Investigation on the Compensation Incentive Structure of Non-employee Directors of a Company---- Taking JP Morgan as an Example

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Abstract. Compensation incentive for non-employee directors is a crucial factor of building a successful company, especially for big company like JP Morgan, keeping non-employee directors always at a high level of contributing and make them perform their loyalty is extremely important. In this passage, the author is going to outline and analyze the non-employee directors' compensation incentive structure of the bank "JP Morgan". The author is using the 2015-2016 and 2020-2021 official proxy statement of JP Morgan as reference to compare and contrast, as well as analyzing how non-employee directors' compensation incentive structure changed over five years. The result of this essay is that the non-employee directors' compensation incentive structure in JP Morgan is properly constructed and well developed, there are special ways to evaluate the performance of non-employee directors. The compensation incentives for non-employee directors did not significantly increase or decrease from 2015 to 2020. This essay will promote people's understanding about the incentive structure of JP Morgan, also get a clear and detailed understanding of how the incentive for non-employee directors benefits the income of the overall company.

Keywords: Compensation incentive; non-employee directors; JP Morgan.

1. Introduction

"Compensation and Incentives: Practice vs. Theory" was written by GEORGE P. BAKER, MICHAEL C. JENSEN, and KEVIN J. MURPHY [1]. The essay mainly talks about the importance of compensation incentive on positively effecting employee's working efficiency and attitude. Also explained the importance of building an appropriate internal incentive structure so that employees will behave themselves. The article also mentioned a lot of theories and economic factors that is crucial for building a success compensation incentive structure [1].

"Executive Compensation and Incentives" was written by Martin J. Conyon, and the essay talked about the purpose of carefully designed executive compensation programs is to attract, retain, and motivate CEOs and senior management to understand executive pay. Standard economic methods are the main agency models. The essay documents changes in executive pay and incentive measures in American firms from 1993 to 2003, considering the reason of the transformation, including agent theory, management changes in the Labor market, the change of company strategy and relevant theory of management showing that, with the passage of time, the board of directors and remuneration committee to become more independent. In addition, the essay proved that contains the association director's compensation committee did not set a higher salary or fewer incentives [2].

"Bank CEO incentives and the credit crisis" was written by Rüdiger Fahlenbracha and René M. Stulz. The essay investigate whether bank performance during the recent credit crisis is related to pre-crisis CEO incentives and we find some evidence that the interests of banks with CEOs are better aligned with those of shareholders, that shareholders are less interested, and that there is no evidence that they are performing better During the crisis, with higher option compensation and bigger compensation the bigger banks didn't do worse and the bank CEOs didn't reduce their equity in anticipation of the crisis or during the crisis so they suffered a huge loss of wealth after the crisis [3].

"CEO incentives and bank risk" was written by James Cashm AcreyWilliam R. McCumber, and Thu Hien T. Nguyen. This article investigate the relationship between CEO compensation and predictors of bank default risk to determine whether short-term incentives can explain the recent excess of bank risk. We investigate warning field monitoring parameters and expected default frequency (EDF) and crisis-related risk bank activity We find only modest evidence that CEO compensation structures contribute to substantial firm-specific heterogeneity in bank risk measures or risk activities The compensation element is generally considered to be the riskiest component, with uninvested options and bonuses either irrelevant or negatively correlated with ordinary risk variables and only positive in predicting the level of trading assets and securitization income [4].

"Bank incentives, contract design and bank runs" was written by David Andolfatto and Ed Nosal. The essay studied the Diamond–Dybvig model as developed in Green and Lin. The essay authors abandoned the idea of the bank as a depositor's union and instead the bank was a selfish agent with a technical advantage in record keeping and looked at the implications of the resulting agent problem for the design of bank contracts and the possibility of a balanced bank operation. For special cases, the authors find that the agent problem may or may not simplify the qualitative structure of bank liabilities [5].

2. Case Description

2.1 Compensation Incentive for Non-employee directors incentive for JP Morgan in 2015

Table 1. Non-employee directors' compensation incentive in JP Morgan in 2015

Director	Fees Earned or Paid in Cash ($)	Share Awards ($)	Total ($)
David M Dipietro	--	103,926	103,926
Kenneth M. Karmin	--	155,995	155,885
H. Mark Lunenburg	--	113,776	113,776
Jonathan Orszag	--	103,926	103,926
Glenn H. Tongue	--	123,634	123,634

The Board's commitment to independence begins with the individual directors. All of the non-management Board members are independent under the standards established by the NYSE and the Firm's independence standards. Each non-management Board Members has only immaterial relationships with JPMorgan Chase. For 2014, each non-management director received an annual cash retainer of $75,000 and an annual grant, made when annual employee incentive compensation was paid, of deferred stock units valued at $225,000, on the date of grant. Each deferred stock unit included in the annual grant to directors represents the right to receive one share of the Firm's common stock and dividend equivalents payable in deferred stock units for any dividends paid. Deferred stock units have no voting rights. Each year non-management directors may elect to defer all or part of their cash compensation [6].

