

WorldatWork Research

# Executive Compensation Case Studies: A Supplement to the WorldatWork Executive Rewards Questionary



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# Introduction

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In 2007, the all-volunteer Executive Rewards Advisory Board of WorldatWork, a group of practitioners working in the executive compensation field, came together to produce the *WorldatWork Executive Rewards Questionary: Optimize Executive Compensation Design*. WorldatWork was proud to publish this interactive dictionary of questions, which contained more than 200 important queries to be considered by practitioners, consultants and compensation committee members when creating or modifying an executive pay package.

This WorldatWork sponsored research report responds to a question that was posed since the publication of the *Questionary*: Would the use of this one-of-a-kind tool have had any effect on some of the highly publicized and embarrassing executive compensation situations of the past decade. The simple answer, as shown in this report, is yes.

This report is designed to illustrate specific, real-world corporate examples of how compensation plans may have differed had the *Questionary* been consulted. It includes 10 case studies taken straight from the headlines of the past 10 years. As in the *Questionary* itself, the questions contained here are grouped into four primary areas:

- Internal environment
- External environment
- Stakeholders
- Disclosure and transparency.

## About the Questionary

Today's practitioners who are responsible for designing compensation plans are working under a microscope as they never have before. They must navigate an intricate system of diverse global business criteria while weighing internal and external competitiveness, accounting for investor and media reaction, and complying with a multitude of regulatory disclosure and transparency requirements. The *WorldatWork Executive Rewards Questionary*, or list of key questions to consider in the design and implementation of executive pay systems, was created for these practitioners. It is the one and only comprehensive list of questions that should be reviewed and carefully considered when either creating or modifying an executive pay plan.

The questions in the *Questionary* cover more than 225 issues that are critical for consideration while planning or modifying a company's executive compensation plan. It includes issues that might arise in aligning compensation with business strategy, regulatory issues, socioeconomic factors, disclosure and transparency rules, communication plans, labor and market pay trends, and even community concerns. Additionally, the credibility and effective administration of an executive compensation plan is supported in the *Questionary* by presenting questions related to external stakeholders and disclosure and transparency. These questions support the notion that time spent to fully think through and develop an effective communication program can be as critical to plan success as the plan itself. ●

# Case Studies

## FANNIE MAE

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In late 2004, both the CEO and CFO stepped down after the company restated earnings by roughly \$10 billion due to accounting irregularities. The departures were publicly referred to as “retirements.” The CEO and CFO received the same severance and retirement packages they would have had they left with unflawed performance records.

### Internal Environment

- How is compensation perceived by employees (fairness, reasonableness)?
- To what extent is the legal department involved in compensation planning, design, administration and disclosure?

### External Environment

- Can opposition by interest groups have a broader effect on your company?
- Have you alerted the appropriate resources (community/media relations/governmental affairs) within the company that this plan may elicit communities'/social or political activists' scrutiny?

- Are there particular communities/social or political activists that will react to this plan?
- How do you anticipate the media will react to this program?

### Stakeholders

- Has the committee consultant been briefed about the proposed program or issue?
- Will other employees perceive this program as fair?

### Disclosure & Transparency

- Have you met with appropriate internal and/or external resources (legal, tax, accounting, audit, HR, shareholder relations, consultant, other) to identify and address disclosure requirements?

The executive compensation program approved by the board included a special option program that granted options to executives that immediately vested once an earnings-per-share goal was met.

The board also gave the freedom to executives to sell vested options and shares at any time, allowing the CFO to collect on the sale of his shares despite the restatement of earnings.

### Internal Environment

- How does expected performance relate to the current business outlook?
- What are the results that need to be achieved in the short and long term?
- Is the legal department comfortable with this design in the current legal/regulatory environment?

### External Environment

- Will this information become public knowledge?

### Stakeholders

- What are shareholder expectations about your compensation programs, and how do they affect plan design?

- Is senior management prepared to support and communicate this program or issue?
- What is the likely perspective of shareholder advocates on this program or issue?
- How and when will you disclose this plan to shareholders (proxy, 10Q/10K)?
- Has the committee consultant been briefed about the proposed program or issue?
- Has the compensation committee/board of directors reviewed similar compensation programs or issues in the past?
- Will the general employee population perceive this program as fair?
- Are compensation committee members/board of director members familiar with similar programs or issues?
- What tools and processes are in place to support compensation committee decision making (e.g., tally sheets)?

#### Disclosure & Transparency

- Have you provided the context/rationale for why certain elements exist in the program and others don't?

In 2004, Fannie Mae chose not to disclose the total value of the CEO and CFO retirement packages in its annual proxy statements.

#### External Environment

- Are there special interest groups that will react to this plan design?
- Are there particular communities/social or political activists that will react to this plan?
- Will this information become public knowledge?

#### Stakeholders

- How and when will you disclose this plan to shareholders (proxy, 10Q/10K)?

#### Disclosure & Transparency

- What is the company's philosophy regarding transparent disclosure in the proxy statement (e.g., minimally compliant versus full disclosure and effective communications)?
- What is the company's position on appropriate level of transparency (disclosing more than is required, simplification of written communications)? ●

## COMPUTER ASSOCIATES INC.

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The CEO and other executives of Computer Associates were granted board and shareholder approval in 1995 for an executive compensation plan that allowed executives to collect stock grants if the common stock price maintained a given price for 60 days. In early 1998 the stock did, and the executives collected their shares. Shortly after collecting their grants, the company announced that its revenue estimates were to be reduced by \$100 million for the next two quarters. The stock lost two-thirds of its value the next day.

### Internal Environment

- How does expected performance relate to the current business outlook?
- What are the results that need to be achieved in the short and long term?

### External Environment

- What are the current economic conditions for your company/industry?
- Are economic trends improving or declining?
- What negative economic results would cause this program not to fund/payout in the first year?

