SNL®
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MONTHLY

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## In This Issue



## Upcoming issues

**Meet the SNL Real Estate Team:** *Throughout the summer, we will be visiting clients in many major cities and we would welcome the opportunity to hear your comments. Contact reit_research@snl.com with any questions or to request further details.*

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*Executive Compensation Review – 2004*

# For Most–High Tide and Green Grass…For All–a New Era Emerges.

*After 4+ years of soundly beating the broader market, REITs have huge momentum. Their executives have recorded strong returns, have very satisfied investors … and are harvesting well-deserved financial reward. But we are likely entering a new strategic era for both performance and compensation, as Management and Boards face the challenges from a growing economy, a maturing industry, and the appropriate context for evaluation.*

***Prepared exclusively for SNL Financial by THE BRADFORD GROUP, Los Angeles – James Wright - CEO.***

You've heard it and read it over and over in the last few years … crisis in executive compensation, disconnect between pay and performance, ineffective and undisciplined governance. True perhaps in some industries and companies, but you cannot point to the real estate sector in general or 2003 in particular as an example. Although the broad issues remain in play amongst the public outcry over corporate scandals, trials, restructurings and business ethic discussions, REITs have enjoyed the sunshine of yield seeking investors amid the slow and uncertain steps toward economic and broader market recovery. The ironic twist of factors - difficult real estate fundamentals in many sectors, yet rising price multiples and investment-demand has driven asset sale/recycling and capital raising/restructuring opportunity for perhaps longer than anyone expected. REITs – highly scrutinized due to the reality of historical real estate risk, have been disciplined and conservative (relative to real estate) in terms of business strategy and operations for many years. Currently, the glow of outperformance avoids much questioning over compensation decisions … a safe harbor for now. Market success has also

*continued on page 3*

## SNL Monthly Top 10

### Top 10 in Realized Option Exercise Value in 2003

*Stock market success meant that the top five executives at these companies were able to realize over $270 million in options in 2003 - more than double the amount they received in all compensation.*

| Company | Property Type | 2003 Total Option Value Realized | 3-Year Price Return |
|---|---|---|---|
| Vornado Realty Trust (VNO) | Diversified | 67,960,000 | 42.9% |
| Catellus Development Co. (CDX) | Industrial | 35,759,590 | 37.8% |
| St. Joe Company (JOE) | Mixed Use | 32,959,110 | 69.5% |
| Camden Propert Trust (CPT) | Multi-Family | 30,596,773 | 32.2% |
| Rouse Company (RSE) | Mall | 25,058,438 | 84.3% |
| Developers Diversified Realty Trust (DDR) | Shopping Center | 24,307,884 | 152.2% |
| Hilton Hotels (HLT) | Hotel | 23,065,399 | 63.1% |
| Capital Automotive REIT (CARS) | Specialty | 13,020,739 | 131.7% |
| Boston Properties, Inc. (BXP) | Office | 11,732,786 | 10.8% |
| Health Care Property Investors, Inc. (HCP) | Health Care | 9,981,900 | 70.0% |
| **SNL REIT Equity Index** | | | **32.6%** |

Source: SNL Financial and THE BRADFORD GROUP allowed executives to cash in on vested options (see SNL Top 10, page 1) and Boards to emphasize market competitive decisions, yet be cautious as stewards of strong governance and protectors of shareholder interests.

This year's analysis of real estate executive compensation will examine not only recent year-to-year trends, but will also look at changing long-term incentive vehicles, the executives earning the most money, trends for the next era of REIT economics, and will explore the relationship of financial and market performance vs. cash and equity compensation over the last three years.

## Compensation Trends Old and New

So, given the "we pay for performance" mantra offered by most real estate executives and their companies, let's look at the trends for the REIT and REOC sectors for 2003. REITs have a stellar record in market return (Table 1) regardless of size or property focus, over the last three years, and have received consistent yet not equal increases in pay (Table 2). Equity REITs over the three-year period 2000 to 2003 have delivered a total return of nearly 63% (42.9% from 2001 to 2003), while compensation of the top 5 executives has risen in the same period by only 23% (37% for CEOs).

Although various sources report a range of figures, REITS fare well compared to increases in the broader market. S&P 500 Company CEOs total compensation rose 27% in 2003 (median – according to The Corporate Library – Reuters research reported a 16% increase) much in tandem with the 26% rise in the S&P 500 index in 2003. Average CEO compensation for REITs rose 23% in 2003 vs. a total return of 37.5% and the fourth year of outperformance of the broader market. The value of option awards in S&P 500 companies fell 17.1% (CEOs by 38%) compared to 32% for REIT executives (top 5), as companies and Boards have diverted from the attention getting option controversy. S&P 500 CEO awards of restricted shares increased 38% in 2003, while Long Term Incentive Plan (LTIP) payment rose 61%. By contrast, REIT executives (top 5) restricted share awards increased by nearly 51%.

REIT cash compensation, however, is one area that may seem a little out of alignment at first blush. CEO bonuses rose 20% for the S&P 500 companies against strong financial and market performance, while REITs paid-out a 12% increase in total cash to CEOs (10% to 12% across the top 5 executives), lower no doubt related to continuing difficult real estate markets influencing weak financial performance, despite strong market returns. Overall, the rise of cash components of compensation despite weaker financial performance, although not alarming or fundamentally unjustified, does raise the question (again) as to what performance criteria and how much weight is associated with each element of compensation. A review of proxy statements rein-


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forces this issue, with some companies indicating specific financial performance criteria related to shorter term (annual) compensation, while others present a very broad and more vague set of criteria blending financial and market return factors to be applied to all incentive compensation. These sweeping criteria can provide the net to allow success to be defined as whatever ends up as succeeding. Good for executives, but potentially creating issues of optics. Despite the extent of cyclical counter performance in real estate, too much application of longer-term shareholder value (and wealth building) criteria applied to current year financial/operating achievement against company objectives creates confusion for analysts and investors, and may also undermine governance.

