New Pay Study Finds CFO Compensation Increased 8% in 2018, with Target Bonuses Reaching 100% of Base Salary for First Time

Structural Differences Among Industries and Moderate Correlations to CEO Pay

When we completed our analysis of CEO compensation this year, we embarked on a study of CFO pay, scanning MDG's database of 4,500+ companies for CFOs in the S&P 500 who have occupied that role continuously during the period 2016-2018—the same screening criteria used for our CEO report, intended to eliminate data noise arising from new hires, promotions, or other disruptions to the status quo.

We also compared CFO to CEO pay. Under SEC law, any individuals who serve as Principal Financial Officer within the applicable year—like any who serve in the capacity of Principal Executive Officer—are required to be named in the proxy statement, regardless of where their compensation places them among executive officers. The three other named executive officers are selected according to pay rank, as presented in the Total column of the Summary Compensation Table, minus the change in pension value and above-market or preferential nonqualified deferred compensation earnings reported in Column H. The CFO and CEO roles are therefore uniquely comparable and complementary because every disclosure must include them every year, whereas other roles may skip years because the remaining named executive officers are identified by an altogether different set of criteria.

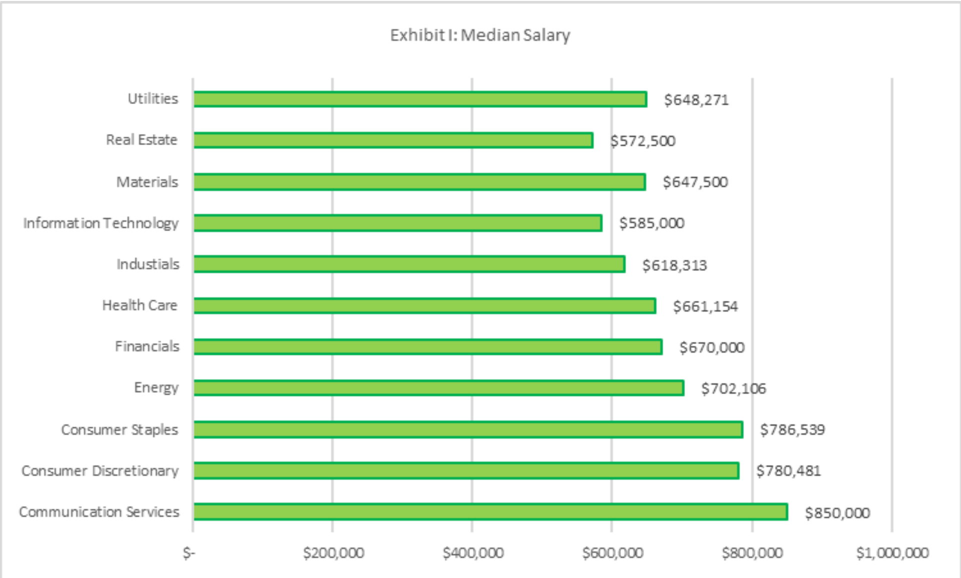
The 2018 proxy season debuted the CEO Pay Ratio, mandated under Section 953(b) of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 ("Dodd-Frank"). A key determinant of the ratio is the selection of a median employee against which to measure the CEO's compensation. Regardless of the methodological rigor applied to identify the median employee, the choice is largely a matter of happenstance; consequently, it is impossible to draw inferences between pay and function. The CFO, on the other hand, is a defined position within the management hierarchy.

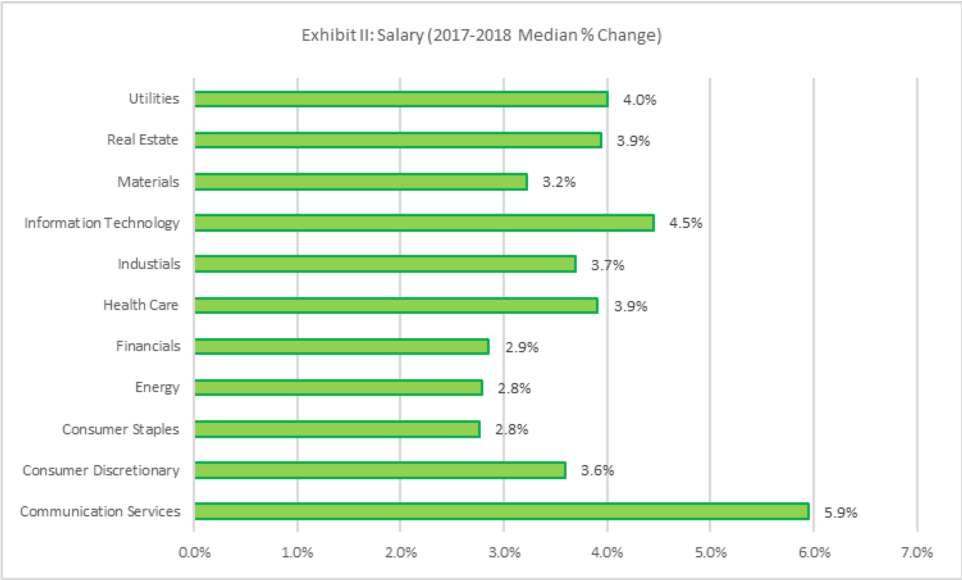
Among our findings, we conclude:

- **CFO-to-CEO pay ratio:** The median ratio was 28.2-46.9%, depending on industry.
- **Base salaries:**
    - The portion of pay attributable to CFO base salaries continued to shrink as more compensation was delivered in the form of short- and long-term incentives; and
    - CFOs tended to receive a greater portion of compensation in the form of base salaries than CEOs.
- **Short-term incentives:**
    - Target short-term incentives reached 100% of salary for the first time;
    - Payouts were significantly above target in 2018, and have been for at least the past three years; and
    - As a percent of target, payouts were higher for CEOs than CFOs, even though they frequently were evaluated on the same criteria.
- **Long-term incentives:**
    - The prevalence of options continued to decline, and the practice of granting performance-based equity increased; and
    - CFOs tended to receive a smaller portion of compensation in the form of long-term incentives than CEOs.
- **There were material distinctions by industries.**

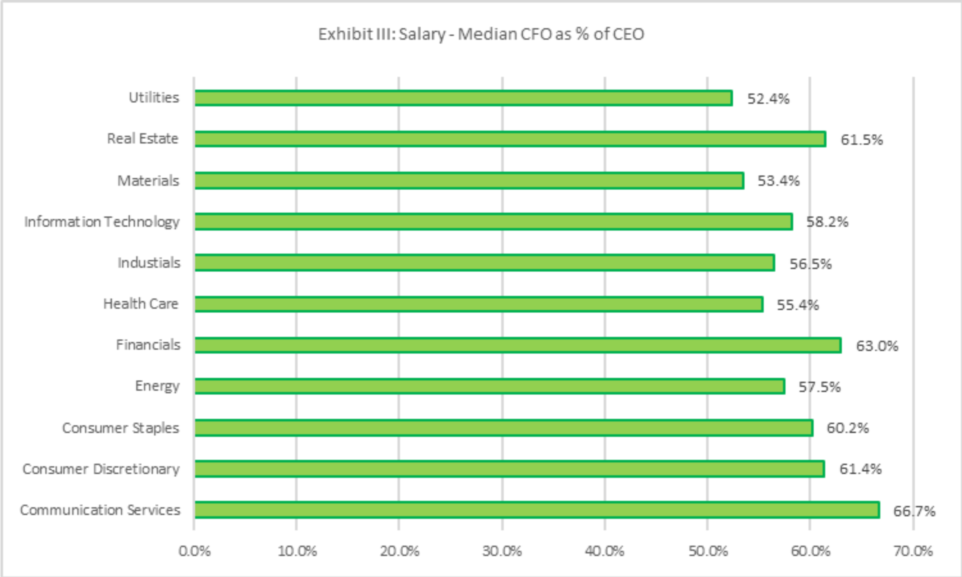
Median Salary Increase was 3.7%, with Significant Differences Among Industry Groups

Median base pay for CFOs in our sample was $664,600 in 2018. Salaries represented a diminishing component of total direct compensation, declining to a median 17.0% in 2018 (from 17.7% in 2017 and 19.0% in 2016). As in our recent similar CEO study, communication services paid the highest salary in absolute terms; it was also highest in terms of year-over-year increase (Exhibits I-II).