- Are there particular communities/social or political activists that will react to this plan?
- To what extent do you want to match or differ from market pay practices?
- How do you anticipate the media will react to this program?

### Stakeholders

- What is the likely perspective of shareholder advocates on this program or issue?
- Will the general employee population perceive this program as fair?

The plan failed to include a provision that adjusted the number of shares issued after accounting for stock splits and other changes in the organization's capital structure. One source indicated this could have been avoided if appropriate people had developed the contract language.

### Internal Environment

- What is the role of finance/accounting in plan design?
- Has your accounting division reviewed this program design from an accounting treatment perspective?
- Is the legal department comfortable with this design in the current legal/regulatory environment?

### Stakeholders

- What is the likely perspective of shareholder advocates on this program or issue?

- Does the compensation committee employ an independent compensation consultant?
- Has the compensation committee/board of directors reviewed similar compensation programs or issues in the past?
- Are compensation committee members/board of director members familiar with similar programs or issues?

The cash bonus-to-salary ratio was unusually high for a company with average performance, such as Computer Associates. At the time, high performing software companies generally had a ratio of 1:3 but Computer Associates had a ratio of 1:5.

#### Internal Environment

- What is the compensation philosophy and objectives? What about market orientation and peer groups?

#### External Environment

- What are market pay practices?

#### Stakeholders

- Is senior management prepared to support and communicate this program or issue? ●
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## NEW YORK STOCK EXCHANGE

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In May 2004, New York attorney general filed a lawsuit against the former CEO and a former director of the New York Stock Exchange (NYSE). The suit was for violation of New York's Not-for-Profit Corporation Law relating to "reasonable" compensation. The CEO's retirement plan built to more than \$139.5 million during his 36-year tenure. He was also due to receive \$48 million in deferred pay over the next four years.

### External Environment

- What regulatory jurisdictions are you subject to?
- Have you alerted the appropriate resources (community/media relations/governmental affairs) within the company that this plan may elicit communities/social or political activists' scrutiny?
- What regulations govern the type of program you are designing?
- Are there particular communities/social or political activists that will react to this plan?
- How do you anticipate the media will react to this program?

### Stakeholders

- Has the committee been adequately prepared to discuss this program or issue in previous meetings?
- Does the committee employ an independent compensation consultant?
- What tools and processes are in place to support compensation committee decision making (e.g., tally sheets)?

### Disclosure & Transparency

- What is the company's position on appropriate level of transparency (disclosing more than is required, simplification of written communications)?

The compensation committee set the CEO's compensation based upon two factors:

- Median compensation paid to CEOs of a select group of peers
- Assessment of NYSE performance.
- But many of the companies chosen for comparison were not comparable in size, revenue or complexity. In addition, the CEO allegedly picked the members of the compensation committee, whose companies were often listed on the exchange.

### Internal Environment

- To what degree does the compensation philosophy align with corporate strategy, culture and organizational resources?
- What are the results that need to be achieved in the short and long term?

### External Environment

- What are market pay practices?
- To what extent do you want to match or differ from market pay practices?
- Will this information become public knowledge?

### Stakeholders

- If the committee has not been adequately prepared, can the committee review and consider this program or issue in a single meeting?
- Are committee members familiar with similar programs or issues?
- Has the committee been adequately prepared to discuss this program or issue in previous meetings?
- Does the committee employ an independent compensation consultant?
- Will the general employee population perceive this program as fair?

- What tools and processes are in place to support compensation committee decision making (e.g., tally sheets)?

### Disclosure & Transparency

- Have you provided the context/rationale for why certain elements exist in the program and others don't?

In the lawsuit, the director was charged with “misleading the NYSE board about the amount of annual compensation the committee was recommending to be approved by the board.”

### Stakeholders

- Has the committee been adequately prepared to discuss this program or issue in previous meetings?
- Does the committee employ an independent compensation consultant?
- Has the compensation committee/board of directors reviewed similar compensation programs or issues in the past?

- Are compensation committee members/board of director members familiar with similar programs or issues?
- What tools and processes are in place to support compensation committee decision making (e.g., tally sheets)? ●

## WORLD.COM

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**B**etween 2000 and 2002 WorldCom CEO Bernard Ebbers obtained unsecured loans amounting to 20 percent of the firm's cash, allegedly at interest rates well below the market rates for large margin loans. Upon leaving the organization, Ebbers still owed \$408 million.

WorldCom subsequently entered bankruptcy and the share price dropped dramatically. Ebbers was then unable to pay back the loan by selling his shares, as he had allegedly planned.

### Internal Environment

- Do you have the necessary systems to operationalize and administer this program?
- Are there key stakeholders or influencers (HR, legal, tax) that need to be part of the program development process?
- Is your finance/accounting department prepared to support any special reporting requirements for this program?
- What are your governance ratings?
- What is the role of finance/accounting in plan design?
- Do you know what financial constraints may affect program design?
- What are your key business objectives and strategic drivers?
- To what extent is the legal department involved in compensation design, administration and disclosure?
- What are the results that need to be achieved in the short and long term?
- Is the legal department comfortable with this design in the current legal/regulatory environment?

### External Environment

- What is the current accounting treatment for this program?

- What regulatory jurisdictions are you subject to?
- What regulations govern the type of program you are designing?
- Are there particular communities/social or political activists that will react to this plan?
- To what extent do you want to match or differ from market pay practices?

### Stakeholders

- Will this program have a negative effect on other programs?
- Will the general employee population perceive this program as fair?

### Disclosure & Transparency

- Have you met with appropriate internal and/or external resources (legal, tax, accounting, audit, HR, shareholder relations, consultant, other) to identify and address disclosure requirements?
- Have you provided the context/rationale for why certain elements exist in the program and others don't?
- What is the company's position on appropriate level of transparency (disclosing more than is required, simplification of written communications)?