Correspondingly, too much emphasis on specific financial performance measures such as FFO and FFO/share as the basis for judging annual incentive may undermine the range of operating and financial activities, challenges and successes, particularly in a difficult real estate market. The strong increases in compensation in 2003 for top REIT executives, and in particular CEOs are well deserved for a variety of other reasons beyond market return or conventional measures of financial performance. REIT capital transactions for debt and equity ($26 billion in 2003 - $2.7 billion in IPOs) have provided the opportunity to restructure debt and strengthen balance sheets, and the frustrations and costs of implementing the financial controls of Sarbanes-Oxley have been demanding, as have the challenges of the commercial real estate markets. Additionally, asset transactions, ventures, cash/payout requirements, operating efficiency/discipline, building strong management teams and developing future leadership all played a role in the determination of compensation. For multi-family and office sectors, providing appropriate incentive to motivating employees under difficult market conditions was (is) a substantial challenge for management over the past few years. In the end, in a year (period) of challenging fundamentals, discretion covers a lot of ground that a few performance measurements often obfuscate.

Table 1

**REIT Market Performance 2001 - 2004**

| | 2004 @ 6/30 (%) | 2003 1 Yr. (%) | 2000 - 2003 3 Yr. (%) |
|---|---|---|---|
| **Price Change** | | | |
| S&P 500 | 2.60 | 26.38 | -15.78 |
| Equity REITs | 2.78 | 28.77 | 32.62 |
| **Total Return** | | | |
| Equity REITs | 5.64 | 37.50 | 62.66 |
| **Market Cap** | | | |
| Over $2.0 Billion | 6.66 | 38.74 | 42.94 |
| $1.0 Billion to $2.0 Billion | 7.83 | 32.84 | 65.89 |
| $500 Million to $1.0 Billion | 9.91 | 41.55 | 79.77 |
| $250 Million to $500 Million | 4.65 | 41.07 | 102.42 |
| Under $250 Million | 1.20 | 40.02 | 116.61 |
| **Property Focus** | | | |
| Healthcare | 1.90 | 56.00 | 161.11 |
| Hotel | 3.86 | 30.49 | 20.37 |
| Industrial | 5.61 | 33.07 | 66.71 |
| Diversified | 6.86 | 42.03 | 63.94 |
| Office | 2.79 | 33.41 | 34.30 |
| Retail | 7.99 | 47.52 | 131.26 |
| Residential | 6.13 | 25.91 | 31.37 |
| Self-Storage | 6.76 | 40.27 | 103.65 |

Source: SNL Financial and THE BRADFORD GROUP

Table 2

**Compensation Growth and Company Performance (%)**

| | 2001 to 2002 | 2002 to 2003 | Period Growth | CAGR |
|---|---|---|---|---|
| **Base Salary and Annual Bonus** | | | | |
| Top 5 Executives | 0.2% | 11.3% | 11.5% | 5.6% |
| CEO | 3.4% | 12.1% | 16.0% | 7.7% |
| COO | -3.6% | 11.9% | 7.9% | 3.9% |
| CFO | 1.8% | 10.5% | 12.4% | 6.0% |
| **Total Compensation (excluding Option Award Value)** | | | | |
| Top 5 Executives | 9.6% | 27.2% | 39.4% | 18.1% |
| CEO | 13.5% | 42.2% | 61.4% | 27.1% |
| COO | -6.7% | 31.7% | 22.8% | 10.8% |
| CFO | -3.6% | 25.8% | 21.3% | 10.2% |
| **Total Compensation (including Option Award Value)** | | | | |
| Top 5 Executives | 6.7% | 15.1% | 22.8% | 10.8% |
| CEO | 11.4% | 23.3% | 37.3% | 17.2% |
| COO | -6.4% | 12.2% | 5.0% | 2.5% |
| CFO | -2.2% | 16.6% | 14.1% | 6.8% |
| **Company Performance Measures** | | | | |
| ***REITs*** | | | | |
| FFOPS Growth | -3.7% | -9.0% | -12.4% | -6.4% |
| Dividend Growth | -4.5% | 1.7% | -2.8% | -1.4% |
| EBITDA Growth | 3.6% | 4.2% | 8.0% | 3.9% |
| Total Return | 3.9% | 37.5% | 42.9% | |
| ***REOCs*** | | | | |
| Net Income Growth | 47.6% | 4.8% | 54.8% | 24.4% |
| EPS Growth | 27.7% | 2.1% | 30.4% | 14.2% |
| Total Return - Hotel | -42.8% | 40.6% | -19.9% | |
| Total Return - Other | -33.0% | 45.4% | -2.6% | |

Note: All compensation figures include both REITs and REOCs.
Source: SNL Financial and THE BRADFORD GROUP

## Options Fade and Restricted Shares Grow – Over-Reaction?

Figures for the past few years also reflect the trend in increased use of restricted share equity awards, and corresponding decline in the use of stock options. Table 3 shows the precipitous decline in the use of stock options in long-term compensation, apparently a reaction to pending regulatory requirements for expensing options, general public

