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May 7, 2011

# Moving the Goal Posts on Pay

By GRETCHEN MORGENSON

PEOPLE scrutinize just about everything Wal-Mart does. As Michael T. Duke, the company's chief executive, put it recently, "What we do and how we perform is watched closely not only by our customers and shareholders, but also by the whole world."

All of which makes a recent decision about executive pay at this giant retailer downright puzzling. In a proxy statement filed a few weeks ago, Wal-Mart's compensation committee said it had replaced a crucial metric for assessing executives' performance: same-store sales, referring to stores that have been open for at least a year. Instead of that measure, Wal-Mart is using total sales companywide, or at its major units, Wal-Mart Stores and Sam's Club.

Why? The change was "intended to align our performance share goals more closely with our evolving business strategy, which emphasizes productive growth, leverage and returns," Wal-Mart said.

The timing was certainly curious. The switch came amid a sustained decline in Wal-Mart's same-store sales, which have been falling for nearly two years. The company's total sales, however, rose 3.4 percent in the latest fiscal year.

Shifting the goal posts meant more money for Mr. Duke in the latest fiscal year than he would have received under the old arrangement. His compensation totaled \$18.7 million, more than \$16 million of

which was performance-based.

Same-store sales are an important metric for investors. A quintessential apples-to-apples comparison, they measure the productivity at established stores and eliminate sales spikes that might occur when new stores open.

Aware that investors obsess over these figures, Mr. Duke told analysts recently that turning around Wal-Mart's same-store sales was his top priority. Last February, when the company announced results that included the seventh consecutive quarterly drop for the figure, its share price fell 3 percent.

So why remove this crucial performance gauge for pay purposes? Wal-Mart did not respond to a request for comment on the matter.

Certainly, past statements about why the board chose to include this measure suggest that it's important. For example, Wal-Mart said in its 2008 proxy that its board had used "comparable-store sales as a performance metric because it believes it is a key driver of shareholder returns, and because investors look to comparable-store sales as an important measure of performance in the retail industry."

Two years later, the company said its compensation committee included same-store sales as one of its benchmarks "because it believed that good performance relative to these metrics is important for our overall financial performance and, therefore, is likely to have a positive effect on shareholder returns."

The committee added that "the combination of these performance metrics was likely to incentivize our executives to achieve performance that is in the best interests of our company and our shareholders."

And yet, a year later, Wal-Mart jettisoned same-store sales from the mix. Explaining the decision, the proxy said the compensation committee concluded that "the combination of these performance metrics was likely to incentivize our executives to achieve performance that is in line with the best interests of our company and our shareholders."

Talk about trying to have it both ways.

KEEP in mind that when Wal-Mart included same-store sales in its pay calculations, that measure had a sizable effect on Mr. Duke's compensation. Indeed, same-store sales accounted for 30 percent of the weighted factors determining his performance pay in fiscal 2010 (which consisted of most of 2009 and the first month of 2010).

Removing same-store sales from its pay-for-performance measures "is a failure to admit failure," says Burt Flickinger III, managing director at the Strategic Resource Group, a retailing consulting firm. "This is the first time since the company was founded that, during a recession, same-store sales were consistently negative in contrast to key competitors like Costco, Target, TJX and BJ's."

Mr. Flickinger says he expects Wal-Mart's same-store sales to keep declining in the coming months.

The switch at Wal-Mart last year followed a shift in 2009 that allowed the company to set performance targets annually. In previous years, the board had set performance targets for three-year periods. The goals had to be met over that time before company executives could receive certain incentive pay awards.

The company's proxy said that shifting to annual targets allowed the board "to set more effective performance goals based on more current information and over a more realistic time frame."

But Mr. Flickinger said Wal-Mart's pay packages seemed especially unfortunate in light of the company's decision late last year to end its longtime profit-sharing programs for lower-level workers. This arrangement was created by Sam Walton, the company's founder, and was a source of considerable pride to him.

"Profit-sharing has pretty much been the carrot that's kept Wal-Mart headed forward," Mr. Walton wrote in his 1992 autobiography, "Sam Walton: Made in America."

Last year, before Wal-Mart eliminated that profit-sharing program, it said it paid roughly \$1.1 billion

in profit-sharing and **401(k)** matches to employees. In the future, it will offer only the 401(k) match.

“Taking away profit-sharing was the ultimate Ebenezer Scrooge story of the last holiday season,” Mr. Flickinger said. “Ebenezer makes all the money, and all the poor Cratchits working in the Wal-Mart stores become poorer and poorer.”

At least one Wal-Mart shareholder has expressed concern that the company’s directors are awarding bonuses to executives despite lagging performance.

“As the union that represents retail workers we are troubled that these bonus payouts come when front-line Wal-Mart associates are getting wages and benefits cut, and seeing their hours reduced,” says John Marshall, senior analyst in the capital stewardship program of the United Food and Commercial Workers. “Wal-Mart’s serious understaffing is part of the reason same-store sales continue to decline, which ultimately hurts the stock price.”

WAL-MART’S annual shareholder meeting is scheduled for June 3. It will be interesting to see whether other shareholders speak out about the changes in the performance pay structure. Shareholder meetings have been fairly quiet this year, but Wal-Mart’s shares have not kept up with either the overall stock market or retail store indexes for the last three years.

A flagging share price has a funny way of focusing otherwise complacent stockholders.



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