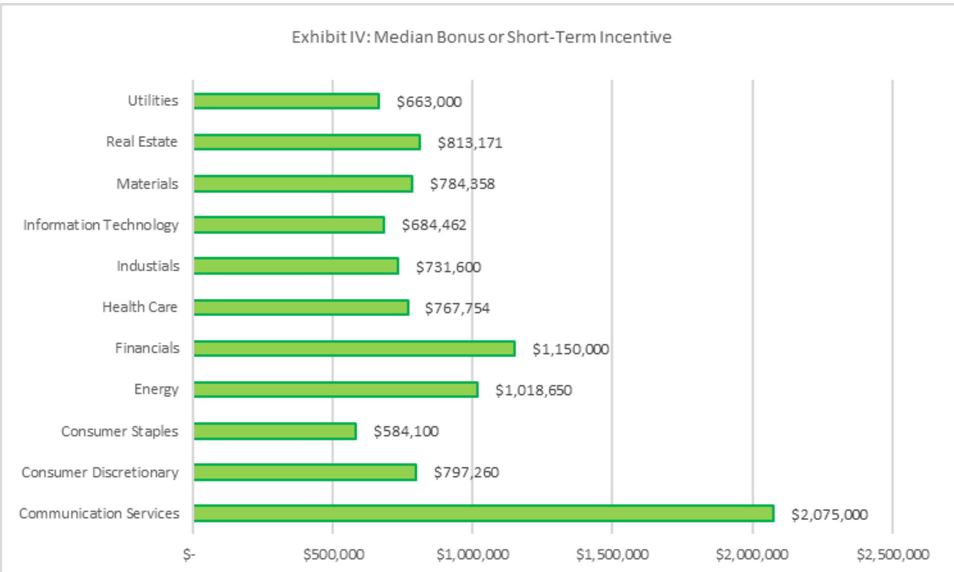


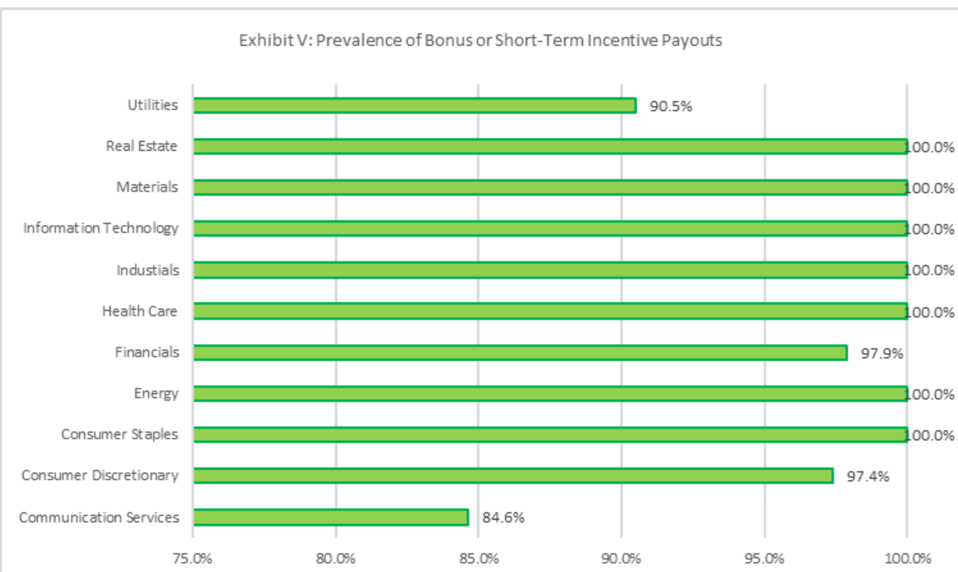
At the median, CFOs collected 58.3% of a CEO's base salary. Here again, the communication services sector led the industry (Exhibit III).



Robust Annual Bonus or Incentive Payouts in 2018

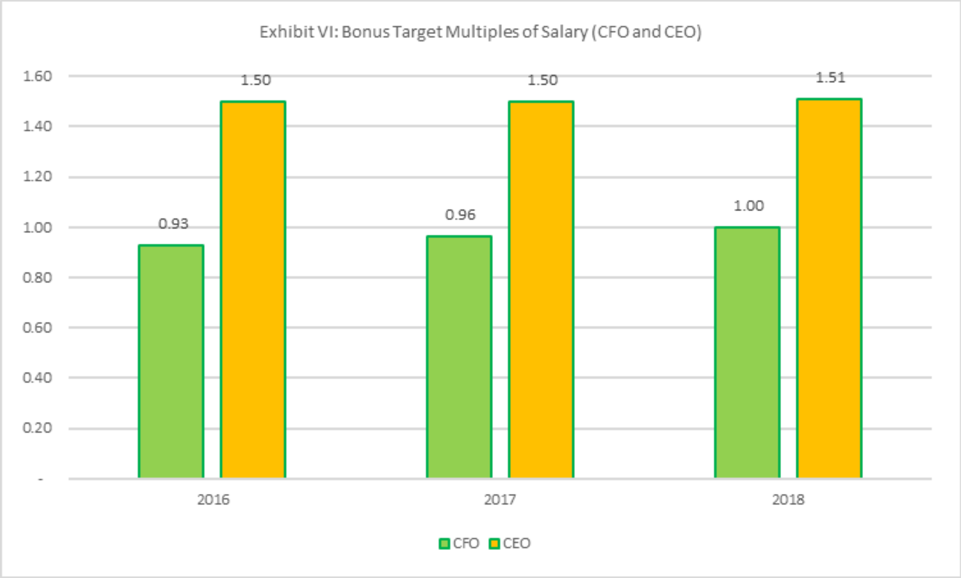
Ninety-eight percent of companies in our sample paid an annual bonus to their CFOs in fiscal year 2018, representing a median 21.4% of total direct compensation (a slight decline from 22.3% in 2017 and 22.9% in 2016). Median payouts of $827,021 were a median 22.0% premium over target (versus 25.0% in 2017 and 22.3% in 2016). The size of annual bonuses varied considerably among industry groups, with communications services the highest by a wide margin; however, only 84.6% of CFOs in this sector received one, the lowest prevalence of all industries (Exhibits IV-V).