Table 3

**REIT Option Grant (vs. Common Shares) Trend - Top 5 Executives 2001 to 2003 (figures in millions)**

| | 2001 | | 2002 | | 2003 | | Period % Change | | |
|---|---|---|---|---|---|---|---|---|---|
| | Options # | Option Value (a) ($) | Options # | Option Value (a) ($) | Options # | Option Value (a) ($) | Options # | Option Value (a) | CAGR Value |
| All REITs | 25.7 | 115.8 | 28.2 | 124.1 | 19.2 | 95.5 | -25.3 | -17.5 | -9.2 |
| Health Care | 4.1 | 7.9 | 1.0 | 3.5 | 1.2 | 4.1 | -70.7 | -48.1 | -28.0 |
| Hotel | 0.6 | 1.4 | 0.1 | 1.1 | 0.1 | 0.5 | -83.3 | -64.3 | -40.2 |
| Industrial | 2.6 | 12.7 | 2.5 | 12.1 | 2.2 | 12.4 | -15.4 | -2.4 | -1.2 |
| Diversified | 3.4 | 20.9 | 2.2 | 11.3 | 2.6 | 9.7 | -23.5 | -53.6 | -31.9 |
| Office | 3.2 | 16.3 | 11.3 | 40.4 | 3.5 | 12.9 | 9.4 | -20.9 | -11.0 |
| Retail | 5.1 | 20.1 | 5.9 | 28.0 | 5.8 | 32.3 | 13.7 | 60.7 | 26.8 |
| Residential | 6.4 | 35.2 | 4.3 | 25.0 | 3.4 | 21.8 | -46.9 | -38.1 | -21.3 |
| Self-Storage | 0.3 | 1.4 | 0.5 | 2.8 | 0.3 | 2.1 | 0.0 | 50.0 | 22.5 |

**REIT Restricted Share Award Trend - Top 5 Executives 2001 to 2003 (figures in millions)**

| | 2001 Award Value $ (b) | 2002 Award Value $ (b) | 2003 Award Value $ (b) | Period % Change Award Value $ (b) | CAGR Value |
|---|---|---|---|---|---|
| All REITs | 92.6 | 152.6 | 230.3 | 148.7 | 57.7 |
| Health Care | 8.2 | 13.6 | 9.9 | 20.7 | 9.9 |
| Hotel | 8.4 | 9.5 | 38.4 | 357.1 | 113.8 |
| Industrial | 7.7 | 9.4 | 36.4 | 372.7 | 117.4 |
| Diversified | 4.1 | 33.9 | 14.4 | 251.2 | 87.4 |
| Office | 18.5 | 23.5 | 49.8 | 169.2 | 64.1 |
| Retail | 20.8 | 41.2 | 52.4 | 151.9 | 58.7 |
| Residential | 22.3 | 20.4 | 25.4 | 13.9 | 6.7 |
| Self-Storage | 2.6 | 1.3 | 3.6 | 38.5 | 17.7 |

a) Option value = options awarded times share price at grant date divided by five.
b) Restricted share value = number of shares awarded times share price at time of award.
Source: SNL Financial and THE BRADFORD GROUP

concern over executive stock options, and the trend in diversification into other vehicles for long-term compensation incentive to align with shareholders. Table 3 also documents the dramatic rise in the use of restricted share awards to REIT executives, in this case where rising share price enhances value growth. Although options have long been touted as strong and well-aligned executive incentive, linked to shareholder risk, and were used extensively in the 1990's REIT growth period, restricted shares have gained in popularity.

Even though the accounting is still favorable, the downside risk of options may be too high for REITs at this time, or the issue of executive ownership levels is a also a focus as many founders transition to professional and more "independent" management. Additionally, some REITs are adopting other creative forms of long-term incentives, including performance units, performance shares and OP Unit options. OP Unit oriented plans are unique to REITs and although may offer attractive tax advantages to recipients, do so at the expense of alignment with shareholders. As the array of long-term incentive vehicles expands, questions of too many programs, redundant measurement, programs too complex, and the proper balance of the up-side and downside risks of each are yet another aspect of the increasingly complicated role of Compensation Committees. A "balanced scorecard" approach would include the risk profile of options, but as the array of alternatives increases, again the systematic strategic framework for compensation decisions emerges as an important aspect of decision-making.

## Expanding Group of Big Winners

More REIT executives have enjoyed large compensation packages over the past few years than ever before. Table 4 shows the increasing membership since 2001 in the "club" of greater than $1.0 million in annual cash compensation (+ nearly 50%), or greater than $3.0 million in annual total compensation (+ over 100%) – of the top 5 named officers according to Proxy Statements. Since 2001 it appears that

Table 4

**Table 4 Market Performance Creates Expanding Size of REIT Compensation**

**Executives Receiving Greater than $1.0 million**

| | 2001 | 2002 | 2003 | Period % Change |
|---|---|---|---|---|
| **Total Cash Compensation** | | | | |
| CEO | 24 | 28 | 40 | 66.7 |
| COO | 6 | 5 | 9 | 50.0 |
| CFO | 4 | 3 | 5 | 25.0 |
| Top 5 Executives | 46 | 50 | 68 | 47.8 |

**Executives Receiving Greater than $3.0 million**

| | 2001 | 2002 | 2003 | Period % Change |
|---|---|---|---|---|
| **Total Compensation (including Option Award Value)** | | | | |
| CEO | 12 | 20 | 31 | 158.3 |
| COO | 3 | 3 | 1 | -66.7 |
| CFO | 1 | 2 | 5 | 400.0 |
| Top 5 Executives | 21 | 29 | 44 | 109.5 |

Source: SNL Financial and THE BRADFORD GROUP

CEOs have been big winners from equity awards with a 150% increase in awards greater than $3.0 million in total compensation, and COOs have faired less well, perhaps due to a changing nature of the position, tougher operational environments, or number of companies with the position. CFOs have been rewarded well for their success at engaging in the Sarbnes-Oxley and other related regulatory quagmire and succeeding in adapting company policy, practice and systems. Table 5 shows the top 10 individual winners among REITs and REOCs executives in cash and total compensation (including and excluding option award value).

