

**LER 590EC Executive
Compensation** University of Illinois at
Urbana-Champaign Spring 2017

Time: Tuesdays, 11 AM – 1:50 PM, March 14-May 2 (2nd half of the semester)
Location: 47 LER Building (504 E. Armory Avenue)
Instructor: Jiwook Jung, Assistant Professor
235 LER Building
Email: jwjung@illinois.edu
Tel.: 217-300-4339

Course Description

Designing an efficient and equitable compensation system for executive managers has a strategic importance with an implication for a broad set of stakeholders. The main objective of this course is to introduce to HR/IR students fundamental concepts and issues about executive compensation and corporate governance. The discussion will focus on the context of publicly traded companies, but the implications will also be relevant to compensation systems for leadership positions in other kinds of organizations. The course will review opposing views on the nature of executive compensation and examine the evidence for each view. The course will also discuss ethical issues, societal concerns, and international comparisons about executive compensation.

To balance theoretical understanding and practical skills, students will examine actual compensation contracts from public corporations and analyze their strategic effectiveness.

Course Requirements

Readings:

This is a reading-intensive course. It is extremely important to come prepared for each class session. Assignments should be read and given some thought in advance of class. You will not be able to successfully complete the course without full understanding of the readings. Exams and other assignments are designed to ensure that you complete the readings and understand the concepts in them thoroughly.

Each week's readings typically consist of one or two conceptual pieces, one or two newspaper articles, and one business case (except for Week 1). The cases are carefully

chosen to illustrate core concepts that are introduced in the conceptual pieces. The cases are intended to help you understand the concepts in a real-world setting and to provide the basis for class discussion.

Some information may seem dated, but consider it as relevant information that helps us understand historical background of the organization. The cases are not intended to provide up-to-date information about the companies or regulatory policies. Keep in mind that our goal is to learn the underlying concepts rather than to know more about the specific companies featured in the cases.

Participation:

Active student participation is essential to successful class sessions. Your ability to contribute comments that are relevant and insightful is highly valued in this course. You will be cold-called to contribute to the class discussion.

Attendance:

Attendance is required at all class sessions. Attendance includes arriving on time and remaining until the end of the session. If you know ahead of time that you cannot attend class due to illness or civic duty (court appearance, jury duty, etc.), please notify the instructor immediately.

Case memos:

You are required to submit a **2-page**, double-spaced memo at each class that has a case reading assignment. You are required to submit **4 out of 5** assigned memos. If you submit more than four, the best four will be used in grade calculations. Use 12-point font size, with at least 1 inch margins all around. Upload your memo to the course website by the beginning of each class (11:00 AM). Case memo questions and submission folders will be displayed one week before each due date. Late memos will not be graded. The questions for the memo will be posted on the Illinois **Compass 2g** website for this course (log in at <https://compass2g.illinois.edu/>). Each memo will be worth 15 percent of the total grade.

Final examination:

The final exam will be at **11:00 AM - 1:50 PM on May 2, 2017 (47 LER)**. The exam will cover all topics of the course. The exam will be open book, open notes. The exam will be administered through the course website (compass 2g) during in the classroom. So you need to bring your laptop to do the test. Detailed guidelines for the exam will be provided later toward the end of the semester. The exam will be worth 40 percent of the total grade.

Course Materials

1. **Compass.** Some readings in PDF are available on the Illinois Compass 2g website for this course. See the section “Course Website” below for more information.
2. **Harvard Business Publishing website.** All cases are available for purchase on the Harvard Business Publishing website at: <https://hbr.org/store/case-studies>.

On the course schedule below, each reading has its source noted in the brackets (e.g., [Compass]). You do not need to purchase any textbook for this course.

Course Website

A website for this course (LER 590EC) is set up at Illinois Compass 2g at <https://compass2g.illinois.edu/>. Required readings, PowerPoint slides, case memo questions, and useful resources will be posted there. Please check frequently for updates. When the level of class attendance declines, the instructor may reduce the amount of information contained in the PowerPoint slides posted on Compass in order to encourage attendance.

Academic Integrity

In order to maintain a vigorous and healthy learning environment in the classroom, it is critical that no member of the class engage in or tolerate academic fraud, such as cheating or plagiarism. We believe strongly in giving certain liberties to students, and in return we expect honest and honorable conduct, including compliance with the University of Illinois’ Student Code (see <http://admin.illinois.edu/policy/code> for details).

Since our reading materials and discussion topics include examples from well-known companies, it is often the case that relevant information can be found in the sources other than designated course materials (for example, the Internet, magazines, newspaper, etc.). Whereas referring to external sources is fine and encouraged, it may be tempting to use or copy information from such sources in your course assignment *without proper acknowledgement of the sources*. Such action is considered **plagiarism** and strictly prohibited. Brief guidelines about what constitutes plagiarism and how to avoid it will be provided during the class, but it is ultimately the students’ responsibility to educate themselves about the risk of plagiarism and avoid committing it. Carefully review the University policy governing academic integrity and plagiarism, including the Student Code Article 1, Part 4, §1-402 “Infractions of Academic Integrity” (http://admin.illinois.edu/policy/code/article1_part4_1-402.html). Not knowing the policy is not an excuse.

