$140 million cash payout for New York Stock Exchange CEO

Jeremy Johnson
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Eyes popped even among Wall Street's high flyers when the New York Stock Exchange (NYSE) revealed its $140 million payout to its Chairman and CEO Richard Grasso. The payment was negotiated as part of a deal to extend the 57-year-old Grasso's current contract, due to expire in 2005, another two years to 2007. It represents $51.6 million accumulated in his pension plan, $40 million in a "supplemental" executive savings account, plus another $47.9 million in "incentive awards."

The payout is extraordinary even by the standards of the brokerage giants that produce billions of dollars of profits—all the more so because Grasso's windfall is in cash, rather than in the stock most executives receive, which is subject to market downturns. Moreover, the NYSE advertises itself as a "not-for-profit" corporation, whose main function is to provide a market where its 1,336 member-owners can trade securities. It is also charged with regulating its members to ensure fair and efficient trading for the investing public, a secondary responsibility that many observers see as an inherent conflict of interest, since the brokers being regulated own the NYSE itself.

Thursday's *Financial Times* of London reported a move by as many as 400 members—consisting mostly of those who rent their seats on the exchange to others—to file legal action to force a renegotiation of Grasso's package. Another group of members is reported to be petitioning for changes in the composition of the NYSE board of directors, whose members are said to be too much under Grasso's influence.

Reports of Grasso's gargantuan pay packages started circulating last May, with estimates of total compensation of $12 million in 2002 and $20 million the year before. In spite of NYSE board member claims of a new "transparency," Grasso's year-by-year pay has yet to be revealed. William Donaldson, chairman of the federal Securities and Exchange Commission (SEC), has demanded this information as part of investigation into possible corruption in the setting of NYSE executive pay. Donaldson was himself the chairman of the NYSE from 1991 to 1995.

Until public scrutiny forced a change this past June, the NYSE board's compensation committee (which sets Grasso's pay), included a number of CEOs of the largest brokerage firms that the NYSE was supposed to regulate. David Komansky of Merrill-Lynch, James Cayne of Bear Stearns, and Henry Paulson of Goldman Sachs were the most well known. The former chairman of the compensation committee was Grasso's long-time friend Kenneth Langone, the director and founder of Home Depot, on whose board Grasso still sits for now, although he has promised to step down.

While these obvious insiders have resigned from the compensation committee, its new chairman, the former New York State comptroller and last year's unsuccessful Democratic candidate for governor H. Carl McCall, lauded Grasso in a press release announcing his $140 million payout. He later said he was "surprised" that the SEC would question the size of Grasso's package, stating, "He was entitled to this money."

McCall, who parlayed his now defunct political career into the Vice-Chairmanship of the private equity fund HealthPoint Partners, specializes in providing image makeovers to corporations caught up in scandal. In January, only two months after losing the gubernatorial election, he accepted a seat on the board of directors of Tyco, Inc., a company notorious for the corruption of its executives led by former chairman Dennis Kozlowski, who looted company assets to the tune of hundreds of millions of dollars. Its current chairman Ed Breen was among the country's highest paid executives in 2002, raking in $62 million for only a few months on the job. At the time of his board appointment, McCall gushed about Tyco's "outstanding management and commitment to the highest standards of corporate governance."

McCall similarly described the NYSE's Grasso, stating with brazen cynicism that "throughout his term, Dick has shown an unwavering commitment to regulation and the interests of America's 85 million investors." In fact, only last April, 10 leading NYSE members were fined a total of $1.4 billion for fraudulently misleading the investing public about the value of certain stocks! In that case, the 10 brokers (and no doubt many others who were not caught) falsely produced favorable research reports to promote companies that were doing business with the brokers' investment banking affiliates.

The largest fine, $400 million, was paid by Citigroup, whose chairman Sanford Weill only a month earlier had been nominated by Grasso to a seat on the NYSE board, supposedly as a representative of the public rather than as a representative of the securities industry. An outcry over the world's largest banker, and parent to the major stock brokerage firm Smith Barney, being presented as an advocate of the general public forced Grasso to withdraw Weill's nomination.

(The NYSE's charter calls for 12 directors from the securities industry and 12 directors representing the "public," plus three from management. In fact, the directors designated to represent the public are top executives of such corporate behemoths as DaimlerChrysler, Viacom and AOL Time Warner, along with wealthy former political figures such as McCall and Bill Clinton's former secretary of state Madeleine Albright.)

More recently, a number of the NYSE's specialist traders—brokers who are designated to make markets in specific stocks—are being investigated for improperly profiting off the price movements in their assigned stocks. The CEO of the largest such specialist firm, Robert Murphy of LaBranche and Co., resigned his vice-chairman's seat on the NYSE board last month in a dispute over the exchange's investigation of his firm.

In part, Grasso's good fortune stems from being in the right place at the right time. After a long climb up the NYSE hierarchy, he succeeded Donaldson as chairman in 1995, as the stock market boom was getting into full swing. Under his watch, the number of companies listed on the NYSE more than doubled to nearly 2,800, with their market value now approaching $15 trillion. Share volume quadrupled, reaching 1.45 billion a day, with the transactions valued at $38 billion daily.

Grasso had a certain ability to put a congenial and reassuring face on the workings of the world's largest stock exchange, whose spectacular growth in the late '90s became based more and more on financial manipulation and fraud carried out to boost the share prices of listed companies.

Using his position as regulator of the exchange's members—who also set his pay—he succeeded in transforming the board's executive compensation policy from being on a par with other quasi-public regulatory bodies (SEC chairman Donaldson earns $142,500 a year), to being comparable with major brokerage houses, where the CEOs regularly took home eight-figure packages. The *New York Times* reports that the board determined Grasso's bonus by taking the average of the CEO pay of the big investment banking companies and reducing it 10 percent.

Since 1998, Grasso's employment contract further provided a guaranteed 8 percent return on all deferred compensation, of which he was entitled to defer 100 percent. As market interest rates dropped, the 8 percent guarantee became highly advantageous, allowing Grasso to accumulate the huge sums in his accounts that he is now cashing in.

There is no evidence of any specific quid pro quo between Grasso and the executives who set his compensation. However, it should also be noted that the NYSE played virtually no role in uncovering the scandals that overtook Enron, WorldCom and many other companies that were supposed to meet minimum standards to maintain their listing on the exchange. Likewise, the NYSE generally left it to state and federal authorities to pursue its broker-members over various schemes to defraud investors.

While McCall, in promoting Grasso's new contract, claims that the NYSE will actually save $3.5 million a year in interest expense, negotiations are still under way on two key elements of the package, namely, the new interest rate guarantee on deferred compensation and the methodology for determining Grasso's bonus. The base salary remains unchanged at $1.4 million, with the bonus set at a "minimum" of $1 million, but no maximum.

Meanwhile, Grasso himself sounds more and more hollow as he continues to try to shore up the image of corporate America. When one television interviewer asked him in July to comment on the one-year anniversary of the passage of the Sarbanes-Oxley legislation (consisting of a few cosmetic reforms, primarily having CEOs sign their company's financial statements), Grasso glibly spoke about "the enormity of reform that's come in a relatively short period of time." When later asked about what reforms he would like to see to rein in executive compensation, he quickly replied, "Well, I think we've seen it."

The size of his own pay package revealed last week would indicate why he sees no need for any further reform in that area—and neither would most of his CEO cronies.