

CEO hypocrisy: How does CSR policy influence the reaction to excessive CEO pay?

ABSTRACT

Previous research suggests that policies on Corporate Social Responsibility (CSR) can be a liability or an asset for an organization in a moral crisis. Drawing from theories of moral evaluation, we provide a single framework to predict how CSR moderates both potential outcomes when an executive morally fails. We hypothesize that executives are more likely to be publicly condemned for immoral acts when their firms are perceived as “doing good” on the same moral domain. In such a case, a moral transgression by an executive gives rise to an inconsistency in moral conduct, which induces the perception of hypocrisy. We also argue that pro-social conduct along moral domains unrelated to the transgression (e.g., diversity and environment) and pro-social conduct raising doubts about the severity of the transgression generate moral credits and credentials, reducing the likelihood of public outcry. Using data of large listed U.S. companies, we find support for the hypocrisy hypothesis by demonstrating that CEOs of firms with high scores in corporate philanthropy are more likely to receive negative media coverage when their pay contract violates distributive justice norms. We also find evidence for the moral credit and credentials effects. Finally, we show that executives appear to care for morally consistent conduct since public judgment triggers a significant subsequent drop in excessive pay in situations characterized by hypocrisy.

Keywords: moral standards, hypocrisy, executive compensation, corporate social responsibility

INTRODUCTION

Top executives serve multiple constituencies and are evaluated along different dimensions. While catering to the financial interests of shareholders is a primary concern for executives (e.g., Puffer & Weintrop, 1991; Tosi & Gomez-Mejia, 1989), stakeholders may be able to exert effective pressure on top executives to perform in line with non-financial norms, such as social and moral standards (Matten & Crane, 2005). Disobeying these standards may well be associated with adverse consequences for managers and their organizations run the risk of failing to create shareholder value. Anecdotal evidence suggests that in some notorious cases, boards even succumbed to the social pressure and fired financially successful, but morally failing top executives.

In a recent example, Robert Nardelli's dismissal as a CEO of Home Depot, Inc. in 2007 was often attributed to his resistance to adapting the level of his compensation package to more reasonable numbers, ignoring basic moral principles of fairness and justice that triggered a deteriorating public support for him. In a cover story of the Business Week (01/15/2007), the authors pointed out that "[j]udged solely by certain company financial measures, Nardelli, 58, should have enjoyed acclaim for transforming Home Depot from a faltering retail chain into an earnings juggernaut." The article continues to argue that "[i]n a season of growing antipathy toward extravagantly paid executives, the directors felt they had no choice" other than to fire him. A corporate insider revealed that "[t]he board loved him and hates the way this ended up". The media seems to have played an instrumental role in his ouster. Negative press articles about his pay arrangements at Home Depot skyrocketed from around four articles per year during his tenure before this date to 27 in his last year at the firm. An analyst commented that "[.] by firing

Nardelli [the board] had “caved” to critics, who were able to enlist the news media [...]” (Jones & Krantz, 2007).¹

The propensity of certain managerial actions to be condemned may not only depend on the specific moral standard that has been violated, but also on the evaluation of the moral conduct of those executives in other instances, provided that observers receive a number of different signals from the various moral choices executives take. The moral evaluation of the transgression specifically becomes complex when the moral conduct is inconsistent, i.e. when executives simultaneously display virtuous and vicious behavior in different domains or in different situations (Monin & Merritt, 2011). Provided that many of those virtuous actions, such as donations to charity, choosing environmental-friendly policies or treating employees favorably are studied under the rubric of corporate social responsibility (Margolis & Walsh, 2003), we are interested in understanding public moral judgment of executives who violated a moral standard and how CSR policies potentially moderate this outcome.

We consider a moral transgression that has received a lot of attention in the past decade, top executives’ remuneration packages that are widely perceived as excessively high (Basu & Palazzo, 2008). We argue that the public’s responsiveness to the moral transgression depends on the firms pro-social activities, commonly referred to as the policy on corporate social responsibility (CSR). Public judgment is generally stronger for companies that exhibit a high degree of social engagement in corporate philanthropy (Reynolds & Ceranic, 2007). This is most likely because philanthropy typically signals altruistic preferences; but in the corporate context, it may as well be motivated by pure self-interest, which is consistent with an

¹ Lin (2009) and Lammers, Stoker, Jordan, Pollmann, and Stapel (2011) documented cases in which CEOs of large firms lost their jobs because of violation of moral standards along domains unrelated to compensation.

instrumental notion of corporate social conduct (Luo & Bhattacharya, 2006). Corporate philanthropy may enhance the social esteem of the company and its management and thereby lends legitimacy to the organization (Suchman, 1995; Wood, 1991). This may positively affect the corporate bottom line through channels such as customer attitudes (Margolis & Walsh, 2003; Orlitzky, Schmidt, & Rynes, 2003). Since executives benefit from increased profits in multiple ways, it is ultimately unclear whether their motivation to engage in such pro-social activities is derived from the moral imperative or from financial incentives. In this context, a moral transgression such as violating pay norms reduces the ambiguity regarding the executives' moral behavior and exposes them to the charge of hypocrisy (Godfrey, 2005; Sonenshein, 2005; Urbany, 2005).

On the other hand, social psychologists indicated that morally inconsistent behavior does not always increase the likelihood of moral judgment (Monin & Merritt, 2011). First, when the moral transgression takes place on another moral domain than the morally positive act does, moral credit accrues which helps reduce the outrage over the transgression (Jordan, Mullen, & Murnighan, 2009; Nisan, 1991; Sachdeva, Iliev, & Medin, 2009). Second, when the transgression's moral interpretation gives rise to ambiguity, a morally positive act ensures that the behavior is construed more benignly and lends to the actor moral credentials, which in turn tames moral outrage (Effron & Monin, 2010; Monin & Miller, 2001). Based on these theories, we argue that moral outrage about excessive compensation levels is lower when firms have strong CSR policies along domains such as employee relations, diversity, and environmental protection. Finally, the question arises of whether executives care for their morally deviating behavior, and how they compensate for it. In other words, we are interested in whether moral outrage represents a constraint for the executive's behavior. While top executives may not share a general moral standard of compensation, we argue that they would care for morally consistent

conduct; specifically, in line with cognitive dissonance theory (Festinger, 1957), we propose that publicly exposing executive hypocrisy (not just perceived excessive remuneration) induces a behavioral change as well as a reduction in excess pay.

We complement the CSR literature which has been primarily concerned with CSR content or internal sense-making thus far (Aguilera, Rupp, Williams, & Ganapathi, 2007; Basu & Palazzo, 2008), and which has deemphasized the role of the individual perceiver when it comes to which moral expectation organizations and their top managers are held (e.g., Lange & Washburn, 2012). First, by drawing from the social psychology of moral judgment (e.g., Monin & Merritt, 2011), we advance theory on CSR as a moderator of the evaluation of top executive moral behavior in order to better understand the social consequences of moral transgressions committed by executives. Taking this approach helps us to make use of a richer set of concepts beyond moral credits, such as moral credentials and hypocrisy, thereby unifying research which either entirely focuses on negative spill-overs from CSR (e.g., Wagner, Lutz, & Weitz, 2009) or on positive spill-overs such as the insurance effect of CSR for corporate returns in times of crisis (Godfrey et al., 2009). Second, we test hypotheses based on these theories on public compensation data of CEOs heading U.S. listed firms for the years 1992 to 2007, which we complement with data on corporate CSR activities and a measure of public moral judgment on the compensation policies based on the amount of negative press coverage subsequent to the CEO pay disclosure. Our paper is distinguished from most of the empirical CSR literature since it uses a direct social response measure instead of indirect measures such as financial returns (Janney & Gove, 2011).

Moreover, even though the violation of compensation practices by executives was at the center of many public discussions, few academic papers have conceptually or empirically

elaborated on this issue (Wang & Murnighan, 2011). Among the exceptions are studies that have shed light on the morality of wages such as Levine (1993) who reported that overcompensation induced discomfort among Japanese workers, and Wade, O'Reilly, and Pollock (2006) who provided some indirect evidence for the existence of a moral constraint on top level wages by suggesting that cross-hierarchy compensation levels were consistent with fairness principles. We deliver direct evidence of the public's response to the disclosure of CEO pay arrangements; study their drivers, and the managerial response to public judgment.

Third, judgment and forgiving have been primarily studied through laboratory experiments (Barden, Rucker, & Petty, 2005; Effron & Monin, 2010; Stone, Wiegand, Cooper, & Aronson, 1997; Wagner, Lutz, & Weitz, 2009). We extend this stream of research on the social psychology of hypocrisy to the study of the perception of top executive behavior. Finally, this study adds to an emerging stream of research which analyzes the moral behavior and judgment of social and corporate elites and shows that power seems to go hand in hand with moral disengagement divulged through hypocritical, corrupt or otherwise unethical behavior (Carney, Yap, Lucas, & Mehta, 2011; Desai, Palmer, George, & Brief, 2011).

PUBLIC PERCEPTION OF VIOLATING COMPENSATION NORMS

We focus on violating norms of fair and equitable compensation as the moral transgression committed by top executives. Certainly, excessive pay levels by industrial CEOs or Wall Street executives do not fail to trigger moral judgment, disgust and sometimes even outrage by large parts of society (Crystal, 1991; Gasparino, 2009; Tett, 2009). Some social movements, such as Occupy Wall Street (which recently gained notoriety), center their protests on the criticism of top executive pay practices. That is, the compensation of some particular executives appears to violate a general sense of justice (Deutsch, 1975).

