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THE NEW EXECUTIVE CLASS

Everyone knows about overpaid CEOs. But now even lower-level executives are getting enormous salaries. They are buying multiple homes, taking lavish vacations and otherwise living large—while their workers watch wages stagnate and benefits shrink. Dude, where's my company? By Vince Beiser

Mike Watt's Punk Afterlife ~ The L.A. River Surrealized ~ Normandy's Forgotten Heroine

Forget overpaid CEOs. Now second- and third-tier execs in American companies are getting enormous salaries—as wages and benefits for many workers stagnate or fall.

Rise of the Corporate Plutocrats

By Vince Beiser

The morning sun glints off the sleek steel contours of the Cessna Citation X, a private jet gracing the tarmac at Santa Monica's airport. Inside are eight wide leather seats, equipped with individual DVD players and served by a well-stocked snack bar. It's undoubtedly a fine way to fly: The Citation's prosperous passengers don't have to deal with crowded parking garages, incompetent ticket clerks or getting their shoes X-rayed. They step aboard and are whisked from Los Angeles to New York in fewer than four hours.

"You sure get used to it," says Glenn Hinderstein, vice president of Netjets Inc., whose company supplies these private aircraft to executives at General Electric, Prudential and many other corporations. "It's a drug there's no Betty Ford for."

Not so long ago, use of a company jet was a rare privilege reserved for top corporate officials—the chief executives, presidents and chairmen whose skyrocketing pay has been well-documented in recent years. (A generation ago, the average chief executive at a big corporation made about 40 times what the average worker did; today it's nearly 400 times as much, says vice dean of faculty Kevin J. Murphy of USC's Marshall School of Business.)

Increasingly, however, those plush leather seats are being occupied by vice presidents, general managers and other second- and third-tier execs. The spreading around of private jet rides is among the more obvious emblems of a profound devel-

Photograph by DONOVAN REESE *Stone/Getty Images*

opment in corporate America over the last 20 years: the enormous swelling in pay and privileges for a burgeoning stratum of executives, and their concomitant distancing from the people who work under them. Today, it's not just the boss, but those second, third or fifth in command who pull down seven-figure salaries, own multiple homes and stay in hotels where rooms cost more than most mortgage payments.

Mehdi Eftekari, general manager of the Beverly Hills Four Seasons Hotel, can tell you all about it. He estimates that some 80% of his clientele are corporate officials whose companies pay for their $700- to $3,000-a-night suites. The most modest come with a DVD player, a giant flat-screen TV, a living room with a wet bar and televisions in each of the two bathrooms. Frequent guests can store extra clothes or toiletries at the hotel to lighten their luggage. A staff VIP liaison tracks their personal preferences, so that when they arrive, their rooms are stocked with favorite drinks, snacks and magazines, as well as bathrobes monogrammed with their initials. The hotel even makes sure the bed is equipped with their preferred pillows.

Twenty years ago, you would have been hard-pressed to find a chief financial officer or head of marketing with access to such a lavish expense account. The typical salaries for such corporate subchieftains barely cracked six figures.

Those days are history. A survey last year of multibillion-dollar corporations by Pearl Meyer & Partners, an executive compensation consulting firm, found them paying CFOs more than $3 million a year; top legal officers, $2.2 million; and human resources executives—human resources executives!—$1.6 million. And those are just the averages. BusinessWeek recently listed 10 executives with jobs below the rank of CEO who last year pulled upward of $29 million each.

We're not talking about corporate criminals of the Enron or WorldCom type—corrupt executives who pocket outrageous sums by scamming the system or ripping off investors. Nor are these the entrepreneurs whose inspirations and nerve started the company, or the investors who risked their capital to fund it. These people aren't even the top boss, who is under the most pressure, the one with whom the buck stops. They're hired hands—company employees just like the people they oversee. Their salaries are set by legal and transparent means in accordance with prevailing industry standards. It's just that those standards have gone completely off the rails. Never mind the imperial CEO; we have entered the era of the executive plutocracy.

