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Executive Pay Out of Control? Try a Reverse Bonus.

Management consultants are paid to supply good ideas. Sometimes they even hit home.

McKinsey & Co. is one of the most respected and savvy management consulting firms on the planet, but earlier this summer, when revenues weren't materializing, it set about raising funds internally, and from its employees, no less. The company asked all 850 partners, including 275 senior-level directors, to return a chunk of prior earnings—as much as \$200,000 each depending on performance and tenure.

Manager's Journal

By Gerald C. Meyers
And Susan Meyers

Presumably this is money they were paid during the flush 1990s, when partners of such firms typically took home millions of dollars each in performance bonuses.

McKinsey claims this is merely a "call on capital" from its senior people, a routine mechanism, really, just to tide the place over until the economy picks up.

But McKinsey isn't being entirely forthright about its cash-back request. The firm created its own cash squeeze by over-hiring and cutting too many big bonus checks. So what happens now to executives who have already spent the dough, or can't readily get their hands

on their investments? That's their problem, McKinsey says. If they need to borrow the pay-back money, McKinsey will assist with bank loans—an apparent admission on McKinsey's part that it had a hand in creating this mess.

McKinsey was following a plan when it lavished money on employees—it was part of a just-in-time strategy to disperse cash to the partners and reduce the tax exposure of the partnership as a whole. But McKinsey misjudged its cash needs, and the economy crossed the firm up. Try as it may, McKinsey cannot perfume this pig.

Or can it? Maybe McKinsey is on to something here. Call it the reverse bonus. It's a first-rate idea, and its timing is beautiful.

Everyone knows that top executives are overpaid. Until now, no one has been willing to do anything about it. But doesn't it make good sense to call back bonuses and

stock options awarded on the basis of a performance that doesn't materialize, or that proves excessive with the passage of time? Isn't this only fair to stockholders and other stakeholders?

Studies indicate that earnings in recent years have been overstated in several industries, including such telecommunications-equipment companies as Nortel, Cisco and Lucent. So-called creative accounting and marketing devices were often employed to boost sales and profits artificially. Customers enjoyed excessive credit that could never realistically be repaid. Even so, compensation committees at many major companies saw fit to award wheelbarrows of money to senior executives for such flaky accomplishments.

Executive pay that was unearned should be returned. Richard McGinn departed Lucent last year with perhaps \$66 million in his jeans. Was John Chambers at Cisco really worth the \$157 million he realized last year? Did Cary Fiorina produce enough to warrant the eight digits she got at Hewlett Packard?

Compensation specialists argue that the market drives executive pay.

They say that to attract key people you have to guarantee a bundle—whether they perform or not.

Ironically, top-level failures like "Chainsaw" Al Dunlap are often paid princely sums just to go away. Stockholders would be more reassured by companies that could call in oversized bonus and stock-option payments. If stock prices fell ex-

cessively or earnings took a dive, company coffers would be replenished by those who had prematurely tapped the till.

To be sure, a reverse bonus plan has its weaknesses and is not always appropriate. In some industries extraordinary risk must be assumed to cultivate breakthrough technologies or major health-care advances. Outcome prediction is especially hazardous here, and some allowances are in order.

This has happened in the industrial world several times in the last century. Few would begrudge Thomas Edison, Henry Ford or Bill Gates great monetary fortune in view of their outsized contributions to our quality of life—even if they, too, occasionally failed. Failure often points the way to a solution. Scientists applaud dead-end research for knowledge that rules out additional unproductive pursuits. So perhaps performance-related pay for the Steven Jobs of the world doesn't make sense. It's a different matter when it

comes to corporate bureaucrats.

McKinsey is offering the rest of us a just solution to unwarranted executive pay. At McKinsey employees have no choice but to pay up. Stakeholders at other companies should demand similar accountability. It's time that business cleans up its act. One of these days companies that ignore the consequences of excessive executive compensation will face a shareholder revolt or further government regulation. McKinsey's reverse bonus may be just the ticket to avoid such unhappiness.

Mr. Meyers, former chairman and CEO of American Motors, is a professor at the University of Michigan Business School. He and his daughter Susan are co-authors of "Dealers, Healers, Brutes and Saviors: Eight Winning Styles for Solving Giant Business Crises (Wiley, 2000).

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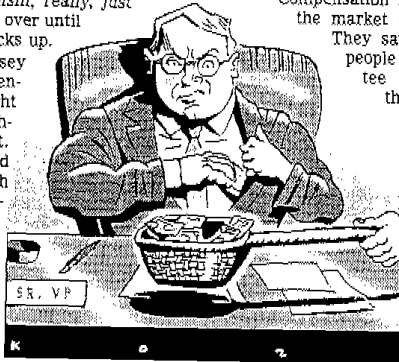
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