There is no standard way of measuring the degree to which a compensation package is perceived as excessive. Clearly, such a measure would depend on various social, political and psychological factors (Kelley & Evans, 1993). However, it should also take into account the scarcity of the skills of the managers and the effort exerted by them, given that these factors may alleviate concerns of excessive compensation. A simple way to capture the effects and other structural differences between pay practices in different economic environments is to focus on pay differentials of CEOs, controlling for differences in effort, the ability and skills required to perform the job, and the exposure to various risks associated with the position. We hence use a measure of excess compensation for CEOs that is based on the deviation from the expected level of pay which we obtain from a wage regression on proxies for the aforementioned factors (Core, Guay, & Larcker, 2008; Wowak, Hambrick, & Henderson, 2011). Pay schemes that are associated with larger positive differences should be more likely to be perceived as excessive. Note that we can be agnostic about what exact level of pay is perceived as excessive; it is not necessarily zero, since the average level of CEO pay might already be regarded as too big (Kuhnen & Niessen, 2012).

Public moral judgment becomes particularly effective for CEO remuneration practices since executive pay levels and compensation structures are transparent due to strong disclosure rules imposed by the U.S. Securities and Exchange Commission (SEC). Moreover, CEOs enjoy a high degree of media attention as individuals. The names of top executives regularly appear in the business press, CEO interviews are broadcast on TV, and top executives have a large exposure on the internet as well (Hamilton & Zeckhauser, 2004; Malmendier & Tate, 2009; Park & Berger, 2004). Since publicity also makes misbehavior more transparent, moral transgressions by CEOs have a relatively high likelihood of attention. We measure public outrage about a moral transgression through the extent they attract negative press reports. Press

media is arguably the most important institution that identifies and disseminates information about moral transgressions by individuals of high public exposure (Dyck, Volchkova, & Zingales, 2008; Gans, 1979; Glasser & Ettema, 1994). We essentially follow an often-used approach (Deephouse & Carter, 2005; Pollock & Rindova, 2003; Sullivan, Haunschild, & Page, 2007; Vergne, 2012), benefitting from the fact that relative to other news sources, newspapers are viewed as more reliable and are more easily recalled (Deephouse & Carter, 2005; Vergne, 2012).

Finally, note that for several reasons, we concentrate on CEOs and the public perception of their compensation packages in the context of the firm's CSR policy. The CEO is often the pivotal decision maker on CSR-related matters in a firm (Atkinson & Galaskiewicz 1988; Galaskiewicz, 1997; Embley, 1993; Kochan, 2002; Marquis & Lee, 2013; Orlitzky & Swanson, 2002) despite the fact that some firms have created special committees or positions for CSR (Strand, 2013; Porter & Kramer, 2002). For example, 71 percent of the firms surveyed in the 2007 UN Global Compact Annual Review name the CEO as the responsible level for managing and developing corporate social responsibility policies. In addition, journalists have a high propensity to attribute a firm's performance to the action of its CEO (Hayward, Rindova, & Pollock, 2004; Meindl, Ehrlich, & Dukerich, 1985) making it the appropriate level of analysis.

HYPOTHESES

In the following section, we derive hypotheses on how moral transgressions by top executives are interpreted in light of possible pro-social actions they took on behalf of their companies. We distinguish between four areas of pro-social activities that were commonly associated with CSR: corporate philanthropy, employee relations, environmental protection, and diversity policy. We use insights from social and moral psychology to argue that the

interpretation of the moral transgression is contingent upon on the actions along these particular CSR areas.

Observers use signals from pro-social actions taken by executives as cues about their moral standards since "[m]oral behavior [...] makes an implicit claim about one's values." (Effron & Monin, 2010: 1620). CSR activities, such as treating employees favorably, engaging in more environmental protection than legally prescribed, or fostering non-discriminating organizational practices, are typically viewed as pro-social behavior and should thus induce observers to attribute moral values to the executives who commissioned them. However, among these activities, donating resources to the weakest and most vulnerable members of the society is arguably socially most highly regarded (Dean, 2003; Piliavin & Charng, 1990). This holds, because unlike stakeholders, such as employees, customers, or environmental groups, receivers of donations have little power and cannot influence management by threatening to withdraw their support (Mitchell, Agle, & Wood, 1997). Hence, at least at first sight, any transfer through charitable donations seems to represent the purest form of altruistic, non-self-serving behavior since it is not enforceable through contractual or power relationships.

However, altruistic preferences inducing moral behavior are inconsistent with a mercenary intent of executives, and "true altruism" defies the notion of reciprocity (Bar-Tal, 1986). When it comes to corporate philanthropy, it is indeed unclear whether altruism is the principal motivator for action. Even though the receivers of donations are unlikely to directly affect corporate revenues, through various indirect channels, non-financial benefits such as social esteem and legitimization (Suchman, 1995; Wood, 1991) as well as financial returns for the company may be associated with this CSR category. In fact, many studies emphasized the positive financial implications associated with corporate philanthropy through increasing the

willingness of customers to pay a premium for the products (Brown & Dacin, 1997; Creyer & Ross, 1996), enhancing the goodwill of stakeholders during times of crisis (Du, Bhattacharya, & Sen, 2007), facilitating the recruitment of talented employees (Turban & Greening, 1997), and promoting dialogue with regulators (Neiheisel, 1995).² In turn, managers may indirectly benefit from corporate philanthropy through higher performance-based pay and increased job security. Hence, corporate philanthropy is consistent with both, managerial altruistic and ulterior selfish preferences.

Corporate philanthropy alone sends a blunted signal on the executives' other-regarding preferences. However, observers may consider managerial actions in different contexts to interpret these activities (Monin & Merritt, 2011). Since executives are exposed to a fundamental agency conflict, observers can use a relatively powerful test of managerial altruistic preferences by considering whether managerial moral behavior depends on the extent to which the cost of behaving morally is borne by the executive. More specifically, we argue that there is an inconsistency in managerial moral behavior when executives act in line with

- a) high moral standards when doing so is associated with low individual costs to the managers, and
- b) low moral standards when doing so is associated with high individual costs to the managers.

Thus, whenever executives generously distribute corporate resources to charity, condition a) is satisfied. While managers enjoy benefits through social rewards and any financial returns that these donations generate through their effects on wages and improved career

² Indeed, it is widely promoted that it "pays to be good", and this link has found strong empirical support in a study by Orlitzky, Schmidt, and Rynes (2003) who showed in a meta study that corporate philanthropy had the highest correlation with corporate financial performance.

prospects, the private wealth of CEOs would remain unscathed from the direct expenses on such activities since executives are typically only marginally invested in the firm. Hence, they do not incur substantial costs associated with these actions. Condition b) is satisfied when top executives accept or negotiate excessive compensation packages (Bebchuk & Fried, 2004; Cowherd & Levine, 1992; Crystal, 1991). Acting morally in this context would require relinquishing excessive pay levels, thereby imposing substantial opportunity costs on the executive. Hence, a moral transgression (excessive pay) might help resolve the ambiguity regarding the interpretation of the morally uncertain behavior (corporate philanthropy).

How do we expect observers to respond to such a behavioral inconsistency? We employ three theoretic approaches to explain moral judgments of moral transgressions (Effron & Monin, 2010). The first one is called the moral credits model which maintains that people consider a history of moral behavior and make forgiving of moral transgressions dependent on the moral credit that has been accumulated in the past (Nisan, 1991). The second one is called the moral credentials model which implies that good deeds induce observers to not condemn the actor for deeds that appear to be transgressions, but whose moral evaluation is ambiguous (Monin & Miller, 2001). Thirdly, the hypocrisy model suggests that observers oppose forgiving a moral transgression which occurs in a context in which the transgressor makes others believe he or she acted consistent with higher moral values (Barden, Rucker, & Petty, 2005).

Effron and Monin (2010) argued that in order to judge whether the moral credits, credentials, or hypocrisy model was appropriate to predict whether forgiving occurs in a specific situation, the determining factor was whether the transgression was ambiguous and occurred along the same or a different moral domain as the morally positive action. First, when the same moral domain is affected, observers will exhibit an aversion to the inconsistency in conduct

since the good deed appears to be associated with selfish motives and such behavior is condemned as hypocritical (Barden, Rucker, & Petty, 2005). Second, when the transgression and the moral action are related to different moral domains, the moral credits model suggests that observers forgive a transgression when previous good behavior produced a “surplus” for the moral account. Finally, the credentials model suggests that ambiguity of the moral behavior is an important driver of moral judgment. When a morally dubious action is performed, a previous good deed helps to construe the dubious action as a non-transgression, erasing the doubt about a possible bad intent that led to the action (Monin & Miller, 2001). The previous action may generate moral credentials that help forgive a transgression even along the same domain when it reduces the moral ambiguity resulting from the transgression.

The two actions, philanthropic donations and the violation of pay norms, share the same moral domain of distributive justice (Deutsch, 1975). Donations immediately shift income towards those members of the society that probably are most in need and hence make the income distribution more equal and equitable. As a result, donations are clearly associated with high scores of distributive justice (Deutsch, 1975). On the other hand, excessive levels of remuneration by definition violate this justice principle. Hence, based on the hypocrisy model, observers will exhibit an aversion to this behavioral inconsistency (Barden, Rucker, & Petty, 2005; Stone & Fernandez, 2008; Stone et al., 1997), and will show no willingness to pardon the transgression but instead tax such behavior as hypocritical. As a consequence, when a firm is highly engaged in corporate philanthropy, perceiving executive pay levels as excessive generates a moral inconsistency which will induce moral outrage about the perceived hypocritical behavior.

Hypothesis 1: The firm's CSR policy in corporate philanthropy positively moderates the effect of excess levels of CEO pay on the likelihood that executives will be subject to negative media coverage.

