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Taking Stock of GCs' Compensation

The average award to general counsel of restricted stock rose by 35 percent, or more than \$250,000, to nearly \$1 million

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When Internet retailer IAC/InterActiveCorp's profits soared by a cool 431 percent last year, it rewarded its general counsel accordingly. Much of the company's growth came from the high-profile acquisition of Ask Jeeves Inc. (renamed Ask.com) and the spin-off of Expedia.com -- two deals that IAC's GC, Gregory Blatt, helped seal.

What was surprising about Blatt's pay package, however, was that the New York-based company opted to award him nearly \$6 million in restricted stock grants (the biggest grant on our 2006 GC Compensation Survey), in addition to his already impressive \$442,500 salary and \$2 million bonus. For his cash compensation alone, Blatt landed in the ninth spot on our roster and earned the distinction of richest newcomer this year. Blatt, who declined to comment for this story, is not the only GC on our list who received big -- if restricted -- grants of company shares. But he is leading the charge.

Companies are embracing these stock grants -- which come with certain conditions, like vesting only after a number of years -- in an effort to compensate and retain top-performing chief legal officers. While we still saw some notable stock option grants -- Occidental Petroleum Corp.'s Donald de Brier received nearly \$7.2 million in stock options in fiscal year 2005, and MGM Mirage's Gary Jacobs got a sweet \$5.5 million -- they continue to fall out of favor overall. Just 73 of the 100 GCs on our survey were awarded options as part of their total compensation package -- six fewer than last year.

While that may not sound like much, the decline in options is mirrored by a surge in restricted stock grants. Sixty-one GCs on our list received some amount of restricted stock in 2005, and the average award rose by 35 percent, to nearly \$1 million. "It is the echo of a trend that started last year," says Jannice Koors, managing director of the New York-based compensation consulting firm Pearl Meyers & Partners. Koors and other compensation experts say restricted stock grants have only one trajectory -- up.

Every year since 1994 we've reported compensation for the chief legal officers of the nation's *Fortune* 500 companies. And apart from the thrill of finding out what the nation's top in-house lawyers earn, the survey has also revealed trends in corporate counsel and executive compensation. We charted the rise of stock options in the mid-1990s as the key to luring top legal talent to hot startups. And we've tracked the decline of options in the last few years as Silicon Valley lost its luster. After Sarbanes-Oxley was



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Need to find
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passed in 2002, cold, hard cash in the form of big-time bonuses made a serious comeback.

So what's new in this year's survey? The real action lies in those bundles of restricted stock. The average grant reached \$987,269 in 2005, more than \$250,000 higher than in 2004. Blatt's restricted stock grant alone was double the highest award of 2004. "Restricted stock has more guarantees for long-term employees," says Koors. And, companies hope, more guarantees that top talent will stick around waiting for their shares to vest.

The rush to restricted stock isn't just the result of recent corporate scandals, or a response to aggressive shareholder groups. And the trend started too early to be a reaction to recent investigations into backdating options at companies like UnitedHealth Group Inc. (whose general counsel, David Lubben, had the largest value of exercisable options on our survey this year). Instead, credit is due to a new set of rules by the Financial Accounting Standards Board that went into effect just in time for 2006's financial reporting periods. The rules require companies to charge options as expenses -- a rude shift for many corporations.

Under the old accounting rules, options equal to the price of stock when they were awarded did not have to be expensed. As a result, companies were happy to reward their top executives with them, because the business didn't have to take a hit on the bottom line. However, the new FASB rules dictate that when options are awarded, their value for the vesting period must be calculated and expensed based on the value of the stock the day it was awarded. Companies can choose to expense options all at once, or over the entire vesting period, which could soften the blow a little. Still, fewer big businesses are viewing options as the most cost-effective reward for a job well done.

In addition to changes in the reporting rules, FASB now requires companies to use the Black-Scholes method for computing the value of the options for fiscal year 2006. That formula takes specific variables into account, like company performance and stock value, rather than the old-school calculation, which banked on a fixed-percentage increase (usually 5 percent or 10 percent) in the price of the options per year. Companies have been anticipating the adoption of Black-Scholes; almost half of those who made our list this year already used this more complicated formula. Rees Morrison, a law department consultant at Somerset, N.J.-based Hildebrandt International Inc., says the Black-Scholes method is more transparent than the old calculation, but it also makes stock options more expensive for companies -- another reason for options' diminished popularity.

There were other notable findings on this year's survey. Thanks to the S&P 500's strong year, stock option cash-outs were up 24 percent in 2005. Fifty-five of the top 100 GCs cashed out their options -- six more than in 2004. The total value of option grants exercised was \$171,109,966 -- \$49 million more than in the previous year. The average gain increased from \$2.5 million in 2004 to \$3.1 million in 2005.

Lehman Brothers Holdings Inc.'s chief legal officer, Thomas Russo, was the cash-out king on this year's list; he took home \$16 million. Others, like Burlington Northern Santa Fe Corp.'s executive vice president of law and government affairs, Jeffrey Moreland, and UnitedHealth Group's general counsel, Lubben, cashed out an impressive \$10.5 million and \$12.1 million, respectively.

Bonuses remained one of the prime ways to reward GCs; they were up 16 percent over 2005 -- nice, but still about half of the 30 percent rise we reported last year. Compensation experts attributed the slow but steady rise to both heightened in-house responsibility in a post-Enron world and a general trend toward performance-based executive compensation. The average bonus on our list came to \$906,820.

Why are bonuses so popular, while simple salary raises aren't? James Wilber, a principal at the Newtown Square, Pa.-based legal management consulting firm Altman Weil Inc., says companies prefer to hold a little back and then reward good performance later: "[Companies] don't front-load the salary to start." And indeed they don't: The average salary of \$564,612 was up a paltry 1 percent from 2004.

Take Lehman Brothers, for example. According to the investment bank's annual report, 2005 was a record-setting year "by almost all measures," with net income and earnings per share going through the roof. The company saw a 26 percent increase in revenue alone. Lehman's Russo came in at an impressive number two overall on our list, and was awarded a \$4.5 million bonus as a result of his company's record growth. With that bonus, he also logged the second-highest take-home pay (salary plus bonus) on our roster, \$5 million. But Russo's salary has remained a constant \$450,000 since we first reported his salary in 1994.

And while he's not exactly washing cars yet, take a look at what the absence of a bonus can do to a GC's compensation: Thomas Gottschalk of the embattled Detroit automaker General Motors Corp. didn't receive one, and he took the biggest dive on our list, from No. 17 to 71.

It's nice to know, though, that some things never change. Benjamin Heineman Jr., the legendary legal chief of General Electric Co., once again topped our overall compensation list. With cash compensation of just over \$5 million -- up only slightly from 2004 -- he



managed to edge out Russo. Then again, Heineman's reign has come to an end. He'll be off our list next year after retiring from GE this winter. Who will take the top berth on our survey? Stay tuned.

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