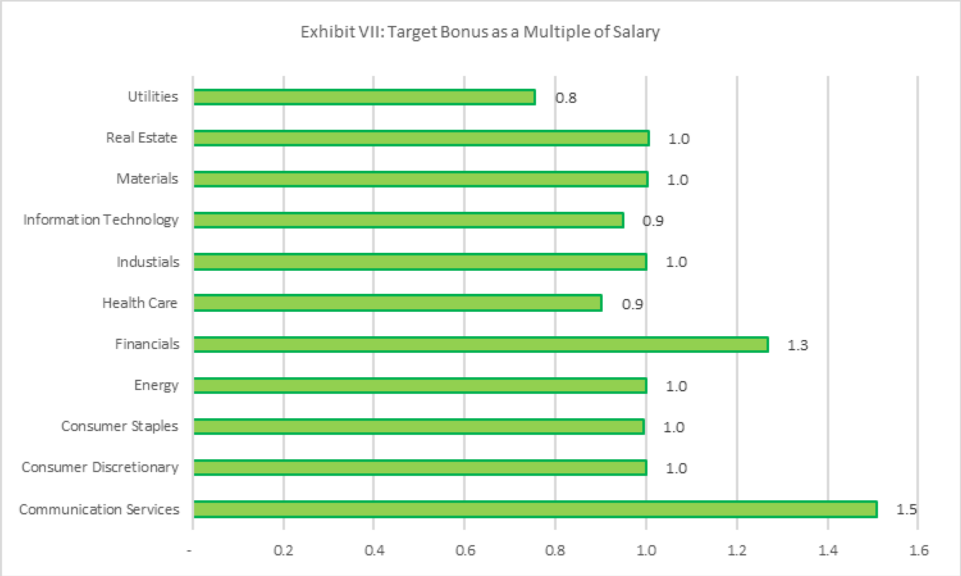


Target Bonuses Reached 100% of Base Salary

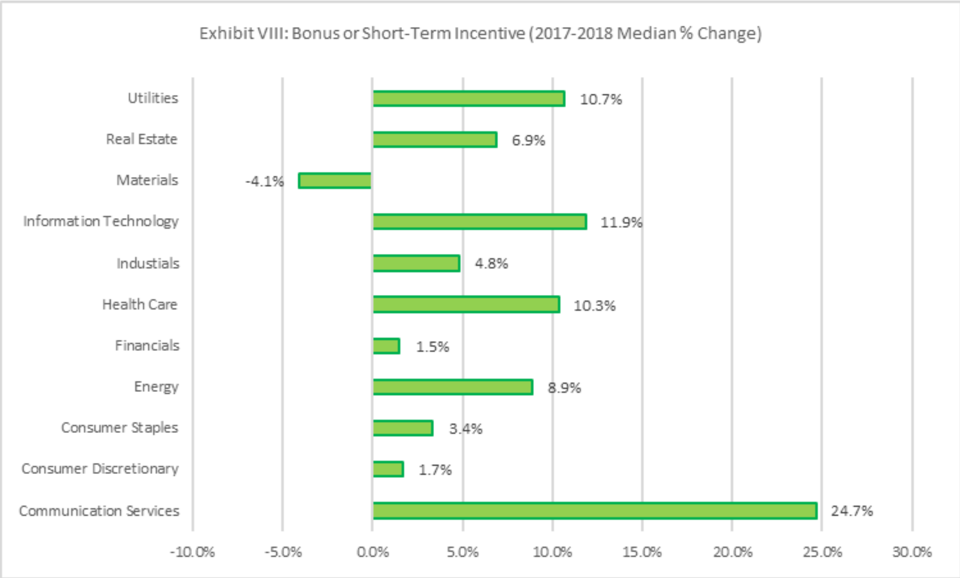
As a multiple of salary, median target bonuses rose significantly over the past three years, from .93 in 2016 to 1.00 in 2018. Over the same period, CEO target bonuses increased at a much more modest rate (Exhibit VI).



Among industries, median targets differ substantially, with bonuses for communication services CFOs targeted at nearly twice the multiple of those in the utilities industry (Exhibit VII).

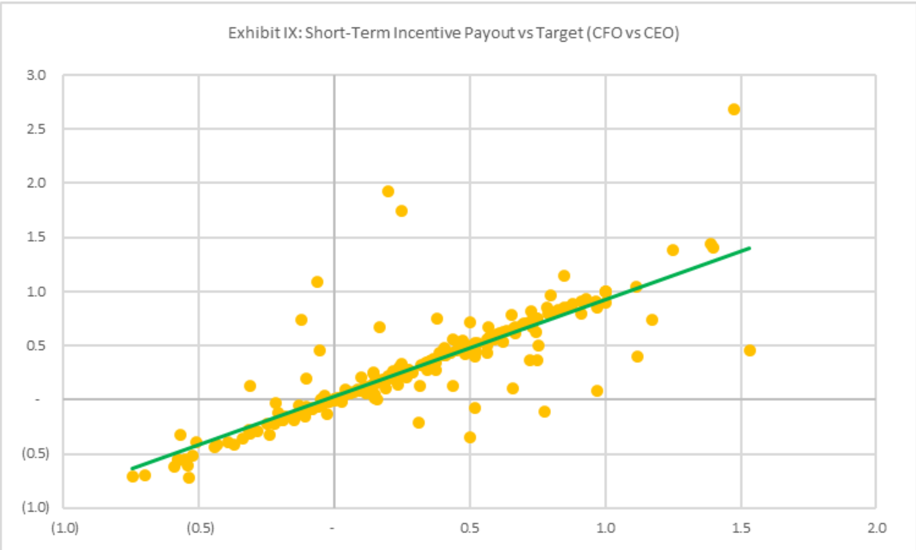


The value of bonuses increased 6.1% from 2017-2018, with the biggest increase coming in the communications services sector and materials lagging, potentially due to soft prices for chemicals and certain extractive industries (Exhibit VIII).

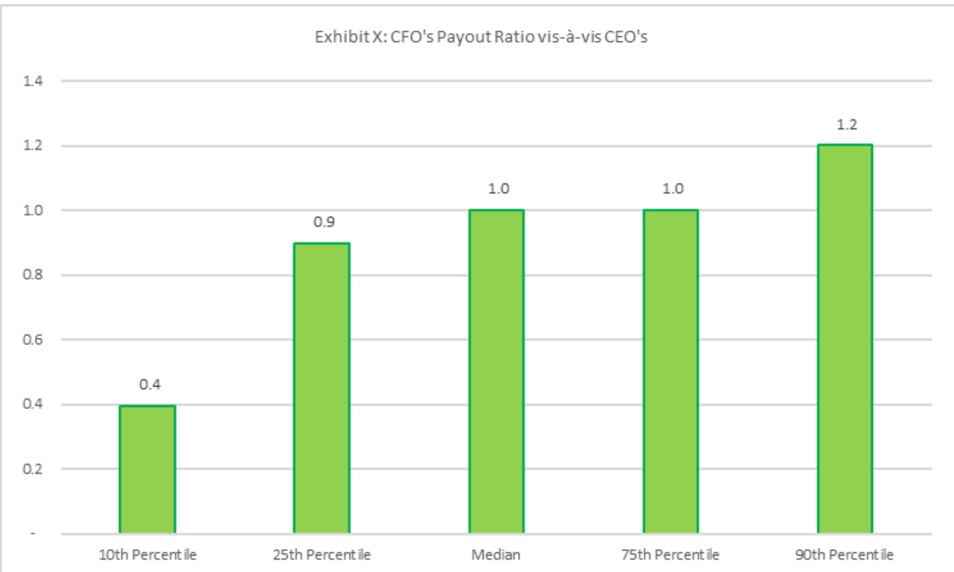


CFOs and CEOs are Evaluated on Common Criteria, but Does Their Pay Reflect This?

As a percent of target (payout ratio), short-term incentive payouts to CFOs closely approximate those made to CEOs. This by itself is not surprising, since the metrics for CEOs and CFOs often are identical (and identically weighted). The threshold-target-maximum payout slope, likewise, typically is the same for all named executive officers. Given those circumstances, one might expect the correlation between CFO and CEO payout ratios to be even higher than the relationship's moderately tight R^2 of 68.8%. Some companies, however, apply slightly different weightings to the metrics or adjust the baseline payouts to recognize individual performance, which accounts for the variance from the regression line (Exhibit IX; X axis = CEO and Y axis = CFO).