Few moral transgressions are free of ambiguity. The interpretation of moral behavior reflects the context in which the behavior takes place, and for every transgression, mitigating circumstances may add moral ambiguity, potentially inducing a more lenient view on the conduct and reducing the probability of moral judgment. Economists have undertaken numerous attempts to explain the observed compensation practices of U.S. top executives. Their arguments for why it might be optimal that some CEOs earn immense wages rested on the positive impact of the market mechanism on the optimal allocation of managerial talent and the increased efficiency in the presence of agency conflicts (e.g., Gabaix & Landier, 2008; Gayle & Miller, 2009). Hence, excessive payouts to CEOs could be understood and morally justified as a result of a compensation system that promotes efficiency and productivity and some observers may concede that in this context, observed pay practices are morally ambiguous.

Even though not everyone will follow this argumentation, this line of argument clearly becomes more convincing when the company that compensates their top executives more generously than the norm displays a general orientation towards monetary incentive schemes and beneficial working conditions for a larger set of employees. In line with the moral credentials theory model which suggests that “good” deeds help to forgive ambiguous “bad” deeds, one would expect the employment policy to mitigate the response to the alleged pay norm violation if it is consistent with it (Monin & Miller, 2001). This argument is strengthened if one considers that excessive pay levels in this study are measured based on peer-comparison, and managerial pay is characterized as excessive when executives at rival firms earn

substantially less, controlling for a number of factors such as performance and firm size. While such a comparison has many merits, it ignores wage distributions at the organizational levels. Given that their own compensation level is well above the norm, managers may give extra benefits to employees as a way to ensure the wage structure in its entirety is perceived as fair (Folger & Konovsky, 1989; Goodman, 1975; Heneman & Cohen, 1988; Meindl, 1989; Wade, O'Reilly, & Pollock, 2006), thereby shedding doubt on the validity of the signal of overcompensation from the peer-comparisons.

Hypothesis 2: The firm's employee-related CSR policy negatively moderates the effect of excess levels of CEO pay on the likelihood that executives will be subject to negative media coverage.

While maintaining distributive justice is an important measure for moral conduct by executives, it is not the only one. Another moral domain that has received substantial attention by organization scholars is procedural justice (Folger & Konovsky, 1989; Lind & Tyler, 1988). Procedural justice is concerned with the perceived fairness of procedures and mechanisms that produce organization-wide employment outcomes (Folger, 1977; Greenberg, 1987). While distributive and procedural justice are linked in particular ways (Cropanzano & Ambrosa, 2001; Lind & Tyler, 1988), the violation of one principle does not in general imply the violation of the other principle. An unequal distribution of income, for example, is not inconsistent with procedural justice if the outcome is, for example, not systematically biased towards some employees with specific individual characteristics that are unrelated to their performance.

On the organizational level, procedural justice has many aspects. One of the most important aspects is related to limiting cultural, gender, or racial bias when it comes to employment-related decisions (Ely & Thomas, 2001; Richard & Kirby, 1998). In organizations

which highlight diversity, discrimination along certain demographic characteristics is actively avoided or restricted, and pay levels or promotion trajectories should be affected by these characteristics to a lower extent than in other firms (Kalev, Kelly, & Dobbin, 2004). As a result, firms that emphasize their diversity policy should be perceived as pursuing higher levels of procedural justices along these dimensions. Since diversity is essentially unrelated to the perceived fairness of top executive pay, we suggest that diversity policies and the CEO's perceived pay norm violation are associated with different moral domains. As a consequence, the moral credit model predicts that the moral judgment of this transgression will be mitigated (Effron & Monin, 2010; Nisan, 1991).

Hypothesis 3: The firm's diversity-related CSR policy negatively moderates the effect of excess levels of CEO pay on the likelihood that executives will be subject to negative media coverage.

Another important dimension of social conduct relates to the environmental policy of the firm. The behavior of firms engaged in the protection of the environment in excess of what is legally required complies with universal moral standards which stress keeping the ecosystem to be intact so that humans and animals do not to have to suffer unnecessary harm (Johnson, 2001). At the same time, the environmental policy of the firm may touch upon issues of distributive and procedural justice. Distributive justice may be affected because pollution-intense production facilities are often located in areas with a low-income population (Grant, Jones, & Bergesen, 2002; Kassinis & Vafeas, 2006). Procedural justice is related to aspects of transparency of the decision-making process and the involvement of people affected by managerial decisions. Provided that aspects of humanity dominate the moral perception of environmental policy and not its distributional implications, we argue that the environmental policy is associated with a

different moral domain than CEO compensation. Hence, similar to the relationship between diversity policy and the perception of excessive CEO compensation, we expect that doing good on environmental issues helps to generate moral credit from observers, inducing them to forgive excessive pay levels of CEOs.

Hypothesis 4: The firm's environmental CSR policy negatively moderates the effect of excess levels of CEO pay on the likelihood that executives will be subject to negative media coverage.

So far, we have hypothesized about the perception of excessive pay levels in the context of the firm's CSR policy. Provided that the moral evaluation of compensation practices depends on it, the CSR policy may also moderate the executive's response to the public judgment. Since there is no general agreement as to what level of compensation represents a moral transgression, one may not expect that CEOs perceive their own compensation in the same moral terms as outsiders. Moreover, executives may employ several strategies to exempt themselves from moral judgment by using arguments of economic efficiency or by pointing to a global increase in earnings for top earners which exempt them from individual responsibility. Hence, one may not expect executives who have been exposed to public criticism for their inappropriate pay levels to respond with any significant changes in attitude or behavior.

However, engaging in hypocritical conduct may potentially threaten individuals in their self-esteem and self-integrity. More specifically, hypocritical behavior is known to generate cognitive dissonance (Fried & Aronson, 1995). According to dissonance theory, individuals may choose responses that allow them to reduce the discomfort created by the dissonance and to reestablish their self-esteem (Aronson, 1992; Cooper, 2007; Festinger, 1957). In theory, executives are provided with a broad variety of ways of reducing dissonance, such as indirectly

modifying attitudes and changing attention, or directly changing the behavior to bring it in line with the implicit claim of their own values. However, Stone et al. (1997) asserted that some strategies of dissonance reduction are preferred over others. Whenever strategies are available that directly affect the questionable behavior, individuals would usually select those to address the dissonance. This holds because doing so is the only way for subjects to ensure themselves and others of their honesty and sincerity. In our context, we expect CEOs to reduce their compensation after being publicly judged when their conduct gave rise to hypocrisy.

Hypothesis 5: Public moral judgment of excess levels of CEO pay induces a subsequent reduction in this measure in situations giving rise to the perception of hypocrisy.

METHODOLOGY

Research Setting and Sample

The sample of CEOs is from Compustat's ExecuComp database. Since 1992, ExecuComp provides information about executives and their compensation for a wide range of firms. We matched the dataset of CEOs to the Center for Research in Security Prices (CRSP)/Compustat North America fundamentals annual database and to the Kinder Lydenburg Domini (KLD) social indicator database Sokrates. KLD provides indicators of CSR policies and CSRP/Compustat information for financial and accounting controls. We included a CEO in the sample when we had complete information on compensation, controls and when the firm was covered by KLD. The dataset was then linked to media coverage of each executive's pay. Our final sample consists of 10,169 observations, composed of 2,882 CEOs at 1,868 firms covering the years 1992 to 2007.

Dependent Variable

Negative Media Coverage. Our dependent variable is negative media coverage of a firm's CEO compensation (Neg. Media Coverage). To measure media coverage, we used the Dow Jones Factiva database which archives a broad set of newspapers and magazines. In Factiva, we located articles with a search strategy similar to Core et al. (2008) which tracks down media reports covering the compensation of a CEO irrespective of the tone. We then evaluated the tone of an article with an automatic Python script that ran over each article and looked for negatively connoted signal words within a narrow range between a CEO's name and words indicating compensation. The list of negative signal words is from Core et al. (2008) and specific to the topic of executive remuneration.³ We used this list because the wording of articles on CEO pay are distinctive from reports about general themes and recent research shows that programs using general dictionaries often developed for other disciplines are prone to misclassify text that is specific to a certain topic (Loughran & McDonald, 2011).⁴ Altogether, the search resulted in approximately 12,500 unique articles of which about a third have a negative tone. A description of the search string we used to locate articles, the list of negative signal words and two exemplary articles are provided in the appendices B, C, and D.

The automated program has a number of pivotal advantages; for instance, it allowed us to deal with a large amount of news coverage for a rich and heterogeneous sample of firms over a number of years. Moreover, the narrow range of words for the indicators of CEO compensation and the negative tone to appear after the executive's name is 32 words at most. That enabled us to establish a fairly direct connection between the CEO, compensation and the

³ We randomly drew around 300 articles to check whether the list in Core et al. (2008), which covers articles until the year 2001, was still valid or had changed significantly. We did not find any substantial differences in the wording of the articles contained in our sample.

⁴ For example, *huge* return on equity compared to *huge* compensation package.

negative signal word. We also tested how the script performed compared to human coding and asked two human coders to independently rate articles of 50 randomly selected CEOs. In contrast to the automated script, the range of words for the indicators of compensation and a negative tone were not restricted. Human coders and the script agreed for 74.3 percent of articles with the script underestimating the number of negative coverage. We then used the cases in which the human coders and the script disagreed as the dependent variable in a regression and included all the controls we used in this study. A statistically significant correlation with any of the controls could have been a sign of a nonrandom distribution of disagreement and potentially posed a threat to our analysis. However, none of the controls were statistically significant.

