

## Duke Energy's Anderson Really Works for His Pay: Graef Crystal

April 6 (Bloomberg) -- Paul Anderson, the chief executive officer of Duke Energy Corp., is one of a handful of U.S. CEOs who mean what they say when they declare their fealty to the principle of pay-for-performance.

Anderson rejoined Duke on Nov. 1, 2003, when the company's performance had been faltering. During the one- and two-year periods ended Oct. 31, 2003, total returns were, respectively, negative 5.6 percent and negative 47.9 percent.

For about the 1 1/2 years that ended in November 1998, he had been the company's chief operating officer. Then he decamped to become CEO of BHP Billiton PLC.

In his earlier period of employment, Anderson's pay package contained the usual elements. For example, in 1998, he earned a base salary of \$612,500 and a bonus of \$551,300. He also received options covering a split-adjusted 800,000 shares.

Upon his return as CEO, his pay package underwent fundamental change. Under his new employment, which ends on Dec. 31, 2006:

- Gone is his salary.
- Gone is his bonus.
- Gone are his fringe benefits.
- Gone, even, are his company car and club memberships.

### Not Empty-Handed

Duke's current proxy, filed with the U.S. Securities and Exchange Commission on March 16, paints a pay landscape populated with zeros. Yes, he did receive \$159,000 of relocation benefits and \$135,000 for security reasons, to defray the cost of personal travel on corporate aircraft for him and his wife. But that was it.

Nevertheless, Anderson didn't go away empty-handed. When he first became CEO, he received three goodies:

- The equivalent of a free share award covering 285,000 shares. They were worth \$5.2 million when he joined the company, and vest purely through the passage of time.
- An award of 360,000 additional free shares, worth \$6.5 million when he joined the company. This time, however, vesting occurs only if Anderson meets performance goals established by Duke's board compensation committee.
- A stock option grant covering 1.1 million shares and carrying a strike price of \$17.45 a share. As of April 1, this option contained a paper profit of \$12 million.

With an all-stock, no-cash package, many readers may wonder just how Anderson is able to pay for groceries and, yes, his electricity bill.

## Annual Dividends

Not to worry. Those 645,000 free shares carry dividend equivalents paid in cash to Anderson as dividends are declared. Like many power utilities, Duke offers a hefty dividend of \$0.275 per share per quarter. That amounts to aggregate annual dividends on all 645,000 shares of \$710,000.

What Anderson has done with his compensation package would be counter-intuitive to most CEOs coming in from the outside. After seeing the mess Duke was in before he re-joined the company, you would think he would be asking for:

- A hefty salary.
- A guaranteed bonus.
- A ton of free shares, with none of them vesting based on future performance.
- Some cushy fringe benefits, including an enhanced pension plan that would credit him with years of service he never had.

You can probably count on the fingers of both hands the number of U.S. CEOs willing to be paid as Anderson has chosen.

## An Exception

One notable example is Richard Fairbank, the CEO of Capital One Financial Corp. He has, over the years, traded in every piece of his normal compensation package for large stock option grants. Once, he even traded in some in-the-money options for a larger grant of at-the-market options.

In a conversation with Stanley Westreich, his board compensation committee chairman, I asked what Fairbank could possibly offer in return for his next round of stock options. Westreich replied that the committee was in serious negotiations over Fairbank's first-born child.

It's impossible to prove a causal connection between the way Anderson is being paid and his performance, but there's no question that he has done extremely well for his shareholders during his not quite 1 1/2-year tenure.

Between Oct. 31, 2003, and the close on April 1, Duke's aggregate total return was 68.2 percent. That compares with a return of 14.4 percent for the Standard & Poor's 500 Index and a return of 40.4 percent for the S&P 500 Utilities Index.

During that same period, Duke ranked in the 86th percentile in stock price appreciation against the individual members of the S&P 500 Index, meaning that the company outperformed all but 14 percent of the companies in the index. Duke also tested out in the 82nd percentile against the 33 companies comprising the S&P 500 Utilities Index.

## Fiorina's Package

There is a parallel between Anderson and Carly Fiorina, who was recently forced out as CEO of Hewlett-Packard Company. They both came in from the outside to become CEO. The similarity stops there.

She came in with a monster pay package that offered her extraordinary downside protection, including a free share grant that was worth \$66 million when granted and a signing bonus of \$3 million.

The pay package she negotiated for herself spoke volumes about someone who really wasn't sure she could do a superb job. And she didn't.

Anderson's pay package says a lot, too -- about a person who is supremely confident that he can do a great job for his shareholders. And he has.

Bob Monks, the shareholder activist and a good friend, once told me: ``Executive pay is the smoking gun of corporate governance." When he uttered those words, he was thinking about pay abuse.

They can be applied in a different context to Paul Anderson. This time, what emanates from the smoking gun isn't bullets, but orchids.

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