

# IT'S GOOD TO BE THE KING CFO

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As the American economy sinks, Chief Financial Officers these days are having to look at whole lots of unpalatable numbers. But there's one set of numbers they still find thrilling to examine: Their own pay.

Using data supplied by Equilar Inc., I analyzed the 2007 total pay packages of 578 CFOs, all of whom were working in companies with \$3 billion or more of market cap at the time I performed the study.

Here's a few basic facts:

- Base salaries ranged from \$100,000 in the case of Jordan Gates of Seattle-headquartered Expeditors International of Washington Inc. to the \$2.9 million paid to David Devoe of New York-based News Corp. The median and average base salaries were, respectively, \$470,000 and \$496,000.
- Total cash compensation (the sum of base salary and annual bonus) ranged from the \$150,000 paid to Thomas Szkutak of Seattle-headquartered Amazon.com Inc. to the \$23.2 million paid to David Viniar of New York-headquartered Goldman Sachs Group Inc. The median and average total cash compensation levels were, respectively, \$931,000 and \$1.2 million.
- In total pay, the bottom of the totem pole was once again anchored by Mr. Szkutak of Amazon. He earned just \$153,000. On a really clear day, and with a powerful set of binoculars, he might have been able to glimpse the \$44.5 million pulled down by Mr. Viniar of Goldman.

## How Total Pay Is Defined

A few words on what I mean by "total pay". It is the sum of:

- Base salary.
- Bonus for annual performance.
- The value at grant of free shares granted during the year.
- The estimated present value at grant (using the Black-Scholes model) of stock options granted during the year.

- The “target” value of prospectively-granted performance shares or units granted during the year.
- The present value of pension accruals made during the year.
- And, as defined by the U.S. Securities and Exchange Commission, miscellaneous compensation.

My figures often differ from the total pay figures listed in the Summary Compensation Table (SCT) in companies’ proxy statement. That’s because the figures for the value of stock option and free share awards included in the SCT are based on accruals made for the year.

For an illustration here, consider that in 2004, 2005 and 2006, Company A gave its CFO option grants, which in each case had a present value of \$10 million at the time of the grant. Each option was exercisable in four annual installments. In 2007, the company did not give its CFO an option grant. In its SCT, the company would record option values for 2007 of \$7.5 million, consisting of one-fourth of the 2004 option award, one-fourth of the 2005 award and one-fourth of the 2006 award. For my part, I would record \$0 option value, because I focused only on the awards made in 2007 – or in this case, the non-award made in 2007.

The reverse can happen, of course. Suppose a CFO joined his company in 2007 from the outside. And when he joined, he received an option with a present value at grant of \$10 million, and with 25 percent per year vesting. The SCT would show the value of his option award to be \$2.5 million, consisting of one-quarter of his \$10 million award for 2007. There would have been no accrued charges for earlier years because the CFO was not an employee in those earlier years. For my part, I would show the value of his option award at \$10 million, the full present value of his 2007 grant.

I believe that my methodology presents a much clearer window on the actions of a board compensation committee in a single year.

### Explaining Differences in CFO Pay

So what explains why one CFO earns \$153,000 in total pay and another one earns \$44.5 million?

You can explain 33 percent of the variation in CFO total pay if you control for two factors:

- The size of the company, as measured by its 2007 sales.
- The pay risk in the CFO’s pay package. My proxy for pay risk is the ratio of stock option present value to total pay. It is based on the assumption that the most risky part of a CFO’s pay package lies in the stock option area, since it is almost always the case that one cannot earn anything from that form of compensation unless the company’s stock price rises.

If I can explain 33 percent of the variation in CFO total pay using those two factors, that means that 67 percent of the variation remains unexplained.

One factor that does not explain a statistically-significant amount of variation in total pay is the so-called excess return of the company, i.e., its actual total return in its 2007 fiscal year less the total return on the Standard & Poor's 500 Index. So much for pay-for-performance!

But there's another factor that actually explains more of the variation in CFO total pay than does the combination of sales and pay risk. And that is the extent to which the CFO's boss, the chief executive officer, earns more or less than a competitive figure compared to other CEOs and based on the same two factors.

In other words, the more the CEO is overpaid, the more likely it is that the CFO will be overpaid, too. And vice versa.

That factor, by itself, accounts for 37 percent of the variation in CFO pay packages.

Think here of the CEO's pay as being the equivalent of a 4,000-h.p. vacuum cleaner, which sucks into its nozzle any pay package that gets close to the nozzle. Unfortunately, even a 4,000-h.p. vacuum cleaner is not powerful enough to even flutter the shirt of a front-line worker.