Since media coverage of CEO compensation was virtually never positive (Core et al., 2008; Kuhnen & Niessen, 2012), we used the number of negative articles that cover a focal firm's CEO compensation as the dependent variable.⁵ We measured media coverage in the year following the disclosure of the compensation package. The media usually report about remuneration in the last and not in the current year as such information is predominantly published in annual reports after the end of a firm's fiscal year.

⁵ While measures such as the Janis-Fadner (1965) coefficient of imbalance and other ratio-based measures are often utilized to reflect media coverage, we followed recent research and used the number of articles instead (see Zavyalova, Pfarrer, Reger, & Shapiro, 2012). This was for three reasons. First, the tone of media coverage of CEO compensation was either neutral or negative but seldom positive. This implies that we cannot use measures such as the Janis-Fadner coefficient of imbalance which assume that all three tones are present. Second, media coverage in our sample has a high variance which will lead to a low criterion validity of ratio-based measures. Third, when using ratio-based measures, one implicitly assumes negative and, in our case, neutral articles are similarly salient to outside observers. This is clearly in contrast to findings from social psychology which indicate that negative information is multiple times more salient than neutrally-framed information (e.g., Baumeister, Bratslavsky, Finkenauer, & Vohs, 2001).

Independent Variables

Measures of CSR policy. We obtained CSR policy measures from KLD. The company uses a wide range of qualitative and quantitative as well as internal and external sources of information to track the social responsibility of a subset of publicly traded U.S. companies, applying consistent criteria from year to year. The dataset is the most accepted measure of CSR (Chatterji, Levine & Toffel, 2009) and has been labeled "one of the best measures of corporate CSP [corporate social performance] available" (Hillman & Keim, 2001, p. 130) or as "the de facto research standard" for measuring CSR (Waddock, 2003, p. 369). While the dataset has received some criticism especially for its coarse structure (e.g. Rowley & Berman, 2000), it nevertheless contains a large cross-section of industries and firms ensuring sufficient variance, has construct validity and is more comprehensive and objective than other measures of CSR (Graves & Waddock, 1994; Sharfman, 1996).

KLD classifies CSR into different dimensions that are further separated into areas of "strength" and "concern". We focused on strengths because the theoretical rationale we developed pertains specifically to how engagement in pro-social actions impacts on the

perception of excessive CEO compensation.⁶ Each dimension and area further contains categories for various subactivities. Categories are assigned to a binary (0,1) measure and are then aggregated into an overall evaluation of each dimension. Firms are awarded a point if they fulfilled some specific criteria. We used the dimensions' sum of points as measures of firms' CSR performance. We operationalized corporate philanthropy (CSR Philanthropy) with KLD's community dimension which covers charitable and innovative giving, support for housing and education, whether the firm runs a volunteer program, has an in-kind giving program or is otherwise engaged in the community. Employee related CSR (CSR Employees) is the dimension for employment relations. It comprises a firm's relation to a labor union, a company's profit sharing program to distribute firm income to its workforce, level of worker involvement, employee firm ownership through stock options, provision of retirement benefits or a strong health and work safety program. Similarly, CSR related to corporate diversity (CSR Diversity) covers whether the CEO or a member of the board of directors is a woman or a

⁶ Although some scholars used the difference between the areas of strengths and concerns to reflect firms CSR related investments and performance, past research clearly indicated that these are empirically and theoretically two different constructs which should not be collapsed into one measure (Godfrey, Merrill, & Hansen, 2009; Mattingly & Berman, 2006). Moreover, combining the two dimensions implies positive and negative firm actions are similarly salient to the media or stakeholders. As argued before, this starkly contradicts the abundant evidence from research in social psychology that positive and negative information or firm actions are not perceived as equally salient (Baumeister, et al., 2001; Fiske & Taylor, 2008; Richey, Koenigs, Richey & Fortin, 1975). However, to dispel any concerns that firms tried to offset CSR weaknesses or acts of corporate social irresponsibility with CSR strengths in the same and/or other dimensions, we excluded the firm-year observations in which a firm was in the top 5 percentile of the distribution in a dimension's areas of strengths and simultaneously within the worst 5 percentile (corresponding to the highest scores) of the distribution in any of the dimensions' areas of weaknesses. In unreported robustness checks, we excluded the top 10 (15) percent of the respective distributions and repeated the analyses. Our results were unchanged. Finally, we repeated our analysis but excluded firms which were in the top 5 percentile of the distribution in a dimension's areas of strengths and within the worst 5 percentile of the distribution in any of the dimensions' areas of weaknesses in any year before or after the current date. The underlying rationale was that firms might built up credit with stakeholder before conducting a moral transgression or, alternatively, that CEOs invest in CSR related policies after a transgression to restore relations with stakeholders (Merritt, Effron, & Monin, 2010).

member of a minority group, the firm provides family benefits or the firm has a hiring program for the disabled. The dimension environment (CSR Environment) reflects substantial revenues from products promoting the efficient use of resources, prevention of pollution, usage of recycled materials and whether the firm was taking significant measures to reduce its impact on climate change.⁷

Excess CEO Pay. We conceptualized excessive CEO compensation (Excess CEO Pay) as a deviation from a norm of CEO compensation (Wiesenfeld, Wurthmann, & Hambrick, 2008) and operationalized it through a well-established and widely used procedure (Core et al., 2008; Fong, Misangyi, & Tosi, 2010; Wade, O'Reilly, & Pollock, 2006; Wowak, Hambrick, & Henderson, 2011). To be more specific, we calculated expected CEO compensation through separate annual cross-sectional regressions of the natural logarithm of total pay on an array of well-proven economic determinants of executive compensation and industry controls.⁸ Residuals of the annual regressions are our measure of excessive CEO compensation. These residuals equal the difference between the logs of expected and observed CEO compensation and essentially reflect the degree to which an executive's remuneration is above or below the compensation norm in the ExecuComp sample. Differences in logs are ratios which circumvented possible distortions in the press' reflection of what constitutes excessive pay in absolute terms (Core et al., 2008).

⁷ We excluded from philanthropy the subactivities for Indigenous People's Relations and Volunteer Programs. The former was moved to another dimension by KLD during the observation period and is available for two years only. The latter has only been collected from 2005 onwards. Employment relations is without No-Layoff Policy which has not been collected after 1994. From environment, we excluded Property, Plant, Equipment because it is not available after 1995. However, keeping these subactivities in the indices does not qualitatively alter our results.

⁸ We provide the regression equation in the appendix A.

In the regressions, we controlled for firms' size with sales in the previous year, a dummy indicating membership in the Standard and Poor's 500 index, CEO tenure, contemporaneous and lagged stock market and accounting returns. Sales and tenure were taken in their natural logarithmic form to limit the influence of extreme outliers. Lastly, we controlled for likely differences in pay practices across different industries by indicators based on Standard Industrial Classification (SIC) codes. Regression results mirror those of earlier studies in terms of the R^2 , signs and sizes of the coefficients and with respect to the levels of significance. Our operationalization of excessive CEO pay is rather conservative as it is likely that the CEO pay norm for the sample of firms in ExecuComp itself is already perceived as excessive (Kuhnen & Niessen, 2012).

Control Variables. Other factors besides excessive executive compensation and a firm's investments into CSR policy may determine the media's decision to cover a CEO's pay; these factors need to be controlled for. We expected the general attention of the press to a firm and to executive compensation to be stimulated by a broad set of factors. As firm controls, we included total assets (Firm Size) and a dummy for membership in the S&P 500 stock market index (S&P500) as proxies for firm size. To account for firms' media visibility, we used the amount of media coverage (negative and neutral) of a firm's CEO compensation in the preceding year (Media Coverage lagged). We further controlled for the number of stock market analysts covering the firm (Analysts). Comparably larger or firms listed on prominent stock market indexes have a higher visibility and stronger appeal to the media (Fombrun & Shanley, 1990; Hayward et al., 2004; Rehbein, Waddock, & Graves, 2004). Past research indicates that equity analysts potentially impact other information intermediaries and stakeholders (Pollock & Rindova, 2003; Rao, Greve, & Davis, 2001). Moreover, events such as missing analysts' consensus forecast that can be framed as a surprise have a higher chance of being seen as

newsworthy by the media (Tuchman, 1978). The variable is also an additional proxy for firm size and visibility as larger and more salient firms are usually followed by more analysts (Bhushan, 1989).

To reflect firm performance, we included contemporaneous and lagged stock returns from CRSP and accounting returns computed as net income before extraordinary items divided by average total assets from Compustat.⁹ Each performance proxy was additionally subdivided into positive (Pos. Stock Ret.; Pos. Acc. Ret.) and negative values (Neg. Stock Ret.; Neg. Acc. Ret.) in year *t* and *t*-1 (adding lagged, e.g. Pos. Stock Ret. lagged). The division of returns accounts for the considerable evidence that journalists attribute a firm's performance to its CEO (Hayward et al., 2004; Meindl et. al., 1985), and that negative performance has a larger perceived salience and impact on media coverage and stakeholders' perception than positive performance (Baumeister et al., 2001; Fiske & Taylor, 2008; Wartick, 1992).

We also included a CEO's tenure (CEO Tenure) with a longer tenure potentially implying that the public is more familiar with a CEO and the press more likely to write about the executive (Chen & Meindl, 1991; Core et al., 2008). We further controlled for whether the CEO is the founder of the firm (Founder CEO). Past research suggests systematic differences in the composition and level of compensation between founder and non-founder CEOs (Tzioumis, 2013; Wasserman, 2006), and journalists' opinion might be impacted by the fact that CEOs founded the company when they report about their remuneration. The measure is a dummy equal to 1 if the CEO joined the firm at least 5 years before the firm went public.