The rise in REIT values has also lead to opportunity to convert value from vested options into cash. The SNL Monthly Top 10 shows the biggest option exercise conversions of 2003. These however, are not just rewards captured from a rising market. They also reflect the long-term achievements of building public real estate into a strong and disciplined market sector. The hard work of building effective operational policy and procedures, and executing sound asset and corporate financial structures is a part of why investors have discovered REITs, and why they continue to build a reliable reputation for portfolio diversification and income. Expectedly, realizing value from options is not the domain of the largest REITs nor annually the most well paid executives, as Table 5 shows the range of implied market cap and ranking in annual total compensation, among these high performing companies over the past three years.

## Building "Pay for Performance" Relationships

Perhaps the most discussed question in the executive compensation "conversation" is the relationship of compensation and company performance. Most often the media finds several companies with highly paid executives and poor performance and touts them as examples of the problem. Incentive compensation decisions should always be related to performance … but putting performance into the right context isn't simple. Even though there are benchmarks of market competitive compensation in any single year, the alignment of performance and compensation can only be understood from looking at multiple years of evidence. So in lies the heart of further investigation of REIT performance and compensation. Time, and the assessment of performance over time, provides the foundation for compensation and the context for decisions. This has been missing from REIT assessments of compensation, and given the discipline and diligence of REIT Board governance, offers a compelling platform for stronger rationalization.

So, lets take a further look at REIT pay and performance, and examine the underlying relationship between compensation and performance over the past few years. As pointed out, the appearance of similar percentage change (direction and magnitude) is only a point-of-departure in the linkage of pay and performance. The heart of the argument would be the establishment of underlying relationships over time, overall and among property types, that would begin to build a strategic framework for compensation decisions by management and committees. For this year's REIT compensation review, we did just that, examining financial performance indicators vs. cash compensation, and market indicators vs. total compensation over a three-year period (Table 6).

From 2001 to 2003, strong and statistically significant relationships exist between EBITDA and FFO vs. cash compensation, as well as from market capitalization and total compensation, as indicated by the correlations shown (other statistics and regression equations available). Beyond the reaction of "okay – so why is this so important," … these relationships are a framework to define the strategic position for company compensation levels, programs and needs, and allows a "dynamic benchmarking" of compensation, able to directly move with company size and anticipated growth. Because the relationship of performance and compensation is not linear, when traditional benchmarking (averages and medians) collapses data without seeing the underlying relationship, it penalizes high performers more than rewarding low performers.

## Beyond the Numbers - What Proxies Tell the Investor World

This year a review of proxy information on compensation and Compensation Committee Reports allowed a further investigation of compensation practices as presented to shareholders, investors and the financial community. In particular, each of approximately 130 REIT proxy statements were reviewed and an inventory of compensation program and decision characteristics was created (Table 7). Expectedly, the review yielded a wide range in the level of explanation of

Table 5

## Top 10 Executives - Total Compensation, including Options - 2003 ($ millions)

The 10 most highly compensated REIT/REOC executives ranked by Total Compensation including the estimated present vlaue of options awarded (1).

| Ticker | Company | Title | Executive | 2003 | 2002 | % Change | 2003 Total Return |
|---|---|---|---|---|---|---|---|
| CDX | Catellus Development Corp. | Chairman | Nelson C. Rising | 13,953,308 | 3,733,110 | 273.8 | 46.6 |
| MPG | Maguire Properties, Inc. | President | Richard I. Gilchrist | 12,950,000 | | 0.0 | 0.0 |
| JOE | St. Joe Company | Chairman | Peter S. Rummell | 12,097,859 | 3,498,491 | 245.8 | 25.6 |
| JOE | St. Joe Company | President | Kevin M. Twomey | 11,785,570 | 2,292,012 | 414.2 | 25.6 |
| HMT | Host Marriott Corporation | President | Christopher J. Nassetta | 11,097,858 | 6,724,522 | 65.0 | 40.0 |
| RSE | Rouse Company | Chairman & President | Anthony W. Deering | 9,836,088 | 5,618,387 | 75.1 | 55.8 |
| LNR | LNR Property Corporation | President | Jeffrey P. Krasnoff | 8,974,578 | 2,111,858 | 325.0 | 41.4 |
| PLD | ProLogis | Chairman | K. Dane Brooksher | 8,708,539 | 5,221,685 | 66.8 | 34.8 |
| HTG | Heritage Property Invt Trust Inc | President | Thomas C. Prendergast | 8,707,728 | 11,347,059 | -23.3 | 23.0 |
| LNR | LNR Property Corporation | Chairman | Stuart A. Miller | 8,291,000 | 1,573,000 | 427.1 | 41.4 |
| | **Average of Top 10** | | | **10,640,253** | **4,680,014** | **207.7** | **37.1** |

## Top 10 Executives - Total Compensation, excluding Options - 2003 ($ millions)

The 10 most highly compensated REIT/REOC executives ranked by Total Compensation excluding the estimated present vlaue of options awarded.