If the compensation committee had secured the loans, Ebbers' shares might have been seized in order to sell them to cover the loan when the stock price was still high enough to do so.

#### Internal Environment

- To what extent is the legal department involved in compensation planning, design, administration and disclosure?

#### Stakeholders

- Has the committee been adequately prepared to discuss this program or issue in previous meetings?
- Does the committee employ an independent compensation consultant?

- Has the compensation committee/board of directors reviewed similar compensation programs or issues in the past?
  - Are compensation committee members/board of director members familiar with similar programs or issues?
  - What tools and processes are in place to support compensation committee decision making (e.g., tally sheets)? ●
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## WALT DISNEY CO.

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In 2003, Walt Disney Co. shareholders filed a lawsuit relating to the \$140 million severance package paid to the former the president. Shareholders contended that the directors knowingly or intentionally “breached their fiduciary duty of due care in approving (the president’s) employment agreement,” and failed to consider the terms of the termination — which was allegedly negotiated exclusively by the CEO.

Although the court agreed with shareholders that the CEO had exclusively negotiated the deal and orchestrated the president’s hire without input from the board of directors, it found that neither he nor the other directors breached their fiduciary duty.

### Internal Environment

- What is the process for developing responses and communicating with shareholders?
- To what degree does the compensation philosophy align with corporate strategy, culture and organizational resources?

### Stakeholders

- What are shareholder expectations about your compensation programs and how do they affect program design?
- How and when will you disclose this plan to shareholders?

- Has the committee consultant been briefed about the proposed program or issue?
- Has the committee been adequately prepared to discuss this program or issue in previous meetings?
- Are compensation committee members/board of director members familiar with similar programs or issues?

### Disclosure & Transparency

- What is the company’s position on appropriate level of transparency (disclosing more than is required, simplification of written communications)?

The court did, however, “criticize the members of the compensation committee for not doing more to inform themselves of the terms of Ovitz’s employment agreement and to become involved in the review and approval process.

### Internal Environment

- Has the committee consultant been briefed about the proposed program or issue?

### External Environment

- Are there particular communities/social or political activists that will react to this plan?
- To what extent do you want to match or differ from market pay practices?
- Will this information become public knowledge?
- How do you anticipate the media will react to this program?

### Stakeholders

- Is senior management prepared to support and communicate this program or issue?
- Has the compensation committee/board of directors reviewed similar compensation programs or issues in the past?
- Are compensation committee members/board of director members familiar with similar programs or issues?
- What tools and processes are in place to support compensation committee decision making (e.g., tally sheets)? ●

## THE HOME DEPOT

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In 2000, the new CEO of The Home Depot entered into an employment contract that eventually awarded him more than \$200 million during a five-year period. A portion of this amount was given to the CEO in the form of a guaranteed annual bonus of at least \$3 million a year. The provision of a guaranteed minimum annual bonus is considered rare by industry standards — a study by the Delves Group indicates that The Home Depot CEO was the only CEO of the 200 largest U.S. revenue companies to have such an agreement. While examples of guaranteed payment exist, the length and size of the payments is considered uncommon.

### Internal Environment

- How does expected performance relate to the current business outlook?
- What are the results that need to be achieved in the short and long term?

### External Environment

- What is the likely perspective of shareholder advocates on this program or issue?
- Has the committee consultant been briefed about the proposed program or issue?
- Are there particular communities/social or political activists that will react to this plan?
- To what extent do you want to match or differ from market pay practices?
- Will this information become public knowledge?
- How do you anticipate the media will react to this program?
- To what extent do you want to match or differ from market pay practices?

### Stakeholders

- Is senior management prepared to support and communicate this program or issue?
- Have you alerted the appropriate resources (community/media relations/governmental affairs) within the company that this plan may elicit communities'/social or political activists' scrutiny?
- Has the compensation committee/board of directors reviewed similar compensation programs or issues in the past?
- Are compensation committee members/board of director members familiar with similar programs or issues?

### Disclosure & Transparency

- What is the company's position on appropriate level of transparency (disclosing more than is required, simplification of written communications)?

In 2005, the CEO received his guaranteed bonus while the amount of money allotted to the nonsalaried employee bonus program decreased by 50 percent.

### External Environment

- Will this information become public knowledge?

### Stakeholders

- How and when will you disclose this plan to shareholders (proxy, 10Q/10K)?
- Will the general employee population perceive this program as fair?

### Disclosure & Transparency

- What is the company's philosophy regarding transparent disclosure in the proxy statement (e.g., minimally compliant versus full disclosure and effective communications)? ●

## ENRON CORP.

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In the late 1990s and into 2001, Enron Corp. provided its executives with compensation packages that included equity stakes in business units. Although many companies use equity in rewards programs, the amounts provided to Enron executives were unusually large (greater than 5 percent) and not tied to long-term performance because executives were allowed to convert their equity into either common stock or receive cash. The CEO and president of a subsidiary received more than \$310 million by converting equity stakes into cash.

### Internal Environment

- What is your corporate strategy?
- What are your key business objectives and strategic drivers?
- How do these short-term objectives (tactical) align with/drive long-term objectives (strategic)?
- What are major challenges to achieving strategic objectives/milestones?
- Do you know what financial constraints may affect program design?
- How does expected performance relate to the current business outlook?
- Has your accounting division reviewed this program design from an accounting treatment perspective?
- What are the results that need to be achieved in the short and long term?
- Is the legal department comfortable with this design in the current legal/regulatory environment?

### External Environment

- Are there particular communities/social or political activists that will react to this plan?
- To what extent do you want to match or differ from market pay practices?
- Will this information become public knowledge?
- How do you anticipate the media will react to this program?

