

# Research & Analysis:

## Executive compensation review '04: Rewards tempered by caution

By James Wright

*Editor's note: This is the first in a four-part series examining executive compensation in the REIT/REOC sector, guest authored by James Wright, CEO of The Bradford Group — a Los Angeles-based advisory firm that focuses on executive compensation and other important corporate-management issues in the real estate industry. The next three parts will run sequentially on a daily basis.*

REITs and REOCs have outperformed the broader markets for more than five years, and for now the momentum seems mainstream. Winds of change and predictions of declining market performance in 2004 did not occur. In an environment of optimistic expectations from improving fundamentals, sustained capital flow and investor confidence, apparently REIT/REOC boards and compensation committees exercised careful discretion in compensation awards not to overreach, while recognizing performance and maintaining market competitiveness. Retaining and recruiting talent remains a priority, as compensation becomes increasingly strategic and the alignment of performance and compensation requires greater context, clarity and disclosure.

Except for the news of increasing CEO separations and the size of some of their associated exit packages — which are often more contractual than discretionary — media stories of egregious executive compensation across American business have subsided over the past two

years. Why? Things have apparently changed and the pendulum has begun to swing. Boards and compensation committees have been even more cautious and diligent in designing performance-contingent incentives and in awarding compensation to key executives — a transition that will likely continue for several more years. This overall director caution is reflected in the real estate industry as well, as most indications from compensation statistics reflect both well-deserved financial rewards, yet a mild softening compared to 2003.

REIT and REOC executives are bullish; for 2004 and so far in 2005, they will let the numbers do the talking: fundamentals are strengthening, financial performance in most sectors is improving and market returns are relatively strong. Perhaps these factors represent the rare perfect set of circumstances for executive compensation, but in reality it is a situation requiring a delicate balance of reward, incentive, retention, governance, market perception, investor confidence and potential changes in the future drivers of the business.

As was true last year, outperformance creates a safe harbor, avoiding much questioning over compensation decisions in an industry heavily owned institutionally, closely scrutinized and not inclined to overstep. Boards have also been careful to temper high market performance directly with compensation, factoring the reality of management control versus windfall and the corresponding opportunity to exercise vested options and in some cases reload.

### Highlights of 2004:

This year's examination and analysis of executive compensation in the REIT/REOC industry, based on data culled from relevant disclosures in companies' most recent annual proxy filings, reveals several important conclusions and directions for the REIT/REOC industry, further developed in this review, including:

- A back-to-back sequence of very strong market performance, as total returns of 31.9% in 2004 for REITs was nearly as strong as 2003's 37.5% total return, and REOC sectors returned 40% to 45% again in 2004. The three-year total return for REITs/REOCs was approximately 65%.

- Improving real estate fundamentals demonstrated in REIT/REOC financial performance in 2004, with the building of a powerful platform for sustained investment and confidence.

- Continuing evidence of an underlying association between executive compensation and REIT/REOC performance, defining a powerful strategic framework that can strengthen leading governance, effective design and clear disclosure. However, though this relationship overall is strong, it is not perfect. Almost a third of REITs/REOCs are significantly out of alignment (over or under) relative to compensation and performance — some for specific strategic or tactical rationale, others less so.

- Despite downward pressures, REIT dividends — at approximately 5% annually — remain an attractive advantage to investors, particularly

compared to 10-year Treasury yields — at 3.92% — and broader market company dividends averaging 1.7%.

- Pricing of REIT/REOC shares has created the "currency" for an active M&A environment, changing and strengthening the industry through consolidation and privatization and fueling a host of IPOs. As of 2004 — and since 2000 — the industry has experienced a net loss of 10 companies, with 41 public/private acquisitions and 31 IPOs.

Conclusions can vary depending on the statistic examined, but indications are that average compensation for the top five executives at REITs/REOCs increased well within the bounds of comparison to 2003 and industry performance in 2004:

- Average cash compensation rose 5.5% versus last year's growth of over 11%, but remained strong over three years at an annual rate of 11.6%.

