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TOWERS PERRIN

HR SERVICES

American University

Proposed Compensation Program for President

DRAFT

September 2004

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Introduction

- At the request of the Board of Trustees, Towers Perrin was retained to conduct a custom survey of compensation and benefits for a group of peer institutions identified by American University.
- The results of the survey covering the total compensation for the President and cabinet positions were documented in a final report that was reviewed with the Compensation Committee.
- This document provides Towers Perrin's thoughts on the implications of the survey results on the compensation program for the President.

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Assumptions

- Compensation programs should be aligned with market practices in terms of both the level or "how much" and structure or "how."
- Past performance warrants a compensation opportunity at the upper quartile of competitive practice.
- The total compensation opportunity should provide a strong incentive to retain the incumbent for an additional five years.
- The President's total compensation must be structured to insure that it would be deemed reasonable within the context of the Intermediate Sanctions.

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Observations – Cash Compensation

- The President's current cash compensation program consists of the following components:
  - Salary $461,000
  - Annual Incentive $200,000
  - Deferred Incentive $110,750
  - Total $771,750
- The 75th percentile of the survey data shows the following compensation levels:
  - Salary $450,571
  - Total $515,000
- Although well conceived and executed, AU's bonus plan is an outlier in the competitive market; the payments to the Presidents of the two institutions in the survey that reported an incentive were modest.
  - Besides American University, none of the institutions in the survey reported both an annual and deferred incentive.
- The President's current cash compensation is nearly 50 percent above the philosophy of providing compensation at the 75th percentile.
- Rolling the annual incentive into salary would produce a level not supported by the competitive data.

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Observations – Split Dollar Contract

- Prior to implementation of the annual and deferred incentive plans, the University purchased a Split Dollar insurance contract for the President. At the time of purchase the cash value at the end of the contract was estimated to be approximately $2.9 million in ten years.
- Due to the negative differential between the actual and projected rate of return, a recent forecast estimated the cash value to be approximately $650,000.
- It would not be typical practice for the employer to "true up" the value of a Split Dollar contract, unless it were the sole source of retirement income and therefore not doing so would significantly erode the post employment benefit commitment.
- In structuring a revised employment agreement for the President, Towers Perrin recommends that no action be taken on the in-place Split Dollar contract. Other forms of cash compensation and benefits should be utilized to deliver a fully competitive opportunity.

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Proposal

- In terms of salary and total cash compensation, the Committee will need to determine a level that balances the President's current opportunity with the custom survey results and data in Towers Perrin's broader higher education database.
- Although the survey did not yield any data on special, one-time awards e.g., retention programs, the precedent and alternative opportunities available to the incumbent warrant consideration of refreshing the initial award that is now fully vested.
- Some University Presidents obtain additional income from serving on outside board(s).
  - Median total compensation (cash and equity) for a corporate board is approximately $75,000 - $100,000.
- The Committee has expressed a desire to have the President focus on the ~~University and restrict him from accepting a position on an outside board. If this is~~ formalized as a policy, the Committee should consider replacing the forgone income.

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Proposal of Comp. Cont. to Board

Salary	500,000
Incentive Compensation (up to 13% of Salary)	65,000
Deferred Compensation (25% of Salary)	125,000
Split-Dollar	109,000
Total	**799,000**