### Stakeholders

- What is the likely perspective of shareholder advocates on this program or issue?
- Has the committee been adequately prepared to discuss this program or issue in previous meetings?
- Does the committee employ an independent compensation consultant?
- Has the compensation committee/board of directors reviewed similar compensation programs or issues in the past?
- Are compensation committee members/board of director members familiar with similar programs or issues?

In addition to the equity stakes, Enron rewarded two executives large cash bonuses of \$54 million and \$42 million.

#### Internal Environment

- Do you know what financial constraints may affect program design?
- What are your key business objectives and strategic drivers?

#### External Environment

- Will the general employee population perceive this program as fair?

- To what extent do you want to match or differ from market pay practices?
- How do you anticipate the media will react to this program?

#### Disclosure & Transparency

- What is the company's philosophy regarding transparent disclosure in the proxy statement (e.g., minimally compliant versus full disclosure and effective communications)?

The chairman/chief executive of a subsidiary allegedly received a 20-percent stake in his unit, thus becoming a minority owner. He eventually converted his stake into more than \$20 million in cash before leaving the company. The executive's stake, however, was not listed on any company's proxy filings, despite the fact that the stake diluted the value of the shareholders' investments.

#### Internal Environment

- Has your accounting division reviewed this program design from an accounting treatment perspective?
- Is the legal department comfortable with this design in the current legal/regulatory environment?

#### External Environment

- To what extent do you want to match or differ from market pay practices?

#### Stakeholders

- Has the board's external adviser received the same materials as the committee, and has he/she had sufficient time to review them?
- How and when will you disclose this plan to shareholders?
- Does the committee employ an independent compensation consultant?
- What tools and processes are in place to support compensation committee decision making (e.g., tally sheets)?

#### Disclosure & Transparency

- Have you met with appropriate internal and/or external resources (legal, accounting, HR, shareholder relations, consultant, other) to prepare the proxy?
- Have you met with appropriate internal and/or external resources (legal, tax, accounting, audit, HR, shareholder relations, consultant, other) to identify and address disclosure requirements?
- What is the company's philosophy regarding transparent disclosure in the proxy statement (e.g., minimally compliant versus full disclosure and effective communications)?
- What is the company's position on appropriate level of transparency (disclosing more than is required, simplification of written communications)? ●

## GE

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In 2002, the details of the former CEO's retirement package was revealed in a divorce court filing. The CEO's wife claimed that he had received approximately \$2.5 million in benefits during the prior year, including use of GE aircraft for personal travel, use of a New York City apartment, use of a chauffeured limousine, office space in New York City and Connecticut, estate and tax advisers, a personal assistant, a communications system and other benefits. The former CEO subsequently asked GE to modify the contract and eliminate everything except the office and administrative support, which had been standard for all retired GE chairmen.

### External Environment

- Have you alerted the appropriate resources (community/media relations/governmental affairs) within the company that this plan may elicit communities'/social or political activists' scrutiny?
- Have you met with appropriate internal and/or external resources (legal, tax, accounting, audit, HR, shareholder relations, consultant, other) to identify and address disclosure requirements?
- Are there particular communities/social or political activists that will react to this plan?
- To what extent do you want to match or differ from market pay practices?
- Will this information become public knowledge?
- How do you anticipate the media will react to this program?

### Stakeholders

- Will this program or issue be considered a sensitive topic for your senior management team?
- What is the likely perspective of shareholder advocates on this program or issue?
- Has the committee consultant been briefed about the proposed program or issue?
- Has the compensation committee/board of directors reviewed similar compensation programs or issues in the past?
- Are compensation committee members/board of director members familiar with similar programs or issues?

After the details of the retirement benefits were revealed, the SEC announced an informal investigation, with an allegation that the company failed to fully disclose the scope of the plan. The company contended that it had provided appropriate information about the CEO's perquisites in its proxy statements and annual reports from 1997-2002, but the SEC concluded that investors were unable to learn the specifics of the benefits. Subsequent to the SEC decision, none of the five highest compensated officers listed in the 2004 proxy statement had employment or retirement contracts.

### Stakeholders

- How and when will you disclose this plan to shareholders (proxy, 10Q/10K)?
- What tools and processes are in place to support compensation committee decision making (e.g., tally sheets)?

### Disclosure & Transparency

- What is the company's philosophy regarding transparent disclosure in the proxy statement

(e.g., minimally compliant versus full disclosure and effective communications)?

- Have you provided the context/rationale for why certain elements exist in the program and others don't?
- What is the company's position on appropriate level of transparency (disclosing more than is required, simplification of written communications)? ●

## UNITEDHEALTH GROUP

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**T**he CEO of UnitedHealth Group retired in 2006 after receiving more than \$2 billion in stock options during his tenure, allegedly by picking the lowest stock price each year for his annual options grants. In March 2007, UnitedHealth restated earnings by \$1.13 billion over a 12-year period.

### Internal Environment

- What are your key business objectives and strategic drivers?
- Has your accounting division reviewed this program design from an accounting treatment perspective?
- Is the legal department comfortable with this design in the current legal/regulatory environment?

### External Environment

- What regulatory jurisdictions are you subject to?
- What regulations govern the type of program you are designing?
- Will this information become public knowledge?
- How do you anticipate the media will react to this program?

### Stakeholders

- Who are the shareholders (institutional, employees, union, etc.) and what are their interests and concerns?
- What are shareholder expectations about your compensation programs, and how do they affect plan design?
- How and when will you disclose this plan to shareholders?
- Has the committee consultant been briefed about the proposed program or issue?
- Has the committee been adequately prepared to discuss this program or issue in previous meetings?
- Will the general employee population perceive this program as fair?

It has been alleged that the CEO had made personal investments with the former chair of the compensation committee. The chair of the compensation committee resigned on the same day as the CEO retired.

### External Environment

- What regulations govern the type of program you are designing?
- Are there particular communities/social or political activists that will react to this plan?
- Will this information become public knowledge?
- How do you anticipate the media will react to this program?

