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No Wonder C.E.O.'s Love Those Mergers

By GRETCHEN MORGENSON

SHAREHOLDERS like it when their companies are acquired, because their stocks rise in value. Chief executives like it, too, because their severance agreements kick in. And that means they can become truly, titanically, stupefyingly rich.

Wallace R. Barr, the chief executive of Caesars Entertainment, is the latest to line up for his barrel of bucks. Last week, Harrah's announced it would acquire Caesars for \$5.2 billion. Thanks to accelerated vesting of options and stock awards, Mr. Barr stands to receive almost \$20 million under so-called change-of-control provisions in his contract. And if Mr. Barr resigns from Caesars "for good reason," the contract says, he is entitled to an additional \$6.6 million after the two companies merge.

A spokesman for Caesars did not return a phone call seeking comment.

Then there was [Wachovia's](#) proposed acquisition of the [SouthTrust Corporation](#) last month. Equilar Inc., a compensation analysis firm in San Mateo, Calif., said the terms of the deal would give Wallace D. Malone Jr., the chief executive of SouthTrust, \$59 million in termination awards, stock awards and options over the next five years if he leaves the bank. He also appears to be entitled to an annual pension of about \$3.8 million.

At least Mr. Malone has said he would donate some of this bounty to charity. A spokeswoman for SouthTrust did not return a phone call seeking comment.

"In theory, change-in-control provisions make sense," said Tim Ranzetta, the president of Equilar. "They encourage executives to act in the best interests of shareholders in transactions that they anticipate will increase shareholder value, which at the same time may harm their own careers. But empirical research seems to indicate that most companies underperform relative to the market after a merger while executives benefit from these large, one-time payouts."

Amazingly few shareholders have carped about these giveaways. The California Public Employees' Retirement System, the big pension fund known as Calpers, voted against last month's merger of two health care companies, [Anthem Inc.](#) and [WellPoint Health Networks](#), citing excessive pay. Executives

stood to receive bonuses, severance payments and vested stock options totaling approximately \$200 million in the deal. Leonard D. Schaeffer, WellPoint's chief executive, was entitled to \$47 million in severance, stock options and enhanced retirement benefits, an Anthem spokesman said.

Nobody else seemed to mind. Shareholders approved the merger on June 28.

One reason that shareholder outrage has been muted may be that few people, beyond the executives themselves and maybe the company's compensation committee, know how costly these pay deals are. Even with all the scrutiny of corporate governance in recent years, a full tally of what executives will earn in retirement or under a change of control is simply not disclosed. Not anywhere.

Experts say that many compensation committees do not understand the size of these pay packages because they do not routinely ask their consultants for detailed lists of the various pay components.

And, my, how the list of goodies can go on. First comes the executives' severance pay, almost always nearly three times salary and bonus. Accelerated vesting of stock options and stock awards quickly follows; sometimes the options are granted with their full terms remaining - up to 10 years - giving them tremendous value.

Then there are the three additional years of pension credits that get tacked on to an executive's pay, as well as the 401(k) match, years of health care benefits and the cash value of perquisites at the time of termination - such as use of the corporate jet, country-club memberships, allowances for financial planning advice, office space and secretarial services. All in one delightfully fat lump sum.

AND don't forget that executives' pensions are often based on the unusually high severance pay, which ratchets the numbers way up.

Of course, one downside to these enormous payments is that they generate stunning tax bills for executives. Good thing their contracts almost always require the companies to pay. And how!

The so-called excise tax gross-up provisions can be so colossal that, according to one pay expert, a major merger was scuttled because the cost to cover executives' tax bills exceeded \$100 million.

While chief executives receive the biggest pile of money and perks, other managers also find their way to the trough, pay experts say. The numbers become really crazy when, as is often the case, the exit agreements of both companies' executives become effective in a merger.

As a result, said Michael S. Kesner, principal in charge of the executive compensation practice at Deloitte Consulting, it is not uncommon for payouts to management to reach 8 percent of a merger's total cost.

Yet shareholders have no way to know about all this in advance because it is hidden from view. The

attitude seems to be: why bother the owners with chapter and verse on what the hired help will get?

Even absent a merger, a company's contractual obligations to its executives are huge. It is an outrage that these obligations - including deferred compensation and supplemental retirement plans - and their amounts, are not disclosed annually, in plain and comprehensible terms.

Compensation disclosure rules, mandated by the Securities and Exchange Commission, have not changed since 1993. During that time, executive compensation packages have become much more creative, not to mention outrageous.

"Disclosure definitely needs to be improved and compensation committees need to know what the totals are," Mr. Kesner said. "That would make a huge difference."

Regulators do not seem focused on increasing disclosure in this area. If they do not force the issue, and soon, firms providing proxy voting advice to institutional investors can help the process along. The big ones, like Institutional Shareholder Services and Glass, Lewis & Company, should advise clients to vote against a company's compensation plan or directors who serve on compensation committees unless they receive the full terms of these contracts.

Jesse M. Brill, a securities and compensation lawyer and chairman of the National Association of Stock Plan Professionals, has some advice for compensation committees of corporate boards: Tally the total compensation that executives are in line to receive, especially in a takeover, or else.

In a recent article in *The Corporate Counsel*, a newsletter covering corporate and securities law issues, Mr. Brill outlined steps that compensation committees must take to ensure they meet fiduciary duties to shareholders in the area of executive pay. The article is at www.compensationstandards.com.

"Once those numbers are put together in one place it's going to open a lot of eyes," Mr. Brill said. "That, combined with the fear of personal exposure, will cause some people to make some very significant changes in compensation."

Which is one of the things the world needs now.