

EXECUTIVE¹⁾ COMPENSATION TRENDS IN KOREA

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Executive compensation is a structural approach for evaluating and rewarding executives in an objective manner. It is a reward program that appraises the management's performance in one term of office and determines the management's base pay, bonus and other compensation measures. The executive compensation program in Korea generally consists of three parts: base pay, short-term incentives and long-term incentives. Short-term incentives are bonus given to the management for one year's performance, such as annual cash bonus. Long-term incentives are reward provided to executives for their management results in three years, such as stock option.

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Trends of Executive Compensation in Korea

Compared to that of advanced economies, especially the U.S., Korea's executive compensation has several characteristics such as less reward, focused short-term incentives and fast introduction of performance-based system like Merit Pay System.

First, executives in Korea have been rewarded less than those in other countries. Compensation gap between executives and

employees does not show striking differences. According to Towers Perrin, executives in the U.S. earn 24 times more than that of average employee and in Japan 10 times; however, Korean executives earn only 6 times more than employees.

Second, executive compensation programs of Korean companies in general comprise of base pay, bonus and focused short-term incentives such as annual cash bonus. The compensation programs in Korea places substantial emphasis on short-term results. In the case of the Doosan Group, the executive compensation program is composed of base pay and bonus, with no additional incentive program. Old base pay, various allowances and operational money have been integrated into the base pay. The bonus is provided to executives based on their annual performance.

Third, very recently, a few companies are considering the introduction of long-term incentive programs such as stock options. In December 1998, 261 companies changed their articles of association to adopt the stock option program. However, only a handful of companies have really decided to grant stock options²⁾.

Forth, executive compensation programs are transforming from the fixed reward form to varied reward forms based on performance, such as "Merit Pay System" (MPS), which is comparable to annual salary system. According to a survey by the Korea Chamber

1) In this article, "executives" refers to CEOs and other major executive members of the management.

of Commerce (KCC), 28.9% of 201 companies already adopted the MPS in 1998, and 44.8% were going to introduce the MPS in March 1999.

Major big business groups such as the Samsung Group, LG Group, SK Group and Hyundai Motor Company are running the MPS as their executive compensation program. The executive compensation program of the Samsung Group, for example, has a structure of base pay (position pay), merit pay, regular bonus and special bonus. The base pay is fixed to the executive's position. The merit pay is given differently commensurate with the evaluation of the management's performance. The regular bonus is of fixed amount and given twice a year as 200% of the base pay. The special bonus varies, depending on the company's performance.

Prospects of Executive Compensation in Korea

Upon completing the current restructuring, executive compensation in Korea is expected to undergo substantial change in coming years. First, companies are likely to pursue differentiation of compensation

content by management goal and strategy. For instance, if a company focuses on short-term results, it would design the compensation where short-term incentives such as annual cash bonus are important. If it places more weight on long-term performance, the company should consider adopting long-term incentives such as stock options.

Second, companies are willing to set proper performance criteria that measure and evaluate executives' performance. In general, it will be necessary to use financial and non-financial criteria such as R&D investment, education, and customer loyalty, etc.

Third, companies are expected to run their executive compensation programs more openly. While the improvement of corporate governance is becoming apparent and transparency of management is being emphasized, a company would be better off to open its executives' compensation structure to the public. **VIP**

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Table 1. Cases of Executive Compensation

Company	Compensation Structure	Criteria
Doosan Group	base pay + bonus	-base pay: corporate and individual performance -bonus: individual performance
SK Group	base pay + bonus + stock options	-base pay and bonus: individual performance -stock options: corporate and individual performance
Samsung Group	base pay + merit pay + bonus + special bonus	-merit pay: individual performance -special bonus: corporate performance
Hyundai Motor Company	base pay + role pay + job pay	-base pay: individual evaluation -role pay: role (position) -job pay: job (performance)