

# **The Legitimacy of CEO Pay: The Discourse of Telecom, the Media and the Public**

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## **Abstract**

This paper investigates how Telecom Corporation of New Zealand Ltd (Telecom) managed its legitimacy after announcing the Chief Executive Officer's (CEO's) pay in 2009 as well as the media's and public's reaction to Telecom's announcement. The findings show that Telecom, the media and the public use the same remuneration logics to justify their positions. These remuneration logics are used to both justify and criticise Telecom's CEO's pay, although the media's and public's arguments are often unsophisticated and focus on the absolute level of CEO pay. Telecom is able to maintain its legitimacy through the use of well-structured, sophisticated arguments.

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**1. Introduction**

After the announcement of the 2009 remuneration of Paul Reynolds, Chief Executive Officer (CEO) of Telecom Corporation of New Zealand Limited (Telecom), New Zealand's two major newspapers printed the following headlines: "Telecom's \$5m boss gets bonus despite profit fall" (New Zealand Herald, 25 August 2009) and "Telecom board defends 'shameless' salary" (NZPA, 25 August 2009). Wayne Boyd, Telecom's Chairman justified Reynolds' remuneration in saying, "Under Paul Reynolds' leadership, our executive team has delivered on the demanding objectives set by the board over the past year" (NZPA, 25 August 2009). However, the announcement sparked much debate in the media and amongst the public about CEO pay. There were hundreds of comments posted on websites beneath news articles and blogs. The public debate culminated in Telecom's Annual General Meeting, where Boyd provided spoke at length about how Reynolds' remuneration was determined.

Public scrutiny of executive remuneration is an international phenomenon, particularly since the Global Finance Crisis and subsequent recession in many economies. In the US, John Thain, former CEO Merrill Lynch, was heavily criticised for bonuses paid to employees and a US\$1.2 million renovation of his office (New York Times, 27 January 2009). In the UK, the government, shareholders and the public have criticised executive bonuses leading to CEOs of several major banks forgoing their 2009 bonuses (Financial Times, 22 February 2010). In Australia, Julia Gillard, Prime Minister is reportedly uncomfortable with the amount CEOs are paid (Sydney Morning Herald, 18 November 2010). Further, these countries have introduced 'say on pay' regulations giving shareholders greater voice at annual general meetings. These examples highlight the significance of executive remuneration to the public in Anglo-Saxon countries.

A company can lose the support of the public if its decisions are perceived to be illegitimate or unjustifiable. For example, “Managing director David Baldwin said Contact lost 41,000 electricity customers in the wake of last October’s board move to increase directors’ fees” (New Zealand Herald, 15 August 2009). Companies will attempt to manage societal expectations and maintain their legitimacy. In an early US study of boards of directors, Harrison (1987) found that companies added committees to their board structure to enhance their legitimacy. However, what is considered legitimate in terms of executive remuneration is cloudy. Regulations and codes of practice are typically concerned with disclosure requirements, although codes of practice do outline processes for determining executive remuneration (Weight, 2008). The shareholders’ and public’s expectations are far more uncertain than regulative and normative expectations.

Research has examined the relationship between executive remuneration and a myriad of variables, particularly firm performance (Tosi et al., 2000; Gerhart et al., 2009). Few studies have investigated executive remuneration in terms of organisational legitimacy. Zajac and Westphal (1995) and Wade et al. (1997) found that US companies use remuneration logics to justify their decisions to the public, and shareholders (as measured by the movement in share price) do respond positively to certain remuneration logics. Also, Core et al. (2008) found that media scrutiny does not alter executive remuneration in US companies. Thus, the evidence indicates that companies do attempt to manage the legitimacy of executive remuneration (Scott, 2008), but the media’s ability to scrutinise executive remuneration may be overstated (Core et al., 2008). However, no studies have examined what individual members of the public think about specific instances of executive remuneration.

The case of Paul Reynolds' 2009 remuneration presents a unique opportunity to study organisational legitimacy and societal expectations. Telecom's 2009 annual report includes a section on CEO remuneration (about 3 pages or 2,000 words), and Wayne Boyd's speech at Telecom's annual general meeting included much explanation of CEO remuneration (about 1,500 words). There are at least 12 newspaper articles and blogs about Reynolds' 2009 remuneration and many of these online media allowed the public to add comments. This paper investigates how Telecom justified Reynolds' remuneration, and how the media and public reacted to the announcement of Reynolds' remuneration. Specifically, this paper identifies and analyses the remuneration logics (or reasons) that Telecom, the media, and members of the public give to justify their position.

This paper is organised as follows. The literature is reviewed in section 2, particularly studies on organisational legitimacy and executive remuneration. The research questions and method is outlined in section 3. The texts are studied using content analysis. Telecom's background including its history, CEO remuneration and firm performance over time, and key events in 2009 are described in section 4. The findings describe what reasons Telecom, the media, and the public give to justify their positions, and analyse the sophistication of their arguments in section 5. A discussion of the findings is presented in section 6. Conclusions including theoretical and practical implications are given in section 7.

## **2. Literature Review**

There is a paradox in the research on executive remuneration. There is no economically significant relationship between executive remuneration and firm performance (Tosi et al., 2000; Devers et al., 2007), yet the majority of listed companies use performance-based remuneration (Weight, 2008; Crombie, 2009). Rost and Osterloh (2009) found that the

sensitivity of CEO pay to firm performance is decreasing over time and conclude that performance-based remuneration is a managerial fashion. In a study of executives' perceptions of stock options, St-Onge et al. (2001) found that there are many reasons why stocks options are used to remunerate executives including to motivate, link pay and performance, and reward executives with valuable skills and experience. In a similar study, Beer and Katz (2003) concluded that performance-based remuneration is used to increase the level of executive remuneration, rather than to link pay to performance.

Prior research has investigated the efficiency of performance-based remuneration, rather than its legitimacy. If performance-based remuneration is a managerial fashion, then companies can use it to enhance their legitimacy in the eyes of stakeholders. However, there has been scant research on how companies legitimate themselves with respect to executive remuneration. Zajac and Westphal (1995; 2004) found that US companies use remuneration logics to enhance their legitimacy to shareholders. They found that when announcing the adoption of long-term incentive plans, shareholders responded more positively if the announcement used the agency and/or human resources logics. But they did not study other remuneration logics.

### *2.1. Discourse on Executive Remuneration*

Remuneration logics are systems of reasoning which organisational and their actors use to explain or justify remuneration practices to themselves and others. Remuneration logics can be found in the press releases and annual reports of companies as well as regulations and codes of practice (Wade et al., 1997; Crombie, 2009). There are many remuneration logics and examples can be found in literature (see table 1). Companies use remuneration logics to provide an explanation to convince shareholders and investors about their remuneration

practices and consequently this affects their legitimacy. Also, codes of best practices are issued by associations (e.g. an institute of directors) and are intended to provide a guide as to what is best practice in terms of executive compensation. This is intended to influence companies and support the legitimacy of regulators and associations. However, research has not investigated whether the media or the public also use remuneration logics to evaluate the remuneration practices of companies.

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## *2.2. Legitimacy Theory*

Suchman (1995, pg. 574) adopted a broad definition of legitimacy, defining it as “a generalised perception or assumption that the actions of an entity are desirable, proper or appropriate within some socially constructed system of norms, values, beliefs and definitions.” This particular definition of legitimacy asserts that a social contract exists between the entity and society. Maintaining legitimacy is an ongoing issue organisations face. Organisations need to provide assurances to society about their ongoing performance through “warm signals” such as speeches or long term contracts (Ashforth and Gibbs, 1990). This contributes to maintaining a social contract with society. Organisations are not able to completely satisfy society’s expectations but maintaining legitimacy is about communicating with audiences and letting them know what is happening.

A potential threat to a company’s legitimacy is negative publicity about an excessive remuneration payout to executives (Core, 2008). To protect their legitimacy, companies use

remuneration logics to justify executive remuneration practices. Wade et al. (1997) studied how a sample of US companies justified their remuneration practices and found that companies either emphasised or downplayed justifications depending on their financial performance. They found that companies that paid their CEO a large amount of base salary were more likely to justify practices by the use of consultants, while companies with high accounting returns tended to downplay market returns in their justification.

Legitimacy theory is often used to describe how companies act in reporting social and environmental disclosures (Cho and Patten, 2007). Disclosures are used to legitimise an organisation's practices or to alter society's perceptions of the organisation. Deegan and Gordon (1996) found that there was a significant increase in Australian companies' environmental disclosures over time, supported by an increase in society's awareness relating to environmental issues. Organisations are also known to increase disclosure if they perceive their legitimacy is threatened. For example, during the 1970s, BHP's environmental disclosures increased when the mining, steel and oil industries were under public pressure (Guthrie and Parker, 1989). Deegan and Gordon (1996, p. 187) also found that disclosure practices by organisations were often "self laudatory" in promoting positive aspects of organisational performance while minimising or failing to disclose negative aspects. This is consistent with Patten (2002), who also found that organisations with poorer environmental performance provided more positive disclosures in their reports.