⁹ Performance variables are ratios and thus prone to extreme values in either direction if the scaling variable become too small or large. We winsorized the 1 percent at each tail of the variables' distribution to mitigate the effects of outliers. Note that winsorizing has no qualitative impact on the results.

Finally, to rigorously control for unobserved factors, our analyses include year and industry fixed effects based on the two digits SIC code industry classification of Waddock and Graves (1997). This approach controls for all industry characteristics that do not vary during the time period of this study and for all common shocks and trends. Table 1 provides an overview over the variables we used.

 Insert Table 1 about here

RESULTS

Table 2 displays descriptive statistics and correlations. Correlations are low to moderate. We addressed concerns of multicollinearity and obtained variance inflation factors for each model. The VIFs are all less than 10, and the average VIF is steadily less than 3 and hence below critical thresholds.

 Insert Table 2 about here

Estimation Method

To test our hypotheses 1-4, we used pooled cross-sectional negative binomial regressions and negative media coverage of a firm's CEO compensation as the dependent variable. Negative binomial regression is a count model that is appropriate in cases when the dependent variables are non-negative integer valued and the distribution of the dependent variable displays signs of overdispersion, e.g. a larger variance than mean. We focused on cross-sectional instead of within firm variation. The structure of CSR policies and the scores KLD assigns tend to change little from year to year in a given firm. This implies that fixed effect estimation is

unlikely to detect a significant relationship between CSR policies, CEO excess compensation and negative reactions in the press even if one should exist. Instead, we acknowledge that some CEOs receive more public attention than others and that this potentially impacts the press' reaction. We specifically addressed this issue in our robustness section.

The data is organized by calendar years and thus might induce autocorrelation. To deal with it, we applied Hubert-White heteroskedasticity robust standard errors clustered on the level of the CEO. Clustering on the CEO level controls for heterogeneity in the residuals and at the same time allows for autocorrelation within a cluster over years (Petersen, 2009). Clustering at the CEO level is, compared to non-clustered heteroskedasticity robust standards errors, a very conservative approach. It produces lower t-statistics and weaker levels of significance.

For all significant interaction terms, we report the regression coefficients, levels of significance and incidence rate ratios (IRR). Regression coefficients in negative binomial models represent differences between the logs of the expected count as a function of the predictor variables. The IRR is the exponential of the regression coefficient and corresponds to the change in the predicted amount of negative media coverage for a one-unit increase in the predictor variable holding all else constant. One advantage of the IRR is associated with the fact that the change does not depend on the level of the other variables. Generally, an IRR above one indicates that the expected count is larger after an increase in the predictor variable by one unit. An IRR below one implies a decrease. To further illustrate effect sizes, we calculated the change in the average marginal effect on the predicted negative media coverage in a situation characterized by a high level of excessive CEO compensation (corresponding to the sample's

top quintile) and an increase of the respective CSR policy measures from 1 to the highest possible values.¹⁰

Findings

Table 3 lists the main results for hypotheses 1-4. Models with the index "a" are regressions with the CSR proxies only while models with the index "b" additionally contain the main variables of interest, namely the interaction effects between the CSR policy indicators and excessive CEO compensation. The interaction effects are pivotal as accusations of hypocrisy do not evolve simply because the firm invests a lot in CSR but because a CEO is at the same time in conflict with norms on CEO pay.

As shown in models 1a/b in table 3, and consistent with hypothesis 1, moral inconsistencies in managers' behavior at firms which score comparatively higher in philanthropy are condemned by observers according to the hypocrisy model and receive more negative press coverage. The interaction effect between philanthropy and excessive compensation is positive and statistically significant ($\beta = 0.14$, IRR = 1.15, $p < 0.01$). An increase in the interaction term by one unit raises the expected negative media coverage by about 15 percent. When the level of excess CEO pay is high (sample's top quintile), an increase in the score for philanthropy from the lowest to the highest value (e.g., 1 to 4) raises the expected negative media coverage by about 52.6 percent.

¹⁰ We discuss changes in percentage rather than using absolute values as the latter are potentially cumbersome to interpret. For example, effect sizes in absolute terms might seem comparatively small. The authors of a recent study who also use negative media coverage as a dependent variable compare effect sizes to the potentially tremendous consequences of ostensibly small changes in equity analysts' recommendations (e.g., from buy to hold) or to the damaging impression of uninspired recommendation letters (Zavyalova et al., 2012).

Results in table 3 also provide support for hypothesis 2. CSR related employment policies promoting efficiency and productivity mitigate the response to excessive CEO pay, which - according to the moral credentials model - is judged less harshly when managers give extra benefits to employees ($\beta = -0.12$, IRR = 0.88, $p < 0.01$). A one-unit change in the interaction term leads to an approximately 12 percent lower number of expected criticism in the media. Given a high level of excess CEO pay, a change in the scores for employee-related CSR from 1 to 5 decreases the expected number of negative press coverage by about 68.8 percent.

Results in models 3a/b and 4a/b in table 3 are consistent with hypothesis 3 but do not support hypothesis 4. Both hypotheses predicted a reaction to excessive CEO compensation according to the moral credits model resulting in lower negatively toned press coverage. More specifically, in hypothesis 3 we argued that a firm's CSR policy scores in corporate diversity induces a more lenient reaction of observers. The respective coefficient of the interaction term is statistically significant on the 5 percent level ($\beta = -0.05$, IRR = 0.95, $p < 0.05$). A one-unit increase in the interaction term decreases the expected negative media coverage by about 5 percent. The expected negative press coverage decreases by about 34.1 percent when level of excess CEO pay is comparatively high and the scores in CSR policies related to diversity increase from the lowest to the highest value (e.g., 1 to 7).

Insert Table 3 about here

With respect to the results of the control variables, proxies for CEO tenure, firm size, the number of analysts following as well as the amount of media coverage of a firm's CEO compensation received in the last year increase negative media coverage. Negative coverage is lower when the incumbent CEO is also the founder of the firm. The significant negative

coefficients on contemporaneous negative stock market and negative accounting return suggest that the media cover a CEO's compensation more negatively when there is a higher negative stock market performance. The positive coefficients for positive contemporaneous accounting, lagged stock market and accounting return suggest that the media write about CEO compensation when operating and stock market performance are high. The proxy for excess levels of CEO pay has the expected positive sign but is significant only in some of the specifications. A potential reason for why the coefficient is not significant might be related to the fact that it is largely explained by the independent variables that determine negative media coverage.

In hypothesis 5, we proposed that executives respond to their morally inconsistent behavior and to the criticism of the press by reducing their pay, which was previously perceived as excessive. Table 4 lists the empirical results of OLS regressions where the dependent variable is the level of excess CEO pay in the following year ($t+1$). Standard errors were clustered on the level of the CEO. We included excess pay in the current year to account for the effects of mean reversion in pay. Large payouts today, e.g. through stock options plans, are usually followed by lower payouts in the following year (Core et al., 2008). The interaction effect between philanthropy, excess CEO pay and negative media coverage (Philanthropy X Excess CEO Pay X Negative Media Coverage) measures the impact on future levels of excess CEO compensation that are due to the criticism. The results in model 2 in table 4 provide strong evidence that the level of excess CEO pay in the following year is lowered as a response to the criticism. We also tested for the impact of public criticism on CEOs' turnover probability but did not find an effect.

Insert Table 4 about here

Alternative Explanations and Robustness Checks

We analyzed a number of alternative explanations and conducted a battery of robustness checks for our findings.

Firm visibility. A potential concern to our study is that companies' size and their visibility matters beyond what we control for. Firms' visibility increases the pressure to conform to external expectations on social conduct (Pfeffer & Salancik, 1978; Zyglidopoulos, Georgiadis, Carrol, & Siegel, 2012), and one might expect that these firms engage more strongly in CSR related policies. At the same time, any newsworthy corporate event is more likely to lead to media coverage for visible companies, as there are potentially more journalists familiar with these firms. Stories about executive pay, especially about excessive levels, often appeal to a broader audience (Jensen, 1979). Hence, CEOs of more visible firms perhaps receive a higher share of negative media coverage for the same level of excessive CEO pay. While we account for firm size with a number controls, we addressed this potential concern by adding an interaction effect between non-negative media coverage and excess CEO pay. Firms' visibility as the real driver of media attention induces a spurious and positive correlation. Quite to the contrary, in non-tabulated results, the interaction effect is constantly insignificant and most importantly negative. Overall, we interpret the results as confirmation for our previous hypotheses and as standing in contrast with firms' sizes or visibility being the driver for our findings.

Selective media coverage. A similar potential threat to our analysis is associated with the fact that only a subset of all firms or CEOs received substantial media attention. If attention is driven by some factors we did not include in our regressions, the coefficients in the regressions may be biased. Ignoring such an issue of selection is often viewed as a sort of an

omitted variable bias, which can be addressed by inserting an explicit measure for the degree of selection (Heckman, 1979). Recent work in management research has posited that the Heckman two-step selection model is a suitable method of controlling for selection-based endogeneity (Bascle, 2008) and as such, it was used in a number of studies in management (e.g., Bednar, 2012).