### Stakeholders

- Is senior management prepared to support and communicate this program or issue?

### Disclosure & Transparency

- What is the company's philosophy regarding transparent disclosure in the proxy statement (e.g., minimally compliant versus full disclosure and effective communications)?
- What is the company's position on appropriate level of transparency (disclosing more than is required, simplification of written communications)?

After the CEO's departure, the board adopted a number of reforms, including creation of a non-executive chairman, a chief ethics officer, and the elimination of severance in connection with change in control.

#### Stakeholders

- Does the committee employ an independent compensation consultant?
  - Has the compensation committee/board of directors reviewed similar compensation programs or issues in the past?
  - What tools and processes are in place to support compensation committee decision making?
  - Are compensation committee members/board of director members familiar with similar programs or issues? ●
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## KB HOME

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**T**he CEO of KB Home departed in 2006 after an internal investigation revealed that he had backdated his own stock options. The company's internal investigation indicated that the CEO and head of HR had probably altered the dates of stock option grants between 1998 and 2005. As a result of the backdating, the company indicated a need to restate more than three years of financial results and incur an additional compensation expense of more than \$41 million.

### Internal Environment

- To what extent is the legal department involved in compensation planning, design, administration and disclosure?
- Has your accounting division reviewed this program design from an accounting treatment perspective?
- What are the results that need to be achieved in the short and long term?
- Is the legal department comfortable with this design in the current legal/regulatory environment?

### External Environment

- What regulations govern the type of program you are designing?
- Are there particular communities/social or political activists that will react to this plan?
- Will this information become public knowledge?
- How do you anticipate the media will react to this program?

### Stakeholders

- What is the likely perspective of shareholder advocates on this program or issue?
- Will the general employee population perceive this program as fair?

Despite the scandal and ongoing investigation at the time of his departure, the terms of the CEO's employment agreement provided him with the ability to collect as much as \$175 million in severance, pension and stock.

### External Environment

- To what extent do you want to match or differ from market pay practices?
- Will this information become public knowledge?
- How do you anticipate the media will react to this program?

### Stakeholders

- Are committee members familiar with similar programs or issues?
- Has the committee consultant been briefed about the proposed program or issue?
- Has the committee been adequately prepared to discuss this program or issue in previous meetings?

- Does the committee employ an independent compensation consultant?
- Will the general employee population perceive this program as fair?
- What tools and processes are in place to support compensation committee decision making (e.g., tally sheets)?

#### Disclosure & Transparency

- What is the company's philosophy regarding transparent disclosure in the proxy statement (e.g., minimally compliant versus full disclosure and effective communications)?

Because of the backdated options scandal, the company adopted a new policy that all stock option grants and the terms of the grants be approved by the compensation committee. The company also appointed a nonexecutive chairman of the board, a chief compliance officer, and did not grant any stock options to executives in 2006.

#### Internal Environment

- Has your accounting division reviewed this program design from an accounting treatment perspective?
- Is the legal department comfortable with this design in the current legal/regulatory environment?

#### External Environment

- To what extent do you want to match or differ from market pay practices?

#### Stakeholders

- What is the likely perspective of shareholder advocates on this program or issue?

- How and when will you disclose this plan to shareholders?
- Has the compensation committee/board of directors reviewed similar compensation programs or issues in the past?
- Are compensation committee members/board of director members familiar with similar programs or issues?

#### Disclosure & Transparency

- What is the company's position on appropriate level of transparency (disclosing more than is required, simplification of written communications)? ●

# WorldatWork Executive Rewards Questionnaire

## INTERNAL ENVIRONMENT

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The internal environment includes factors that are unique to each company and essential to consider when developing compensation plans that are effective in supporting the business strategy.

### Business Strategy

#### Strategic Drivers

- A. What is your company's mission/core values?
- B. What is your corporate strategy?
- C. Where are you in the business life cycle (startup/high growth/mature/decline or renewal)?
- D. What are your competitive advantages and vulnerabilities?
- E. What are your key business objectives and strategic drivers?
  - i. How are they measured?
  - ii. Are the strategic drivers consistent across divisions?
  - iii. If not, how does this affect plan design?

#### Short- and Long-Term Goals

- A. What are the results that need to be achieved in the short and long term?
- B. How do these short-term objectives (tactical) align with/drive long-term objectives (strategic)?
- C. What are the major milestones in these tactical and strategic objectives?
- D. What are major challenges to achieving those objectives/milestones?
- E. How does expected performance relate to the current business outlook?

### Human Capital

- A. What is your human resources strategy and how does it align with the corporate strategy?
- B. Does the plan you are considering support the broader HR strategy?
- C. How competitive is your industry for human capital?
  - i. Do you anticipate economic conditions that might affect your competitive posture for human capital?
- D. What is the availability of critical talent in your industry?
- E. Do competitiveness and availability of critical talent vary by business unit?
- F. What is the current employer-employee value proposition?
  - i. Do you anticipate economic conditions that might affect your employee value proposition?
- G. What is your company's philosophy regarding employee mobility and how does this affect plan design?

### Compensation Philosophy

- A. What is the compensation philosophy and objectives?
  - i. Market orientation
  - ii. Target pay position (total and key elements)
    - a. Are you going to position consistently within each business unit?
    - b. Is your target pay position sustainable in a severe economic downturn?
    - c. If not, how will your target pay position be modified in weak economic periods?

- iii. Performance leverage of compensation
  - a. Have you assessed your programs for unnecessary and excessive risk?
- iv. Performance perspective (corporate vs. division)
- v. Peer groups
  - a. Is the peer group consistent between business units?
- vi. Does this fit within total rewards philosophy/strategy?
- B. To what degree does the compensation philosophy align with corporate strategy, corporate culture, organizational resources?
- C. Are current compensation programs aligned with the philosophy? If not, why not?
- D. How effective is the compensation philosophy?
  - i. Is your compensation philosophy sustainable in a severe economic downturn?
- E. Do divisions across your company compete for talent? If so, do they compete equitably or do pay packages vary considerably?
- F. How is compensation perceived by employees (fairness, reasonableness)?
- G. What effect would the proposed plan have on total compensation opportunity?