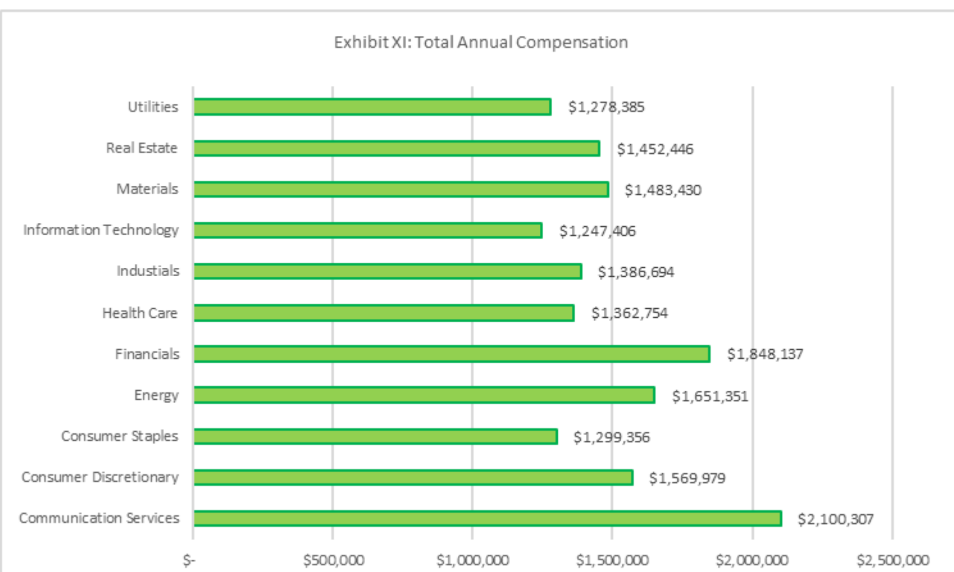


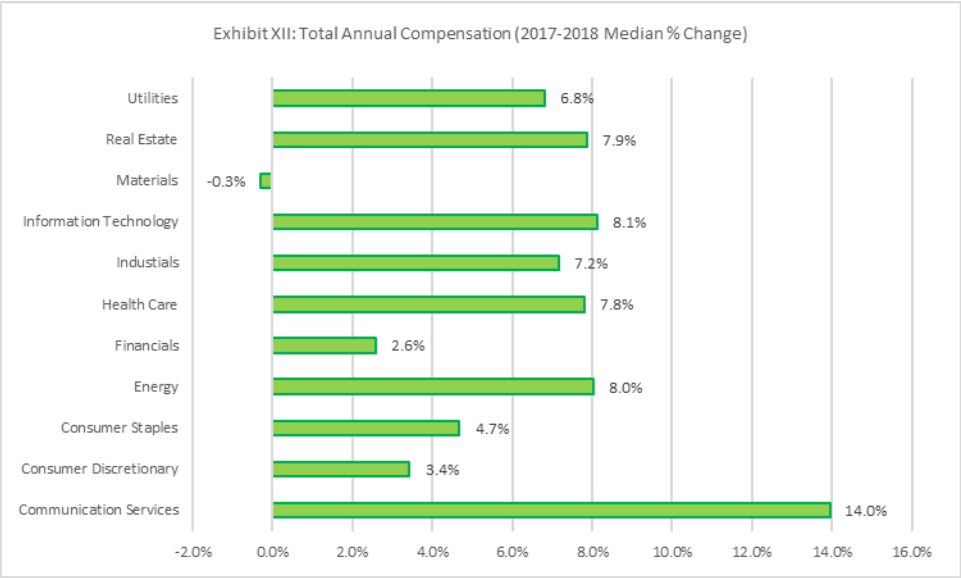
Comparing the CEO's payout ratio to the CFO's permits us empirically to measure the impact of the variance. Using 1.0 to represent perfect alignment between CEO and CFO payout ratios, we calculated the distribution and observed a strong bias in favor of the CEO. At the 10th percentile, the payout ratio for CFOs was 40% of that for CEOs, but at the 90th percentile it was only 120%. In other words, there were very few cases where the CFO exceeded target by a greater percentage than the CEOs who were evaluated on essentially the same criteria and subject to the same payout slope. When they were rewarded with a larger payout, moreover, the premium tended to be relatively modest (Exhibit X).



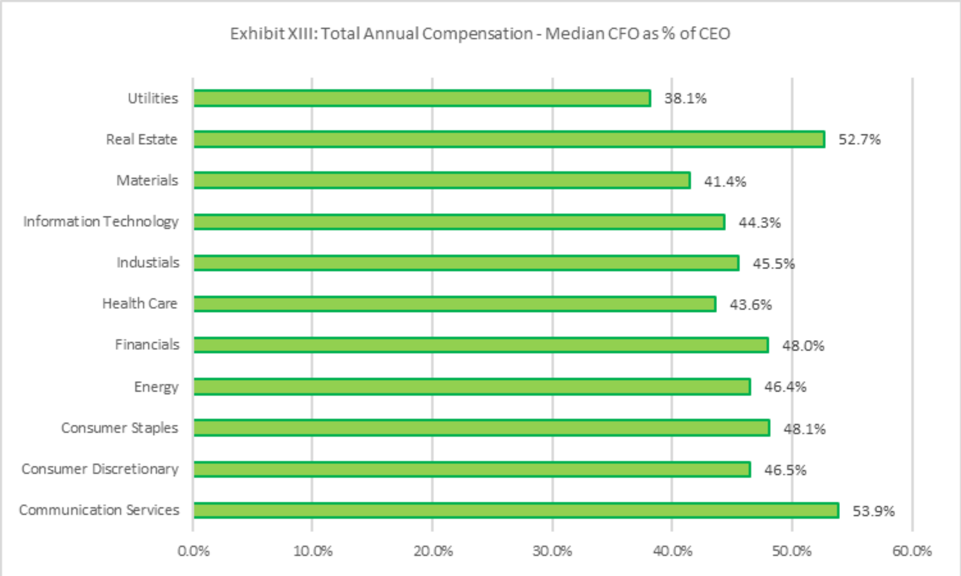
Total Annual Compensation Increased a Median 6.4% in 2018

Median total annual compensation (the sum of salary and annual bonus) reached $1,461,249 in 2018, with substantial differences depending on industry (Exhibits XI-XII).