WHILE LIFE HAS GROWN EVER LUSHER AT THE TOP end of the corporate food chain, it's increasingly precarious for those farther down. As income for top executives shot up, average American workers' salaries have barely kept pace with inflation—and many are finding their jobs, health coverage and retirement prospects in jeopardy.

In fact, the boom in executive pay is only one aspect of a deeper and even more disturbing trend: the growing inequality in American society. Today, as economist James K. Galbraith points out, pay is more lopsided than at any time since the Great Depression.

"I don't hate rich people," says Chris Barber, a 41-year-old Pavilions employee standing in the parking lot of a West Hollywood Pavilions he picketed during the recent grocery workers' strike. "When I hear about someone making money, I say 'good for them,'" he says. "But the people who run public companies shouldn't live like royalty. Bill Gates built his company through entrepreneurship and smarts. But these people were placed in jobs at a company someone else created."

Barber has been working in the grocery business since he was 16. When he came to California from West Virginia in 1987, he was making $10 an hour. Adjusted for inflation, that's about $16 in today's terms. When he went out on strike last fall, Barber was making $17.90 an hour. In other words, all the raises he had received over 16 years came to a grand total of $1.90 an hour.

That's pretty typical of what's happened to blue-collar America during the last two decades. If ordinary workers' annual pay had risen at the same rate as CEO pay since 1990, a report by the Institute for Policy Studies points out, they would be making $75,338 today—instead of the $26,899 they are taking home. Adjusted for inflation, that's only marginally more than what they made in 1980.

Executives' salaries aren't to blame for this—bloated as they are, they still generally constitute only a tiny fraction of major companies' revenues—but they are a symptom of the larger trend. According to the Congressional Budget Office, between 1979 and 1997 the richest 1% of American families—those who had an annual income of at least $677,900 in '97—saw their incomes more than double. But for families in the middle, income grew by only 10%. For the lowest 20%, it actually fell. That helps explain why the number of Americans living below the poverty line swelled by more than 1 million last year. Other studies have confirmed the basic conclusion: The rich are not only getting richer, they are getting *much* richer—while most people are barely holding on to what they've got.

The American dream may still be of a country where anyone can, and has the right to, become fabulously wealthy. But ever since the days of the New Deal, many Americans have embraced the idea that working people have the right to a certain degree of security in their job, an ability to get an education, access to medical care and a chance to retire with some degree of safety. That idea is losing ground faster than you can say "The Apprentice."

WALTER B. WRISTON WAS A MASTER OF THE UNIverse in 1983. As chief executive of banking giant Citicorp, he was one of America's most powerful and highly remunerated corporate magnates. In that single year, he was paid more than most people see in their entire lives: $1.2 million.

That's a lot of money, even today. But it's a fraction of that taken home by Robert Willumstad, who as chief operating officer of Citicorp's successor, Citigroup Inc., occupies a position lower than Wriston held. Willumstad's total last year: $30.6 million. And the exec in the position equivalent to Wriston's? Last year, Sanford Weill retired as CEO of Citigroup. Weill's pay over his last decade averaged almost $98 million a year—more than 80 times what Wriston made a generation earlier.

Wriston does not object to people getting rich. Still, "by any measure of common sense," he says, "when you have someone making hundreds of millions of dollars, this has gone too far."

Firms say they need to pay these amounts to attract top talent. But there's often no connection between executive pay and corporate performance. A study released this year by Rutgers University analyzed more than 1,500 U.S. companies over a 10-year period. It found no correlation between higher executive remuneration and bigger gains for shareholders.

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–former Citicorp CEO Walter B. Wriston

Worse, many companies have seen their earnings and stock prices fall while their executives' pay keeps rising. Occidental Petroleum suffered a 14% decrease in net income in 2002, but CEO Ray Irani's bonus increased to give him a total take-home of more than $24.3 million, twice what he'd hauled in the year before. SBC Communications Inc.'s profit fell 25% last year, and its stock price dipped as well, but Chairman Ed Whitacre still got a fat raise that boosted his take-home pay to $24.8 million. And then there's Michael Eisner, whom Forbes magazine recently declared one of the worst bosses in America in terms of financial performance. Over the last six years, Eisner averaged $121 million in annual compensation, while shareholders were stuck with an average annualized return of minus 5% for the same period.