#### Talent Attraction/Retention/Development

- A. What is the organization's philosophy regarding attraction, motivation, retention?
- B. How effective is the organization at attracting and retaining talent?
- C. How does compensation affect employee engagement?
- D. How will the program support the recruitment of critical talent/hot skills?
- E. How will the program support the retention of critical talent/hot skills?
- F. How will the program support talent development?

#### Infrastructure

- A. Do you have measurement systems that will provide the performance metrics you need for your new program?
- B. Do you have the necessary systems to operationalize and administer this program?

- C. Do you have the ability to audit the administrative effectiveness of this program?
- D. Is your financial reporting/accounting function capable of administering this program?

#### Organizational Culture

- A. What degree of change in compensation programs will the organization accept?
- B. Are there key stakeholders or influencers (HR, legal, tax) that need to be part of the program development process?
- C. Do you have a performance focus or entitlement orientation in your compensation programs?
- D. If you do have a performance orientation is it individual- or team-based?
- E. Does it vary by business unit?

#### Global

- i. Are there any additional cultural considerations for introducing this program in other countries?
- ii. Are there cultural issues that will interfere with the program's effectiveness?
- iii. How can these issues be mitigated or managed?
- iv. Will the program deliver the desired results across the countries in which your company operates?
- vi. Will international economic conditions affect the organization's readiness for change?

#### Organizational Resources & Parameters

##### Legal

- A. To what extent is the legal department involved in compensation planning, design, administration and disclosure?
- B. Have you had legal issues with plans of this type in the past?
- C. To what extent will existing legal obligations affect your plan design?
- D. Are there current legal issues and/or company litigation issues that may affect plan design?
- E. Is the legal department comfortable with this design in the current legal/regulatory environment?
- F. Is your legal department prepared to support any special reporting requirements for this program?

### Finance/Accounting

- A. What is the role of finance/accounting in plan design?
- B. Has your accounting division reviewed this program design from an accounting treatment perspective?
- C. Do you know what financial constraints may affect program design?
  - i. Authorized share capital
  - ii. Current burn rate
  - iii. Overhang
  - iv. Dilution
  - v. Self-funding
  - vi. Internal hurdle rate of return
  - vii. Cash-flow requirements
  - viii. Severe economic downturn
  - ix. Impact of currency fluctuations
- D. Will your finance department accept plan/program volatility?
  - i. Would increased economic volatility change finance's view of the new plan?
- E. Is your finance/accounting department prepared to support any special reporting requirements for this program?

### Tax

- A. What is the role of the tax department in plan design?
- B. How risk-tolerant is your tax department?
- C. What are the tax implications for the company in your proposed plan design?
  - i. Can anticipated taxes be minimized for the company through design changes?
- D. What is the anticipated tax impact of this program on program participants?
  - i. Are participants aware of this anticipated tax impact?

### Global

- i. Do the tax implications vary across countries?
- ii. How can these issues be mitigated/managed?

### Investor Relations

- A. What is the process for developing responses and communicating with shareholders?
- B. What are your governance ratings and what impact do they bring to bear on design? ●

## STAKEHOLDERS

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**S**takeholders include individuals or organizations that have a financial interest in the company and whose interests must be considered when designing a compensation plan.

### Shareholders

- Is this program required to be approved by the shareholders? If not, skip this section.
- A. Who are the shareholders (institutional, employees, union, etc.) and what are their interests and concerns?
- B. What are shareholder expectations about your compensation programs, and how do they affect plan design?
- C. How do shareholders react to suggested voting guidelines from external groups (ISS, labor unions)?
- D. What is the likely perspective of these shareholder advocates on this program or issue?
  - i. Would shareholder advocates have a different view of this program in a severe economic downturn?
- E. How do shareholders react to media coverage of hot-button issues?
- F. What is your organization's shareholder proposal process?
- G. What have been the major proxy challenges? By whom have you been challenged?
- H. What have the outcomes of the challenges been, in terms of votes?
- I. How and when will you disclose this plan to shareholders (proxy, 10Q/10K)?
  - i. Would this disclosure process be modified in a severe economic downturn?

### Compensation Committee/Board of Directors

- Is this program required to be reviewed by the compensation committee of your board of directors? If not, skip this section.
- A. Has the committee reviewed similar compensation programs or issues in the past?
- B. If so, what was the outcome of that review?
- C. Has the committee been adequately prepared to discuss this program or issue in previous meetings?
- D. If not, can the committee review and consider this program or issue in a single meeting?
- E. Are committee members familiar with similar programs or issues?
  - i. From their respective companies?
  - ii. From other compensation committees?
- F. Do you know what questions committee members are likely to ask regarding your program or issue?
- G. Do you know committee perspectives on this program or issue?
- H. Does the committee employ an independent compensation consultant?
- I. What is the role of the compensation committee consultant?
- J. Has the committee consultant been briefed about the proposed program or issue?
- K. Do you know the consultant's views regarding this program design or issue?
- L. Are there other advisers to the committee and what are their perspectives?
- M. Has the board's external adviser received the same materials as the committee, and has he/she had sufficient time to review them?

- N. Do you have necessary backup materials to answer any questions that might be raised in the committee meeting?
- O. What tools and processes are in place to support compensation committee decision making (e.g., tally sheets)?
  - i. How can you use these (or create new tools) to support decision making on this program?

