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Telecommunications

Lucent Throws A Pay Party

Daniel Lyons, 05.06.04, 6:30 PM ET

Lucent Technologies may be a shadow of its former self, but there is one place where this company still puts world-class numbers on the board, and that's executive compensation.

In two years since becoming chief executive, Patricia Russo has received compensation worth more than \$44 million, according to Equilar, a San Mateo, Calif., firm that tracks executive compensation.

And since January 2002, when Russo rejoined Murray Hill, N.J.-based Lucent (nyse: [LU](#) - [news](#) - [people](#)) as chief executive, her four top lieutenants--all Lucent lifers--have received "cash retention payments" totaling \$10 million to keep them from leaving.

Moreover, in fiscal 2003 these four executives--[Frank D'Amelio](#), [William O'Shea](#), [Janet Davidson](#) and [James Brewington](#)--were paid salaries totaling \$2.4 million and bonuses totaling \$2.8 million. Plus they were granted 3.75 million options.

A Look At Lucent

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In addition, in 2003 Russo and her top four execs were awarded \$3.5 million in long-term incentive plan bonuses that won't be paid until 2005. Ultimately Russo and her team could earn as much as \$11 million from this three-year plan.

So how well has this dream team performed?

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Lucent's share price has dropped 40% since Russo took over in January 2002--from \$5.87 to \$3.50--and the company has lost \$10 billion in market value, falling to \$15 billion. Russo says Lucent's market cap has shrunk because telecom spending has declined sharply during the past two years. (And to Russo's credit, during the 2003 fiscal year, which ended Sept. 30, Lucent's stock rose nearly 200% to \$2.16 from 75 cents.)

How about earnings? In fiscal 2003 Lucent reported a net loss of \$1.2 billion on sales of \$8.5 billion. This year Lucent is expected to report a net profit, but there's a catch: The profit is being delivered by an accounting credit from a pension fund surplus, without which Lucent would post a net loss of several hundred million dollars this year. (Lucent argues that the pension fund credit has been an ongoing contributor to earnings, and that its earnings have been trending up.)

To be sure, Russo's team has cut operating expenses to \$623 million per quarter from \$1.8 billion, boosted gross margins to 40% from 12%, and improved Lucent's customer-satisfaction scores.

But they have also slashed the research and development budget by \$2 billion, causing Lucent to fall behind in key product areas, which may become evident in 2005 and 2006.

(Lucent's spinmeisters point out that the company's \$1.5 billion R&D spending in 2003 represented 17.5% of Lucent's \$8.5 billion in revenue, while its \$3.5 billion R&D spending in 2001 was only 16.5% of that year's \$21.3 billion in revenue.)

Some Lucent retirees are appalled by how much top execs are making, especially since Lucent, crying poor, slashed health benefits for its 127,000 U.S. retirees last year. "I think they should reduce salaries and perks to the officers," says **Ken Raschke**, president of the Lucent Retirees Organization, an activist group formed in 2003. "I think they ought to be a little more noble and make some sacrifice themselves."

Russo says Lucent employees are sharing the sacrifice--they, too, have had their benefits cut. Russo also argues that Lucent must pay competitive salaries to attract and retain talented executives, especially during hard times. "To suggest that we should not compensate people for the job they are doing in weathering the worst storm ever in our industry is just wrong-headed," Russo says.

She adds that before 2003 Lucent's executives went three years without bonuses, and insists Lucent's compensation for top executives is in line with other companies in its industry.

How does Lucent compare? At **Cisco Systems** (nasdaq: [CSCO](#) - [news](#) - [people](#)), a networking company with twice Lucent's sales (\$18.9 billion in fiscal 2003, which ended July 26) and ten times Lucent's market value (\$150 billion), the five top execs last year received cash compensation (salary and bonus) that was 50% of what Lucent paid its top five people: \$4.2 million at Cisco versus \$8.4 million at Lucent.

That is in part because Cisco's chief executive, **John Chambers**, has taken a \$1 annual salary and zero bonus since April 2001, when Cisco, like Lucent, saw its business stall as customers slashed orders.

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Last year San Jose, Calif.-based Cisco granted its top five executives 6 million options, while Lucent granted its top five execs 6.25 million options--though using Black-Scholes methodology, Equilar calculates the value of Cisco's options grants to be \$65 million, nearly ten times greater than the value of Lucent's grants.

The bottom line: At Cisco, which in fiscal 2003 earned a net profit of \$3.6 billion, top executives are taking lower pay today and betting their company will be stronger in the future. At Lucent, which barely ekes out a profit, leaders are doing a touchdown dance and taking their cash right now, thank you.

Where will these companies be in a few years? Here's a clue. Having gutted R&D, Lucent today fills holes in its product line by reselling equipment made by...Cisco. Funny old world, isn't it?

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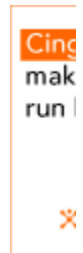
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