How did this sort of lunacy become business as usual? The answer boils down mainly to a mutually reinforcing set of economic and cultural shifts.

Beginning in the 1980s, mutual funds and other institutional investors became major Wall Street players, controlling huge blocks of company stocks. Those forces wanted returns fast, and could bring tremendous pressure on corporate boards to replace a management team that wasn't performing up to their standards. As a result, chief executives suddenly found themselves getting fired in unprecedented numbers.

Boards seeking sweeping changes began to recruit executives from outside the company rather than from within, and began relying on consultants to help them determine compensation. This process has an insidious ratcheting effect. Consultants are asked to divine the average rate for an executive in a given industry. But few boards pay just the average; after all, they've selected their man specifically because of his above-average abilities. So they pay him a notch—or five—above the average. That overpayment then enters the consultant's databases, driving up the average and setting a new benchmark for the next candidate.

Moreover, the riskiness of their positions has encouraged executives to insist on "golden parachutes"—guarantees that if they are toppled from their aerie atop the corporate pyramid, they'll receive plenty of cash to cushion the fall. "Golden handshakes," or massive signing bonuses, also have become common. "They should be called golden condoms, because they protect the executives and screw the shareholders," says Graef Crystal, a leading executive compensation expert. Michael Ovitz is undoubtedly the most famous golden parachutist—he walked away with $109.3 million in 1996 after being ousted as Disney president after 14 months on the job.

That sort of thing didn't happen 20 years ago. President Jimmy Carter's Treasury secretary, W. Michael Blumenthal, was in considerable demand when he returned to the private sector. But when he signed on as CEO of Burroughs Corp., then a major mainframe computer maker, "it never occurred to me to ask for a signing bonus," he says. "Neither coming in nor going out was there a golden anything."

Vince Beiser last wrote for the magazine about families of murder victims who forgive the killers.

'I make an awful lot of money. For me personally, I'm probably not prepared to work for less.'

–Hilton CEO Stephen F. Bollenbach

One of the most important components of executive pay is the stock option, which is the right to buy a stock for a set price within a certain period. If you have, say, 100 Exxon options priced at $10 each, and Exxon is trading at $50 a share, you get to buy $5,000 worth of shares for $1,000. Options came into vogue in the 1980s, especially among new technology companies that wanted to reward managers without having to part with scarce cash. Best of all, as far as corporate boards were concerned, they were essentially free. Thanks to a baffling quirk of American financial rules, stock-option grants don't have to be reported as an expense for accounting purposes, so they don't show up as a cost affecting the bottom line.

Given that illogical but entirely legal incentive, and the stock market's precipitous rise, companies started awarding options by the truckload. By the 1990s, it was not uncommon for top executives to pick up hundreds of thousands, or even millions, in stock options in addition to their salaries. The titanic take-home pay of Weill and Willumstad, for instance, was mainly proceeds from cashed-in options.

An executive's pay is set by members of the board's compensation committee, who usually inhabit the same rarefied socio-economic strata. In fact, they often are executives at other corporations. And executives still tend to be overwhelmingly wealthy, white, Protestant and male. (In a study of Fortune 500 chief executives in the mid-1990s, MIT professor Peter Temin found only a handful of nonwhites and a single woman.)

In such a milieu, million-dollar payouts seem standard. Consider, for example, the five members of Beverly Hills-based Hilton Hotels Corp.'s compensation committee. They include such top executives as A. Steven Crown, a general partner with investment powerhouse Henry Crown & Co. and a scion of one of America's wealthiest families, and former baseball commissioner Peter Ueberroth, a man certainly familiar with high salaries.

It's easy to see how this works. Say you're a corporate executive on another company's board. You're asked how much a fellow very much like yourself, who does a similar job and perhaps you know because your boxes adjoin at Staples Center, should be paid. You make millions of dollars a year; why shouldn't he?

