By Amanda Balbi, Stephen Barlas, Ashutosh Srivastava, Jeff Thomson

GOVERNMENT

SEC Concessions on Pay-Ratio Reporting Deemed Insufficient by Some

By Stephen Barlas

The Securities & Exchange Commission (SEC) proposed a new rule in September that would require public companies to calculate and report on the ratio of their CEO's compensation to the median compensation of company employees. The rule, required under the Dodd-Frank Act, has been brewing at the SEC for a while. The SEC's main concern for not proposing the rule sooner was the cost of obtaining pay figures for employees, which it admitted may be "substantial" in some instances. When announcing the proposal, the SEC noted that companies will have the flexibility of calculating the pay ratios in the way that best suits their company. They can use statistical sampling or "another reasonable method" of their choosing to calculate the company-wide median, or they can identify a median employee, based on any consistently applied compensation measure, and then calculate the annual total compensation for that employee.

The disclosure requirement would be required in any annual report, proxy, or information or registration statement that requires executive compensation disclosure pursuant to Item 402 of Regulation S-K. Emerging-growth companies, smaller reporting companies, and foreign private issuers are exempt from the requirement.

The House Financial Services Committee has already passed a Republican bill to eliminate this requirement. Opposition to the pay-ratio proposal from corporate groups, which propelled the House legislation (Burdensome Data Collection Relief Act, H.R. 1135), has to do with its presumed cost—an issue the SEC tried to respond to—and the argument that a pay ratio isn't a "material" disclosure that companies should have to make.

Timothy J. Bartl, president of the Center on Executive Compensation, a trade group for *Fortune* 500 human resource executives, said "the Center strongly opposes the pay ratio requirement in the Dodd-Frank Act and will continue to work for its repeal in Congress."

Opposition to SEC's Floating NAV Grows

Hearings in the House Financial Services Committee at the end of September provided a big boost to the corporate financial community's opposition to the SEC's money market fund (MMF) reform proposal. Sheila Bair, chair of the Systemic Risk Council, told the Committee that "by allowing stable NAV [net asset value] to remain for institutional government funds and floating NAV for institutional prime funds, the new rules will cause significant money to flow from commercial paper issuers to agency issuers. On a relative basis, this will artificially raise the cost of borrowing for corporations (whose debt is in the floating NAV 'institutional prime' space), and artificially subsidize borrowing by the Treasury and these government-sponsored entities (Fannie Mae, Freddie Mac and the Federal Home Loan Banks) whose debt is in the stable NAV 'institutional government' space." She also said, "The liquidity 'gates and fees' option is potentially worse than existing law as it retains the existing structural weakness of the stable NAV, but adds increased investor uncertainty about potential gating and fees."

The SEC has suggested a two-tier approach to MMF regulation: a floating NAV for prime and tax-exempt institutional MMFs and/or liquidity fees and redemption gates for MMFs that continue to use a stable share price. The SEC could adopt one of those alternatives, both, or neither.

Bair was chair of the Federal Deposit Insurance Corporation (FDIC) during the 2008 recession, when she gained attention for taking a tougher tone toward big

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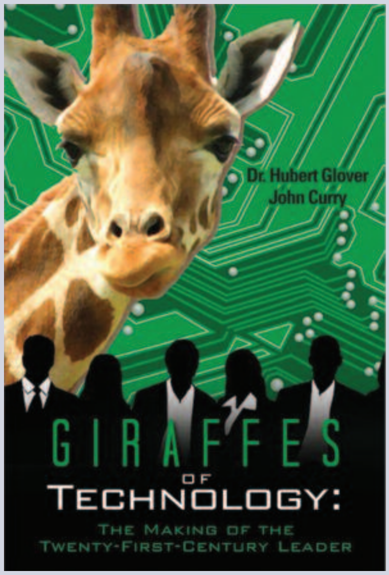
BOOKS

21st Century Leadership

"At one of our first meetings, I deliberately sat on the floor and asked the seated staff to rise—a simple yet symbolic gesture. I wanted them to understand that I wasn't standing above them, glaring down, commanding. My leadership would be focused on supporting them to become leaders themselves, so they could advance their professional lives during a frightening period (that bump) in their careers."