There are four aspects of organisational legitimacy (Ashforth and Gibbs, 1990; Suchman, 1995). Firstly, gaining legitimacy is an important step for new organisations or organisations who introduces new product lines. Secondly, maintaining legitimacy is an issue organisations are faced with and coupled with the dynamicity of society's values; organisations need to be

responsive to any potential threat to their legitimacy. Thirdly, defending legitimacy occurs when an organisation's legitimacy is threatened. Lastly, should an organisation find itself in a crisis, it must attempt to repair its legitimacy. However, there has been scant research on how organisations gain, maintain and defend the legitimacy of their CEOs pay.

It is usually the executives of large, publicly traded firms who are the subject of public criticism. This discourse on executive remuneration is important as it shapes society's expectations about executive remuneration. Society will be influenced by articles and press releases issued by media, professional associations and academics. Phillips, Lawrence, and Hardy (2004) proposed a model showing the relationships between action and discourse. They argue that action affects discourse through the production of texts such as books and annual reports. In the case of executive remuneration, the legitimacy of CEO pay depends on society's perception based on press releases issued by media, professional associations and academics.

### *2.3. The Media and Executive Remuneration*

Media produces a vast array of discourse that appears in print and on websites, which allows society to gather and evaluate information about events in the world. Core, Guay, and Larcker (2008) argued that the media tailors news to a positive or negative tone depending on public opinion. The media also acts as a "watchdog" for larger firms, where the public is likely to find the story interesting (Core, et al., 2008, p. 3). They also found that the press focuses on excess pay, where it is defined as "the residual from an expected compensation model that controls for standard economic determinants" as opposed to raw pay (Core, et al., 2008, p. 2). Moreover, they also found that despite the negative press coverage, there was no



evidence that it caused the firm to change their remuneration policies, suggesting that the media are not the most powerful stakeholder of publicly listed companies.

However, the media does have the ability to influence the legitimacy of an organisation (Brown and Deegan, 1998). Organisations will either defend or change their practices depending on society's response or their perception of society's possible response. Liu, Taylor, and Harris (2006) found that organisations provided additional disclosures when the company received media attention on executive remuneration. This is consistent with other studies which found a positive correlation between increased public pressure and environmental disclosures (Brown and Deegan, 1998; Patten, 2002). Although there has been extensive research on the impact of media on environmental disclosure, little research has been done on how stakeholders respond to reports in the media of executive remuneration.

The media is a powerful force in shaping society's perceptions of reality, and can set the public agenda by making the public aware of the issues (McCombs, 2004). The concentration of media coverage also influences the importance of topics (McCombs, 2004). The media also responds to the public's demands for information. If a large proportion of the news was dedicated to a topic, it will be acknowledged as being more important and of interest to the public. Hamilton and Zeckhauser (2004) explored the issue of media coverage of CEOs and found that media coverage is determined by market forces such as audience demands. Consequently, major newspapers tend to focus on publications that will "entertain and attract" readers and are more likely to focus on negative news about CEOs (Hamilton and Zeckhauser, 2004, p. 7).

Over the past decade, a new form of media, blogging, has become increasingly important. Merriam-Webster, cited in Kelleher and Miller (2006) announced the word of the year in 2004 to be “blogs.” A blog can be defined as “a web page with minimal to no external editing, providing on-line commentary, periodically updated and presented in reverse chronological order, with hyperlinks to other online sources” (Drezner and Farrell, 2004, p. 5). There are many advantages of blogs which have contributed to their popularity. Blogs are easy to set up on the internet, making it an inexpensive and a convenient way to capture a range of audiences. The flexibility of blogging allows members of the public to express their comments to audiences, while at the same time interacting with others, displaying a variety of opinions. Blogs enables members of society to express their opinions quickly, which increases society’s response to external events (Herring, et al., 2007). In the context of executive remuneration, blogs are an important forum for public debate, but there has been no research on blogs and executive remuneration.

#### *2.4. Gap in the Literature*

The literature review highlights that it is the media’s and public’s opinion can influence companies, and companies use remuneration logics to justify their executive remuneration practices to stakeholders, particularly shareholders. Companies are required to disclose how much and how the CEO is remunerated in their annual reports. Drawing on this information, the public forms an opinion of the company which can add to or subtract from organisational legitimacy. The media can shape the public’s perceptions of executive remuneration. However, what are societal expectations on executive remuneration and how an organisation manages the legitimacy of executive remuneration has been rarely studied. It is expected that companies will face a legitimacy crisis if the media’s and the public’s response to their executive remuneration practices is negative and homogenous. In this case, companies will

alter their executive remuneration practices or risk losing legitimacy. On the other hand, if the media's and public's response is heterogeneous, then companies will be able to defend their executive remuneration practices without a loss of legitimacy.

### **3. Research Method**

This research investigates how Telecom justified Paul Reynolds' 2009 remuneration and how the media and the public reacted to the announcement of Reynolds' remuneration. The remuneration logics (or reasons) embedded within this discourse on executive remuneration are identified and analysed. The findings generate insight into what are societal expectations and how organisational legitimacy can be managed. By studying the public's reaction to Reynolds' remuneration, this research highlights the nature of societal expectations. By studying Telecom's announcement and subsequent defence of Reynolds' remuneration, this research shows how an organisation can manage its legitimacy. Thus, this research extends the literature on executive remuneration and legitimacy theory.

This research draws on an interpretative methodology as it emphasises, "the role of language, interpretation, and understanding in social science," (Chua, 1986, p. 613). While the methods for how the CEO should be remunerated has become taken-for-granted (Crombie, 2009), these interpretations are socially constructed and open to interpretation. It is likely that Telecom (i.e. the board of directors), the media and the public will interpret Reynolds' remuneration and performance differently. Using the case study method and content analysis, this research seeks to understand how Telecom, the media, and the public justify their opinions. Instead of evaluating whether Reynolds' remuneration is justifiable, this research evaluates why Telecom, the media and the public believe Reynolds' remuneration is or is not justifiable.

### *3.1. The Case Study*

The case study is focused on the announcement of Reynolds' remuneration on 21 August 2009 and the subsequent media and public debate, which culminated in Telecom's annual general meeting on 1 October 2009. There was negligible media interest in Reynolds' remuneration following the annual general meeting. Telecom's 2009 annual report and minutes from the annual general meeting were collected. Also, 7 newspaper articles and 5 blogs published in this period were collected. The public was able to comment on many of these documents as they were published online. The public's comments were also collected. There were 359 comments, but 237 comments were discarded because they did not include specific references to Reynolds' remuneration, leaving 122 comments that were analysed.

The main assumption is that the members of the public who commented on the newspaper articles and blogs are representative of the general population. The identity of these people is entirely anonymous. There is no way of knowing whether the sample is or is not representative. However, this risk is mitigated as all newspaper articles and blogs about Reynolds' remuneration were collected, ensuring comments on these documents were from the widest possible readership. Further, two of the bloggers are well-known, John Minto and Bruce Sheppard, and have opposing political views. John Minto is a left-wing union supporter, while Bruce Sheppard is a right-wing shareholder activist. As the readers of these blogs are likely to have diverse political views, the comments should not be skewed by political ideology.

### *3.2. Content Analysis*

Content analysis of the documents collected was used to understand how Telecom, the media, and the public justified their opinions. This is consistent with prior research on disclosure in annual reports (e.g. Smith and Taffler, 2000; Beattie and Thomson, 2007). Bryman and Bell (2007, p. 304) defines content analysis as “an approach to the analysis of documents and texts that seeks to quantify content in terms of predetermined categories and in a systematic and replicable manner.” Drawing on the literature, an inventory of remuneration logics is identified. A close reading on several of Telecom’s annual report, several newspaper articles and blogs, and some of the public’s comments confirms the presence of these and other remuneration logics. Both researchers reviewed a range of texts and discussed their findings, in order to be certain that all the remuneration logics were identified.

Once the sample of texts was collected, all of the relevant sections of the texts (i.e. those on Reynolds’ remuneration) were copied into Microsoft Excel <sup>TM</sup>. The content analysis consisted of two coding phases. First, the tone of the media’s and public’s discourse were categorised as supporting, not supporting or neutral towards Reynolds’ remuneration. The unit of analysis was the whole text, e.g. newspaper article, blog and comment. Second, the presence of the remuneration logics in Telecom’s, the media’s, and the public’s discourse were coded. Again, the unit of analysis was the whole text. 10 remuneration logics were identified, but there were many other remuneration logics that were rarely used. These were included in the other category. For example, a few members of the public suggest that Reynolds’ remuneration was justified because his income is taxed. The remuneration logics, descriptions and examples are shown in table 2.

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The remuneration logics are systems of reasoning used by organisations and individuals to explain or justify their decisions or opinions to themselves and others. The 10 remuneration logics cover many aspects of Reynolds' remuneration. The absolute level, market, human resources, responsibility, and experience logics are concerned with how much Reynolds is remunerated. The agency, contribution, effort, pay-for-performance, and target logics are concerned with how Reynolds is remunerated. Essentially, the remuneration logics are principles which organisations use to structure executive remuneration. The media and the public can use the remuneration logics to evaluate the efficacy of Telecom's executive remuneration structure or practices. However, the remuneration logics do not provide principles for every aspect of Reynolds' remuneration. For example, they are silent on how much remuneration should be paid in cash or equity, and the length of the vesting period for long-term incentive schemes.