| Ticker | Company | Title | Executive | 2003 | 2002 | % Change | 2003 Total Return |
|---|---|---|---|---|---|---|---|
| CDX | Catellus Development Corp. | Chairman | Nelson C. Rising | 13,953,308 | 3,733,110 | 273.8 | 46.6 |
| MPG | Maguire Properties, Inc. (2) | President | Richard I. Gilchrist | 12,950,000 | | 0.0 | 0.0 |
| JOE | St. Joe Company | Chairman | Peter S. Rummell | 12,097,859 | 2,048,491 | 490.6 | 25.6 |
| JOE | St. Joe Company | President | Kevin M. Twomey | 11,785,570 | 1,422,012 | 728.8 | 25.6 |
| HMT | Host Marriott Corporation | President | Christopher J. Nassetta | 11,097,858 | 6,724,522 | 65.0 | 40.0 |
| LNR | LNR Property Corporation | President | Jeffrey P. Krasnoff | 8,835,378 | 1,986,658 | 344.7 | 41.4 |
| LNR | LNR Property Corporation | Chairman | Stuart A. Miller | 8,151,800 | 1,447,800 | 463.0 | 41.4 |
| HTG | Heritage Ppty Invt Trust Inc. | President | Thomas C. Prendergast | 7,910,568 | 9,414,979 | -16.0 | 23.0 |
| HMT | Host Marriott Corporation | Executive VP | W. Edward Walter | 7,347,490 | 2,965,983 | 147.7 | 40.0 |
| SLG | SL Green Realty Corp. | Chairman | Stephen L. Green | 7,256,250 | 1,700,000 | 326.8 | 35.8 |
| | **Average of Top 10** | | | **10,138,608** | **3,493,728** | **313.8** | **35.5** |

## Top 10 Executives - Base Salary + Annual Bonus Compensation - 2003 ($ millions)

The 10 most highly compensated REIT/REOC executives ranked by Total Cash Compensation - Base Salary + Annual Bonus + Other Annual Compnsation.

| Ticker | Company | Title | Executive | 2003 | 2002 | % Change | 2003 Total Return |
|---|---|---|---|---|---|---|---|
| MLS | Mills Corporation | Chairman | Laurence C. Siegel | 4,400,000 | 2,360,000 | 86.4 | 57.9 |
| HOT | Starwood Hotels & Resorts | Chairman | Barry S. Sternlicht | 3,782,146 | 2,182,058 | 73.3 | 55.6 |
| WBR | Wyndham International Inc. | Chairman | Fred J. Kleisner | 3,262,868 | 796,517 | 309.6 | 157.7 |
| RA | Reckson Assoc. Realty Corp. | Executive VP | Philip Waterman | 3,058,655 | 1,456,195 | 110.0 | 24.0 |
| HLT | Hilton Hotels Corporation | President | Stephen F. Bollenbach | 3,000,000 | 2,000,000 | 50.0 | 36.2 |
| CDX | Catellus Development Corp. | Chairman | Nelson C. Rising | 2,967,373 | 2,601,625 | 14.1 | 46.6 |
| CEI | Crescent RE Equities Co. | Chief Executive Officer | John C. Goff | 2,904,231 | 1,650,000 | 76.0 | 12.7 |
| AFR | American Finl Realty Tr (2) | President | Nicholas S. Schorsch | 2,862,818 | | 0.0 | 0.0 |
| SLG | SL Green Realty Corp. | President | Marc Holliday | 2,532,960 | 1,500,000 | 68.9 | 35.8 |
| TRZ | Trizec Properties, Inc. | President | Timothy H. Callahan | 2,450,000 | 1,254,360 | 95.3 | 73.0 |
| | **Average of Top 10** | | | **3,122,105** | **1,755,639** | **98.2** | **55.5** |

1) Options awarded times share price at option grant date, divided by five.: 2) Not public company in 2002.
Source: SNL Financial and THE BRADFORD GROUP

Table 6

### REIT 2001 to 2003 Compensation and Performance - % Change and Relationship (1)

| | Financial Performance | | | | | | Market Performance | | |
|---|---|---|---|---|---|---|---|---|---|
| REIT Sector | Total Cash Growth a | FFO Growth | FFOPS Growth | Dividend Growth | EBITDA Growth | Correlation 2001 to 2003 b | Total Compensation Growth c | Total Return | Correlation 2001 to 2003 d |
| Healthcare | 14.0 | 29.6 | 14.5 | -10.9 | 15.1 | 0.77 | -22.8 | 161.1 | 0.95 |
| Hotel | 9.7 | -92.0 | -89.8 | -60.9 | -48.6 | 0.98 | 77.6 | 20.4 | 0.94 |
| Industrial | 4.0 | 10.5 | 3.6 | 15.3 | -2.1 | 0.88 | 50.7 | 66.7 | 0.95 |
| Diversified | 6.7 | 60.8 | 18.6 | 5.6 | 24.4 | 0.97 | -0.9 | 63.9 | 0.98 |
| Office | 27.5 | -1.1 | -3.6 | 0.5 | -2.9 | 0.51 | 18.9 | 34.3 | 0.68 |
| Retail - e | 6.7 | 59.0 | -7.7 | 16.8 | 44.9 | 0.83 | 35.9 | 131.3 | 0.87 |
| Residential - MF | 7.5 | -14.3 | -24.5 | -2.7 | -10.2 | 0.84 | -14.7 | 31.4 | 0.92 |
| Self-Storage | 20.6 | 17.6 | 0.8 | 2.5 | 14.5 | NA | 25.9 | 103.7 | NA |
| All Equity REITs | 11.7 | 5.7 | -15.3 | -3.5 | 4.8 | 0.78 | 21.6 | 62.7 | 0.86 |

