# CEO Pay: Aligning Stakeholder Interests Using the 1% Solution

## Description

The uproar surrounding the compensation fiasco at **Bombardier, Inc.** (TSX:BBD.B) has forced the company to defer more than half the incentive pay awarded six executives in 2016 until 2020.

"We are doing a mea culpa on the way we communicated this; we should have spoken more quickly to the population," CEO Alain Bellemare told the TVA Network. "I think at a certain point, we have to recognize what happened. We [also] have to understand why compensation policies are built the way they are if we want to keep our head offices strong in Montreal."

There are two problems with this statement.

First, if you have to communicate to the world why and how you're paying your executives, there's a good chance you understand you're not being honest with shareholders or rank-and-file employees on this issue.



Second, if excessive compensation is the only carrot to get world-class talent to live and work in Montreal, that speaks volumes about how the rest of the world views the city and its place in the global economy. If I lived in Quebec, I'd be far more concerned about the latter.

Although my most recent article about Bombardier first appeared April 3, I wrote it shortly after reading about the company's generous executive compensation in *The Financial Post* March 29 before protests forced it to postpone the pay packages until at least 2020.

"*The Financial Post* revealed March 29 that Bombardier, Inc. (TSX:BBD.B) compensated its top five executives and Board Chairman Pierre Beaudoin to the tune of US$54.5 million over the past two fiscal years, despite delivering US$6.3 billion in losses," I said. "While the fat cats in the C-suite got paid handsomely for undertaking a turnaround plan that is still very much in doubt, almost 15,000 current employees found out they'll be on the unemployment line by the end of 2018."

Bombardier is by no means the only guilty party in corporate Canada when it comes to overpaying executives; Bellemare was only 53rd in *Canadian Business* magazine's latest ranking of the top 100 highest-paid CEOs. But then, most of the other executives haven't been the recipients of billions of dollars of government loans.

Investors continue to worry about dual-class share structures when the real problem is executive compensation; for every Bombardier, there's a **Fairfax Financial Holdings Ltd.** (TSX:FFH) or **Canadian Tire Corporation Limited** (TSX:CTC.A), whose shareholders have done just fine with a controlling shareholder.

However, there's a way out of this mess by simply aligning the interests of all the stakeholders, not just the shareholders.

I call it the 1% Solution

Take Canadian Tire, for example.

It grew operating profits from $1.094 billion in fiscal 2015 to $1.105 billion in fiscal 2016. Employees of all stripes, including executives, would receive 1% of the annual operating profits or 50% of the growth, whichever is less.

So, 1% of the operating profits was $11.1 million in 2016; 50% of the growth was $5.5 million. Therefore, $5.5 million would be put aside for all employees based on the previous year's cash salary and cash bonus. In 2016, Canadian Tire had personnel expenses of $1.2 billion, the lion's share of which was for salaries.

The CEO's cash salary and cash bonus would be divided into $1.2 billion with the resulting percentage paid out from the $5.5 million. So, if the CEO got $5 million in cash salary and $2 million in cash bonus the previous year, he or she would receive 0.64% of the $5.5 million, which works out to $35,000.

It might not seem like a lot, but then Canadian Tire's operating profit only increased by 1% in 2016.

A compensation system that controls how much is paid in salary, bonus, and profit sharing with no regard to stock price ensures everyone is focused on building a profitable business, not goosing the stock.



My proposal eliminates the games played regarding stock options and awards. However, because the so-called at-risk compensation goes way down, that increases the required amount of stock that must be held by executives, all of it bought on the open market. Executives should have to pay to play.

In Bombardier's case, if Bellemare and company really believe in its turnaround, my 1% Solution would see them do just fine come 2020.

But we all know this would never happen because there are too many who benefit from this most egregious form of shareholder and stakeholder abuse.

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