What you need to know

Executive
Compensation Plans

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What you need to know:

Executive Compensation Plans

Different components affect the makeup of executive pay, a number that is largely tied to company performance. A CFO's focus is on creating an executive compensation plan that reflects shareholder expectations while also being affordable and competitive in the industry. Recently, these plans have been trending toward relying on long-term performance measures to prevent executives from taking short-term risks at the expense of the long-term performance of the organization. Tying executive pay to stock options increases an executive's incentives to improve company performance in the long run.

FAST FACTS

- Executive pay plans create tax advantages for both the executive and the company they work for.
- An average executive's base salary makes up roughly 30% of total compensation.
- Incentives as a percentage of total executive compensation are about 60%.
- Perks such as use of a company jet, personal drivers, and home communication systems are given to maximize executive work time.

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An Overview

Executive pay plans create tax advantages for both the executive and the company they work for. These plans can face scrutiny from the public due to the lavish rewards that executives cash in. With this said, creating a pay plan that effectively communicates the details and avoids poor perceptions, is important for the CFO's.

The Base Salary

An executive's base salary makes up roughly 30% of total compensation. This number varies greatly depending on the company, but typically, companies try to keep an executive's base salary at $1 million or less, as this is the maximum amount a company can deduct as an expense for tax purposes.

Types of Incentives

Although long-term incentives make up a larger part of total incentives, short-term incentive measures such as profit margins and increasing market share are also tied into executive compensation. Incentives, as a percentage of total executive compensation, are about 60%. Long-term measures such as earnings per share and return on assets are typically paid out as part of executive pay every three to five years.

Perks & Benefits

While perks and benefits only make up about 10% of total executive compensation, executives can take advantage of special retirement plans not available to all employees. Because of the great demands placed on executives, perks such as use of a company jet, personal drivers, and home communication systems are given to maximize executive work time.

Contact our Tax team at

414.271.7800 with any questions

FYI

With things always changing, be sure to talk with Reilly, Penner & Benton to learn what the most current rules, regulations and changes may apply to you when working with Executive Compensation Plans.

A CFO's Role

A company's CFO must minimize risky behavior of the CEO by analyzing how incentives influence behavior and how those behaviors influence the firm's performance. CFO's must also find a balance between competitive and affordable pay.

Possible Issues

Executive compensation has come under fire in the recent past due to the losses incurred by both public and private investors. A large majority of the public believes CEO's are overpaid, but don't understand the market challenges and complexities the job entails. What the public often fails to realize is that executive compensation is about beating global competition by attracting top executive talent to create shareholder wealth for a company. Designing a sound executive compensation plan involves many complex accounting, regulatory, tax, and documentation issues. Having a well-designed plan will align executive compensation with the company's goals and objectives which can lead to retaining top talent and creating greater return for shareholders.