### REIT 2003 - 1-Year Compensation and Performance - % Change and Relationship

| | Financial Performance | | | | | | Market Performance | | |
|---|---|---|---|---|---|---|---|---|---|
| REIT Sector | Total Cash Growth a | FFO Growth | FFOPS Growth | Dividend Growth | EBITDA Growth | Correlation 2003 b | Total Compensation Growth c | Total Return 1-Year | Correlation 2003 d |
| Healthcare | 12.3 | 22.3 | 18.4 | 6.5 | 19.0 | 0.85 | -9.5 | 56.0 | 0.98 |
| Hotel | 2.8 | -78.7 | -77.5 | 11.4 | -27.3 | 0.98 | 70.8 | 30.5 | 0.99 |
| Industrial | 6.6 | 5.1 | 6.3 | 5.2 | -3.8 | 0.80 | 50.2 | 33.1 | 0.90 |
| Diversified | 14.3 | 8.9 | -2.5 | -4.5 | 3.7 | 0.97 | -22.7 | 42.0 | 0.85 |
| Office | 20.5 | 7.4 | 8.6 | 2.8 | 6.8 | 0.52 | 12.8 | 33.4 | 0.67 |
| Retail - c | 9.8 | 21.6 | -13.8 | 8.0 | 21.9 | 0.84 | 13.3 | 47.5 | 0.85 |
| Residential - MF | 4.3 | -14.1 | -17.3 | -8.7 | -6.3 | 0.77 | 0.9 | 25.9 | 0.86 |
| Self-Storage | 30.4 | 3.1 | -2.9 | 1.2 | 1.3 | NA | 29.9 | 40.3 | NA |
| All Equity REITs | 11.0 | 3.2 | -9.0 | 1.7 | 4.2 | 0.56 | 10.6 | 37.5 | 0.81 |

(1) Aggregate compensation level of Top Five (5) Executives.
NA = Insufficent data.
a) Total Cash Compensation - Base Salary + Annual Bonus + Other Annual Compensation
b) Relationship between Total Cash and EBITDA, FFO relationship (all REITs) = 0.54 (3-year) and 0.55 (1-year).
c) Total Cash Compensation + Value of Equity Award (including option award value).
d) Relationship between Total Compensation and Market Cap.
e) Includes - Regional Malls, Shopping Centers and Other Retail REITs
Source: SNL Financial and THE BRADFORD GROUP

compensation plan and programs, as well as the degree of clarity in the criteria and rationale for decisions on the part of Compensation Committees. It also provided some interesting insight into the challenges of governing executive compensation faced by Boards and Management, and offered opportunities for improving the art and science of effective compensation plans and their disclosure. Some highlights in addition to the information by property group in Table 7 include:

Many explanations of the evaluation criteria and the methods for incentive compensation were vague. Although few companies clearly presented the essence of the specific methodology for determining bonuses (15.6% for Annual Bonus and 2.3% for long-term incentives), industry experience however, concludes that many more companies have specific methods for determining incentive payouts that are not that well defined in the Proxy.

Bonus award guidelines using performance targets related to percentage of base salary are far more prevalent in the industry than would be discerned in a review of the Proxy Statements, ironic in world where clarity in rationale enhances governance oversight.

Many companies offer general and broad evaluation criteria for incentive compensation, listing multiple factors and indicating absolute and relative performance measures, but do not provide distinction as to which criteria are considered, and to what degree, for annual vs. long-term incentive.

Almost all mention comparison against "market competitive" compensation levels, but less than half define this broad and sweeping rationale with specific levels such as median or 75th percentile. Peer groups companies are not mentioned except in some cases with the performance graph, are critical to the reliance on "market competitive" decisions. The importance of retention and the dependence on the market competitive rationale would argue for more disclosure information rather then less.

In almost all cases, the discussion of compensation was disaggregate (presenting each component of compensation separately), rarely mentioning total cash vs. equity compensation relative to total remuneration, nor changes in compensation from prior years.

Despite requirements for 3 years of disclosure of compensation, growth/change over these several years and comparisons to performance over the same period were not presented in any REIT proxy. Change from year to year is at the heart of decisions and the association with performance.

Statements of compensation philosophy were nearly universal, and eerily similar (and in some cases nearly identical), but discussion of a company compensation strategy was sparse.

Plenty of verbiage was presented relating to the purposeful decisions of "aligning" executives and compensation to strategic objectives, but a specific compensation strategy built to integrate with company strategy was virtually never mentioned as an approach or component of governance.

In no case was management incentive payout on an aggregate basis, relative to financial performance, profits, price change or value added mentioned or considered in the Compensation Committee Report, despite a range of standard economic theories of real estate management value added in publicly held companies.

REITs are following the trend for diversification of long-term compensation vehicles, using performance vesting, performance units, performance shares, and shareholder value plans, even going further with unit and option programs on underlying OP Units.

Compensation Committees are appropriately conservative and cautious. Many believe that the more you say, the more you open yourself to be criticized. Yet, it seems that the optics of sweeping general policy oriented language regarding shareholder alignment, strategic objectives and appropriate discretion leaves an equal vulnerability. Further, "meeting the spirit and letter of SEC disclosure" requirements means something different to each company, Board and their counsel. These strongly impact the Proxy presentation. However, in a more demanding world of scrutiny, and in an industry maturing and increasing as a standard investor alternative, simple disclosure must transition to meaningful communication.

## Looking Ahead – Issues and Strategy for REIT Compensation

Many trends and changes are occurring and should be included in the thinking and planning of executives and Boards over the next year or more. A few of the many important trends and changes include:

CEO and senior team level base salary focus is moving away from annual orientation to multi-year structures/adjustments, shifting more emphasis onto performance based compensation structures.

The continuing challenge in separating job "expectations" from "performance" emphasizes the need for clarity in the definitions of performance criteria, weighting and compensation practices, particularly as national surveys (multiple industries) find 60% to 80% of companies report lackluster results. The issues – communication, measurement and alignment.

