CAUX ROUND TABLE

Moral Capitalism *at Work*

Business and Public Policy Round Table
July 23, 2013
University Club of St. Paul

"The Pay Problem"

Guest Speaker: Donald P. Delves, Founder and President, The Delves Group

Chair and facilitator: Steve Young, Global Executive Director, Caux Round Table

Participants: Grant Abbott; Peter Bell; Tony Blaine; John Buettner; Marilyn Carlson-Nelson; Nicholas Conant; Karen Harris; Ron Heinz; Fred Kiel; Deb Knutson; Bob MacGregor; Sue Miller; Kristy Modrow; Charles Montreuil; Rob Scarlett; Gary Stern; Al Zdrazil

Staff: Jessica Fiala; Jed Ipsen

We have a system where many make little and a few make a lot. Is this inevitable? Is it necessary? What do we do about it?

Attendees responded to the above questions, commenting that CEO pay is expected to be high, even if the individual's work is primarily focused on maintaining the status quo. For lower classes, pay is tied to effort and results. In turn, this places CEO pay out of relationship to value created.

The connection to a culture of wealth was also noted, wherein the rich decide what compensation the rich receive. Within this system there is simultaneously a strong animus/antagonism towards working classes and their attempts to increase their own wages. The system is maintained and perpetuated by CEO compensation advisors assuring companies that high compensation packages are indeed needed to retain executives. A contradiction was also highlighted – that CEO compensation may continue to rise even when a company is performing poorly. In response to this current environment, it was deemed that we need leaders, not simply "CEOs."

Don Delves proceeded to outline the history of CEO compensation and its rise and fall alongside variances in trends, legislation and company performance.

The question of CEO duration was raised. It was perceived that perhaps in the past, CEOs created careers at single companies, whereas some perceived that there is now more movement, a point debated by other attendees. With the impression of increased movement comes the concern that CEOs new to a company are unaware of company culture, buried skeletons, internal or board conflicts and underlying persistent problems. Does the impression that one may leave quickly lead to a diminished sense of loyalty and responsibility? Does the fear that one may be fired by a board within a year lead to actions designed for quick results rather than long-term stability? If someone holds a position for a short period, do they risk being ineffective? If a CEO stays on too long, does a company start to need "fresh blood?"

One suggested solution would be for companies to invest in a group of top executives, to support and grow its own future leaders early in their careers. Each industry has its own timelines, specialized modes of operation and needs. There is not a "cookie-cutter" CEO who can thrive in and advance any company. But, are business schools teaching the opposite? While certain skills do transfer from one context to another, are we teaching the next generation of business leaders that it is not necessary to specialize?

Are we paying for the right things? How do you create a virtuous cycle where everyone wins? If CEOs own stock in the company, company success means higher compensation for the CEO. Can you create a system where everyone in the company benefits from success?

In part, concern over CEO compensation is related to the dramatic economic disparity in the United States. While the larger issue is complex and difficult to change, CEO pay is perhaps perceived as one clear distinction that could be altered. Disparities, however, are multifold – wealth disparities, income disparities, consumption disparities. While the notion that higher income brackets consume more may be common, it is the middle class' ability to consume that drives the economy through its cumulative mass impact. If increases in the cost of living are not reflected in wages, the ability to consume is stifled and the economy as a whole suffers.

In lieu of higher wages, employers often offer benefits, a politicized issue in the context of recent debates over Obamacare. Yet, although a significant cost for employers, these benefits do not offset other costs of living for workers. Therein lies a conundrum where companies feel they are paying more, yet workers are not necessarily receiving more in terms of basic wages.

The focus, thus far, has been on the United States and company responsibilities to workers in this country. In our global economic environment, however, employees, CEOs, etc., are not solely based in the United States. In a global context, discussions of CEO pay are, for example, not concerned with the U.S. healthcare system.

Across contexts, anxiety is in part linked to the experiences of lower income brackets. Does high compensation actually foster a strong economy for all? Shareholders have more influence now than they use to, but is this good? Shareholders are merely investors and do not necessarily care about employees. Is our current system set up in a manner that could produce benefits for all?

Many jobs that formerly sustained middle classes have been replaced by technology or outsourced, forcing middle class workers into lower paying jobs not designed to sustain a middle class lifestyle. How can we create jobs that will allow individuals to participate in the work force at a level that both produces value and sustains a middle class quality of life?

When you look at categories of stakeholders in Corporate Social Responsibility approaches, employees are number two. But, when you look at corporate action, very little focus is given to employees. In particular, the level of appreciation of human resources ("HR") has been in decline. Within business schools and the corporate world, HR departments are moving down in the hierarchy of importance. Globally, this de-emphasis is puzzling, particularly given the high rates of unemployment among youth around the world. How can we run societies when a high percentage of youth are unemployed and lack hope for a better future? What do governments do when their debt is too high to be able to carry this portion of the population or reinvigorate the economy?

One response is to promote financial literacy to children so they can learn what a budget is, how to manage it and the importance of saving. While significant, such work does not solve the problem of unemployment, but it does provide the necessary knowledge base for individuals to take full advantage of employment.

In a flatter, more competitive global context, executive pay becomes even more important – it is our future. A company (or a country) will succeed through innovation and innovation starts at the top with a leader that is both innovative and capable of motivating and inspiring others for innovation. The model of CEOs focused on self-advancement or shareholders alone does not produce needed results. Motivation and innovation must work throughout a company and focus on employees and customers, as well. Within the U.S. context, one must acknowledge that this is a high-cost country with a high-cost quality of life compared to other nations. An expressed concern over executive compensation is "does it get in the way of good leadership?" Are we incentivizing executives to be good citizens or to increase value for shareholders? Unless we shift the focus away from money, we are incentivizing greed amongst a few, not creating a sustainable economic system for the entire country.

Linking CEO compensation to stock prices ensures that CEOs benefit from company success. Can we spread this model to other areas of the workforce? Can individuals in other areas of the service economy – restaurants, hotels, retail – also benefit from the success of their employer? Can we create a system where those workers can earn enough to support a family?

Perhaps one solution comes from transparency and communication with employees, involving them in the process by explaining the costs to the employer to retain an employee and, therefore, the needed outputs from the employee. Creating a sense of responsibility, partnership and active involvement can tie individual performance to unit and company-wide performance. Is the solution based in ideals of a free society? Does this come down to the actions of individuals?

Decisions emanate not from legislation, but from value systems. What are needed are corporate leaders who partner with government leaders. What are needed are leaders with good core values.