The Heckman model has two stages. The first stage is a Probit regression which calculates a firm's likelihood of being covered by the media and computes the correction factor known as the inverse Mills ratio. The ratio is then included as a control correcting for potential selection effects in the second stage (Hamilton & Nickerson, 2003). For the first stage regressions, we used a dummy that is equal to 1 if the firm received at least one article covering its CEO compensation and 0 otherwise. Besides the proxy for philanthropy-related CSR investment and the respective interaction effects with excessive pay, we included all the controls we used in the second stage regressions and additionally the state a firm's headquarter is located in as recorded in Compustat. Firms that are geographically more proximate to a media outlet and its reader base have a higher likelihood of being covered (Shoemaker & Reese, 1996) but it is unlikely that the distance mattered for the tone of media coverage in the circumstances we consider in this study. The inverse Mills ratio was then used as a covariate in the negative binomial regression with our measure for negative media coverage as the dependent variable. A significant inverse Mills ratio in the second stage would be an indication of problems of endogeneity. Again, we included all the controls we incorporated in the main regressions of table 3 and used standard errors clustered on the level of the CEO. In non-tabulated results, the inverse Mills ratio was not significant in any of the models, which lifts concern of endogeneity due to a selection bias. Moreover, our conclusion for the CSR policy proxies, interaction effects and controls are qualitatively similar to those of table 3.

Expected vs. excess CEO pay. To assure that our findings are due to excessive CEO compensation and not purely driven by the level of the remuneration package, we included CEOs' total remuneration split into the excessive and expected parts. The latter is the amount that could have been predicted using the computation for excessive pay introduced earlier. The underlying rationale is that the media do not cover excessive pay but sensationalize large compensation packages as such, regardless of whether or not these are economically justified (Jensen, 1979). In addition to the variables used in the specifications of table 3, we included interactions between the expected part of CEO compensation and the measures for CSR policy. Our earlier conclusions do not change. All interaction effects between expected CEO pay and the CSR policy related variables have a negative coefficient and are in most models statistically insignificant, strongly indicating that the joint effects of compensation and CSR policy on negative media coverage are due to the excessive part of the whole remuneration package.

Quality of corporate governance. In our analysis, we did not include a proxy for firms' quality of corporate governance. Managers of firms, which pay excessive wages, may also have the discretion of funneling more corporate funds into CSR activities suggesting that such factors might bias our coefficients. Moreover, negative media coverage might be driven by worries of managerial profligacy rather than moral inconsistency at firms with a weak governance structure. As a proxy for firms' quality of governance, we included the entrenchment (Entrenchment) index of Bebchuk, Cohen, and Ferrell (2009). Again, our results do not change qualitatively and the variable for the quality of governance is not significant in any of the models.¹¹

¹¹ Our results do not change if we use the G-Index of Gompers, Ishii and Metrick (2003).

Year and industry fixed effects. Finally, we tested whether year and/or industry fixed effects have affected the results. We assume that the media adjust for differences in executive compensation and CSR related investments across industries and time. To examine the robustness of our results, we repeated our analyses without year and industry fixed effects. These non-tabulated results yield the same inferences.

GENERAL DISCUSSION

The past two decades have witnessed an enormous increase in the level of top executive remuneration, which has periodically triggered public expressions of moral indignation. In the context of growing social inequality, increasing top level wages has often been perceived as moral transgressions, and executives receiving generous payouts were portrayed as greedy and morally dubious. However, the moral space within which executives operate is still largely unexplored terrain, and there is a large variance to be explained regarding which manager is more likely to attract public judgment for a violation of moral-based compensation standards. This study's goal is to shed light on the role of the organization's CSR policy concerning the question of how observers discriminate between executives when singling out targets for their public outrage.

We propose that the share of public moral judgment directed at executives depends on the firms' investments in CSR in different areas. Moral standards at which firms are held by external observers are more stringent if firms are perceived as "good firms" since moral judgment is triggered by the perception of hypocrisy that arises from the inconsistency in the moral conduct. However, theories of social psychology hold that hypocrisy requires inconsistent moral conduct along the same moral domain. In contrast, when moral conduct affects different

moral domains, inconsistent behavior may rather generate moral credit or credentials and thus help to forgive the transgression.

Using a measure of public moral judgment that is based on the reaction of the media to excess levels of CEO remuneration, we obtained supporting evidence for the hypocrisy and moral credentials hypotheses and partial support for the moral credit hypothesis. Executives at high-philanthropy firms have a higher probability of attracting negative press for excessive compensation practices than do those working at low-philanthropy firms. Pro-social activities shedding doubt on the moral infringement such as providing employee support or scoring high on the dimension of diversity seem to limit the extent of public outrage. Only the coefficient associated with the influence of activities on environmental protection is statistically not significant. Hence, there is substantial support for the notion that mechanisms already identified in the lab seem to govern the feedback process triggered by morally inconsistent conduct in the noisier organizational context (Barden, Rucker, & Petty, 2005; Effron & Monin, 2010; Stone et al., 1997).

On the flip side, our results have some interesting implications for the role of social conduct of firms on the moral judgment of managerial behavior. While the dominant perspective posits CSR investments as a mechanism of avoiding social sanctions (Aguilera et al., 2007) or of generating an insurance-like effect shielding against negative consequences of moral transgressions such as excessive executive compensation in the future (Godfrey, Merrill, & Hansen, 2009), we propose a model that explicitly incorporates both outcomes. First, CSR may raise the moral expectations of stakeholders by which they judge firms and management, but these presumptions also spill over to other domains such as executive compensation. But moral ambiguity surrounds CSR engagement. Managers of firms emphasizing their CSR contributions

face the risk of being perceived as acting strategically and being motivated by selfish preferences of managers, giving rise to the perception of hypocrisy (Porter & Kramer, 2002). In support of this view, our evidence suggests that observers use additional signals of managerial conduct to generate their moral assessment. Second, note that CSR investments can indeed perform the role of cushioning outrage. Our results confirm that executives may receive a smaller share of public judgment when large executive pay packages are accompanied by employment relations that foster workers' benefits or provide monetary benefits to large parts of the work force and thus shed doubts on the severity of the transgression. To some extent, the same may hold when the moral discrepancy in executives' conduct affects a different moral category, such as social investments related to firms' diversity policy or the protection of the environment.

The study touched upon issues of the moral divide between society, the business and corporate elite. We find that the exposure to public criticism of CEO pay arrangements have no significant effect on future excess pay levels; it hence seems that executives are not sensitive to public moral judgment, and that they do not share more generally accepted standards of fair pay. This result is broadly in line with papers such as Carney et al. (2011) and Desai et al. (2011) who demonstrated that moral standards are not entirely shared by corporate elites. However, this claim requires a caveat since our evidence is suggestive of executives displaying a preference for morally consistent conduct as public moral judgment leads to next-period decreases in excess compensation for executives who are susceptible to hypocritical conduct.

Our findings also carry significant implications for firms and managers. In order to successfully steer companies and their own careers, it is instrumental that managers understand the moral constraints that society imposes on their conduct. In particular, managerial decision-

making should take into account the complex psychological mechanisms that form moral standards at which this behavior will be held by stakeholders. A recent proposal by the leadership team of Goldman Sachs may serve as a case in point. In early 2010, the team discussed the idea of expanding a program that required executives and top managers to give a certain percentage of their earnings to charity every year. With this, Goldman Sachs hoped to soften criticism over the size of its bonuses. Quite to the contrary and in line with the hypocrisy hypothesis, the idea alone was critically commented on in public (Story, 2010). Hence, managers should be aware that, despite the positive effects that corporate philanthropy might often have on firm performance (Lev, Petrovits, & Radhakrishnan, 2010), it comes at a cost of being more susceptible of moral judgment in connection with remuneration levels.

Finally, we urge readers not to misinterpret our results as a case against corporate philanthropic engagement or other pro-social activities. Instead, they should rather be taken as a cautionary warning that in order for the desired positive outcomes of CSR related investments to be achieved, managerial behavior must be morally consistent across different moral domains and contexts.

LIMITATIONS AND FURTHER RESEARCH

There are several limitations to our study which at the same time suggest fruitful avenues for future research. First, we hypothesize about and tested implications of morally inconsistent conduct and ignore facets of morally consistent conduct. Provided that organizations whose conduct is morally consistent but only in line with low moral standards can cause severe social damage, it seems to be important to understand how such a behavior is sustained, and whether there is a failure of the mechanism associated with social sanctions to single out violations. On a related note, our study focuses entirely on externally imposed, social sanctions for moral

infractions. However, we ignore possible heterogeneity of internal vs. external motivation of executives and the differential impact of social sanctions on these two types of managers. Moreover, we disregard the role of the board in the relationship between public judgment and managerial behavior. Collecting information on executives and board members that could help differentiate between internally and externally motivated individuals should shed further light on the issue of the responsiveness to moral judgments.

Another issue that seems to be interesting to pursue is related to the moral behavior and career outcomes of managers. Financial market pressure on executives failing to deliver sufficient financial returns through the threat of take-overs (Jensen, 1986; Kennedy & Limmack, 1996; Martin & McConnell, 1991) and through actions taken by institutional and activist shareholders (Parrino, Sias, & Starks, 2003; Westphal & Bednar, 2008) is a well-studied phenomenon. Given that standard economic models do not explain empirical turnover patterns well (Jenter & Kanaan, 2011; Puffer & Weintrop, 1991), considering this alternative route to CEO turnover could prove useful. In our study, we show that the perception of excessive CEO compensation and the moral judgment does not significantly affect the turnover probability. However, there is a dearth of systematic research on the drivers and consequences of public pressure as a result of morally failing executives for moral violations that are perhaps viewed as more serious than violations of fair compensation principles.

Other limitations are grounded in our proxy for public outcry; as our measure of moral judgment, we used media coverage. In the past and for most of the period our study covers, individuals were equipped with very limited options of expressing their anger and outrage on a larger stage. Nowadays, social media such as Twitter or Facebook provide many more opportunities for individuals to make their opinions known, and it would be interesting to study

whether the formation of widespread beliefs about moral transgressions has changed with the introduction of the new technology.