In turn, that means that overpaying a CEO does not measure the full extent of damage visited on a company's shareholders. Overpay the CEO, and you likely overpay quite a few others, too.

Herewith are three tables. The first presents the 30 most relatively-highly-paid CFOs. The second presents the 30 most relative-lowly-paid CFOs. In each case, I am comparing the CFO's 2007 total pay to a multiple regression result, which controls for both company size and pay risk. (I did not take account of whether or not the CEO was overpaid, because that would be incestuous.)

Please scroll down to view this table.

## THE 30-MOST RELATIVELY-HIGHLY-PAID CFOs:

COMPANY	CFO	ACTUAL TOTAL PAY (000)	PERCENT DEVIATION
GOLDMAN SACHS GROUP INC	VINIAR, DAVID	\$44,458	612%
COMCAST CORP	ANGELAKIS, MICHAEL	\$25,762	533%
CITIGROUP INC	CRITTENDEN, GARY	\$37,122	524%
CYPRESS SEMICONDUCTOR CORP	BUSS, BRAD	\$9,097	481%
BOSTON SCIENTIFIC CORP	LENO, SAM	\$19,941	393%
BANK OF NEW YORK MELLON CORP	VAN SAUN, BRUCE	\$15,620	340%
TYCO INTERNATIONAL LTD	COUGHLIN, CHRISTOPHER	\$15,616	245%
EMERSON ELECTRIC CO	GALVIN, W. J.	\$11,279	234%
CROWN CASTLE INTERNATIONAL CORP	MORELAND, BENJAMIN	\$4,980	231%
PLAINS EXPLORATION & PRODUCTION	TALBERT, WINSTON	\$4,824	229%
GOOGLE INC.	REYES, GEORGE	\$14,928	228%
CROWN HOLDINGS INC	RUTHERFORD, ALAN	\$7,693	211%
SPX CORP	O'LEARY, PATRICK	\$6,115	183%
MOTOROLA INC	MEREDITH, THOMAS	\$12,699	174%
COMMUNITY HEALTH SYSTEMS INC	CASH, W. LARRY	\$9,329	173%
ANNALY CAPITAL MANAGEMENT INC	FAGAN, KATHRYN	\$4,959	173%
NEWS CORP	DEVOE, DAVID	\$9,577	165%
CBS CORP	REYNOLDS, FREDRIC	\$11,195	161%
PFIZER INC	D'AMELIO, FRANK	\$12,042	161%
MORGAN STANLEY	KELLEHER, COLM	\$14,993	153%
PROGRESS ENERGY INC	SCOTT III, PETER	\$6,563	153%
AMERICAN CAPITAL STRATEGIES LTD	ERICKSON, JOHN	\$4,464	150%
VERTEX PHARMACEUTICALS INC	SMITH, IAN	\$3,348	150%
ALLIED CAPITAL CORP	ROLL, PENNI	\$2,904	139%
APOLLO GROUP INC	D'AMICO, JOSEPH	\$8,886	133%
ST JOE CO	MCCALMONT, WILLIAM	\$2,927	131%
NATIONWIDE HEALTH PROPERTIES	KHOURY, ABDO	\$2,444	130%
NORTHROP GRUMMAN CORP	PALMER, JAMES	\$9,207	129%
OMNICOM GROUP INC	WEISENBURGER, RANDALL	\$6,518	128%
ANADARKO PETROLEUM CORP	WALKER, R.A.	\$7,723	128%

Please scroll down for the next table.