Even if you don't think he should, the culture of the boardroom tends to discourage argument. As investor Warren Buffett once put it, "When the compensation committee—armed as always with support from a high-paid consultant—reports on a mega-grant of options to the CEO, it would be like belching at the dinner table for a director to suggest that the committee reconsider."

Sometimes board members have even baser motives for wanting to curry favor with a company's shot-caller. It's not uncommon for directors to work at companies that do business with the CEO's company—business that CEO could take elsewhere if displeased. The chief executive also influences pay and perks for board members, which can be lavish. Hilton's board members get at least $40,000 a year, plus free rooms in Hilton properties year-round. Not bad for a gig that mainly entails attending a handful of meetings a few times a year. That *Continued on Page 41*

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can attract what Blumenthal calls "rice bowl directors." "They're there because they like the board fees," he says. "You get maybe $50,000 a year, a corporate plane picks you up for the meetings, there's an annual dinner in some sunny place…they're not going to break that rice bowl by getting cross with the CEO."

All of these factors have combined to drive up CEO pay—and pay for lesser executives too. "The CEO's pay package is like a 4,000-horsepower vacuum cleaner," says Crystal. "It sucks into its nozzle any pay package near it. But if you're a regular worker, you're so far away your tie won't even flutter."

ECONOMIC FORCES ASIDE, perhaps the most potent force driving up executive pay over the last two decades is something less tangible: a prodigious sense of entitlement.

It's true, as executives often point out, that by and large the companies they run and the global economy in which they operate are both bigger and more complex than they were 20 years ago. Managing a major corporation is an intellectually taxing job. But so is being a surgeon, and they make an average of $73,100 a year. It's stressful, but so is being a cop, and they make less than $40,000. A high corporate post does carry enormous responsibility, but so does being a president of the United States—who is paid $400,000 a year.

The prototype executive of the 1950s and 1960s was the gray-suited Organization Man. But in the early 1980s, with Wall Street on the rise, big-time businessmen began to assume the cachet of movie stars and sports heroes. Suddenly, guys such as Lee Iacocca and Jack Welch were writing bestsellers, grinning from the covers of major magazines and yukking it up with Leno and Letterman.

The boom in business media that accompanied the surging stock market fed, and fed on, this growing cult of the executive. "With an eye to a national audience, the business media focus not on the complexities of organizations or on rapid changes in the business environment, but rather on the actors involved . . . making much of winners and losers, of who is up and who is down, of who is a good CEO and who is not," writes Harvard economist Rakesh Khurana in his recent book "Searching for a Corporate Savior." "The press has thereby turned CEOs—once as unknown to the American public as their secretaries, chauffeurs and shoe-shiners—into a new category of American celebrity."

Stephen F. Bollenbach, Hilton Hotels Corp.'s co-chairman and CEO, is an unabashed example of how expansive executives' sense of self has become. To him, the gargantuan sums he and his colleagues take home are right and proper. "By and large, executives earn what they're paid, and the market economy works to make that so," he declares.

Bollenbach, 62, is a beefy, well-groomed man dressed in a crisp white shirt and blue tie when I meet him at Hilton's Beverly Hills headquarters, a jigsaw of rectangular buildings fronted with speckled marble. His large, sunny office has floor-to-ceiling windows that look out on verdant hills to the north, a massive blond wood desk, and a sitting area with a table and green leather chairs.

"I make an awful lot of money," he acknowledges. "For me personally, I'm probably not prepared to work for less."

Bollenbach, chief executive since 1996, pulled in more than $23 million last year, most of it by cashing in stock options. His salary and bonus alone, duly approved by the compensation committee of Crown, Ueberroth et al., came to at least $3 million—more than four times what the man doing his job 20 years ago made, after adjusting for inflation.

ONE OF THE MOST POIGNANT scenes of the months-long grocery strike was surely when a delegation of workers tried to take their case personally to Safeway CEO Steven Burd at his home in an exclusive Bay Area suburb. They were turned back at the entrance to his gated community.