That quote from *Giraffes of Technology: The Making of the Twenty-First-Century Leader*, by Hubert Glover and John Curry, is Glover describing a pivotal early experience from his time heading up a subsidiary of PricewaterhouseCoopers (PwC) that had been through three CEOs in nine months. Employees were fearful of losing their jobs, trust and motivation were at a minimum, and the moment called for a nurturing and authentic symbol of the leadership style to follow. Opening a book review with a quote from the book might seem an unusual way to begin, but this quote succinctly expresses all that I found provocative, symbolic, relevant, and inspiring about Glover and Curry's book.

Why did they title it *Giraffes of Technology*? In 21st Century business, especially in the United States, organizations and their leaders often embrace a top-down, autocratic style in the quest to achieve short-term gains (e.g., quarterly profits for shareholders). Yet many studies in the area of servant leadership show that a nurturing, empathetic, and values-oriented approach creates greater business value in the long run. According to the authors, the giraffe is the least offensive beast in the wild. It bears no ill will toward any other animal. They view the giraffe as a metaphor for a leader with a unique lookout post—one who incents followership rather than intimidating others in the herd to behave in a certain manner.



Glover's symbolic yet authentic leadership moment at PwC epitomizes another behavior of the giraffe. At birth, the calf is dropped from its mother's pouch six feet to the ground, building speed that severs the umbilical cord. All of us, in our personal and professional lives, fall from the womb, from the security of our homes and loved ones, or from the safety zone that often defines our day jobs. At that meeting with his staff, Glover not only showed he would be a genuine leader who would help the team work through a difficult period, but he also demonstrated that, by picking himself up, he would pick up the rest of the team and rise above the disruption from constant leadership changes and stress.

Glover and Curry organize *Giraffes of Technology* using six herbivore-inspired leadership traits that CEOs and managers must embrace over the next decade to create and enable sustainable organizations that enrich society. Today's technology triggers a business environment that requires adapting to untidy change—change that isn't easy but is necessary. The six chapters in the book are rooted in unique themes, or metaphors, centered on the behaviors of the giraffe in the wild: acting as a lookout post to focus on the long run vs. the short run; communicating with others as gentle giants; dealing with a violent birth; moving forward to inspire a never-stop-learning mind-set; dealing with the predator lions who seek to disrupt change; and blending into new herds to enable diversity of people and thought.

It's an inviting, engaging read. Glover and Curry combine a touch of *Back to the Future* with a sense of *Animal Kingdom* to provide an inspiring look at the kind of leaders businesses need to succeed in the 21st Century.

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banks than other federal regulators. She's now somewhat of a public interest advocate since the Systemic Risk Council is jointly funded by the CFA Institute and Pew Charitable Trusts to monitor and encourage regulatory reform of U.S. capital markets focused on systemic risk.

Another issue for corporations that put short-term cash in MMFs is the accounting and tax implications of a floating NAV. Marie Chandoha, president and CEO of Charles Schwab Investment Management, Inc., said, "Given that clients may make hundreds of transactions within a money market fund every year, the burden on tracking this information seems wildly out of proportion with the potential revenue gain for the Treasury." Chandoha added that, "earlier this year, the Department of the Treasury issued a proposed Revenue Procedure that addresses one aspect of the tax implications for a floating NAV fund—the wash sale rule. The proposal includes a *de minimis* exception from the loss disallowance rule if the loss is less than 0.5% of the taxpayer's basis. While we support this proposal, we note that it does not eliminate the requirement to track compliance with the wash sale rule."

NEWS

IFAC's CFO Paper

By Amanda Balbi

On October 10, 2013, IFAC (International Federation of Accountants) released a new discussion paper, *The Role and Expectations of a CFO*, about the changing role of the CFO and how accountancy organizations and employers can prepare their accountants for the future.

While on the career path, accountants are encouraged to continue their education and develop their financial skills. But in order to become a CFO, accountants and other financial professionals need to break out of the finance sector and expand their skill set. IFAC posits recommendations that organizations and employers can implement to help develop their professional accountants.

The role of the CFO in the 1990s was to ensure the organization's financial health and transparency, among other financial control operations. IFAC reports that the role has become more complex for a few reasons, including globalized capital and markets and changing expectations. The CFO is now expected to drive the organization toward its goals in addition to being a financial leader.

IFAC says a CFO should be an effective organizational leader and leader of the finance and accounting function, be able to balance responsibilities, act as a navigator for the organization, and possess professional qualities.

As a leader and key member of senior management, the CFO has to be able to communicate well with his or her team—sometimes acting as a mediator—maintain and create sustainable value, and make decisions. It's a considerable difference from being a professional accountant in a financial setting.