### Management

- A. What is the anticipated management decision-making process for the program or issue?
- B. Who on the senior management team needs to know about this program or issue?
  - i. What specifically do they need to know?
- C. Who is typically the influencer, decision maker or derailer of similar decisions within the company?
- D. Do you have an executive sponsor or champion for this program or issue?
- E. What is your plan or process to develop support for the desired outcome?
- F. Will this program or issue be considered a sensitive topic for your senior management team?
  - i. Have they considered similar issues in the past?
  - ii. What was the outcome of previous considerations?

### Plan Participants

- A. Who will participate in, or be affected by, this program?
  - i. What are the participants' needs and how do programs address those needs?
  - ii. Would participants' program needs be different in a severe economic downturn?
  - iii. What is your proposed process to gather this information?
- B. Will participants have a "say" in the design of this program or issue resolution?
- C. Are there opinion leaders within the participant group?
  - i. How will you ensure the buy-in of these opinion leaders?
  - ii. Will you consult these leaders during the design phase or only during communication phase?
- D. Are there one-off programs/benefits, or deals that will affect compensation program design for those individuals?

- E. How have past and current plans been received?
- F. Will this program have a negative effect on other programs?
  - i. If so, can this negative impact be mitigated through plan design?

### Other Employees

- A. Will the general employee population be advised about this program?
  - i. If not, is there any risk of nondisclosure?
    - a. Would the risk of nondisclosure increase in a severe economic downturn?
  - ii. If so, when and how will they be advised?
- B. What type of compensation and benefits treatment have other employees recently received?
  - i. Have they recently been asked to give up or receive reduced compensation or benefits?
- C. Will they perceive this program as fair?
  - i. Would a severe downturn in the economy or company performance change their view of this program's fairness?

### Communication Strategy

- A. What is your proposed communication strategy?
  - i. Who needs to know what (management, participants, other employees)?
  - ii. What communication channels will you use (face-to-face, print, Web)?
  - iii. Who will be the primary communicators of the new program?
    - a. Will they have credibility with participants?
  - iv. What are formal/informal communication processes?
  - v. Would a severe economic downturn necessitate a change to this communication strategy?
- B. Is senior management prepared to support and communicate this program or issue?
- C. Have you allowed adequate time for discussions?

### Global

- i. Will there be implications/requirements for translating materials?
- ii. How will communications be tailored to cultural sensitivities in each country? ●

## EXTERNAL ENVIRONMENT

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The external environment includes factors outside of an organization's control that affect how a company may operate its business and are essential to consider when designing compensation plans.

### Regulatory

#### Regulatory Bodies

- A. What regulatory jurisdictions are you subject to?
- B. Are the regulations consistent or in conflict with one another?
- C. Does this program require approval by external regulatory bodies?
- D. What is the anticipated process to submit this program for approval?
- E. What is the anticipated timeline for program approval?
- F. Is it clear which jurisdiction will have final approval?
- G. What are the anticipated reactions of current regulators to this program?
  - i. Would a severe economic downturn affect regulators' view of this program?
- H. How have they historically responded to programs of this type?

#### Regulatory Compliance

- A. What regulations govern the type of program you are designing?
- B. Are there processes in place to track compliance?
- C. Does the cost of compliance substantially erode the benefit delivered?
- D. What is the potential impact of any anticipated legislation on programs of this type?

#### Global

- i. Will this program be subject to global regulation in the company's area of operations?
- ii. Does it conflict with regulations in any participating country?
- iii. Can/should the program be modified to comply with regulations in those countries?

#### Accounting Treatment

- A. What is the current accounting treatment for this program?
  - i. Will this treatment have a negative effect on your company?
  - ii. Can any negative impacts be mitigated through program design?
- B. Are there anticipated accounting changes on the horizon that could affect the current accounting treatment for your program?
  - i. Can any of the anticipated changes be mitigated through program design?

#### Global

- A. Does the accounting treatment differ from country to country?
  - i. Will this treatment have a negative impact on your company?
  - ii. Can any negative effects be mitigated through program design?
- B. Are there anticipated accounting changes on the horizon that could affect the current accounting treatment for your program?
  - i. Can any of the anticipated changes be mitigated through program design?

**Tax**

- A. What is the current tax treatment for this program?
  - i. Will this treatment have a negative effect on your company?
  - ii. Can any negative effect be mitigated through program design?
- B. Are there anticipated tax changes on the horizon that could affect the current tax treatment for your program?
  - i. Can any of the anticipated changes be mitigated through program design?

 **Global**

- i. What are the tax implications of this program for the company and employees in participating countries?
- ii. Are there any other considerations (e.g., eligibility, entitlement issues, representation)?

**Legal**

- A. What legal requirements/jurisdictions do you need to consider when designing this plan?
- B. What are the reporting requirements of these jurisdictions for your plan?
- C. Are these current requirements anticipated to change in the near future?

 **Global**

- i. What legal requirements/jurisdictions in the countries in which your company operates do you need to consider when designing this plan?
- ii. What are the reporting requirements of these jurisdictions for your plan?
  - a. Are these current requirements anticipated to change in the near future?

**Economic/Industry/Labor Market****Economic Trends**

- A. What are the current economic conditions for your company/industry?
- B. Are economic trends improving or declining?
- C. How cyclical/volatile is the industry?
- D. How do current economics affect compensation planning?

- E. How will your proposed program react in the current economic forecast?
- F. What negative economic results would cause this program not to fund/payout in the first year?
  - i. What is the probability that these negative results will occur in the first year of this program?

 **Global**

- i. What are the current economic conditions for your company/industry in the countries in which your company operates?
- ii. Are economic trends improving or declining?
- iii. How do current economics affect compensation planning?
- iv. How will your proposed program react in the current economic forecast?
- v. What negative economic results would cause this program not to fund/payout in the first year?
- vi. What is the probability that these negative results will occur in the first year of this program?