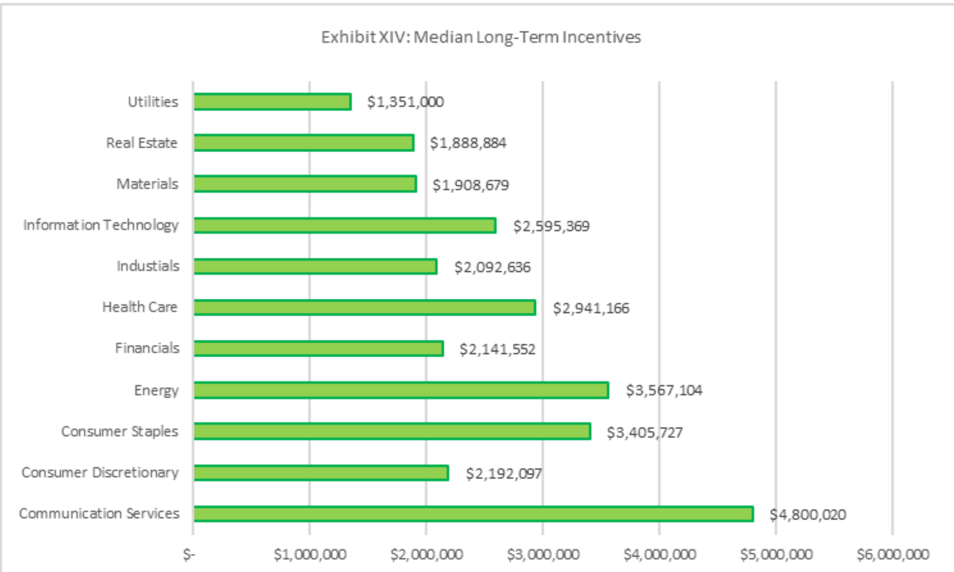


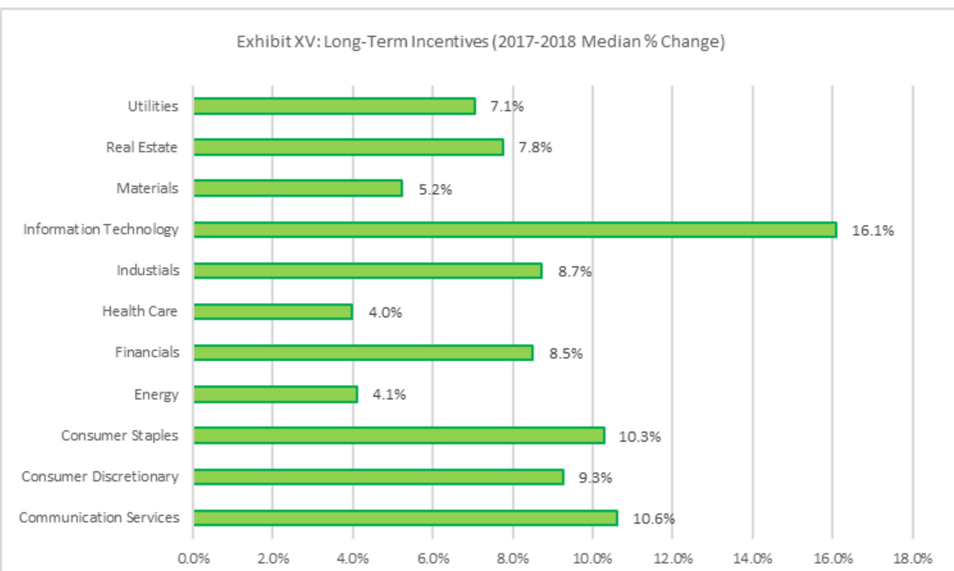
CFOs collected a median 45.4% of CEO's total annual compensation, ranging from 38.1% in the utilities to 53.9% in the communication services sector (Exhibit XIII).



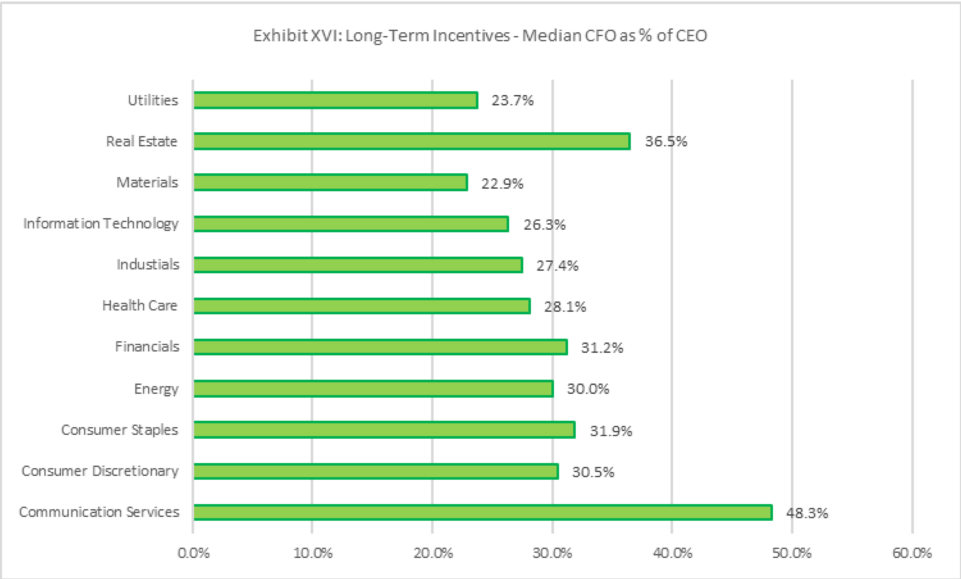
The Predominant Component of CFO Pay Remained Long-Term Incentives

Every CFO in our sample received long-term incentives of some type in 2018, with a median value of $2,288,645 representing a median 8.7% increase over the prior year. As a percent of total direct compensation, long-term incentives continued to expand, to a median 60.3% in 2018 from 59.3% in 2017 and 58.5% in 2016. As with salary and short-term incentives, CFOs in communication services received the largest grants; however, CFOs in the information technology sector experienced the largest percent increases over the prior year.