We also focused on public judgment of only one moral transgression in a specific country. There is ample space to investigate the relationship between CSR investments and other moral infractions or transgressions of formal rules and laws and within different institutional contexts and cultures. Suitable areas are, for example, corporate corruption, accounting frauds or events with hazardous results for the environment or the community such as oil spills. Similarly, one may consider further dimensions of ethical corporate conduct such as human rights, which we ignore for reasons of non-availability for most years of observation.

In closing, the empirical investigation of the moral interpretation of top executive behavior is still in its early stage. Using the theoretical framework we developed in this paper is a potentially promising strategy to further analyze the various reactions to other moral transgressions.

TABLE 1
Definition and Source of Key Variables

Variable	Definition	Source
Negative Media Coverage	Amount of negative coverage of a firm's CEO compensation in the year after CEO pay is disclosed	Factiva
CSR Philanthropy	Community dimension	KLD
CSR Employees	Employee relations dimension	KLD
CSR Diversity	Diversity dimension	KLD
CSR Environment	Environment dimension	KLD
Excess CEO Comp.	Excessive CEO remuneration (detailed calculation, see appendix A)	ExecuComp
Tenure	Log(Years in office)	ExecuComp
Founder	Dummy with value of 1 if the CEO was CEO at the firm 5 years before it went public	CRSP, ExecuComp
Analysts	Log(Number of financial analysts following a firm)	I.B.E.S
Media Coverage lagged	Amount of media coverage (negative and neutral) of a firm's CEO compensation lagged by one year	Factiva
Firm size	Total assets	Compustat
S&P500	Dummy = 1 if firm is in the S&P 500 index year t and zero otherwise	ExecuComp
Pos. Stock Ret.	Positive stock returns	CRSP
Pos. Stock. Ret. lagged	Positive stock returns lagged by one year	CRSP
Neg. Stock Ret.	Negative stock returns	CRSP
Neg. Stock Ret. lagged	Negative stock returns lagged by one year	CRSP
Pos. Acc. Ret.	Positive return on assets computed as net income before extraordinary items divided by average total assets	Compustat
Pos. Acc. Ret. lagged	Positive return on assets computed as net income before extraordinary items divided by average total assets and lagged by one year	Compustat
Neg. Acc. Ret.	Negative return on assets computed as net income before extraordinary items divided by average total assets	Compustat

TABLE 2
Means, Standard Deviations, and Correlations of Key Variables^a

Variable	Mean	SD	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)	(13)	(14)	(15)	(16)	(17)	(18)	(19)	(20)
(1) Negative Media Coverage	0.36	1.59	1.00																			
(2) CSR Philanthropy	0.27	0.62	0.15	1.00																		
(3) CSR Employees	0.39	0.67	0.05	0.18	1.00																	
(4) CSR Diversity	0.71	1.09	0.19	0.42	0.24	1.00																
(5) CSR Environment	0.17	0.44	0.05	0.15	0.22	0.13	1.00															
(6) Excess CEO Pay	0.00	0.91	0.03	0.07	-0.01	0.07	-0.03	1.00														
(7) Founder	0.06	0.23	-0.02	-0.05	-0.07	-0.03	-0.05	-0.05	1.00													
(8) Tenure ^b	1.62	0.92	0.04	-0.04	-0.07	-0.06	-0.06	-0.00	0.40	1.00												
(9) Analysts ^b	3.25	0.87	0.15	0.22	0.22	0.25	0.08	0.17	-0.02	0.00	1.00											
(10) Media Coverage lagged ^b	0.75	0.51	0.38	0.18	0.09	0.25	0.04	0.03	0.03	0.25	0.16	1.00										
(11) S&P500	0.38	0.48	0.14	0.18	0.20	0.24	0.11	0.00	-0.05	-0.01	0.36	0.16	1.00									
(12) Firm size ^b	8.06	1.62	0.22	0.39	0.19	0.40	0.12	0.10	-0.13	-0.05	0.44	0.29	0.43	1.00								
(13) Pos. Stock. Ret.	0.24	0.33	0.00	-0.03	-0.03	-0.04	-0.05	0.01	0.03	-0.00	-0.03	-0.01	-0.01	-0.09	1.00							
(14) Pos. Stock Ret. lagged	0.26	0.37	0.00	-0.05	-0.02	-0.04	-0.06	0.00	0.04	0.03	-0.01	-0.02	-0.01	-0.08	-0.02	1.00						
(15) Neg. Stock Ret.	-0.07	0.13	-0.01	0.03	-0.04	-0.01	0.02	-0.02	-0.03	0.01	-0.09	0.01	0.04	0.06	0.35	-0.10	1.00					
(16) Neg. Ret. lagged	-0.07	0.15	-0.01	0.04	-0.01	-0.00	0.03	-0.01	-0.02	0.05	-0.06	0.02	0.06	0.12	-0.25	0.34	0.05	1.00				
(17) Pos. Acc. Ret.	0.06	0.06	0.01	-0.02	0.09	0.02	-0.02	0.02	0.04	0.07	0.07	0.01	0.14	-0.26	0.11	0.20	0.15	0.19	1.00			
(18) Pos. Acc. Ret. Lagged	0.06	0.06	0.01	-0.03	0.09	0.02	-0.03	0.01	0.05	0.07	0.10	0.00	0.13	-0.25	-0.03	0.14	-0.01	0.15	0.77	1.00		
(19) Neg. Acc. Ret.	-0.01	0.03	0.00	0.05	0.00	0.03	0.02	-0.04	-0.03	0.03	-0.03	0.03	0.09	0.13	0.01	0.02	0.28	0.28	0.25	0.14	1.00	
(20) Neg. Acc Ret. lagged	-0.01	0.04	0.00	0.06	0.02	0.03	0.03	-0.02	-0.02	0.05	-0.02	0.00	0.09	0.15	-0.16	0.01	0.10	0.32	0.15	0.24	0.45	1.00

^a $n = 10,169$

^b Logarithm.

TABLE 3
Pooled Cross-Sectional Negative Binomial Analysis Results

Variable	Dependent Variable: Negative Media Coverage _{t+1}								
	(1a)	(1b)	(2a)	(2b)	(3a)	(3b)	(4a)	(4b)	(5)
CSR Philanthropy	-0.01 (0.05)	-0.04 (0.06)							-0.06 (0.06)
CSR Philanthropy X Excess CEO Pay		0.14** (0.05)							0.19** (0.05)
CSR Employees			-0.06 (0.05)	-0.06 (0.05)					-0.08 (0.05)
CSR Employees X Excess CEO Pay				-0.12** (0.04)					-0.13** (0.05)
CSR Diversity					0.06 ⁺ (0.03)	0.07* (0.03)			0.08* (0.03)
CSR Diversity X Excess CEO Pay						-0.05 ⁺ (0.03)			-0.06* (0.03)
CSR Environment							-0.05 (0.07)	-0.05 (0.07)	-0.04 (0.07)
CSR Environment X Excess CEO Pay								0.05 (0.06)	0.07 (0.07)
Excess CEO Pay	0.05 (0.03)	0.02 (0.03)	0.04 (0.03)	0.11** (0.04)	0.05 (0.03)	0.11* (0.05)	0.05 (0.03)	0.04 (0.04)	0.15** (0.05)
Founder CEO	-0.35 ⁺ (0.21)	-0.36 ⁺ (0.20)	-0.35 ⁺ (0.21)	-0.34 ⁺ (0.20)	-0.35 ⁺ (0.21)	-0.35 ⁺ (0.21)	-0.35 ⁺ (0.21)	-0.35 ⁺ (0.21)	-0.36 ⁺ (0.20)
CEO Tenure ^a	0.10* (0.04)	0.11* (0.04)	0.10* (0.04)	0.10* (0.04)	0.11* (0.04)	0.11* (0.04)	0.10* (0.04)	0.10* (0.04)	0.11** (0.04)
Analysts ^a	0.26** (0.07)	0.26** (0.07)	0.27** (0.07)	0.27** (0.07)	0.25* (0.07)	0.25** (0.07)	0.26** (0.07)	0.26** (0.07)	0.25** (0.07)
Media Coverage lagged ^a	1.04**	1.03**	1.03**	1.03**	1.02*	1.03**	1.04**	1.04**	1.01**