The main limitation of content analysis is that it reduces the data to a series of numbers. For example, the remuneration logics are either present or absent in the texts. To overcome this limitation, the content analysis is supported by a qualitative, narrative analysis of the texts. This provides a richer, deeper understanding of the discourse on executive remuneration. This can be in the form of disclosure on how much the CEO is paid and how the organisation justifies these decisions using remuneration logics. The narrative analysis places an emphasis on the meaning of the text, which supports the interpretive methodology that language has an influence in shaping the world (Bryman and Bell, 2007; Potter, 1997). Data in the form of

comments made by the public are examined to explore the relationship between discourse and the social world. This enables comparisons between Telecom's, the media's and public's discourse to be made, and contextualises the findings from the content analysis.

### *3.3. Limitations and Assumptions*

The methods used in this study have certain inherent limitations. Firstly, the case study method used can be criticised as being difficult to replicate. The exact context of the firm, society, and media scrutiny occurred at one point in time. However, this study could be replicated when outlier pay is announced elsewhere in the world. Secondly, there are problems of generalisation where one case might not be representative of all cases. This research is based on a qualitative case study on a single company in New Zealand at a point in time. It does not capture society's dynamicity and factors that constantly cause society to change. For example, a major post-study event relating to Telecom was the failure of its new XT network, and this may have changed the public's perception of Reynolds' remuneration.

Generalisation is also difficult in different countries where values may differ. The Oxford Mini Dictionary (1981, p. 432; 58) defined socialism as "political and economic theory that resources, industries, and transport should be owned and managed by the State," while capitalism is defined as "a system in which trade and industry are controlled by private owners." Consequently a country with values of a capitalist nature will differ from those of a socialist nature. Thirdly, this research involves interpretation of comments and documents which may be criticised as being too subjective. In some aspects, data will be interpreted according to the researcher's point of view. Fourthly, the data collected may be limited in scope as it might not reflect all groups of society and stakeholders equally. Comments on blogs might not be representative of the whole population. However, this is mitigated by

having John Minto's blog representing the left-wing views while Bruce Sheppard's blog leans towards the right-wing views.

#### **4. Background**

Prior to 1987, the New Zealand Post Office was a government department comprising telecommunication, banking and postal services. Following the election of the Fourth Labour Government on 26 July 1984, the public sector was radically changed including the corporatisation and privatisation of many government departments. The New Zealand Post Office was broken up into three state-owned enterprises on 1 April 1987, one of which was Telecom. As a state-owned enterprise, Telecom was legislated to act in a commercial manner. Then the government deregulated the telecommunications industry and prepared Telecom for privatisation. In 1990, Telecom was sold for \$4.25 billion to a consortium led by Ameritech and Bell Atlantic. As part of the conditions of sale, Telecom was listed on the New Zealand, Australian and New York Stock Exchanges in 1991 and the consortium significantly reduced their shareholding over time. Telecom has been New Zealand's largest publicly listed company until recently.

Table 3 shows Telecom's financial performance from 1991 to 2009. During the 1990s, Telecom's financial performance was very stable as its earnings and dividends grew steadily. The financial figures do not reflect the turbulent times as both telecommunication's technology and Telecom's business model radically changed (Erakovic and Wilson, 2006). While Telecom faced competition in the 1990s, it did not intensify until early 2000s when Telstra (an Australian company) and Vodafone (a UK company) had gained a significant market share. This is reflected in Telecom's financial performance which became increasingly volatile in the 2000s. The high profit in 2007 was due to the sale of Telecom's



directory business, Yellow Pages, for \$2.24 billion. Telecom has invested heavily in technology and expanded its revenue base over time while still providing a high dividend yield for shareholders. However, Telecom's billion dollar investment in AAPT (Australian Associated Press Telecommunications) has been unsuccessful with much of its value being written off over time.

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Figure 1 shows the total shareholder return for Telecom and all companies listed on the New Zealand Stock Exchange (NZX) from 1992 to 2010. It is assumed that all dividends are reinvested. As Telecom's market capitalisation was the largest on the NZX, representing about 20-30%, the return indexes of Telecom and the NZX are highly correlated. The effects of the dotcom bubble are highlighted by the rapid fall of Telecom's return index from 2000 to 2001. Telecom's adjusted share price went from \$2.62 in 1992 to \$6.54 in 1997 and then to \$8.97 in 1999 (as at the balance date). It subsequently fell back to \$5.54 in 2001. Similarly, the Global Financial Crisis has affected both the NZX's and Telecom's return indexes from 2008 to 2009. Further, Telecom's share price fell rapidly from \$4.51 in 2007 to \$2.73 in 2009 as the Government signalled in 2006 its intention to unbundle Telecom's cooper network. Overall, Telecom's market performance has been more volatile than its financial performance.

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Figure 2 shows how much Telecom remunerated its CEOs from 1997 to 2009<sup>1</sup>. Telecom has had four CEOs: Dr. Peter Troughton (1987 to 1992); Dr. Roderick Deane (1992 to 1999); Theresa Gattung (1999 to 2007); and Dr. Paul Reynolds (2007 to current). Telecom's CEOs' remuneration packages are comparable to those in Anglo-Saxon countries with a significant performance-based component. Generally, the short-term incentives are dependent on financial performance targets, while the long-term incentives are dependent on market performance targets. The remuneration figures in figure 2 are taken Telecom's annual reports and include actual (e.g. cash) and expected (e.g. share options and restricted shares) remuneration. For example, Telecom used the Black-Scholes methodology to determine the value of the share options awarded. Telecom's CEO will have received a different amount of remuneration than is reported as actual performance invariably differs from expected performance.

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The amount of remuneration that Telecom's board of directors has awarded its CEOs over time has increased every year except in 2000, 2006 and 2008. Gattung's remuneration in 2000 was low because she was CEO for only part of the year as Deane retired part way through the financial year. In 2006, Telecom reported a net loss of \$435 million, resulting in Gattung's short-term incentive to decrease from \$1.32 million in 2005 to \$0.66 million in

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<sup>1</sup> The Companies Act 1993 required companies to disclosure from 1997 onwards the number of employees receiving remuneration greater than \$100,000 (in \$10,000 bands) and directors' remuneration. Hence, there is no information available on how much Telecom remunerated its CEOs prior to 1997. Also, as the mandatory disclosure requirements are limited, the breakdown of the CEOs' remuneration has only been voluntarily disclosed since 2003.

2006 (although her salary increased from \$1.1 million in 2005 to \$1.25 million in 2006). In 2007, Gattung's remuneration included a \$1.8 million severance payment. Putting aside this severance payment, Reynolds' remuneration in 2008 was higher than Gattung's remuneration in 2007. While figure 2 shows that Telecom does use performance-based remuneration as the CEOs' short- and long-term incentives have varied with performance, the sensitivity of total CEO remuneration to performance is questionable. Total CEO remuneration has steadily increased over time despite significant declining and volatile financial and market performance in recent years.

Table 4 shows Telecom's CEO remuneration in 2009 relative to other New Zealand listed companies. Telecom's market capitalisation is the second highest, CEO pay is the highest in absolute terms, and CEO pay is the fifth highest in relative terms. Telecom is the only telecommunications company listed on the New Zealand Exchange, so direct comparisons are not possible. However, telecommunications and energy companies are similar in that they both operate in competitive markets and manage a network of lines. On that basis, Telecom is overpaying its CEO relative to energy companies. CEO remuneration at Telecom is certainly at the top-end of the market, but whether its CEO's remuneration is unjustified is a matter of opinion. The legitimacy of CEO remuneration at Telecom is investigated in the findings section.

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Table 5 shows the number of articles in the New Zealand Herald on executive remuneration from 1994 to 2009. The number of articles has increased since 1997 when the reporting of remuneration became mandatory. The percentage of these articles that include comment on Telecom is also shown. Coverage of Telecom constituted 14% of the total coverage on executive remuneration. This highlights that executive remuneration has been a consistent topic of media and public interest over time. In 2009, 25% of articles on executive remuneration related to Telecom. As Reynolds' 2009 remuneration was by far the highest that a CEO of a New Zealand listed company has ever received, the media and public scrutiny was significantly higher than in any other year.

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Table 6 shows the timeline of events from the appointment of Dr Paul Reynolds as CEO to Telecom's 2009 Annual General Meeting. Telecom has declining earnings leading up to the announcement of Reynolds' 2009 remuneration. Also, Telecom had frozen executives' salaries, but short- and long-term incentives were still paid. The announcement of Reynolds' remuneration led to much debate in the media and public. In particular, two well-known blog writers posted opposing views on Reynolds' remuneration. John Minto, a left-wing union supporter, wrote two blogs attacking Reynolds' remuneration. Bruce Sheppard, a right-wing shareholder activist, wrote one blog supporting Reynolds' remuneration (although his support is qualified). These and other blogs and newspaper articles attracted many comments from members of the public. This media and public scrutiny culminated in Wayne Boyd's speech

at Telecom's annual general meeting, defending Reynolds' remuneration. The next section presents an analysis of these events.

