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## **Executive Pay and the Stimulus Bill**

Washington, D.C. — CEO pay analysts at the Institute for Policy Studies today blasted the congressional conference committee action that stripped a \$400,000 cap on bailout executive pay out of the stimulus legislation.

“This move spits in the face of an American people justifiably furious over excessive pay for power suits,” notes IPS CEO pay expert Sarah Anderson.

Anderson calls the reported rationale for the move — a Congressional Budget Office finding that capping executive compensation would cost the federal treasury \$10.8 billion in lost tax revenue over ten years — “an example of bean-counter tunnel vision.”

“By this reasoning, Congress should let companies dump their toxic waste in the nearest river,” she notes. “Think how much more in corporate profit taxes we could be collecting if factories didn’t have to follow environmental standards.”

In reality, adds Institute associate fellow Sam Pizzigati, capping executive pay at \$400,000 — as originally proposed by Senators Bernie Sanders (I-Vermont) and Claire McCaskill (D-Missouri) — would likely increase, not decrease, tax revenues over the next ten years by speeding the recovery of financially failed enterprises.

“Over-the-top rewards for executives,” explains Pizzigati, “only create incentives for the sorts of reckless and risky behaviors that brought on our current economic mess in the first place. Capping executive pay would encourage execs to concentrate on business, not their personal portfolios.”

In place of the Sanders-McCaskill cap, the stimulus legislation does include a “prohibition” on payouts by TARP recipients for any “bonus, retention award, or incentive compensation.” But the legislation then offers a loophole to that restriction, a provision that allows bailed-out companies to award executives extra pay in the form of “long-term restricted stock.”

This loophole, note the IPS analysts, does include one redeeming feature: a stipulation that this restricted stock not have a value greater than one-third of the total “annual compensation of the employee receiving the stock.”

The stimulus legislation provisions on executive compensation, Anderson points out, represent just a first stab at meaningful CEO pay reform. The White House has already promised a deeper examination into executive excess.

“We’re encouraged by President Barack Obama’s announcement last week that the

administration plans to examine broader executive pay reforms,” notes Anderson. “Given Congress’s failure to take tough enough action on executive pay in the stimulus bill, we need this deeper examination now more than ever.”

### A detailed analysis of the executive pay provisions in the stimulus bill

This chart summarizes the key executive pay provisions in the stimulus bill and compares them with the language in the original TARP legislation, as well as the Treasury Department Rules announced by President Obama on February 4.

Restriction in Stimulus Bill	Comparison with Original TARP	Comparison with new Treasury Rules
<p><b>Limits on pay:</b> No measurable limit. Requires only that Treasury ensure that “incentive compensation for senior executives does not encourage unnecessary and excessive risks that threaten the value of the financial institution during the period that any assistance under this title is outstanding.”</p>	<p><b>No significant change.</b> The proposed reform merely extends this language in the existing law to all participating firms. The Conference Committee scrapped a strong amendment that passed the Senate which would’ve capped all compensation for all employees of all TARP recipients at \$400,000.</p>	<p>Sets a \$500,000 pay cap for senior executives, but only in firms receiving vaguely defined “exceptional assistance.” Additional pay for these executives must be in restricted stock, claimable once the firm has repaid the government (or earlier in some cases).</p>
<p><b>Bonuses:</b> Prohibits bonuses, retention awards, and incentive compensation, with the exception of restricted stock that can be claimed after TARP funds have been repaid and does not exceed 1/3 the amount of annual compensation of the employee. The provision applies to varying numbers of employees, depending on the size of the TARP aid:  <b>\$25 mill or less:</b> applies to only the most highly paid employee  <b>\$25 mill to \$250 mill:</b> at least the top 5. Treasury Secretary may increase the number if it’s in the public interest.  <b>\$250 mill to \$500 mill:</b> senior executives and at least 10 next most highly compensated employees (or more if Treasury so chooses).  <b>\$500 mill or more:</b> senior executives and at least the 20 next most highly compensated employees (or more if Treasury so chooses)            The prohibition on bonuses will not apply to any bonus required to be paid under an employment contract.</p>	<p><b>New.</b></p>	<p>See text above on restricted stock.</p>
<p><b>Clawback:</b> Bonuses or other awards to senior executives or any of the next 20 most highly</p>	<p><b>No significant change.</b> The proposed reform merely extends the language in the</p>	<p>Same as in stimulus bill.</p>

compensated employees that are based on materially inaccurate financial reports must be returned to the institution.	current law from the top 5 to the top 25 executives of all participating firms.	
<b>Severance:</b> Ban on “golden parachutes” to any senior executive or the next 5 most highly compensated employees while TARP assistance is outstanding	<b>No significant change.</b> Extends restrictions on failing institutions to all participating firms and for all senior executives plus the next 5 most highly compensated employees.	Same as in stimulus bill for the top 10 executives. In addition, it prohibits golden parachutes for the next 25 executives that exceed the value of the employee’s annual compensation.
<b>Perks:</b> Firms must have a policy regarding excessive or luxury expenditures, which may include: entertainment, office renovation, jets, or other activities that are not reasonable business expenditures.	<b>New, but not a significant change.</b> Merely requiring a firm to have a policy is unlikely to result in significant reduction of these and other types of perks, such as tax gross-ups.	Same as in stimulus bill.
<b>Earnings manipulation:</b> The bill includes a prohibition on “any compensation plan that would encourage manipulation of such institution’s reported earnings to enhance the compensation of any of its employees.”	<b>New.</b> This provision is presumably designed to discourage executives from “cooking the books” to inflate the value of their personal stock options. But Treasury officials would likely have problems monitoring this prohibition.	
<b>Say on Pay:</b> shareholders will be allowed an annual nonbinding vote on executive compensation.	<b>New.</b> This provision may draw additional attention to outrageous compensation packages, but since it is nonbinding, it is unlikely to have significant impact.	Same as in stimulus bill, except it applies only to firms receiving “exceptional assistance.”
<b>Prior Payments to Executives:</b> Treasury Secretary will review compensation already paid to executives of TARP recipients to examine whether such payments were “contrary to the public interest” and shall seek to renegotiate appropriate reimbursement.	<b>New.</b> This is a watered-down version of an amendment offered by Senators Wyden and Olympia Snowe that would have required firms to repay bonuses paid in excess of \$100,000 or face an excise tax of 35%.	

### Significant Additional Provision in the Original TARP Bill: Tax Deductibility Cap

The stimulus bill let stand one provision of the original bailout bill that places a \$500,000 cap on the tax deductibility of executive pay. This set an important precedent in reducing the taxpayer subsidy for excessive executive compensation. The current U.S. tax code places a \$1 million cap on tax deductibility for executive compensation, but this provision has been meaningless in practice because it allows exceptions for “performance-based” pay. Most companies simply limit top salaries to around \$1 million and then add on to that total various assortments of “performance-based” bonuses, stock options, and other long-term compensation. The TARP closed this loophole by making the exception for “performance-based” pay inapplicable in the case of executives of bailed-out firms.

## **Contacts:**

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## **About IPS**

The Institute for Policy Studies, a progressive multi-issue think tank founded in 1963, has published 15 widely publicized yearly reports on executive pay. The latest, [Executive Excess 2008](#), found that five tax loopholes that benefit top executives cost taxpayers more than \$20 billion per year.

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