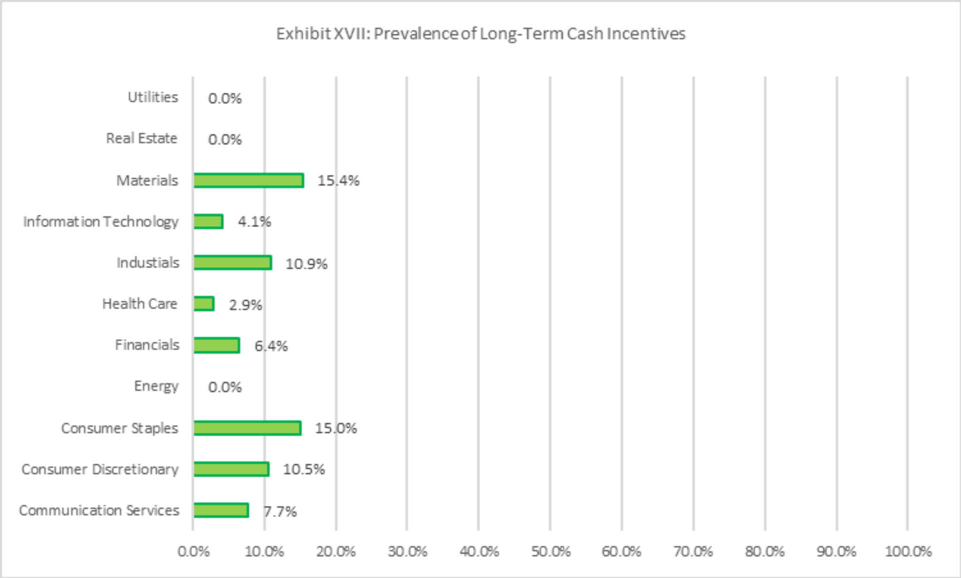


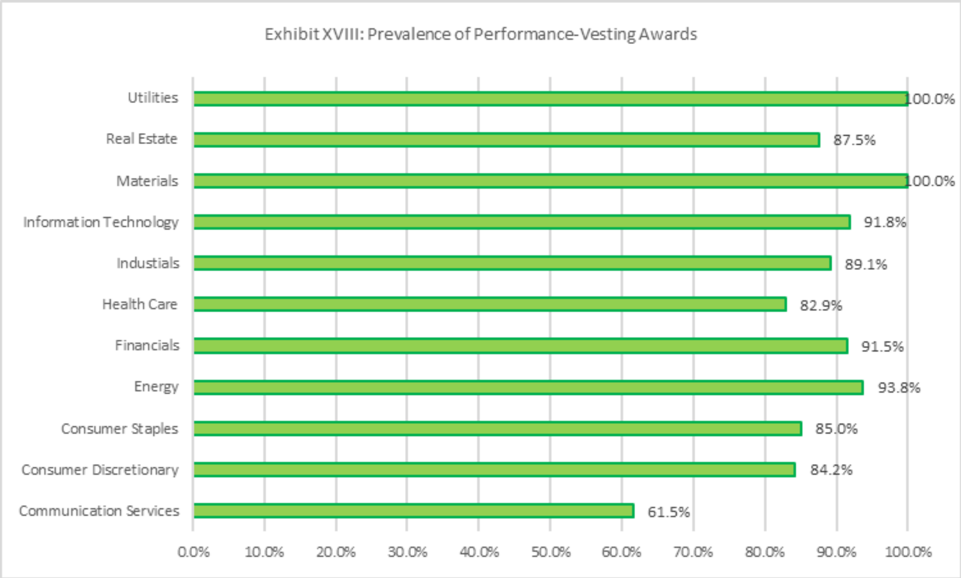
At the median, the value of long-term incentives awarded to CFOs was 30.0% of those for CEOs. CFOs in the utilities sector received only 23.7% of a CEO's grant, and the value didn't exceed the fifty-percent mark in even the highest-paying sector (Exhibit XVI).



The prevalence of performance-vesting equity (in the form of shares, options, or units) continued its long-time upward trajectory. Eighty-eight and a half percent of our sample granted it, up from 84.5% in 2017 and 78.9% in 2016. Grants of time-vesting restricted stock increased more modestly over that period (77.6% in 2018, up from 75.8% in 2017 and 74.2% in 2016). Grants of time-vesting options, on the other hand, continued to lose favor, becoming a minority practice for the first time in 2018 (awarded to 48.5% of our sample CFOs in 2018, vis-à-vis 50.9% in 2017 and 52.5% in 2016). Long-term cash incentives, always a minority practice, also declined (to 6.5% in 2018, from 8.7% in 2017 and 9.0% in 2016).

A sector-by-sector analysis reveals preferences for specific types of long-term incentives, with the largest use of time-vesting stock or unit awards and smallest use of time-vesting options or stock appreciation rights in the real estate and utilities industries. As discussed in our CEO study, companies with a relatively high dividend yield make stock options an inefficient vehicle for long-term incentives. Cash incentives are likewise entirely absent from these sectors, presumably to conserve capital for the distribution of cash dividends (Exhibits XVII-XX).





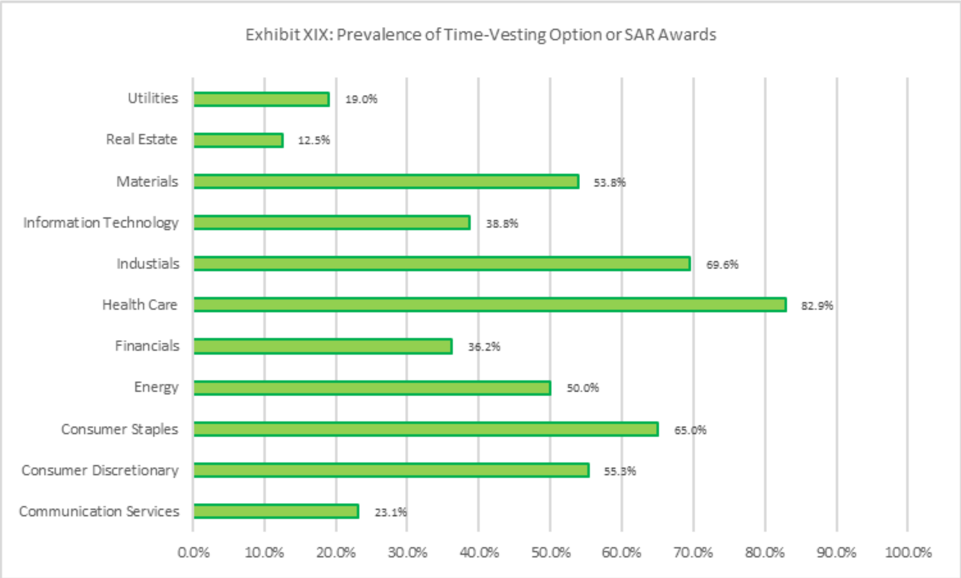


Exhibit XIX: Prevalence of Time-Vesting Option or SAR Awards
Utilities
19.0%
Real Estate
12.5%
Materials
53.8%
Information Technology
38.8%
Industrials
69.6%
Health Care
82.9%
Financials
36.2%
Energy
50.0%
Consumer Staples
65.0%
Consumer Discretionary
55.3%
Communication Services
23.1%
0.0%
10.0%
20.0%
30.0%
40.0%
50.0%
60.0%
70.0%
80.0%
90.0%
100.0%