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## **5. Findings**

This research identifies the remuneration logics that Telecom, the media, and members of the public use to explain or justify their position on Dr. Paul Reynolds' 2009 remuneration. Also, this research analyses the discourse of Telecom, the media and the public to gain insight into what is legitimate or socially acceptable, and how Telecom manages societal expectations. The main findings are a content analysis of Telecom's annual report and annual general meeting minutes, newspaper articles and blogs as well as members of the public's comments on these articles and blogs. The narratives underlying the content analysis for each group are discussed and then compared. In light of these findings, Reynolds' 2010 remuneration is also discussed, particularly changes in the way his remuneration was disclosed in the annual report.

Upon announcing Reynolds' 2009 remuneration, the New Zealand Herald article stated that Reynolds earned \$5 million while the Dominion Post article stated that Reynolds earned \$7 million. The figures are different because the New Zealand Herald article did not include Reynolds' 678,910 performance rights (valued at \$2.1 million), which may be unrealised if absolute and relative total shareholder return hurdles are not met in three years. In fact, Reynolds' cash remuneration is \$3,831,450 (salary of \$1,700,000, performance incentive paid in cash of \$1,837,500, and special payments of \$243,950) and unrealised remuneration is

\$3,325,000 (performance incentive paid in restricted shares of \$1,225,000 and performance rights of \$2,100,000). To evaluate the efficacy of Reynolds' 2009 remuneration, the complexities of equity-based remuneration (e.g. vesting periods and hurdles) need to be considered. While Reynolds' remuneration is accurately described in newspapers articles, the difference between realised (or cash) and unrealised (or conditional) remuneration is not clearly explained.

The remuneration logics capture some of the complexities of Telecom's CEO remuneration package, but none of the remuneration logics focus on the distinction between realised and unrealised remuneration. The number of times the remuneration logics are present within the discourse of Telecom (annual report and annual general meeting), the media (7 newspaper articles and 5 blogs) and the public (122 comments) is presented in table 7. Telecom used a variety of remuneration logics to justify Reynolds pay in the annual report, and these and other remuneration logics were used by the Chairman at the annual general meeting. Newspaper articles did not use any remuneration logics, except for 'absolute level'. While they focused on reporting 'the facts' of Reynolds' remuneration, they also sensationalised the amount of remuneration he received. Blogs did use a variety of remuneration logics to evaluate the efficacy of Reynolds' remuneration. Many of the public's comments included multiple remuneration logics. Those using the 'absolute level' logic generally opposed the amount of remuneration Reynolds received.

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The most frequently present remuneration logics in the discourse are: Absolute level, pay-for-performance, effort, market, and responsibility. This suggests that societal expectations are: irrespective of position, there is an absolute level of remuneration that anyone should be able to earn; and a CEO's remuneration should reflect their responsibility and effort, changes in firm performance, and the market level of remuneration. However, these societal expectations are not clearly defined constructs. As the remuneration logics are principles rather than rules, it is difficult and highly subjective to judge Reynolds' remuneration using remuneration logics. The media's and public's opinion of Reynolds' remuneration is divided based on political ideology. Those against Reynolds' remuneration believe that it is inequitable because the gap between Reynolds' remuneration and the average worker is too wide. Those for Reynolds' remuneration believe that it is justified because it is determined by market forces.

### *5.1. Telecom's Discourse*

Telecom's discourse is akin to rhetoric as it is designed to persuade the reader that Reynolds' remuneration is justified. The annual report uses the remuneration logics and references to external advisors to justify Reynolds' remuneration. The discourse is heavily entrenched in the pay-for-performance logic: "performance-based so that the package is directly linked to performance outcomes" (Telecom, 2009, p. 124). The section of the annual report on CEO remuneration covers: the employment agreement, termination benefits, general remuneration, performance incentive scheme, performance rights scheme, and performance entitlements scheme. There is no discussion of how the CEO's fixed remuneration is determined, but there is detailed discussion of how the CEO's pay is linked to performance. However, the specific targets on which the CEO's remuneration depends are not disclosed. The section of CEO

remuneration concludes with a table detailing the components of Reynolds' remuneration, but no total figure is given.

Telecom's Chairman Wayne Boyd discussed executive remuneration at the annual general meeting in both his initial address and then during formal business. Boyd's speech included many remuneration logics used to persuade the audience of the efficacy of Reynolds' remuneration. Other justifications were also given. For example, Boyd said that, "*...it is appropriate that the executive team is rewarded for leading what is already New Zealand's most complex business through a complete rebuild.*" Boyd also highlighted that Telecom discloses more information about executive remuneration than is required under New Zealand law and Stock Exchange listing rules, and that Reynolds' employment contract was fully disclosed to the public upon his appointment. Implicitly, Boyd is suggesting that the shareholders and the public should not be surprised by Reynolds' remuneration.

During formal business, Boyd provided much detail of Telecom's executive remuneration practices. This was probably due to the amount of questions submitted by shareholders prior to the annual general meeting. Again, Boyd justified Reynolds' remuneration using a variety of remuneration logics. For example, he appealed to the market logic in saying, "*And we compete for executive talent in a highly competitive global market.*" The remuneration logics used were consistent with those used in the annual report. A PowerPoint slide was shown to illustrate the components of Reynolds' remuneration. It was also highlighted that more than two thirds was at risk and that both short and long-term incentives are performance tested. Boyd emphasised that, "*Under Paul Reynolds' leadership, our executive team has delivered on the demanding objectives set by the Board over the past year.*"



The components of Reynolds' remuneration were separately described and justified. Boyd explained that Reynolds will only receive his performance rights only if the targets are met in three years when the rights and entitlements vest, highlighting the unrealised component of the remuneration. A variety of performance objectives on which Reynolds' short-term incentives are dependent were disclosed including group financial performance, customer satisfaction, and leadership. Each performance objective was explained in detail including how Reynolds had met the 2009 targets. Boyd concluded with a reassurance that the Board is monitoring national and international surveys in relation to executive remuneration. Surprisingly, there were no questions from the audience on Reynolds' remuneration, but there was one question on the Chief Financial Officer's remuneration.

### *5.2. The Media's Discourse*

Table 7 shows that the media uses a variety of remuneration logics to justify their position, and these are the same remuneration logics as Telecom uses. Although the newspaper articles focus on describing Reynolds' remuneration and sensationalising the amount he was paid. The blogs evaluate Reynolds' remuneration in greater depth than the newspaper articles, and use many of the remuneration logics to evaluate it. Of the 7 newspaper articles, 2 were neutral and 5 were unsupportive of Reynolds' remuneration. Of the 5 blogs, 2 were supportive and 3 were unsupportive of Reynolds' remuneration. Two main reasons were given why Reynolds' remuneration was unjustified: Telecom's profits had decreased and Reynolds' pay relative to the average worker is too high. One main reason was given for why Reynolds' remuneration was justified: Reynolds has a difficult job to improve Telecom's performance as it faces a challenging competitive and regulatory environment.

There were three blogs attacking Reynolds' remuneration. John Minto a well-known political activist and left-wing union supporter wrote two blogs on Reynolds' remuneration. The first blog focused on Telecom's history and the plight of the line engineers. He agreed with Union leader, Andrew Little's assertion that Reynolds' pay is "shameless greed". The second blog focused on the ratio of CEO to worker pay. He argued that the ratio should be set at 10 times the minimum yearly wage and regulated by the Government, so that CEOs are incentivised to increase both the their and the average workers' remuneration. Tapu Misa's blog also focuses on the ratio between CEO and average worker pay. She argued that societal problems are positively correlated with this ratio, and concludes that, "*we all pay the price when we become more unequal and unfair as a society*".

There were two blogs supporting Reynolds' remuneration. Kerre Woodham argued that Reynolds' remuneration is deserved because it is comparable to other telecommunication companies around the world and his job is particularly difficult. Also, Woodham argued that people should not be paid equally because history has shown that Communist societies fail. Bruce Sheppard provides the balanced discussion of Reynolds' remuneration. He argues that Reynolds is improving Telecom's culture and putting customers first. Given that Telecom uses performance-based remuneration, Reynolds met the board's performance targets, and Reynolds is an internationally mobile executive, Sheppard believes that on balance Reynolds' remuneration is justified. As the Chairman of the Shareholders' Association, Sheppard argues that excessive remuneration is justifiable as long as the CEO is delivering shareholder value. Overall, Sheppard believes that Reynolds is revitalising Telecom's future prospects.

*5.3. The Public's Discourse*

Table 8 shows the number and percentage of comments that were supportive, neutral, or unsupportive of Reynolds' remuneration. The researchers expected that the vast majority of the public's comments would be unsupportive of Reynolds' remuneration. Surprisingly, the public's opinion of Reynolds' remuneration was heterogeneous. Only 38% of the public's comments were unsupportive, while 35% were neutral and 27% were supportive. The opinions of members of the public were not swayed by tone of the newspaper article or blog on which they were commenting. For example, comments from members of the public on John Minto's blog ranged from "totally agree" to "Communist drivel".