Those workers were striking to retain—not expand, just retain—their healthcare benefits. They had good reason to worry. In 1979, 70% of private-sector workers had employer-provided healthcare, according to the Washington, D.C.-based Economic Policy Institute. By 2000, that number had dropped to 63%. That number now has dropped to 60%. The rest have become part of the 45 million Americans with no health insurance. And that number is set to continue to grow: a Kaiser Family Foundation report found that almost one-third of the Fortune 500 companies they surveyed already have or probably will soon stop paying health insurance premiums for their retired workers.

Jobs themselves have become less secure. In the 1950s, more than one-third of all U.S. workers were represented by a union. Today, it's less than half that. Even after the mass layoffs of

recent years, nationwide unemployment is still relatively low. But a growing number of workers, according to the U.S. Labor Department, are self-employed—contractors, home-business operators, day laborers, freelance writers, people with livelihoods more precarious and benefits far scanter than regular employees. And studies have found that although most workers who lost their jobs in the 1980s and '90s eventually found new ones, those new jobs, on average, paid less than their previous ones.

Low-skilled, poorly educated workers no longer get hired in factories with solid hourly wages and benefits packages; most new jobs are in the non-unionized service sector. That helps explain why it's getting harder for low-income people to clamber into the middle class and beyond. As Aaron Bernstein of BusinessWeek recently wrote, tens of millions of workers are stuck, many permanently, in low-wage, dead-end jobs, and many middle-income workers are losing opportunities as well, as their white-collar jobs are outsourced overseas.

"The result," Bernstein writes, "has been an erosion of one of America's most cherished values: giving its people the ability to move up the economic ladder over their lifetimes." Instead, we have "an economy that is slowly stratifying along class lines," wherein only those who can afford a college degree have a shot at moving up the ladder. Author Michael Lind put it starkly in a recent Atlantic Monthly article: "We face the possibility of a new feudalism, in which most Americans provide personal services for the rich few."

Some corporate executives have little incentive to create jobs, well-paid or otherwise; their brief is to generate profits. Often, in fact, they are rewarded for cutting the company's payrolls. Last year, Merrill Lynch & Co. CEO E. Stanley O'Neal finished a three-year restructuring that axed more than 20,000 jobs. His directors showed their pleasure by nearly doubling O'Neal's pay to some $28 million. AT&T Corp. chief David Dorman laid off some 9,400 workers last year. While they were out job hunting, he was counting up various raises that boosted his pay to more than $18 million.

As income for the wealthy has grown, the taxes they pay on it have shrunk. Thirty-five years ago, the top federal tax rate was 69%; today it's less than half of that. There is a certain Darwinian logic to this. After all, the rich need publicly funded resources less than the rest of us. Why pay for public parks when you do your relaxing at a country club or beach house? Why pay for public schools when your kids go to private ones? Why worry about Social Security when you have a fat 401(k)? Why even worry about cities when you live in a gated community—as some 8 million mostly white, affluent Americans already do?

THERE IS PLENTY OF HAND-WRINGING these days about out-of-control executive pay. William J. McDonough, president of the Federal Reserve Bank in New York, has called the growing chasm between pay for executives and ordinary workers "terribly bad social policy and perhaps even bad morals."

There is even some concrete action. Recent federal regulations are forcing corporate boards to include more independent directors. Many companies are beginning to declare options as expenses (something regulators may soon force them to do), and others are phasing them out completely. Irate shareholders have introduced resolutions at hundreds of company annual meetings aimed at trimming excessive pay. At Disney, the shareholder revolt against Eisner extended to anger over Ovitz's $100-million-plus severance, which served as audacious evidence that even those executives who fail spectacularly are handsomely rewarded by the corporate plutocracy.

"There are people who realize that we have to do something, not just wait for the stock market to pick up and everyone to be happy again," says Paul Hodgson, executive pay expert with the Corporate Library, an independent research group. "But I don't know if it's enough people to create a sea change."

There's certainly no sign of a turning tide this year. Executive salaries were up in 2003, led by CEO pay that Forbes reported totaled $3.3 billion for the heads of America's 500 biggest companies. ■