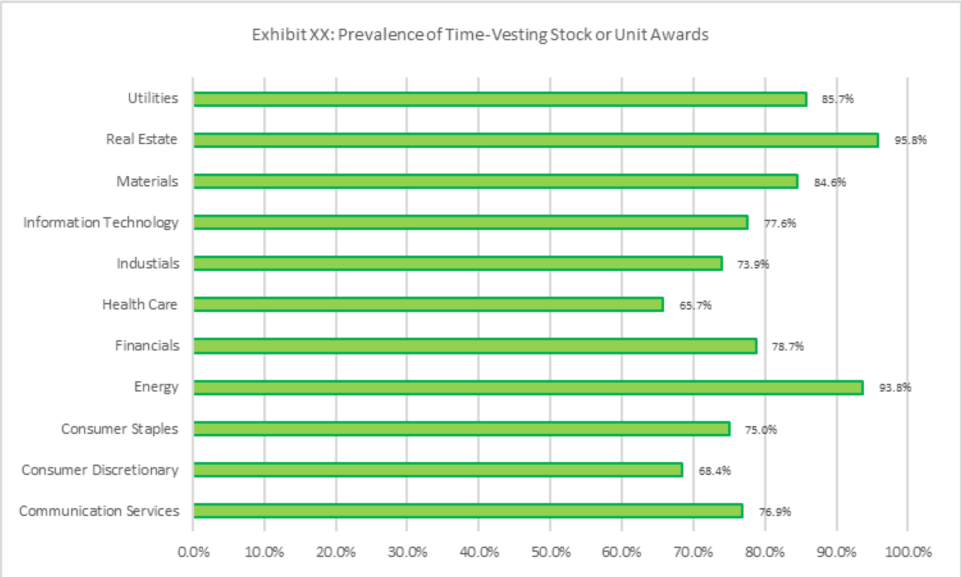
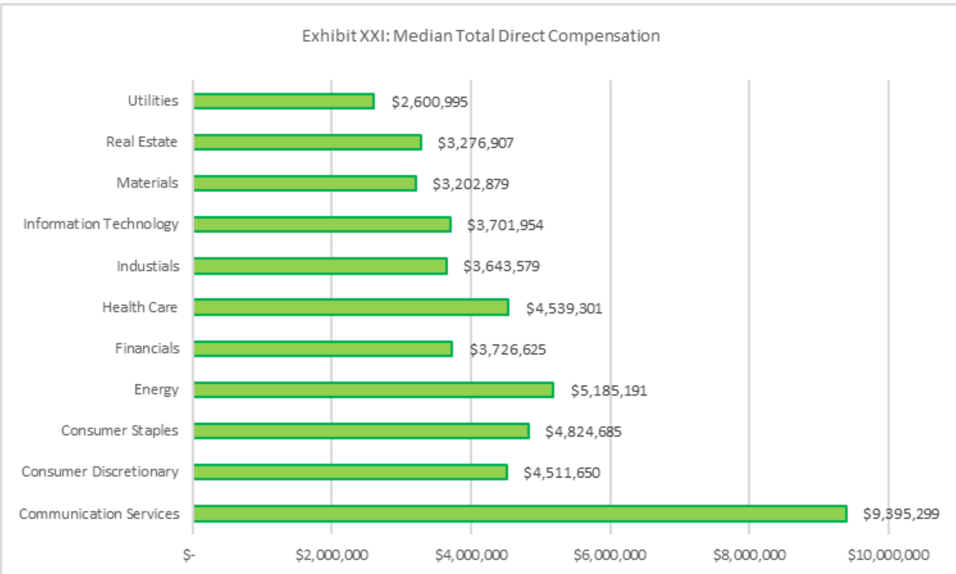
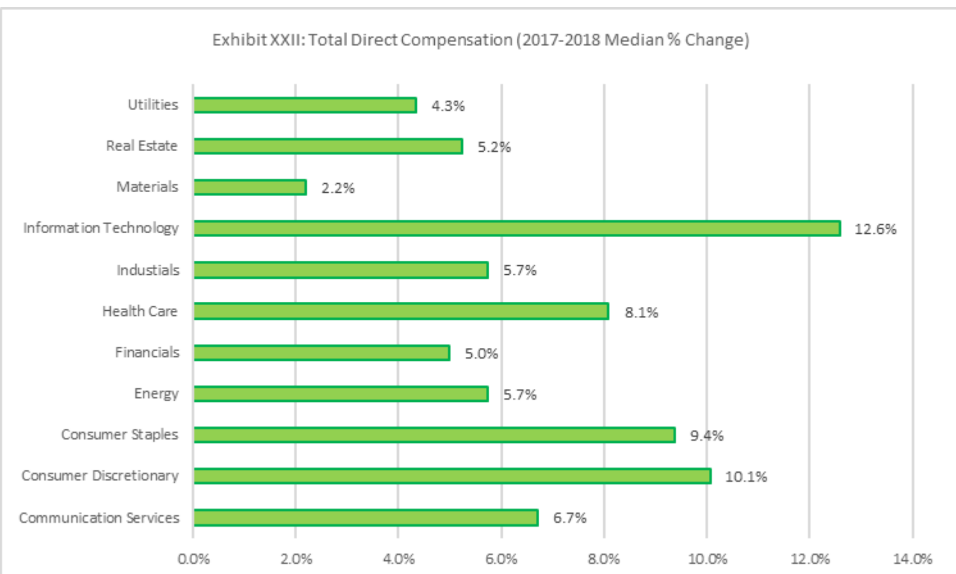


Exhibit XX: Prevalence of Time-Vesting Stock or Unit Awards
Utilities
85.7%
Real Estate
95.8%
Materials
84.6%
Information Technology
77.6%
Industrials
73.9%
Health Care
65.7%
Financials
78.7%
Energy
93.8%
Consumer Staples
75.0%
Consumer Discretionary
68.4%
Communication Services
76.9%
0.0%
10.0%
20.0%
30.0%
40.0%
50.0%
60.0%
70.0%
80.0%
90.0%
100.0%

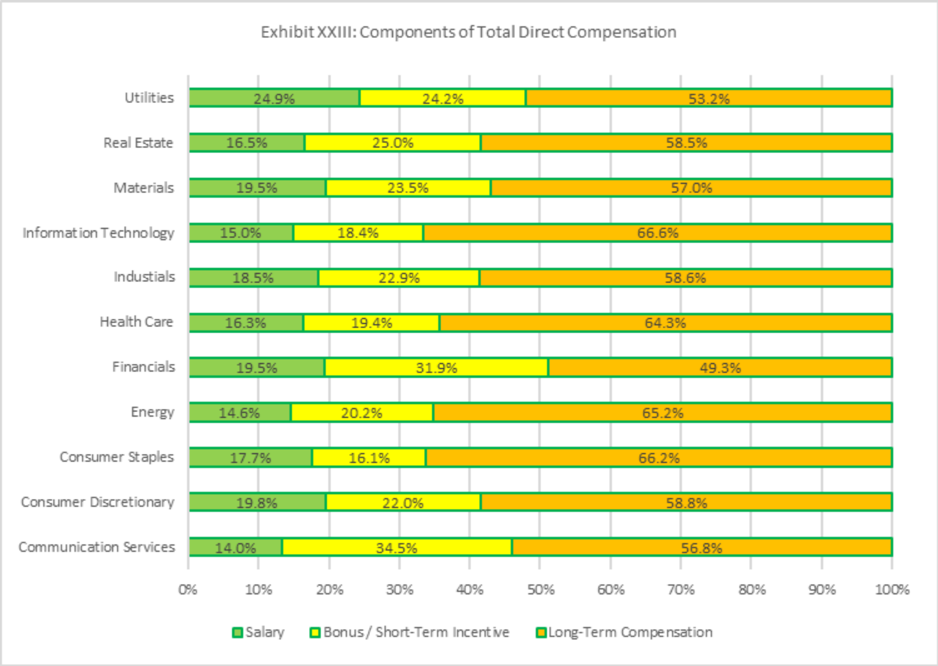
Total Direct Compensation Rose to Median $3,879,337; Total Remuneration Reaches $4,192,741

The median increase in total direct compensation (the sum of total annual compensation and long-term incentives) was 8.0% in 2018, somewhat below the 9.8% increase in 2017. The communications services sector, with its combination of highest base salary, highest bonus, and highest value of long-term incentives, provided the most generous package by far to CFOs; its year-over-year growth, however, was more towards the middle of the pack (Exhibits XXI-XXII).