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Insert table 8 here

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While there were 359 comments posted, only 122 comments specifically discussed Reynolds' remuneration. These comments ranged from a short sentence to several paragraphs. Members of the public used a variety of remuneration logics to justify their opinion including some that used multiple remuneration logics. Table 9 shows the presence of the remuneration logics in the public's disclosure. Their comments have been categorised by their tone. The absolute level logic was the most frequently used followed by effort, market, and pay-for-performance. Interestingly, the remuneration logics were used to both justify and criticise Reynolds' remuneration. This highlights that the remuneration logics are part of New Zealand society's shared understanding of how remuneration is determined.

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Comments supporting Reynolds' remuneration mainly included the effort, absolute level, market, and responsibility logics. For example, one person argued that, "*people like Reynolds... earn their keep... CEO roles are hard work... [and] Telecom met their planned targets.*" Several people commented that the media and other comments were envious of Reynolds' remuneration. For example, one person suggested that, "*...if more people spent their time working towards achieving what these people have, and less time complaining about them, New Zealand would be much better off.*" Other people gave examples of how Reynolds has improved Telecom's performance. For example, one apparent Telecom employee stated that, "*This has been reflected with the steepest rise in staff engagement in our business ever recorded... he's [Reynolds has] earned his bonus this year.*"

Comments neutral towards Reynolds' remuneration mainly included the absolute level, effort, and market logics. The neutral comments tended to evaluate the media's or another member of the public's arguments, but without offering an explicit opinion on Reynolds' remuneration. For example, one person commented, "*As for Mr Reynolds, the board pays him what they think he is worth.*" The remuneration logics were used to support or refute the arguments of others, but without offering their own opinion. For example, one person argued that, "*I suspect Reynolds can demand "international pay" because he is internationally mobile. Therefore, a mobile commodity can demand international prices.*" Other neutral comments were positive or negative towards other aspects of Telecom's business and related Government decisions. For example, one person believed that, "*The mistake was to have*

*privatised it [Telecom]. The ongoing mistake is in not replacing it [Telecom's network] – physically – with state owned fibre.”*

Comments opposing Reynolds' remuneration mainly included the absolute level and pay-for-performance logics. Paradoxically, Telecom's board of directors argues that Reynolds' remuneration is justified because it is linked to performance, whereas many members of the public argued that Reynolds' remuneration was not related to performance. For example, one person commented that, *“I thought executives were bonused [sic] on performance... with profits down 43.9% he should be taking a 43.9% salary cut.”* Other arguments focused on the ratio of CEO and average worker pay as well as political philosophy. For example, one person contended that, *“The argument that CEO's are so much better than the rest of us they deserve incomes like 5 million per year is laughable. Its obvious that the big business propaganda machine has done its job and the vast majority of the moronic commentators on this page are sufficiently indoctrinated in right wing economic theory.”*

The public's comments traversed a wide range of issues, some of which were related to Reynolds' remuneration. The public's comments often included tangential issues such as the history of Telecom and the technicians' dispute over their contract. However, the depth of the public's comments was limited. For example, one shareholder believed that, *“If we paid peanuts, we'd get another monkey, we don't want to go back to those days.”* While many comments discussed the relative level of Reynolds' remuneration, few comments made specific references to other CEOs' remuneration. Similarly, people did not evaluate the components of Reynolds' remuneration in any depth. For example, one person commented that, *“I wonder how much he would have got if he actually increased profits!”* The critical distinction between cash and unrealised remuneration was rarely made by members of the

public. The arguments of members of the public are mainly ideological or principle-based, rather than critiquing the process by which Reynolds' remuneration is determined and the different remuneration schemes.

#### *5.4. Comparative Analysis*

In this section, Telecom's, the media's, and the public's discourse on Reynolds' remuneration are compared and contrasted.

##### *5.4.1. Telecom's and the Public's Discourse*

There are significant differences between the remuneration logics that Telecom and the public used. While both Telecom and the public used a variety of remuneration logics, the public's arguments were simplistic compared to Telecom's. The public's comments were mainly concerned with the absolute level of Reynolds' remuneration, not recognising that half of the \$7 million is unrealised for at least three years and largely dependent on total shareholder return targets. For example, one person argued that, "*These executive salaries are obscene and a disgrace and the recession has revealed the inherent rot in the capitalist model*". Further, Telecom's discourse was highly formalised and organised, whereas the public's discourse was often unorganised and contained grammatical and spelling errors. Telecom's discourse appears to be more persuasive as a result.

##### *5.4.2. Telecom's and the Media's Discourse*

Telecom's discourse de-emphasised the amount of Reynolds' remuneration. They did not include a total remuneration figure in the annual report. Contrastingly, the media highlighted the amount of Reynolds' remuneration. Also, the media emphasised the opinions of those who opposed Reynolds' remuneration. For example, one headline read, "*Union slams*

*Reynolds' pay*". While both Telecom and the media used the pay-for-performance logic, they used this logic in different ways. The media reasoned that Reynolds' pay was unjustified because Telecom's profits have fallen, despite Telecom's profits being greater than market analysts' expectations. Generally, the media's discourse was unsophisticated. They tended to describe Reynolds' remuneration, although in limited detail, and then compare it to the average worker, the Prime Minister's remuneration, or Telecom's profits. Again, the difference between cash and unrealised remuneration was not widely discussed. Further, the different incentives schemes were not critiqued. However, the blogs did examine Reynolds' remuneration in greater depth, particularly Bruce Sheppard's blog.

#### 5.4.3. The Media's and the Public's Discourse

The media's and the public's discourse was quite similar. Both the media and the public focused on the absolute level of Reynolds' remuneration and had unsophisticated evaluations of the remuneration schemes. Further, the agency logic was absent in both the media's and public's comments, indicating that they did not consider the shareholder's perspective. While Telecom's profits and share price have certainly declined rapidly in recent years, Telecom's performance relative to other telecommunications companies and NZX listed companies was rarely mentioned. The media and the public tended to believe that a fall in the absolute level in profits should translate to a fall in the total CEO remuneration. However, the public's discourse used the remuneration logics to a greater extent than the media's. Also, the public's comments were more opinion-based, whereas the media's comments were more fact-based.

#### 5.5. *Postscript*

While this research is concerned with Reynolds' 2009 remuneration and events leading up to Telecom's annual general meeting in October 2009, there are three significant events that

occurred after October 2009. First, Telecom's new mobile network failed repeatedly in February 2010 and this prompted the resurgence of media and public debate on Reynolds' remuneration. For example, the Sunday Star Times headline on 28 February was, "*Call to stop CEO's \$3m bonus*". The Sunday Star Times reported that Bruce Sheppard, who previously supported Reynolds' 2009 remuneration, believed that Reynolds' 2010 remuneration should be cut as he should share the blame for the failure of the XT network. Some senior and middle managers resigned as a result of the XT network failures. After the XT network's reliability improved, the media's and public's interest in Telecom and Reynolds' remuneration diminished once again.

Second, Reynolds' 2010 remuneration was significantly lower than his 2009 remuneration. Consequently, the media's and public's interest in Reynolds' 2010 remuneration was negligible. In fact, there was only one newspaper article mentioning it. Reynolds' 2010 remuneration was \$5,072,614 (2009: \$7,156,450) consisting of a salary of \$1,750,000 (2009: \$1,750,000), a performance incentive of \$900,000 (2009: \$3,062,500), performance rights and entitlements of \$2,084,503 (2009: \$2,100,000), and special payments of \$338,111 (2009: 243,950). Cash remuneration was \$2,628,111 (2009: \$3,831,450) and unrealised remuneration was \$2,444,503 (2009: \$3,325,000). Reynolds' performance incentive declined 71%, despite Telecom's financial performance holding at 2009 levels. Recall that Reynolds' performance incentive increased in 2009 following a significant decrease in Telecom's financial performance. From an external perspective, the change in Reynolds' remuneration is difficult to decipher.

Third, Telecom altered how Reynolds' remuneration was disclosed in the 2010 annual report. Figure 3 shows how Reynolds' 2009 remuneration was disclosed. While Reynolds' total



remuneration is not shown, it can easily be derived by adding the figures. It also shows Reynolds' 2008 and 2009 performance incentives, highlighting a significant increase. Figure 4 shows how Reynolds' 2010 remuneration was disclosed. Both Reynolds' total remuneration and the value of the long-term incentives are not shown in 2010. Only the number of performance rights and entitlements are given. To calculate the value of these long-term incentives, "Note 22 Employee share schemes" on pages 102-104 must be read in conjunction with the disclosure on page 136. Curiously, the value of the performance rights, \$583,333, that have lapsed in 2010 is disclosed in footnote 3. Also, there is no comparison of performance incentive between 2009 and 2010. Further, the different components of Reynolds' remuneration are labelled "fixed" or "at risk". These cosmetic changes can only have been made to obfuscate Reynolds' total remuneration and give the reader a more favourable impression of Reynolds' remuneration.

