

The Executive's Balance Sheet

by John Egan

Executives are not isolated from the broad market pressures affecting many constituents and certainly all investors. To profile an executive as an individual isolated from the current economic environment reaping substantial rewards from employment, in our judgement is an inaccurate depiction of the times.

Many remuneration disclosures while complying with accounting standards do not reflect actual money received.

Executives own real estate, the value of which in many instances has declined substantially. Many executives have an investment portfolio. Some of these investments may be supported by margin loans including substantial investments in their own employer.

In the current environment, many executives anticipating options/rights vesting would have been disappointed either because the securities did not vest arising from failure to meet performance benchmarks and/or the decline in share price or if vested, delivered value substantially below reward expectation.

Grants that might be contemplated for 2009 under long term incentive plans or deferred annual incentives are unlikely to provide enhanced cash flow to executives before 2012.

The above picture in our judgement is a reasonable portrayal of the circumstances facing many executives. They have a benefit over retired investors, in that they continue to receive their base remuneration, but little prospect of substantial adjustments to that remuneration in the current economic setting.

In summary we see the executive challenge as including:

- Probability of substantially diminished annual bonus payments in the 2009 year.
- Limited prospect of receiving any benefit under prior long term incentive plan awards in the current calendar year.
- Future earnings upside unlikely to arise until the 2012 financial year.

In this context many executives are sharing the burden along with shareholders in their employer.

Many executives have debts that exceed their share portfolio value and will be challenged in the current economic environment in a way not previously foreseen.

Boards will be challenged in balancing executive expectation and financial need with the challenges of the current economic environment and the expectations of shareholders whose interests they represent.

In a number of cases boards are aware of the personal financial circumstances and financial stress of their CEOs, executives and some senior management, a knowledge which they need to ensure does not sour the employment relationship or unduly influence their deliberations on their executive's remuneration arrangements going forward.

Boards further need to be mindful that individual financial stress can also be a key driver for executives engaged in active negotiations surrounding contract renewal.

These are difficult times and boards must respond appropriately at arms length with a considered position taking into account the total environment, including shareholders, other stakeholders and commentators, corporate and individual performance, governance issues and now government regulatory proposals, all while ensuring corporate sustainability and the organisation's readiness to participate fully in the global economy's recovery.

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