Less emphasis on strictly annual bonus criteria, allowing elements of multi-year performance evaluation using rollover, deferral and payout multiple opportunities designed for achievement of applicable real estate development, investment, financial and operating incentive criteria.

## Payout of a portion of cash incentive in shares, and the use of deferred compensation programs.

Benchmarking methods will transform as the availability of data increases and the issues inherent in Peer Group definition, sampling and static metrics give way to dynamic relationship and a broader context.

Although potentially delayed, FASB policy regarding Share Based Payments will likely be implemented soon, changing the accounting treatment of long-term compensation awards and option pricing methods, and as well creating greater parity among vehicles, opportunities for creative structuring, and unique consideration for other than time vesting.

Compensation decisions will reduce their reliance on the "peer and market mirrored" bottom-up assessment of disaggregated compensation components, building instead an assessment process from top-down, emphasizing total compensation comparisons, relationship to performance over time, and a strategic framework for decisions able to adapt to the specific needs of companies.

Pressure for greater disclosure and greater clarity in disclosure as part of the response to public company issues of executive compensation. Companies and their Boards will discover that disclosure is much more than just presenting facts, and its lasting value is one of communication – the company's message should dominate over the mandatory – emphasizing not just compensation value, but more so … the value of compensation.

Boards and Compensation Committees will need to be more involved, comprehensive and more strategic in their governance of executive compensation, and it should be reflected in their compensation for meeting the challenges.

At the confluence of executive compensation, leading

Table 7

## REIT Compensation Program Characteristics - Top 5 Executives - As Presented in Annual Proxy Statement 2003

Percentage of Equity REITs overall and within each Property Sector

| | Equty REITs (1) | Health Care | Hotel | Industrial | Diversified | Office | Retail (2) | Residential/MF | Self-Storage |
|---|---|---|---|---|---|---|---|---|---|
| **# of Companies =** | 128 | 6 | 10 | 10 | 12 | 24 | 35 | 19 | 3 |
| **Cash Compensation Awards - 2003** | | | | | | | | | |
| Ave. Max CEO Opportunity as % of Base | 154.5 | 225.0 | 173.3 | 256.0 | 125.0 | 150.0 | 117.0 | 110.0 | 200.0 |
| Average CEO Payout as % of Base | 81.1 | 80.8 | 74.8 | 83.6 | 60.9 | 103.8 | 80.1 | 80.1 | 66.7 |
| % of CEOs Reporting $0 Bonus Award | 25.0 | 33.3 | 20.0 | 10.0 | 33.3 | 16.7 | 0.0 | 31.6 | 33.3 |
| Bonus Payout (all or a portion) in Stock Required | 9.4 | 0.0 | 0.0 | 0.0 | 16.7 | 12.5 | 5.7 | 15.8 | 33.3 |
| **Criteria for Annual Cash Awards (3)** | | | | | | | | | |
| - Financial/Operating Performance (a) | 69.5 | 33.3 | 60.0 | 70.0 | 75.0 | 75.0 | 65.7 | 78.9 | 100.0 |
| - Income (b ) | 3.1 | 0.0 | 0.0 | 20.0 | 8.3 | 0.0 | 0.0 | 0.0 | 0.0 |
| - Cash Flow (c ) | 2.3 | 0.0 | 10.0 | 0.0 | 8.3 | 0.0 | 0.0 | 0.0 | 0.0 |
| - Dividend Payout (d) | 1.6 | 16.7 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 5.3 | 0.0 |
| - Total Return (e) | 24.2 | 0.0 | 10.0 | 20.0 | 41.7 | 25.0 | 20.0 | 36.8 | 0.0 |
| - Individual (f) | 47.7 | 33.3 | 40.0 | 30.0 | 50.0 | 58.3 | 54.3 | 57.9 | 66.7 |
| - Other/Discretionary (g) | 82.0 | 100.0 | 70.0 | 70.0 | 91.7 | 70.8 | 94.3 | 73.7 | 100.0 |
| Defined as Entirely Discretionary by Committee | 21.1 | 0.0 | 0.0 | 0.0 | 25.0 | 16.7 | 31.4 | 36.8 | 0.0 |
| Specific Formula to Determine Bonus Award (3) | 15.6 | 16.7 | 30.0 | 20.0 | 16.7 | 16.7 | 14.3 | 10.5 | 0.0 |
| **Selected Cash Compensation Programs In Place** | | | | | | | | | |
| Multi-Year Bonus Plan (3 yrs or <) | 3.1 | 0.0 | 0.0 | 0.0 | 0.0 | 8.3 | 2.9 | 5.3 | 0.0 |
| LTIP - Cash Plan (3 yrs or >) | 7.8 | 0.0 | 0.0 | 0.0 | 0.0 | 8.3 | 5.7 | 21.1 | 0.0 |
| Deferred Compensation Plan | 18.8 | 33.3 | 0.0 | 30.0 | 33.3 | 25.0 | 8.6 | 31.6 | 0.0 |
| **Long-Term (LT)/Equity Compensation Awards - 2003** | | | | | | | | | |
| Grants of Options - Common Shares | 39.8 | 66.7 | 10.0 | 60.0 | 41.7 | 37.5 | 34.3 | 36.8 | 66.7 |
| Restricted Shares (w/, w/o Performance Vesting) | 67.2 | 66.7 | 80.0 | 80.0 | 58.3 | 70.8 | 68.6 | 57.9 | 66.7 |
| Restricted Shares and No Options | 39.1 | 33.3 | 70.0 | 40.0 | 41.7 | 41.7 | 42.9 | 21.1 | 33.3 |
| Options and No Restricted Shares | 11.7 | 33.3 | 0.0 | 20.0 | 25.0 | 8.3 | 8.6 | 0.0 | 33.3 |
| Both Options and Restricted Shares | 28.1 | 33.3 | 10.0 | 40.0 | 16.7 | 29.2 | 25.7 | 36.8 | 33.3 |
| Neither Options or Restricted Shares | 21.1 | 0.0 | 20.0 | 0.0 | 16.7 | 20.8 | 22.9 | 42.1 | 0.0 |
| Awards of OP Units/or OP Unit Options | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Performance Unit Awards - Shares | 7.0 | 16.7 | 0.0 | 10.0 | 0.0 | 4.2 | 5.7 | 10.5 | 0.0 |
| Performance Unit Awards - OP Units | 0.8 | 0.0 | 0.0 | 0.0 | 0.0 | 4.2 | 0.0 | 0.0 | 0.0 |
| **Criteria for LT/Equity Awards (4)** | | | | | | | | | |
| - Financial/Operating Performance (a) | 23.4 | 33.3 | 30.0 | 40.0 | 16.7 | 12.5 | 20.0 | 42.1 | 0.0 |
| - Income (b ) | 2.3 | 0.0 | 10.0 | 10.0 | 0.0 | 4.2 | 0.0 | 0.0 | 0.0 |
| - Cash Flow (c ) | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| - Dividend Payout (d) | 2.3 | 16.7 | 0.0 | 0.0 | 0.0 | 0.0 | 2.9 | 5.3 | 0.0 |
| - Total Return (e) | 34.4 | 33.3 | 50.0 | 60.0 | 8.3 | 29.2 | 28.6 | 42.1 | 0.0 |
| - Individual (f) | 25.8 | 16.7 | 40.0 | 30.0 | 8.3 | 20.8 | 28.6 | 26.3 | 66.7 |
| - Other/Discretionary (g) | 88.3 | 83.3 | 80.0 | 90.0 | 100.0 | 83.3 | 88.6 | 94.7 | 100.0 |
| Specific Formula Determines LT Incentive Award (3) | 2.3 | 0.0 | 0.0 | 10.0 | 8.3 | 0.0 | 0.0 | 5.3 | 0.0 |
| **Selected LT/Equity Compensation Programs in Place (5)** | | | | | | | | | |
| OP Unit Awards or Options | 3.1 | 0.0 | 10.0 | 0.0 | 0.0 | 4.2 | 2.9 | 5.3 | 0.0 |
| Performance Units (h) | 21.9 | 16.7 | 20.0 | 20.0 | 16.7 | 25.0 | 17.1 | 31.6 | 33.3 |
| Investment - Shareholder Value | 2.3 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 15.8 | 0.0 |
| Other Plans (I) | 14.1 | 16.7 | 10.0 | 0.0 | 16.7 | 25.0 | 8.6 | 15.8 | 33.3 |
| Defined Benefit Plan | 4.7 | 0.0 | 0.0 | 0.0 | 8.3 | 0.0 | 11.4 | 0.0 | 0.0 |
| Executive Ownership Guidelines | 5.5 | 0.0 | 10.0 | 0.0 | 8.3 | 12.5 | 2.9 | 5.3 | 0.0 |