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## **6. Discussion**

Organisations undertake certain actions to legitimise their operations within society. As one of the largest companies in New Zealand, Telecom is constantly in the spotlight of the public in regards to its company performance, operations and policies. Maintaining legitimacy is

important for Telecom. However, it is difficult to know how much of Telecom's organisational legitimacy depends on the legitimacy of Reynolds' remuneration. Telecom does provide significantly more disclosure on executive remuneration than is mandatory. Also, Wayne Boyd provided significantly more explanation of executive remuneration during Telecom's 2009 annual general meeting than occurred at previous annual general meetings. It appears that Telecom does attempt to manage the legitimacy of its executive remuneration practices.

This is similar to the environmental disclosures by companies where researches has found that companies use disclosure as a legitimising tool (Patten, 2002; Cho and Patten, 2007). Companies may also use disclosures to enhance their reputation. Communication with stakeholders in society is important to build and maintain organisational legitimacy. Being one of the largest companies in New Zealand, Telecom needs the support of the public and disclosing more information than is required by law may put Telecom in a favourable position as it is more transparent with its practices. Drawing from Deegan and Gordon's (1996) findings, it can be said that Telecom has increased its executive remuneration disclosures due to society's interest, thereby aiming to legitimise its practices.

Consistent with legitimacy theory, previous research have found that companies use remuneration logics to justify executive remuneration practices (Wade, et al., 1997; Crombie, 2009). This is evident in Telecom's annual report and chairman's speech at the annual general meeting, where a variety of logics were used to justify their executive remuneration practices. Telecom emphasised that a significant portion of Reynolds' remuneration was linked to firm performance including financial and total shareholder return targets. To strengthen Telecom's rhetorical argument, Reynolds' fixed remuneration was barely mentioned as this does not

vary with performance. Other remuneration logics used also relate to Reynolds' achievements. However, the underlying assumption that incentives are required to motivate Reynolds is not discussed.

Failure of an organisation to meet societal expectations can lead to a loss of organisational legitimacy. For example, customers could switch to a competitor and shareholders could sell their shares. From the organisation's point of view, managing legitimacy is about managing society's perceptions. This is seen as a defence mechanism as to prevent or limit challenges from shareholders or the public. The findings show that Telecom has maintained its legitimacy as it was responsive to the media's and public's criticism of Reynolds' remuneration. Telecom provided additional disclosures in the annual general meeting upon request by Bruce Sheppard which outlined Reynolds' key performance indicators. Telecom also defended its legitimacy by publicly defending Reynolds' remuneration and arguing that he has met the required performance targets.

Consistent with Core et al.'s (2008, p.3) findings, the media acts as a "watchdog" for large organisations such as Telecom where its history and news attracts the public's interest. The media also focuses on excess pay by sensationalising Reynolds' pay in their headlines. However, the media does not appear to be as powerful as McCombs (2004) alleged. The media is only one stakeholder in society and they are not the most powerful. Organisations also tend to form their response based on society's reaction to an event. In this case, the public's response was diverse. The public's comments showed that the public was not afraid to disagree or agree with the opinions expressed in newspaper articles and blogs.

## **7. Conclusion**

Telecom's, the media's, and the public's discourse on executive remuneration share a common set of remuneration logics. These remuneration logics represent principles which underpin how much and how Reynolds is remunerated. The principles are open to interpretation. For example, Telecom used the pay-for-performance logic to defend Reynolds' remuneration, whereas the media and the public used the pay-for-performance logic to attack Reynolds' remuneration. The media's and public's opinions of Reynolds' remuneration were heterogeneous. Political ideology was an important determinant of the media's and public's opinion; people with right-wing views were supportive, while people with left-wing views were critical of Reynolds' remuneration. Overall, Telecom was able to defend Reynolds' remuneration with relative ease; Boyd used a variety of remuneration logics to justify Reynolds' remuneration in more depth than normal at the 2009 annual general meeting.

The findings have significant implications for legitimacy theory. Telecom's organisational legitimacy is comprised of multiple dimensions, where the legitimacy of Reynolds' remuneration is only one dimension. By using a taken-for-granted set of remuneration logics (Crombie, 2009), Telecom was able to maintain its organisational legitimacy. While the media sensationalised Reynolds' remuneration and highlighted the decline in Telecom's profits, they were not able to persuade the public that Reynolds' remuneration and, by extension, Telecom was illegitimate. In fact, the public's reaction to Reynolds' remuneration was heterogeneous, not homogenous. To maintain legitimacy, Telecom only needed to appear legitimate in the eyes of powerful stakeholders. However, there were long-term implications for Telecom as Reynolds' remuneration in 2010 was much lower than in 2009 and the disclosure of Reynolds' remuneration in 2010 was altered to disguise the total amount

of remuneration paid. This indicates that Telecom wanted to avoid a repeat of the media's and public's scrutiny of Reynolds' remuneration.

The findings have significant practical implications. The content analysis showed that the media and the public use a variety of remuneration logics to evaluate the efficacy of Reynolds' remuneration, but the evaluation is relatively unsophisticated. The media focused on how Telecom's profit had declined and the ratio of CEO to average worker pay. The public focused on whether Reynolds' remuneration was justified in light of market conditions and his achievements. However, the media's and public's evaluation rarely examined the components of Reynolds' remuneration, how Reynolds' remuneration is determined, and split between cash and unrealised remuneration. Also, the media and public gave few examples of other CEO's remuneration to illustrate whether Reynolds' remuneration was unjustified or justified. To effectively critique Reynolds' remuneration, a more sophisticated approach is needed.

This research is exploratory as there are few studies that have examined the legitimacy of CEO pay. As news articles and blogs are typically saved on electronic databases, there is much potential to study similar situations to Telecom and Reynolds' 2009 remuneration. For example, CEOs of major banks in the UK were not able to legitimately retain their bonuses in 2009 (Financial Times, 22 February 2010). Studying the discourse of these banks, the Government, media and the public could yield new insights into how organisations (fail to) manage their legitimacy. Perhaps, the UK banks believed that the bonuses had to be forgone to maintain organisational legitimacy. Alternatively, the banks' rhetoric may not have been persuasive. They may not have employed remuneration logics to the same degree as Telecom, which could explain why the bonuses were not socially acceptable. Such studies could also

be replicated in the US, where banks and other firms were bailed out by the Government following the Global Financial Crisis, which led to much media and public scrutiny of executive remuneration. By studying multiple instances of media and public scrutiny of executive remuneration, an in-depth understanding of the legitimacy of executive remuneration can be developed.

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<b>Remuneration Logics</b>	<b>Explanations of CEO Pay</b>	<b>Empirical Evidence</b>
Agency	Incentive schemes can be designed to align the interests of executives with those of shareholders.	The agency logic has been institutionalised in the U.S. and is often presented as a solution to poor performance (Zajac and Westphal, 1995) as well as when large bonuses are awarded (Wade et al. (1997).
Experience	The CEO's pay should reflect his/her experience or skills.	St-Onge et al. (2001) found that executives believe more share options are awarded to more experienced individuals.
Human Resources	As talented executives are a scarce resource, compensation is needed to attract and retain them.	Executives use the human resources logics to rationalise the adoption share option plans (St-Onge et al., 2001). Point and Tyson (2006) found that the human resources logic has become taken-for-granted in the U.K.
Market	The CEO's pay will depend on the market forces of supply and demand.	Executives believe that for an executive compensation scheme to be competitive, it must include a share option plan (St-Onge et al., 2001).
Motivation	Incentive compensation schemes will enhance the CEO's effort.	St-Onge et al. (2001) found that executives perceived share option plans as an important motivational tool.
Pay-for-Performance	The CEO's pay should be linked to the firm performance.	Wade et al. (1997) and Point and Tyson (2006) found that firms use the pay-for-performance logic to justify the CEO's pay.
Responsibility	Executive remuneration should be linked to the level of a CEO's responsibility.	Executives believe that share options plans are most effective in situations where executives have high managerial discretion (St-Onge et al., 2001).

**Table 1: Remuneration Logics in the Literature**

<b>Remuneration Logics</b>	<b>Description</b>	<b>Example</b>
Human Resources	CEO is viewed as a scarce resource and remuneration is needed to attract and retain the best talent.	“attract and retain top executives” “attract the right talent”
Responsibility	The level of remuneration is determined on the complexity and position of the job in the company.	“scope and complexity of the role” “these people make the big decisions in the company”
Market	The CEO’s pay depends on the forces of supply and demand, so the CEO’s remuneration should be comparable to their peers.	“competitive global market” “Reynolds salary is a market price”
Effort	The company’s remuneration schemes are designed to reward the CEO for personal achievement.	“should be rewarded for it” “deserved the \$5million payout” “The guy has worked hard...”
Target	The company’s remuneration schemes are designed to reward the achievement of company’s objectives or targets.	“he was set a target and met it” “achieving pre-specified target levels of performance”
Agency	Remuneration schemes can be used to align the interests of the CEO with those of the shareholders.	“to closely align with the interests of shareholders”
Pay-for-Performance	The CEO’s pay should be linked to the firm’s performance.	“average performance receiving a ridiculous payment” “performance based”
Experience	The CEO’s remuneration is determined by their level of experience and value.	“international experience and value” “Paul has a wealth of experience”
Absolute Level	The CEO’s absolute level of pay is too high.	“\$5million is an obscene amount of money” \$5million income is close to 200 times the minimum wage”
Contribution	The CEO’s remuneration is determined by their contribution to the company’s performance.	“what has he put into it” “no one’s contribution actually earns millions”
Other	Other explanations that are not often mentioned such as fairness and the payment of tax	“fair and proper salary” “both Reynolds and Telecom pay a tremendous amount of tax...”

