills's textile plant in Lawrence, Massachusetts, leaving 3,000 employees with nowhere to work. Milling around in the parking lot during the fire, most of the workers thought their jobs were gone forever, but those standing near then owner and CEO Aaron Feuerstein heard him say, "This is not the end."

For three months after the fire, Feuerstein attracted massive media attention for spending millions of dollars to keep all of his 3,000 employees on payroll with full benefits. Feuerstein explained his action as an investment: "I consider our workers an asset, not an expense — I have a responsibility to the worker, both blue-collar and white-collar." He also explained his rationale for maintaining the mill's location in Lawrence, rather than moving to the South or overseas in search of lower labor costs. "I have an equal responsibility to the community. It would have been unconscionable to put 3,000 people on the streets and deliver a death blow to the cities of Lawrence and Methuen." His investment paid off: plant production pre-fire was 130,000 yards per week; post-fire it increased to 230,000 yards.

Feuerstein has faced a second leadership challenge within the past year, as he struggled to lead the company out of bankruptcy. As part of a deal worked out with lenders Feuerstein has recently stepped down from his position as CEO, but he hopes to buy the company back in the future.[50]

John Mackey, Whole Foods Market

Depending on who you talk to, grocery store chain Whole Foods Market is a model of enlightened, bottom-up management or a fiercely anti-worker employer hostile to unions. The truth is apparently a bit of both. While Whole Foods Market CEO John Mackey aggressively fights efforts to unionize the

"I rejected my bonus because we had a couple of years where we hadn't performed up to our standards."

— Costco CEO James Sinegal

company's grocery stores, he also eschews the typical executive-suite perks and limits his salary to no more than 14 times the pay of the average frontline employee. In addition, all employees can qualify for stock options, and the company says that 94 percent of them go to nonexecutive staff. The Whole Foods example prompts this question: If this particular anti-union CEO can see the benefits of limiting his own pay, why do so few of his fellow CEOs at other corporations do the same?

Richard Kinder, Kinder Morgan Energy Partners

No question about it, Rich Kinder is rich. The former Enron president (he quit in 1996) was already a multi-millionaire when he formed Kinder Morgan Energy Partners with his college friend, William Morgan. Although Kinder ranks 356th among the world's richest people,[51] he accepts no extra perks for his work at Kinder Morgan. The 5-year CEO collects a $1 annual salary with no bonus, no stock options, no restricted shares. Kinder does own roughly 20 percent of the company, but has never sold any of his shares, which are now valued at $1.6 billion.[52] You might, however, never guess his billion-dollar net-value: Kinder avoids executive excesses like exclusive facilities and other perks, instead staying in economy hotels, and flying coach class when traveling. "There is just no rational reason why I deserve anything more," he explains.[53]

James Sinegal, Costco Wholesale Corp.

When James Sinegal, CEO of Costco Wholesale, claims to have an "open door" policy, he's not kidding. In fact, his office doesn't even have a door — or walls, for that matter. Sinegal has rejected many of the excessive CEO perks that have come to symbolize top-dog status at U.S. companies. A simple partition separates his work area from his co-workers, and Sinegal fields all of his incoming calls rather than relying upon an administrative assistant.[54]

Sinegal believes in reasonable pay, both for himself and his employees. Concerning his workers' pay packages ($41,000 plus health benefits for a full-time clerk), he explains, "I don't see what's wrong with an employee earning enough to be able to buy a house or having a health plan for the family."[55] Sinegal himself receives $350,000 in salary, about eight and a half times as much as that full-time clerk and roughly double the salary of a Costco warehouse manager. He thinks the salaries of some chief executives are outrageous and obscene: "It's difficult for people who are working for a living to understand [high CEO pay]," he says.

As Sinegal himself points out, "Bear in mind I have been rewarded by the stock;" in 2003 he cashed in $1.5 million worth of stock options. But he doesn't accept perks where they aren't warranted, continuing, "I rejected my bonus because we had a couple of years where we hadn't performed up to our standards. We were more profitable than the year before, but we didn't hit the standards we had set for ouselves, so we didn't think we were entitled."[56]

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CEO Pay Resources

The reports listed below are available online at www.FairEconomy.org.

Executive Excess 2003: CEOs Win, Workers and Taxpayers Lose. CEOs at companies with the largest layoffs, most underfunded pensions and biggest tax breaks were rewarded with bigger paychecks.

More Bucks for the Bang: CEO Pay at Top Defense Contractors. CEOs at the nation's largest military contractors rose 79 percent in 2002, compared to a six percent increase for typical CEOs.

Executive Excess 2002: CEOs Cook the Books, Skewer the Rest of Us. Finds that CEOs of companies under investigation for accounting irregularities earned 70 percent more from 1999 to 2001 than the average CEO at large companies.

Titans of the Enron Economy: The 10 Habits of Highly Defective Corporations, April, 2002. This prescient report showed how many of the problems dramatically revealed by the Enron scandal are woven tightly into the fabric of American business. It ranked the worst companies in 10 areas and gave Enny Awards to companies with Enronesque behavior, including General Electric, Citigroup, AOL TimeWarner, WorldCom and Halliburton. Includes 12-step program for breaking Enronesque habits.

Executive Excess 2001, August, 2001. Among the findings: Job-cutting CEOs made higher than average salaries in 2000 amid layoffs and a slumping stock market. CEOs at companies that paid zero corporate taxes got larger raises than the average CEO.

The Bigger They Come, The Harder They Fall, April, 2001. A seven-year survey of the dismal financial return to investors in companies with high CEO pay.

Executive Excess 2000, August, 2000. Updates the decade-long trends in CEO pay, charts the explosion in executive pay at dot-com companies, and highlights the huge, and growing gap in pay between private-sector CEOs and their counterparts in the federal government.

A Decade of Executive Excess: The 1990s, September, 1999. This edition focused on major trends of the decade, economic arguments against exorbitant CEO pay, the most undeserving CEOs of the decade, and a survey of what can be done.

Executive Excess 1998: CEOs Gain From Massive Downsizing, April, 1998. Focuses on layoff leaders, international banking executives, job-shifters to Mexico, and the citizens' response to runaway executive pay.

Executive Excess 1997: CEOs Gain From Massive Downsizing, May, 1997. Focuses on layoff leaders and efforts to close the wage gap.