To help professional organizations bridge the gap, IFAC recommends appropriate education and training through mentorships and coaching, lifelong learning for continued growth, and networking with other professionals. Employers, specifically, should invest in training and development of technical, leadership, and analytical skills and provide opportunities for job rotation to further develop accountants' business acumen.

This discussion paper is intended to be a dialog between organizations, employers, and other stakeholders to develop better strategies for preparing future finance leaders. If you would like to comment on the paper, visit www.ifac.org/publications-resources/role-and-expectations-cfo-global-debate-preparing-accountants-finance-leaders.

Sharing Your IMA Life

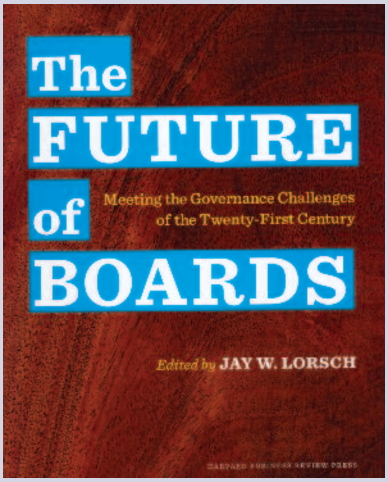
Most IMA® members share a strong spirit of camaraderie. What have your experiences as a member of IMA been like? Do you have a story about them you'd like to share? If so, please consider writing an IMA Life column that will be published in *Strategic Finance*. You can be a student member, a young professional, in the midst of your career, or retired. If you would like to write an IMA Life article, please e-mail Kathy Williams at kwilliams@imanet.org.

BOOKS

Managing Boardroom Challenges

The growing complexity of today's businesses, rapid technological changes, globalization, and increasingly assertive investors have made the role of corporate boards more challenging than ever. The success of companies today depends on the ability of their boards to navigate them through these challenges. *The Future of Boards*, edited by Jay W. Lorsch, is a collection of eight essays covering the most important challenges corporate boards face today. Key topics include the role of boards in strategy formulation and implementation, CEO succession and compensation, group dynamics within the boardroom, independent chairmanship of boards, and the concept of lead director.

In the essay "Focusing on Strategy to Govern Effectively," Krishna Palepu, a Harvard Business School professor and leading expert in business strategy, opines that strategy formulation and implementation is the responsibility of the company's management, and the board may not have the necessary expertise and time to get deeply involved. The board, however, shouldn't passively approve the strategy presented by management. Instead, it should actively review the underlying assumptions and implications and monitor the implementation. Palepu outlines a basic framework for strategic engagement that can help board members actively engage in discussions related to their company's strategy.



One of the most important and challenging responsibilities of the board is to plan CEO succession. Joseph Bower, Harvard professor and author of *The CEO Within: Why Inside Outsiders Are the Key to Succession Planning*, mentions in his essay, "Managing Your CEO's Succession," that the best way for any board to manage CEO succession is to make sure it doesn't have to choose the CEO's successor. The job of identifying potential successors and mentoring them should be done by the CEO and management. CEOs typically are reluctant to choose their own successor, but the board's job is to encourage them to do so. Once a pool of potential successors is identified, the board should regularly interact with them and assess their strengths and weaknesses. This will ensure that when the time comes to make a decision, the company has an abundance of well-groomed options.

Another essay addresses one of the most sensitive topics in corporate governance: executive compensation. In "The Pay Problem—Time for a New Paradigm for Executive Compensation," Lorsch and Rajesh Khurana, Harvard professor of leadership development, question the assumptions behind a typical CEO compensation plan and urge board members to align executive pay packages with long-term company results. They also highlight the fact that incentives have a motivational effect only if they reward outcomes that the executives have control over. They propose a compensation plan that includes both monetary and nonmonetary rewards and encourages collaborative behavior within the executive team.

The other essays cover a range of topics related to board leadership. Some questions posed include: (1) Should the CEO or an independent director chair the board? (2) Should there be a lead director? (3) What are the group dynamics among the board members, how do they impact the company, and how can companies manage them?

The Future of Boards isn't only an outstanding assessment of the challenges boards currently face. It's also a provocative and insightful analysis of these challenges and a blueprint of how boards should work to overcome them. I highly recommend this book for CEOs, board members, and anyone interested in corporate governance or working with boards.—Ashutosh Srivastava,
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