(1) Manufactured Home REITs (5) and Specialty REITs (4) are included in Total REITs, but are not separated by Sector.
(2) Includes Regional Mall (9) + Shopping Center (18) + Retail: Other (8) Specialties.
(3) Description of weighting of various performance criteria and nature of the formula are presented in summary form in Proxy Statement/Committee Report.
(4) As defined, presented and represented in Proxy Statement disclosure on Executive Compensation and supported by the Compensation Committee Report - any or all may be measured on absolute an or relative basis vs. Peer or Industry Index, or at Company, Business Unit or Division level.
(5) Specific active Programs generally other than those defined in Company adopted Incentive Plans (Omnibus Plans).
a) FFO/FFO/Share targets, AFFO, NOI, Same Store NOI, ROI, or ROE.
b) Net Income or EPS
c) Cash Flow or EBITDA
d) Yield/Dividend Growth or Payout Ratio
e) Total Return - FY or Multiple Years
f) Individual Performance, REIT market compensation benchmarks, terms of employment agreeements, and for Long-Term incentive - position/level, tenure, and current holdings.
g) Other Criteria - e.g. - asset transactions, capital restructure events, operating performance, etc./ Dominantly at Committee Discretion/ No Weightings Used/ Not defined in Proxy or Compensation Committee Report/or Criteria same for Bonus and Long-Term incentive decisions.
h) Usually an alternative LT vehicle in adopted Company Incentive Plans.
I) For example - Purchase Plans, Development Bonus Plans, Dividend Unit Plans, Profit Share, Shareholder Value Plan.
Source: THE BRADFORD GROUP

governance and the future of REITs are many questions and considerable opportunity. The year 2003 has been good for REITs and REOCs and their executives, for the most part. The market performance and income record is remarkable, but investor's long-term affair with the industry is unknown. REIT Boards have been cautious not to create an issue related to compensation, but the high tide of market performance could change the environment. Attracting, retaining and motivating REIT leadership is where the rubber meets the road for compensation, and why effective assessment methods, policy and practice are critical to management and to Boards. We may soon be in search of the opportunity to integrate recent market history with the potentially slow improvement of real estate fundamentals and future financial performance. Both the art and the science of compensation decisions and governance will continue to evolve, and the search for an effective and defensible method to demonstrate pay and performance relationships over time is here now as a strategic challenge.

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*Editorial Note: Data used in this article was compiled by SNL Financial and is available in the 2003 SNL Real Estate Executive Compensation Review. For more information please call (434) 977-1600 and ask for the Sales Department.*