**Table 2: The Remuneration Logics**

Year	Revenue	Net Profit After Tax	Total Assets	EPS	DPS	ROA	ROE
1991	\$ 2,477,300	\$ 336,700	\$ 4,717,600	\$ 0.20	\$ 0.10		
1992	\$ 2,617,100	\$ 403,600	\$ 4,848,400	\$ 0.23	\$ 0.15	8%	15%
1993	\$ 2,511,400	\$ 107,000	\$ 4,755,500	\$ 0.30	\$ 0.18	2%	4%
1994	\$ 2,539,000	\$ 527,000	\$ 4,563,200	\$ 0.26	\$ 0.24	11%	24%
1995	\$ 2,868,800	\$ 619,600	\$ 4,562,700	\$ 0.32	\$ 0.30	14%	30%
1996	\$ 2,957,600	\$ 716,200	\$ 4,586,600	\$ 0.37	\$ 0.34	16%	34%
1997	\$ 3,133,500	\$ 580,900	\$ 4,618,300	\$ 0.37	\$ 0.38	13%	31%
1998	\$ 3,398,000	\$ 820,200	\$ 5,164,000	\$ 0.47	\$ 0.42	17%	61%
1999	\$ 3,496,000	\$ 888,000	\$ 5,242,000	\$ 0.50	\$ 0.45	17%	83%
2000	\$ 4,384,000	\$ 789,000	\$ 7,981,000	\$ 0.45	\$ 0.46	12%	71%
2001	\$ 5,705,000	\$ 661,000	\$ 8,972,000	\$ 0.52	\$ 0.20	8%	42%
2002	\$ 5,580,000	-\$ 187,000	\$ 8,246,000	\$ 0.41	\$ 0.20	-2%	-11%
2003	\$ 5,206,000	\$ 709,000	\$ 7,755,000	\$ 0.40	\$ 0.20	9%	46%
2004	\$ 5,385,000	\$ 754,000	\$ 7,500,000	\$ 0.47	\$ 0.27	10%	38%
2005	\$ 5,759,000	\$ 916,000	\$ 7,421,000	\$ 0.42	\$ 0.38	12%	40%
2006	\$ 5,852,000	-\$ 435,000	\$ 6,203,000	-\$ 0.16	\$ 0.35	-6%	-25%
2007	\$ 5,642,000	\$ 3,024,000	\$ 8,276,000	\$ 0.49	\$ 0.35	42%	131%
2008	\$ 5,793,000	\$ 710,000	\$ 7,405,000	\$ 0.48	\$ 0.29	9%	22%
2009	\$ 5,649,000	\$ 398,000	\$ 7,036,000	\$ 0.34	\$ 0.24	6%	15%
<i>Average</i>	<i>\$ 4,260,721</i>	<i>\$ 649,379</i>	<i>\$ 6,308,068</i>	<i>\$ 0.36</i>	<i>\$ 0.29</i>	<i>11%</i>	<i>36%</i>

**Table 3: Telecom's Financial Performance from 1991 to 2009**

Company name	Market Capitalisation		CEO Pay		CEO Pay to Market Capitalisation	
	(000)	Rank	(000)	Rank	(%)	Rank
Fletcher Building Limited	\$3,977,386	1	\$1,245	8	0.0313	20
Telecom Corporation of New Zealand Limited	\$3,630,113	2	\$7,156	1	0.1971	5
Contact Energy Limited	\$3,373,309	3	\$1,624	5	0.0481	17
Trustpower Limited	\$2,286,043	4	\$1,010	15	0.0442	19
Vector Limited	\$2,151,628	5	\$1,220	9	0.0567	16
Auckland International Airport Limited	\$1,972,642	6	\$1,298	6	0.0658	14
Fisher & Paykel Healthcare Corporation Limited	\$1,680,360	7	\$1,066	14	0.0634	15
Sky Network Television Limited	\$1,620,485	8	\$1,288	7	0.0795	13
Sky City Entertainment Group Limited	\$1,306,882	9	\$2,564	3	0.1962	6
The Warehouse Group Limited	\$1,241,672	10	\$3,800	2	0.3060	1
Air New Zealand Limited	\$1,148,604	11	\$2,441	4	0.2125	4
New Zealand Refining Co Ltd	\$1,050,000	12	\$1,200	11	0.1143	9
Ryman Healthcare Limited	\$1,035,000	13	\$470	20	0.0454	18
Port of Tauranga Limited	\$891,214	14	\$710	17	0.0797	12
Infratil Limited	\$762,688	15	\$1,010	16	0.1324	8
Mainfreight Limited	\$651,905	16	\$1,140	12	0.1749	7
New Zealand Oil & Gas Limited	\$608,191	17	\$545	18	0.0896	11
Sanford Limited	\$478,319	18	\$545	19	0.1139	10
Fisher & Paykel Appliance Holdings Limited	\$449,026	19	\$1,130	13	0.2517	3
Tower Limited	\$425,655	20	\$1,217	10	0.2859	2
<i>Average</i>	<i>\$1,537,056</i>		<i>\$1,634</i>		<i>0.1294</i>	

**Table 4: CEO Pay of Largest 20 Publicly-Listed Companies in New Zealand in 2009**

<b>Year</b>	<b>Total</b>	<b>Telecom</b>	<b>% of total articles on Telecom</b>
1994	5	0	0
1995	4	0	0
1996	14	2	14
1997	21	3	14
1998	16	2	13
1999	18	3	17
2000	14	2	14
2001	5	0	0
2002	12	4	33
2003	14	2	14
2004	12	1	8
2005	22	0	0
2006	10	1	10
2007	23	5	22
2008	21	1	5
2009	40	10	25
<b>Total</b>	<b>251</b>	<b>36</b>	<b>14</b>

**Table 5: New Zealand Herald's Coverage of Executive Remuneration**

<b>Date</b>	<b>Event</b>	<b>Synopsis</b>
28/06/07	Announcement of new CEO, Dr. Paul Reynolds	Telecom announced that Dr. Paul Reynolds has been appointed as its new Chief Executive Officer, taking over from Theresa Gattung on 27 September 2007. He was also appointed as Managing Director on 4 October 2007.
07/11/08	Quarter 1 Results	Net Earnings for the period was \$149,000,000 (Down 33.8% from September 2008 quarter).
13/02/09	Media release – Salary freeze for Telecom executives	Telecom’s CEO Paul Reynolds announced that Telecom’s executive team, and most senior managers, will not receive salary increases this year, as the company sharpens its focus on managing costs in the current economic environment. However, short- and long-term incentives were still paid, although this fact did not receive any media attention.
	Quarter 2 results	Net Earnings for the period was \$163,000,000 (Down 58.9% from period ending December 2008).
08/05/09	Quarter 3 results	Net Earnings for the period was \$322,000,000 (Down 23% from the period ending March 2009).
21/08/09	Telecom Annual Report released	CEO remuneration and financial performance are disclosed in the annual report
	Quarter 4 results	Net Earnings for the period was \$400,000,000 (Down 43.9% for the year ended June 2009).
25/08/09	Blog: Paul Reynolds Pay	Written by “Cactus Kate”
26/08/09	Blogs: A Boil on the country’s backside; Telecom Board defends pay	Written by John Minto; newspaper article
01/09/09	Blog: Put a cap on eye-popping incomes; Notice of Annual Meeting of Shareholders	Written by John Minto
08/09/09	Corporate Review – Creating a profile of the 2009 financial year for Telecom	Telecom company document
29/09/09	Blog: Is Paul Reynolds worth his pay cheque?	Written by Bruce Sheppard
1/10/09	Telecom AGM	Annual General Meeting and discussions

**Table 6: Timeline of Events related to Reynolds’ 2009 Remuneration**



Remuneration Logics	Telecom		Media		Public	
	Presence	Rank	Presence	Rank	Presence	Rank
Absolute Level	0 / 2	11	10 / 12	1	63 / 122	1
Pay-for-Performance	2 / 2	1=	6 / 12	2	18 / 122	4
Effort	2 / 2	1=	4 / 12	3=	30 / 122	2
Contribution	2 / 2	1=	0 / 12	10=	7 / 122	9
Target	2 / 2	1=	1 / 12	7=	11 / 122	8
Market	1 / 2	8=	2 / 12	5=	24 / 122	3
Human Resources	2 / 2	1=	1 / 12	7=	12 / 122	7
Responsibility	2 / 2	1=	2 / 12	5=	14 / 122	6
Experience	1 / 2	8=	1 / 12	7=	5 / 122	10
Agency	2 / 2	1=	0 / 12	10=	0 / 122	11
Other	1 / 2	8=	4 / 12	3=	15 / 122	5