## THE 30-MOST RELATIVELY-LOWLY-PAID CFOs:

COMPANY	CFO	ACTUAL TOTAL PAY (000)	PERCENT DEVIATION
STARBUCKS CORP	CASEY, MICHAEL	\$811	-69%
M&T BANK CORP	JONES, RENE	\$976	-69%
ILLINOIS TOOL WORKS INC	KROPP, RONALD	\$1,488	-70%
ENTERPRISE PRODUCTS PARTNERS	FOWLER, RANDALL	\$1,021	-70%
HERTZ GLOBAL HOLDINGS INC	DOUGLAS, ELYSE	\$1,129	-70%
WEYERHAEUSER CO	BEDIENT, PATRICIA	\$1,269	-71%
COMMERCE BANCSHARES INC	CLARK, BAYARD	\$559	-71%
OFFICE DEPOT INC	MCKAY, PATRICIA	\$1,466	-72%
MASSEY ENERGY CO	TOLBERT, ERIC	\$567	-72%
OLD REPUBLIC INTERNATIONAL	MUELLER, KARL	\$700	-72%
HOST HOTELS & RESORTS, INC.	HARVEY, LARRY	\$618	-72%
PEPCO HOLDINGS INC	BARRY, PAUL	\$712	-73%
WHOLE FOODS MARKET INC	CHAMBERLAIN, GLENDA	\$680	-73%
SEAGATE TECHNOLOGY	POPE, CHARLES	\$725	-75%
C H ROBINSON WORLDWIDE INC	LINDBLOOM, CHAD	\$617	-75%
CARNIVAL CORP	BERNSTEIN, DAVID	\$697	-76%
O REILLY AUTOMOTIVE INC	MCFALL, THOMAS	\$526	-77%
WALGREEN CO	RUDOLPHSEN, WILLIAM	\$1,239	-79%
TESORO CORP	SCHWETHELM, OTTO	\$996	-79%
SOUTHWEST AIRLINES CO	WRIGHT, LAURA	\$535	-80%
WATSON PHARMACEUTICALS INC	DURAND, MARK	\$357	-80%
NVR INC	SEREMET, DENNIS	\$437	-80%
EQUITY RESIDENTIAL	PARRELL, MARK	\$409	-80%
HORTON D R INC	WHEAT, BILL	\$529	-81%
TEPPCO PARTNERS LP	MANIAS, WILLIAM	\$586	-83%
ONEOK PARTNERS LP	DINAN, CURTIS	\$384	-83%
RELIANT ENERGY INC	DOBSON, RICK	\$665	-84%
BERKSHIRE HATHAWAY INC	HAMBURG, MARC	\$724	-87%
HOSPITALITY PROPERTIES TRUST	KLEIFGES, MARK	\$145	-90%
AMAZON COM INC	SZKUTAK, THOMAS	\$153	-95%

By scrolling down once more, you can view a third table, showing some examples of the close relationship between overly high or overly low CEO pay and overly high or overly low CFO pay. The percentile rank refers to the positioning of the actual pay to the competitive pay predicted by my pay models. If an executive's actual pay were equal to his competitive pay, his percentile rank would be 50, or at the median. A percentile rank of 100 means that, relative to other executives, and after controlling for company size and pay risk, the CEO or CFO is the most highly-paid executive in my study. And, of course, a percentile rank of 0 means just the opposite.

COMPANY	CFO	CEO PERCENTILE RANK	CFO PERCENTILE RANK
OCCIDENTAL PETROLEUM CORP	IRANI, RAY	100	100
CYPRESS SEMICONDUCTOR CORP	RODGERS, THURMAN	100	100
PEOPLE'S UNITED FINANCIAL, INC	SHERRINGHAM, PHILIP	98	100
GOLDMAN SACHS GROUP INC	BLANKFEIN, LLOYD	97	100
TYCO INTERNATIONAL LTD	BREEN, EDWARD	96	99
NEWS CORP	MURDOCH, RUPERT	96	98
MORGAN STANLEY	MACK, JOHN	96	97
EMERSON ELECTRIC CO	FARR, DAVID	94	99
BANK OF NEW YORK MELLON CORP	KELLY, ROBERT	93	100
SPX CORP	KEARNEY, CHRISTOPHER	90	98
CROWN HOLDINGS INC	CONWAY, JOHN	89	99
DEVELOPERS DIVER. REALTY CORP	WOLSTEIN, SCOTT	100	96
PLAINS EXPLOR. & PROD. CO	FLORES, JAMES	100	99
ALLIED CAPITAL CORP	WALTON, WILLIAM	99	96
ANADARKO PETROLEUM CORP	HACKETT, JAMES	96	96
HEALTH NET INC	GELLERT, JAY	95	89
STATE STREET CORP	LOGUE, RONALD	94	92
COCA COLA CO	ISDELL, NEVILLE	90	81
US BANCORP	DAVIS, RICHARD	5	5
URBAN OUTFITTERS INC	SENK, GLEN	4	4
O REILLY AUTOMOTIVE INC	HENSLEE, GREG	2	1
WALGREEN CO	REIN, JEFFREY	1	1
TEPPCO PARTNERS LP	THOMPSON, JERRY	1	0
HOST HOTELS & RESORTS, INC.	WALTER, EDWARD	1	3
M&T BANK CORP	WILMERS, ROBERT	1	4
ENTERPRISE PROD. PARTNERS L P	CREEL, MICHAEL	0	3
SOUTHWEST AIRLINES CO	KELLY, GARY	0	1