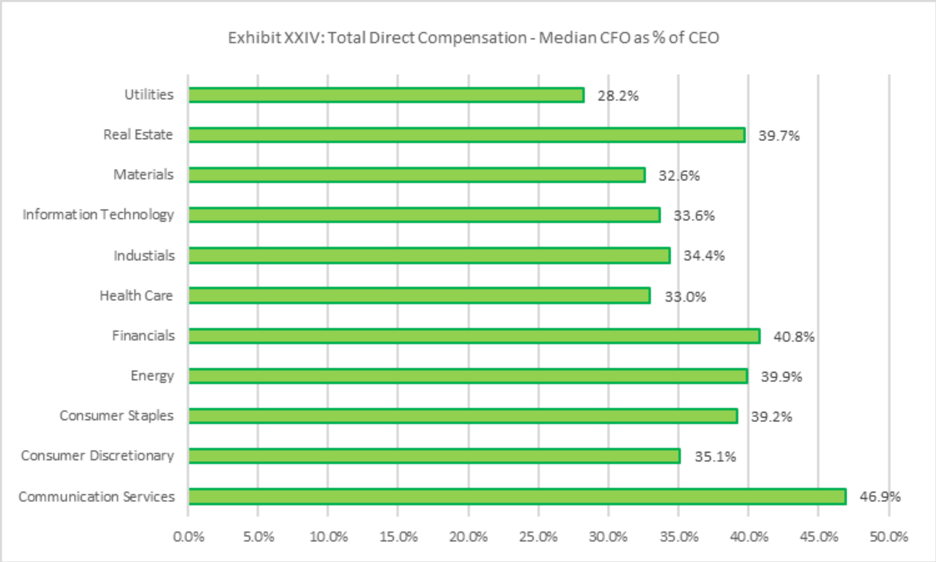




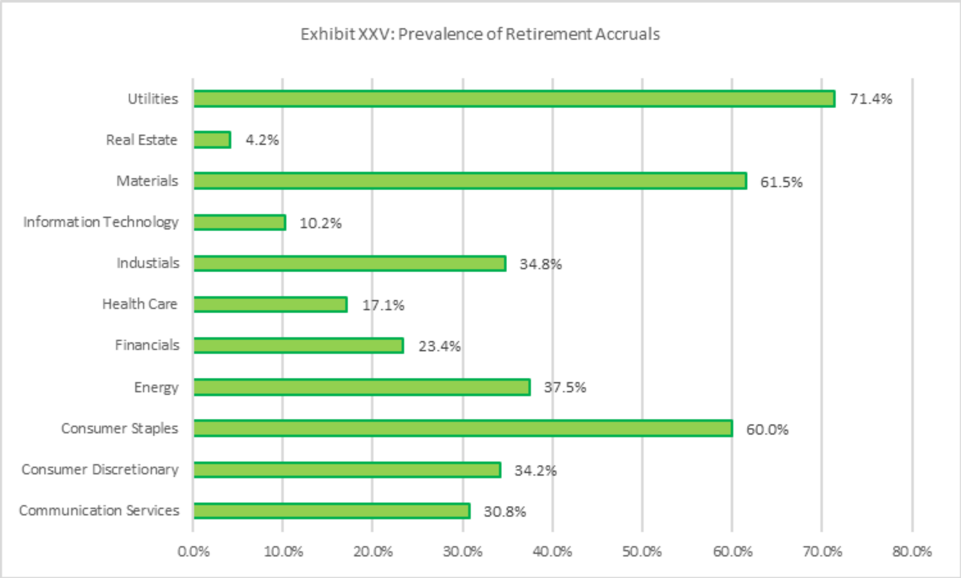
The mix of salary, bonus, and long-term incentives that collectively comprise total direct compensation differs considerably among industries. The information technology sector, with its traditional emphasis on equity-based pay, is most heavily leveraged towards long-term compensation. Communications services and the financials industry have the heaviest weighting in short-term incentives. For financial companies, this emphasis may reflect in part the ongoing engagement of the CFO in preparing the analyses and enhanced public disclosures mandated under Section 165 of Dodd-Frank. Utilities pay the greatest portion of total direct compensation in the form of base salary (Exhibit XXIII).



The degree to which CFOs are paid less than CEOs depends on the industry, and medians vary widely. At the median, CFOs in the communications services sector are paid nearly half of their boss's total direct compensation, whereas CFOs at public utilities earn scarcely more than a quarter (Exhibit XXIV).



Retirement accruals and miscellaneous compensation contributed only modestly to CFO compensation. At the median, retirement accruals were $178,815 (37.9% of the CEO's) and all other compensation was $65,938 (47.2% of the CEO's). Only 30.1% of the CFOs accrued retirement benefits, with strong concentrations of participation in mature industries and little participation in some others (Exhibit XXV).

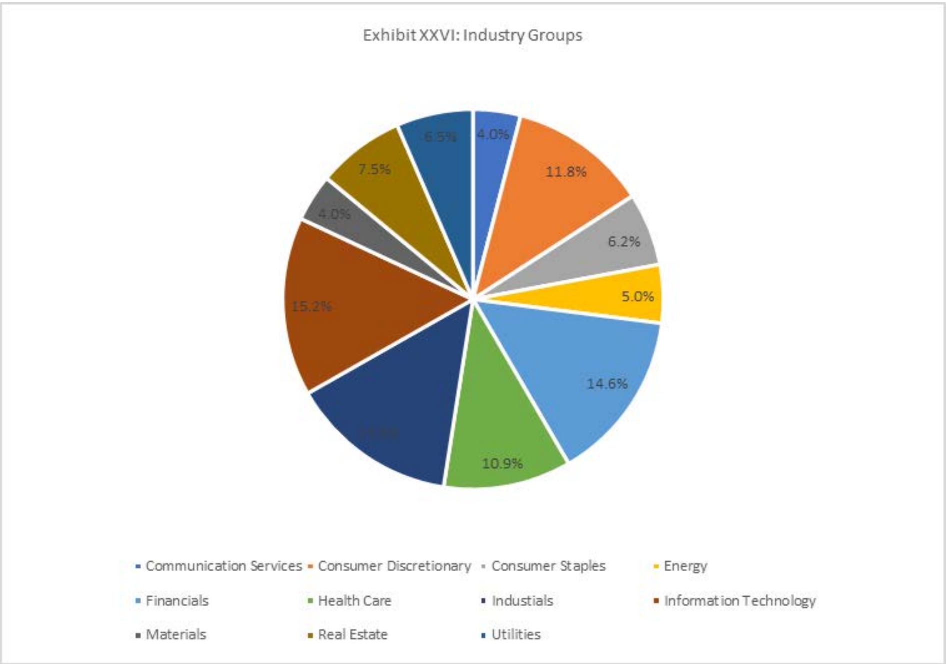


CFO Pay and CEO Pay: Alike, Yet Different

CFO pay is not CEO pay writ small. The more modest size of the total package reflects the CFO's role in implementing strategy rather than setting the firm's overarching strategic direction, and the differentials in short-term incentive payouts may indicate that the CFO bears an outsized responsibility for the management of financial risk. On the other hand, CFOs' relatively hefty base salaries (52.4-66.7% of CEO base pay) guarantee somewhat more stability than the CEO's highly leveraged total direct compensation package.

Demographics

Our analysis of constant incumbents (executives who held the CFO position for the full 2016-18 period) covered 322 companies in the S&P 500, in all 11 of S&P's industry groups (Exhibit XXVI).



The median revenue for this sample was $10.096 billion. Median assets were $20.553 billion and median market capitalization at fiscal year-end was $19.769 billion. Eighty-eight and a half percent of the CFOs in our sample were male and median age was 55. Only 3.7% occupied a seat on the board of directors.

For comparisons with CEO pay, we used a slightly different sample, including only the 268 companies where both CEO and CFO were constant incumbents over the 2016-2018 period. CEOs who were founders of their enterprises were eliminated from the analysis, since their compensation packages tend to be very different from non-founders and thus could distort the side-by-side comparison with CFOs (none of whom were founders).

Methodology

The following data elements were analyzed:

- Salary: as reported in the Summary Compensation Table
- Annual bonus: actual short-term payouts (sum of bonus and short-term portion of non-equity incentive payouts from the Summary Compensation Table); target short-term incentives as reported in the Grants of Plan-Based Awards Table
- Long-term cash incentives: target long-term cash incentives as reported in the Grants of Plan-Based Awards Table
- Performance-vesting equity: target share- and option-based grants as reported in the Grants of Plan-Based Awards Table

- Time-vesting options: target option-based grants as reported in the Grants of Plan-Based Awards Table
- Time-vesting stock: target stock-based grants as reported in the Grants of Plan-Based Awards Table
- Retirement accruals: change in actuarial value and above-market interest on nonqualified deferred compensation as reported in the Summary Compensation Table
- All other compensation: all other compensation as reported in the Summary Compensation Table

Statistics were independently arrayed, so medians for each data element cannot be added to other medians.

About Main Data Group

Main Data Group is a provider of executive compensation benchmarking and corporate governance analytics. Its mission is to empower executive compensation professionals with comprehensive total rewards and corporate governance information in an affordable, easy-to-use online service. For more information contact us at info@maindatagroup.com or by filling out our contact form at www.maindatagroup.com.

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