**Table 7: Remuneration Logics in the Discourse of Telecom, the Media, and the Public**

Public	
Tone	Comments
Agree (Supportive)	33 or 27%
Neutral	43 or 35%
Disagreed (Unsupportive)	46 or 38%

**Table 8: Tone of the Public’s Discourse**

Public Themes	Tone		
	Agreed	Neutral	Disagreed
Absolute Level	12	19	32
Effort	14	10	6
Market	9	8	7
Pay-for-Performance	3	3	12
Responsibility	8	3	3
Human Resources	6	4	2
Target	6	4	1
Contribution	4	1	2
Experience	3	1	1
Agency	0	0	0
Other	6	4	5

**Table 9: Remuneration Logics Present in the Public’s Discourse**

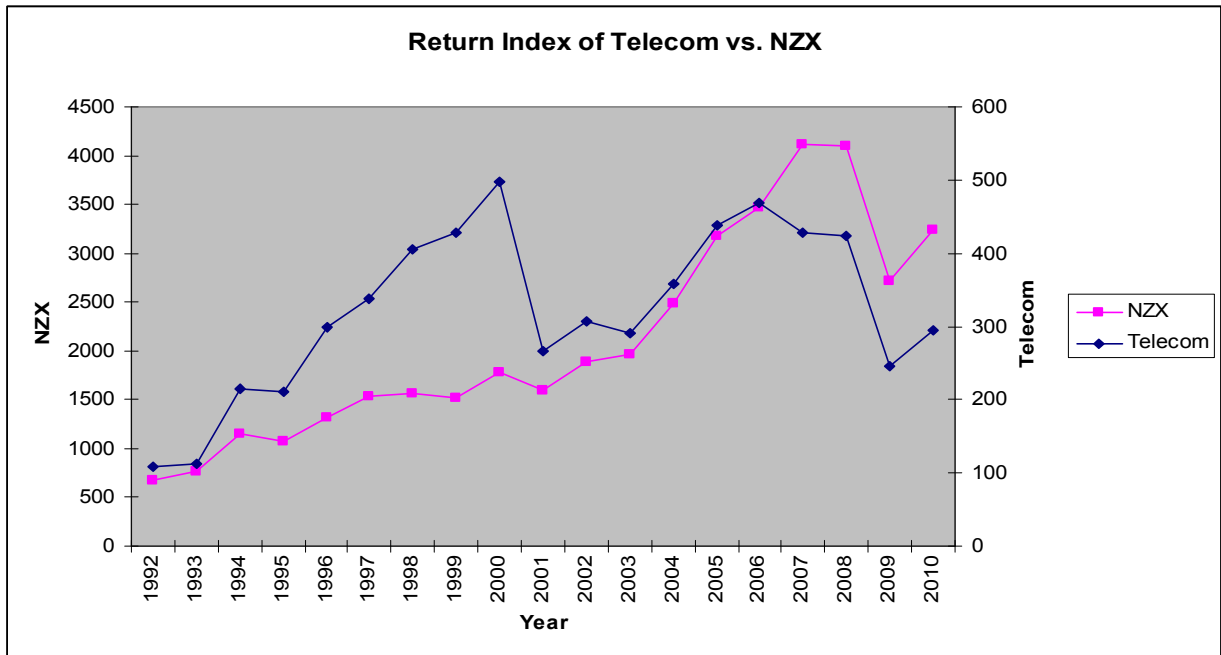


Figure 1: Return Index of Telecom and NZX

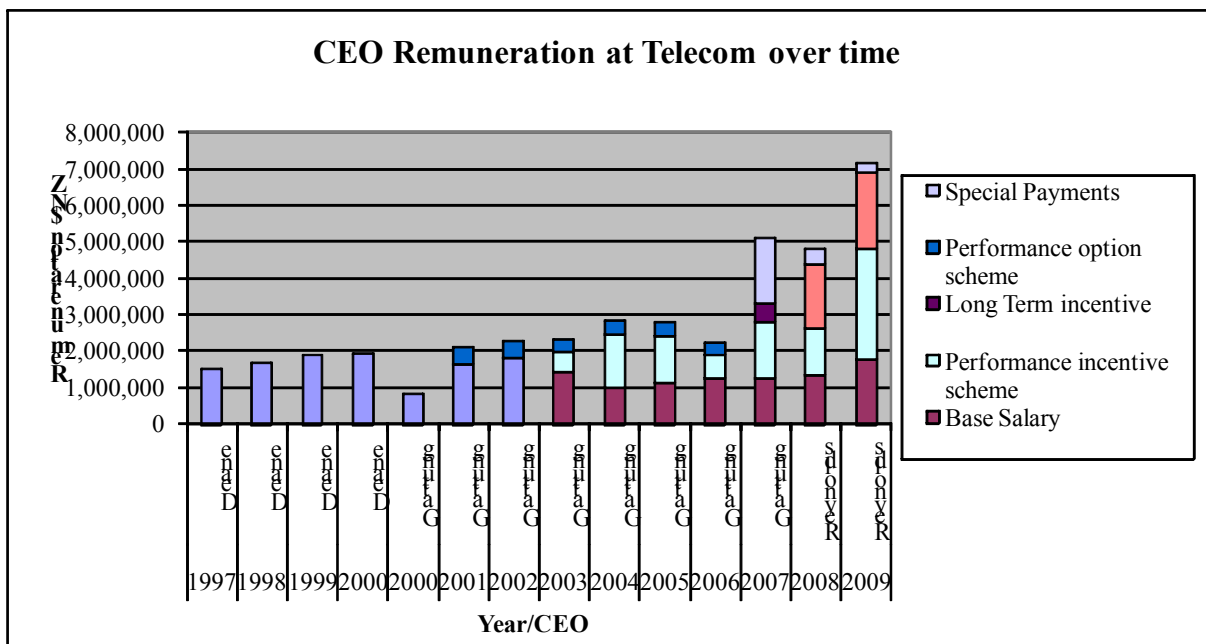


Figure 2: CEO Remuneration at Telecom

	BASE SALARY (Paid during year ended 30 June 2009)	PERFORMANCE INCENTIVE SCHEME <sup>1</sup> (Paid during year ended 30 June 2009)	PERFORMANCE INCENTIVE SCHEME <sup>2</sup> (Earned during year ended 30 June 2009)	PERFORMANCE RIGHTS SCHEME <sup>3</sup>	SPECIAL PAYMENTS <sup>4</sup>
<b>Paul Reynolds</b> Chief Executive Officer	NZ\$1,750,000	NZ\$1,312,500	NZ\$3,062,500	NZ\$2,100,000	NZ\$243,950

- The performance incentive scheme is delivered in two parts, a 60% cash payment and 40% as fully paid ordinary Telecom shares subject to restrictive conditions. This amount is the actual annual incentive earned for the previous year ending 30 June 2008 and paid in August 2008, being the 2009 financial year.
- As noted above this figure is made up of a 60% cash payment and 40% as restricted shares. This figure is the actual annual incentive earned for the year ending 30 June 2009 and paid in August 2009, being the 2010 financial year.
- 668,790 share rights were issued with a value at the time of issue of NZ\$2,100,000. The share rights will vest over a three year period subject to the achievement of specific performance hurdles set by the board.
- Special payments include payment for personal travel between NZ and the UK and accommodation payments as provided in Dr Reynolds' employment agreement.

**Figure 3: Disclosure of Dr. Paul Reynolds' Remuneration in 2009**

(Source: Telecom 2009 Annual Report, p.126)

BASE SALARY (NZ\$) FIXED	PERFORMANCE INCENTIVE (NZ\$) <sup>1</sup> AT RISK (Earned in FY10, paid in FY11)	LONG-TERM INCENTIVE AT RISK		SPECIAL PAYMENTS <sup>4</sup> (NZ\$)
		Granted in FY10 <sup>2</sup>	Lapsed in FY10 <sup>3</sup>	
1,750,000	900,000	678,910 share rights 95,998 performance entitlements	134,100 share rights	338,111

- The performance incentive scheme is delivered in two parts, a 60% cash payment and 40% as fully paid ordinary Telecom shares subject to restrictive conditions. This amount in aggregate is the gross actual annual incentive earned for the year ending 30 June 2010 and paid in the 2011 financial year. The gross amount earned for the year ending 30 June 2009 and paid during the 2010 financial year was NZ\$3,062,500 of which 60% was granted in cash and 40% as 280,258 fully paid ordinary Telecom shares subject to restrictive conditions.
- The share rights and performance entitlements will vest over a three-year period subject to the achievement of specific performance hurdles set by the board.
- 134,100 of the share rights granted to the CEO in the 2008 financial year, with a value of NZ\$583,333 at the time of grant, lapsed during the 2010 financial year.
- Special payments include payment for personal travel between New Zealand and the United Kingdom, gross accommodation payments and obtaining tax advice.

**Figure 4: Disclosure of Dr. Paul Reynolds' Remuneration in 2010**

(Source: Telecom 2010 Annual Report, p.136)