This policy applies to **all** written assignments of this course, including case memos and exam answers. Any incidence of plagiarism will be handled according to the official University policies and reported to the University administration.

Schedule

Week 1	Mar 14	<u>Introduction and Corporate Governance</u> <ul style="list-style-type: none">- Margaret M. Blair. 1995. <i>Ownership and Control</i>. Washington, DC: Brookings Institution. Chapter 2, pp.17-76 (skip pp.33-44, sections “More on the role of debt and equity,” “The mix of debt and equity matters,” and “How real is the distinction between debt and equity.”) [Compass]- Peter Eavis. 2013. Executive pay: Invasion of the supersalaries. <i>New York Times</i>, June 29, 2013. [Compass]
Week 2	Mar 21	Spring Break (no class)
Week 3	Mar 28	<u>Executive Compensation: A Primer</u> <ul style="list-style-type: none">- Kevin J. Murphy. 1999. “2.3. The components of CEO pay,” “2.4. Who sets CEO pay?” from <i>Handbook of Labor Economics</i>, Vol. 3, edited by O. Ashenfelter and D. Card, Elsevier: New York, pp. 2497-2518. [Compass]- General Electric Co., Form DEF 14A, “Other definitive proxy statements,” also entitled “Notice of 2015 annual meeting and proxy statement,” filed at the U.S. Securities and Exchange Commission (SEC) on March 10, 2015. [Not on Compass or Harvard]- Case: “CEO Compensation at GE: A Decade with Jeff Immelt” Harvard Business School, Case #9-112-003. [Harvard Business Publishing]- Case memo due
Week 4	Apr 4	<u>Stock Options and Long-Term Incentive Pay</u> <ul style="list-style-type: none">- Randall A. Heron, Erik Lie, & Tod Perry. 2007. On the use (and abuse) of stock option grants. <i>Financial Analysts Journal</i>, 63(3): 17-27. [Compass]- Mark Maremont and Charles Forelle. 2006. Bosses’ pay: How stock options became part of the problem. <i>Wall Street Journal</i>, December 27, 2006. [Compass]- Case: “Executive Compensation at Nabors Industries: Too Much, Too Little, or Just Right?” Stanford Graduate School of Business Case: CG-5. [Harvard Business Publishing]- Case memo due
Week 5	Apr 11	<u>Pay For Performance</u> <ul style="list-style-type: none">- Michael C. Jensen and Kevin J. Murphy. 1990 [2010]. CEO incentives: It’s not how much you pay, but how. <i>Harvard Business Review</i>, May-June, pp.3-18 (Reprinted in 2010 in the <i>Journal of Applied Corporate Finance</i>, 22(1): 64-76). [Compass]- Lucian Bebchuk and Jesse Fried. 2004. <i>Pay Without Performance: The Unfulfilled Promise of Executive Compensation</i>. Cambridge, MA:

- Harvard University Press. Chapter 1, pp.15-22. [**Compass**]
- Robin Ferracone. 2011. CEO pay: When highly paid is not overpaid. *Forbes*, April 19, 2011. [**Compass**]
- **Case:** “General Dynamics: Compensation and Strategy (A)” Harvard Business School, Case #9-494-048. [**Harvard Business Publishing**]
- **Case memo due**

Week 6 Apr 18

Psychological and Political Factors

- Lucian Bebchuk and Jesse Fried. 2004. *Pay Without Performance: The Unfulfilled Promise of Executive Compensation*. Cambridge, MA: Harvard University Press. Chapter 2, pp.23-44; Chapters 5-6, pp.61-86. [**Compass**]
- Peter Whoriskey. 2011. Cozy relationships and ‘peer benchmarking’ send CEOs’ pay soaring. *Washington Post*, October 3, 2011. [**Compass**]
- **Case:** “AFL-CIO: Office of Investment and Home Depot.” Harvard Business School, Case #9-407-097.[**Harvard Business Publishing**]
- **Case memo due**

Week 7 Apr 25

Policies and Ethics about Executive Compensation

- Steven N. Kaplan. 2008. Are U.S. CEOs overpaid? *Academy of Management Perspectives* 22(2): 5-20. [**Compass**]
- James P. Walsh. 2008. CEO compensation and the responsibilities of the business scholar to society” *Academy of Management Perspectives* 22(2): 26-33. [**Compass**]
- Jesse Eisinger. 2013. In shareholder say-on-pay votes, more whispers than shouts. *New York Times*, June 26, 2013. [**Compass**]
- **Case:** “Al Dunlap at Sunbeam.” Harvard Business School, Case #9-899-218. [**Harvard Business Publishing**]
- **Case memo due**

Week 8 May 2

Final Exam (in class)