Table 2. Annual Compensation for non-management directors in JP Morgan in 2015

Compensation	Amount ($)
Board Retainer	75,000
Lead Independent Director retainer	30,000
Audit and Risk Committee chair retainer	25,000
All other committees chair retainer	15,000
Audit and Risk Committee member retainer	15,000
Deferred stock unit grant	225,000

2.2 Compensation Incentive for Non-employee directors incentive for JP Morgan in 2021

The cash compensation spends of JPM in 2021, every non-employee director can get 100,000 US dollar for cash retainer. The detail of each and every kind of compensation that JPM spend during 2021 was shown below, and the units are all in US dollar. Board retainer costs 100,000; Lead Independent Director retainer coasts 30,000; the Audit and Risk Committee chair retainer costs

25,000; the Audit and Risk Committee member retainer costs 15,000; the All-other committees chair retainer costs 15,000; the Deferred stock unit grant costs 250,000; the Bank Board retainer costs 15,000; the Bank Board's chair retainer costs 25,000; and the J.P. Morgan Securities plc Board retainer costs 110,000.

There are incentive grants that JPM uses. According to the table of incentive compensation awarded to NEOs, the chairman and CEO gets 5,000,000 $ cash compensation and 28,000,000 $performance share units. But he did not get any incentive compensation on stock. The Co-President & Co-Chief Operating Officer; CEO Corporate & Investment Bank Daniel Pino gets 9,722,026 unit of restricted stock units and 9,722,026 $ performance share units. But he did not get any cash compensation in 2021. The Co-President & Co-Chief Operating Officer; CEO Consumer & Community Banking Gordan Smith gets 8,700,000 $ for cash compensation, 6,525,000 for restricted stock unit, and 6,525,000 unit of performance share. The CEO Asset & Wealth Management Mary Callahan Erdoes gets 7,900,000 $ for cash compensation, 5,925,000 for restricted stock unit, and 5,925,000 unit of performance share. The Co-CEO Consumer & Community Banking; Former Chief Financial Officer Jennifer Piepszak gets 6,300,000 $ for cash compensation, 4,725,000 for restricted stock unit, and 4,725,000 unit of performance share. According to the statistic, in the last three years, 0.1% of JPM's profit was paid to CEOs' incentive and salary. The vesting schedule of JPM in 2021 was:"1-PSUs vest in year three including any dividends that are reinvested over the vesting period; 2-SARs cliff vest in year five; 3-SARs vest in five equal installments, in years one, two, three, four and five; 4-PSUs vest in five equal installments, in years three, four, five, six and seven including any dividends that are reinvested over the vesting period; 5-PSUs and RSUs vest in five equal installments, in years three, four, five, six and seven; 6-RSUs vest in two equal installments, in years two and three [7]. "

There were 10 board meetings, which focus on the communication between meetings as appropriate; 8 executive sessions of independent directors, which was Led by Lead Independent Director; 43 Meetings of principal standing committees; and 9 Meetings of specific purpose committees.

The Centre believes that it is important to align the interests of OC members with those of shareholders. To achieve this, OC members should comply with the shareholding guidelines and retention policy. The guideline include While on the Operating Committee, each member is required to accumulate either a minimum of between 200,000 and 400,000 shares (1 million shares for the CEO); or a minimum fixed dollar value of shares of between $10 million and $30 million ($75 million for the CEO).A special compensation method for JPM is in 6 stages. They are business principles, strategic framework, compensation philosophy, performance assessment, pay determination, and pay mix. The company's strict disciplinary performance salary cycle began to formulate strategic plans, budgets and priority matters at the company's scope, business or functions and personal levels. These are reviewed by the board of directors, approved by CMDC, and conveying priority internally and outside. One of the key factors that CMDC considers when evaluating the performance of OC members is that they have achieved progress in realizing the goals related to the company's diversity, fairness, and inclusive priority [8].

There is also Consistently Strong Absolute Performance award, which was awarded to Mr. Dimon because of his stewardship, the Board awarded him $34.5 million in total annual compensation for 2021.

According to the concept of salary, CMDC uses a balanced and disciplinary method to evaluate the performance of OC members throughout the year and four extensive aspects: Business results, including many years of absolute and relative performance; Risk, control and behavior, including feedback received from the company and control professionals; Customer/customer/interest -related person, including the participation in the community and the commitment of providing economic opportunities for communities with insufficient service, and solving environmental and social problems, such as climate change and racial equality; Team cooperation and leadership, including creating diversified, tolerance, respect, and responsible environment, as well as cultivating employees, managers and leaders, as the key driving force for the human capital management strategy [9].

3. Conclusion

This essay specifically outlined the non-employee compensation incentive structure, including their salary, stock incentives and so on. Also analyzed the compensation incentive of the company. The essay also found out a special procedure of how the company JP Morgan evaluate the performance and behavior of a non-employee director throughout a year and accordingly practice the compensation incentive. The essay concludes that the company JP Morgan have a great expenditure on the non-employee directors' compensation incentive comparing to other bank companies in US, it is both a positive thing and a negative thing since it can both decrease the income level of the company, but also can attract high quality directors and help them demonstrate their loyalty.

This essay fills the gap of no one have produced an essay stating and analyzing the non-employee compensation incentives structure in JP Morgan. Therefore, people who wants to learn about JP Morgan does not have any reference to read, but with my essay, they have an essay to refer to and study on. My essay to helpful for scholars who wants to investigate on the incentive structure of JP Morgan or people who want to get an inspiration of analyzing the incentive structure of JP Morgan.

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