**Industry Trends**

- A. What is the degree of consolidation in your industry?
- B. Is this trend accelerating or declining?
- C. What is the likelihood of change of control?
- D. What is the likelihood of a major acquisition or divestiture?
- E. How do these affect your compensation plan design?

**Labor Market Trends and Pay Practices**

- A. What are the current demand/supply characteristics of your labor market?
  - i. Is a particular skill set or expertise in especially high demand at present?
- B. What are market pay practices?
- C. How reliable and accurate is compensation market data for programs of this type?
- D. Do you need to develop alternate sources of data?
- E. To what extent do you want to match or differ from market pay practices?
  - i. Do you need to pay a premium for a particular skill set or expertise?

- ii. If new/unusual, will it help create a competitive advantage for your company in attracting/retaining human capital?
- iii. How quickly will market leaders react to imitate your program?

## Community

### Media

- A. Will this information become public knowledge?
- B. Have you alerted your communications department that this plan may elicit media scrutiny?
  - i. What is the likelihood the media will focus on this program?
  - ii. How do you anticipate the media will react to this program?
    - a. Would a severe economic downturn alter the media's view of this program?
  - iii. Will media reaction affect your plan design?
  - iv. Will media reaction affect the timing of your announcement?

### Special Interest Groups

- A. Are there special interest groups that will react to this plan design?
  - i. How have they reacted to similar programs?
- B. Should any of these concerns be mitigated through plan design changes?
- C. Can opposition by these interest groups have a broader impact on your company?
- D. Have you alerted the appropriate resources (legal, government relations) within the company that this plan may elicit special interest group scrutiny?
  - i. What is the likelihood that special interest groups will focus on this program?
    - a. Would a severe economic downturn lead to a different/stronger focus on this program?
  - ii. How do you anticipate special interest groups will react to this program?

- E. Will special interest groups' reaction affect your plan design?
- F. Will special interest groups' reaction affect the timing of your announcement?

### Socio-Political Environment

- A. Are there particular communities/social or political activists that will react to this plan?
- B. What are the sensitivities of the communities or governmental bodies or entities in which the company operates (living wage, executive pay, highest-to-lowest ratio, layoffs, divestiture)?
  - i. Would a severe economic downturn increase sensitivities to this program for community or governmental bodies?
- C. Can the company's lobbyists influence the community or governmental bodies to view this program positively?
- D. Should these sensitivities be mitigated through program design changes?
- E. Have you alerted the appropriate resources (community/media relations/governmental affairs) within the company that this plan may elicit communities'/social or political activists' scrutiny?
  - i. What is the likelihood communities/social or political activists will focus on this program?
  - ii. How do you anticipate communities/social or political activists will react to this program?
  - iii. Will communities'/social or political activists' reactions affect your plan?
  - iv. Will communities'/social or political activists' reactions affect the timing of your announcement? ●

## DISCLOSURE & TRANSPARENCY

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**D**isclosure and transparency includes regulatory requirements and an organization's philosophy regarding the extent to which an it provides complete and easily understandable compensation information.

### Public Disclosure/Transparency

- A. Have you met with appropriate internal and/or external resources (legal, tax, accounting, audit, HR, shareholder relations, consultant, other) to identify and address disclosure requirements?
  - i. What are the disclosure requirements for this program (SEC, FASB, IRS, DOL, other)?
  - ii. Are these disclosure requirements different by agency?
  - iii. How do the requirements differ by plan type?
  - iv. How do the requirements differ by employee group?
  - v. What is the effect of disclosure requirements on this program (company, legal, executive, tax, investor relations)?
  - vi. Should any disclosure issues be mitigated by plan design changes?
- B. What transparency trends are emerging in your industry?
- C. What is the company's position on appropriate level of transparency (disclosing more than is required, simplification of written communications)?
  - i. What is the appropriate level of disclosure for the various constituents, taking into consideration proprietary information, confidentiality, competitive advantage/risk?

### Global

- i. How do public disclosure/transparency requirements differ by country?
- ii. Will there be additional documentation requirements?

### Regulatory Filings

- A. Have you met with appropriate internal and/or external resources (legal, accounting, HR, shareholder relations, consultant, other) to prepare the proxy?
  - i. Have you provided the context/rationale for why certain elements exist in the program and others don't?
  - ii. Do you want to provide more information than required?
  - iii. Do you want to consider disclosing what you do not offer your executives?
  - iv. Is information communicated consistent year-to-year in order to maximize shareholder understanding?
  - v. Does the compensation, discussion and analysis (CDA) letter clearly link compensation programs to the business strategy?
- B. What is the company's philosophy regarding transparent disclosure in the proxy statement (e.g., minimally compliant versus full disclosure and effective communications)?
  - i. Have you provided the context/rationale for why certain elements exist in the program and others don't?
  - ii. Do you want to provide more information than required?
  - iii. Do you want to consider disclosing what you do not offer your executives?
  - iv. Is information communicated consistent year-to-year in order to maximize shareholder understanding?
  - v. Does the compensation, discussion and analysis (CDA) letter clearly link compensation programs to the business strategy?

### Compensation Committee

- A. Does the charter of the compensation committee require approval of this plan? If so:
  - i. Have they reviewed similar plans in the past?
  - ii. What was their reaction?
- B. What are sensitive committee issues that might raise concern with this plan? ●

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Diane Vavrasek is an HR Manager specializing in labor relations for a Fortune 25 company. She was selected for the firm's human resources development program in 2007 upon receiving her master's degree in industrial and labor relations from Cornell University. While on program, her three rotations included: the coordination and execution of salary planning and talent review processes for the global supply chain organization; an international HR role at a manufacturing facility outside of Budapest, Hungary; and a labor

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Vavrasek is a Pace University alumnus, having earned a bachelor's degree in business administration with a major in public accounting. She subsequently worked as an associate auditor at PricewaterhouseCoopers. She is a member of the Society for Human Resource Management (SHRM).



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