	(0.07)	(0.07)	(0.07)	(0.07)	(0.07)	(0.07)	(0.08)	(0.08)	(0.07)
S&P 500 Index	0.21*	0.22*	0.21*	0.21*	0.21*	0.21*	0.21*	0.21*	0.24**
	(0.09)	(0.09)	(0.09)	(0.09)	(0.09)	(0.09)	(0.09)	(0.09)	(0.09)
Firm size	0.41**	0.41**	0.42**	0.42**	0.39**	0.39**	0.41**	0.41**	0.40**
	(0.04)	(0.04)	(0.04)	(0.04)	(0.04)	(0.04)	(0.04)	(0.04)	(0.04)
Pos. Stock Ret.	0.13	0.12	0.13	0.11	0.13	0.13	0.13	0.13	0.11
	(0.11)	(0.11)	(0.11)	(0.11)	(0.11)	(0.11)	(0.11)	(0.11)	(0.11)
Pos. Stock Ret. lagged	0.20*	0.20*	0.20*	0.20*	0.21*	0.20*	0.20*	0.21*	0.20*
	(0.09)	(0.09)	(0.09)	(0.09)	(0.09)	(0.09)	(0.09)	(0.09)	(0.09)
Neg. Stock Ret.	-0.81**	-0.81**	-0.82**	-0.86**	-0.79**	-0.80**	-0.81**	-0.81**	-0.83**
	(0.29)	(0.30)	(0.29)	(0.29)	(0.30)	(0.30)	(0.30)	(0.29)	(0.29)
Neg. Stock Ret. lagged	-0.27	-0.28	-0.27	-0.31	-0.25	-0.26	-0.26	-0.27	-0.31
	(0.27)	(0.27)	(0.27)	(0.27)	(0.27)	(0.27)	(0.27)	(0.27)	(0.27)
Pos. Acc. Ret.	2.14*	2.10*	2.20*	2.19*	1.99*	1.99*	2.16*	2.15*	1.97*
	(0.90)	(0.90)	(0.91)	(0.91)	(0.91)	(0.91)	(0.90)	(0.89)	(0.91)
Pos. Acc. Ret. lagged	1.75*	1.74*	1.77*	1.87*	1.71*	1.69 ⁺	1.74*	1.72*	1.75*
	(0.86)	(0.87)	(0.86)	(0.87)	(0.87)	(0.86)	(0.87)	(0.87)	(0.86)
Neg. Acc. Ret.	-2.72**	-2.62*	-2.75**	-2.72**	-2.67**	-2.72**	-2.74**	-2.74**	-2.62**
	(1.03)	(1.03)	(1.03)	(1.01)	(1.03)	(1.03)	(1.03)	(1.04)	(1.00)
Neg. Acc. Ret. lagged	-0.58	-0.57	-0.57	-0.69	-0.54	-0.52	-0.56	-0.53	-0.56
	(0.98)	(0.98)	(0.98)	(0.96)	(0.98)	(0.98)	(0.97)	(0.97)	(0.98)
Intercept	-7.72**	-7.70**	-7.76**	-7.78**	-7.49**	-7.50**	-7.72**	-7.72**	-7.55**
	(0.39)	(0.39)	(0.39)	(0.39)	(0.40)	(0.40)	(0.38)	(0.38)	(0.40)
Observations	10,169	10,169	10,169	10,169	10,169	10,169	10,169	10,169	10,169
Chi-squared	1438.45	1352.36	1395.77	1452.11	1354.22	1367.82	1360.99	1390.29	1520.69
Log pseudo-likelihood	-5608.31	-5604.59	-5607.05	-5600.16	-5605.77	-5602.86	-5608.04	-5607.77	-5587.44

Industry and year fixed effects were included as controls.

^a Logarithm.

Levels of significance:

⁺ p < 0.10

* p < 0.05

** p < 0.01

TABLE 4
Pooled Cross-Sectional OLS Analysis Results

Variable	Dependent Variable: Excess CEO Compensation _{t+1}	
	(1)	(2)
Excess CEO Pay	0.63 ^{**} (0.04)	0.64 ^{**} (0.04)
CSR Philanthropy	0.02 ⁺ (0.01)	0.04 [†] (0.02)
CSR Philanthropy X Excess CEO Pay		-0.02 (0.04)
CSR Philanthropy X Excess CEO Pay X Negative Media Coverage		-0.09 ^{††} (0.03)
Founder CEO	-0.06 (0.04)	-0.07 (0.04)
Analyst ^a	0.04 ^{††} (0.01)	0.03 ^{††} (0.01)
Entrenchment	0.04 ^{††} (0.01)	0.04 ^{††} (0.01)
Media Coverage lagged ^a	0.02 (0.02)	0.03 (0.02)
Intercept	-0.23 ^{**} (0.04)	-0.24 ^{**} (0.04)
Observation	6,315	6,315
R ²	0.43	0.43

Industry and year dummies were included as controls.

Levels of significance:

^a Logarithm.

⁺ p < 0.10

* p < 0.05

** p < 0.01

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APPENDIX A

We operationalized excessive CEO compensation as the difference between expected and observed pay using the whole ExecuComp database as sample. Observed compensation was total CEO compensation as reported in ExecuComp. Expected compensation was computed as follows:

$\text{Log}(\text{Expected Total Compensation})_{it} = \alpha + x_{it} \beta + u_{it}$, where x_{it} included $\text{log}(\text{Sale})_{it-1}$, SP500_{it} , $\text{log}(\text{Tenure})_{it}$, RET_{it} , RET_{it-1} , ROA_{it} , ROA_{it-1} and dummies for two digit SIC codes.

$\text{Excessive CEO compensation}_{it} = \text{Log}(\text{Observed Total Compensation})_{it} - \text{Log}(\text{Expected Total Compensation})_{it}$

APPENDIX B

We used the following search string to locate articles in Factiva:

(CEO NAME or CEO NAME'S) near20 (compensation or salary or bonus or option* near10 grant or option* near10 receiv* or option* near10 exercis* or restricted stock or (pay near5 00) or (was paid near5 00) or (pay near5 million*) or (was paid near5 million*)) and (CEO NAME or CEO NAME'S) same (compensation or salary or bonus or option* near10 grant or option* near10 receiv* or option* near10 exercis* or restricted stock or (pay near5 00) or (was paid near5 00) or (pay near5 million*) or (was paid near5 million*)) "and ((CEO NAME or CEO NAME'S) same (FIRM NAME or FIRM NAME'S)).¹²

¹² The term "near20" ("near10") locates a word in the subsequent bracket within 20 (10) words after the CEO's name, "same" locates words within the same paragraph and "*" allows for differing endings of a word. "or" as well as "and" are congruent to their natural usage.

APPENDIX C

String used to code articles as negative-toned:

(CEO name or CEO names or executive* or CEO*) near25 (high* near7 (salar* or bonus* or pay* or paid or compensat* or benefit*) or excess* near7 (salar* or bonus* or pay* or paid or compensat* or benefit* or option*) or lofty near7 (salar* or bonus* or pay* or paid or compensat* or benefit* or option*) or hefty near7 (salar* or bonus* or pay* or paid or compensat* or benefit* or option*) or large near7 (salar* or bonus* or pay* or paid or compensat* or benefit* or option*) or rich near7 (salar* or bonus* or pay* or paid or compensat* or benefit* or option*) or big* near7 (salar* or bonus* or pay* or paid or compensat* or benefit* or option*) or outsize* near7 (salar* or bonus* or pay* or paid or compensat* or benefit* or option*) or huge near7 (salar* or bonus* or pay* or paid or compensat* or benefit* or option*) or generous near7 (salar* or bonus* or pay* or paid or compensat* or benefit* or option*) or exorbitant* near7 (salar* or bonus* or pay* or paid or compensat* or benefit* or option*) or fat* near7 (salar* or bonus* or pay* or paid or compensat* or benefit* or option*) or gargantuan near7 (salar* or bonus* or pay* or paid or compensat* or benefit* or option*) or bonanza* near7 (salar* or bonus* or pay* or paid or compensat* or benefit* or option*) or jumbo near7 (salar* or bonus* or pay* or paid or compensat* or benefit* or option*) or whopp* near7 (salar* or bonus* or pay* or paid or compensat* or benefit* or option*) or astound* near7 (salar* or bonus* or pay* or paid or compensat* or benefit* or option*) or ridiculous* near7 (salar* or bonus* or pay* or paid or compensat* or benefit* or option*) or stagger* near7 (salar* or bonus* or pay* or paid or compensat* or benefit* or option*) or hand- some* near7 (salar* or bonus* or pay* or paid or compensat* or benefit* or option*) or lucrative near7 (pay* or compensat* or option*) or critic* near7 (pay* or compensat*) or best near7 paid or reap* adj7 million* or self-serving or largesse or overpaid or lavish or perks or perquisites or windfall* or earn* more than or was paid more than or receiv* more than or made more than)

APPENDIX D

Illustration from the sample of articles

Two illustrations from the sample of newspaper articles. Both cover the compensation of Robert Nardelli of Home Depot. Excerpt 1 is negatively toned, excerpt 2 neutrally. Each article counted at most as one observation for a specific CEO regardless of how many times the CEO was named in the article.

Caption: identifier that the article covers the compensation of a CEO, negative signal word

Excerpt Article 1:	Tone = Negative
Title:	Living wage would help poor and benefit Chicago: Let's remember what the big-box bosses earn while wailing about the high cost of their hired help.
Date:	26 July 2006
Source:	The Chicago Sun-Times

Oh, speaking of a lot of money, let's pause to remember what the big-box bosses earn while wailing and gnashing their teeth about the high cost of their hired help. The CEO of Wal-Mart, H. Lee Scott, earned \$23 million in 2005 while Home Depot's Robert Nardelli collected a staggering \$200 million in compensation since 2000, according to published reports. I have some suggestions for these guys on a few places to cut their bloated budgets.

Excerpt Article 2:	Tone = Neutral
Title:	Home Depot in 2001 Gave CEO Nardelli A \$5 Million Bonus, Other Compensation
Date:	1 April 2002
Source:	The Wall Street Journal

ATLANTA – Home Depot Inc. awarded its chairman and chief executive, Bob Nardelli, a \$5 million bonus, deferred stock valued at \$9 million and one million stock options in addition to his \$1.5 million salary last year, the company's proxy shows.

Mr. Nardelli, 53 years old, hired from General Electric Co. in December 2000, also received

\$7.25 million in other compensation in 2001, much of it related to his initial hiring and relocation. Nearly \$5 million of that other compensation reflected forgiveness and related tax payments on part of a \$10 million loan that will be forgiven in full if Mr. Nardelli remains with the company for five years.

Under his employment contract, Mr. Nardelli receives a minimum \$3 million bonus. Mr. Nardelli's stock options for last year, with an exercise price of \$36.20, were valued by the company at between \$22.8 million and \$57.7 million. Home Depot, the nation's largest home-improvement retailer, valued his total deferred stock granted since his hiring at \$48.7 million, according to the proxy.