- Financial performance for 2004 as measured by the average of individual company FFO growth rates was 25.3%, while the year-to-year growth of average FFO (\$) among all companies was only 1.8% in 2004, but 13.5% per year over the three-year period.

- Average total compensation rose nearly 10% in 2004 versus 6.1% in 2003, and has sustained growth of nearly 15% per year over the past three years.

- Average market capitalization rose 24.1% in 2004 — 17.9% per year over three years — while average net income growth rose 69.1% in 2004 and 24.7% per year over three years.

In an examination of the value of retention and performance on REIT/REOC executive teams in the industry, research revealed that executives who have held the same position in the same company since 2001 received between a 3% and 14% premium in average total cash compensation increase

in 2004 and between a 5% and 10% premium in average total compensation value, compared to similar figures for the position overall. Other observations include:

- Use of restricted shares and performance units/shares in long-term awards continues to be favored as a percent of total compensation, but aggregate share award value declined by 4% in 2004. Stock option awards continued to decline — by 27% in 2004 — but option-award value increased by 18% in 2004 due to market pricing.

- REIT/REOC CEO compensation appears quite conservative compared to statistics from CEOs outside the real estate industry indicating average compensation increases below national averages in almost all categories.

- The aggregate value of the 10 highest REIT/REOC executives based on total compensation in 2004 remained unchanged from 2003.

- Rising market values offered the financial incentive to exercise vested option again in 2004, as the top 10 REIT/REOC companies in realized option exercise value among their top five executives, as per the proxy review, increased by 1.7% over the top 10 companies in 2003 — seemingly a conservative conversion level compared to industry performance.

- Increasing compensation levels for the top five REIT/REOC executives as presented in the proxy review was again demonstrated in 2004 as more reached the "clubs" of \$1.0 million benchmark in annual total cash compensation (up 43% in 2004), and/or the \$3.0 million mark in total compensation value (up 27%).

### Enduring market strength?

Many predicted REITs would witness the other side of an economic cycle in 2004 by losing ground to capital

shifts to other growing industries and fall victim to increasing interest rates. But stronger real estate fundamentals from economic growth have strengthened REIT/REOC financial performance and increases in short-term interest rates have not pushed long-term rates into a range where REIT returns have been challenged by other investments — a situation still unclear to many economists. Most CEOs in the real estate industry believe rates will have to rise by 3% or more before it will break the momentum. Market performance in price change and total return for the industry was strong nearly across the board in 2004 (Table 1), reinforcing a remarkable three-year performance. A tough first quarter of 2005 was followed by a rally in the second quarter, ending the first half of 2005 again far ahead of the broader markets.

The growth of REIT/REOC market values in 2004 reflects investor confidence, opportunity for greater income versus other vehicles, the issuance of equity, foreign investment and the overall strength of the market and the industry. M&A activity is a testament to the currency value of real estate stock prices, economies of scale, the costs of meeting regulation, and the abundance of capital seeking placement in real estate as an asset class. Evidence of the power of real estate capital and pricing can be seen in the table below, which shows M&A and IPO activity since 2000.

In 2004, REIT equity and debt offerings totaled \$26 billion, with \$2.7 billion in IPOs. Although still strong, 2005 to date has shown some tapering of this pace, as debt and equity offerings in the first half of 2005 declined to \$11 billion from \$15 billion in 2004.

As REIT/REOC fundamentals improve, the more defensive strategies of managing occupancy and cash for div-

Table 1  
**Summary of Total Return and Price Change - REITs and REOCs**

	Three-Year - 2001 to 2004		One-Year - 2003 to 2004		2005 - YTD - 6/30/05	
	Total Return	Price Change	Total Return	Price Change	Total Return	Price Change
<b>Price Change</b>						
S&P REIT	NA	54.68%	NA	24.78%	NA	3.54%
S&P 500	NA	5.56%	NA	8.99%	NA	-1.70%
NASDAQ	NA	11.54%	NA	8.59%	NA	-5.45%
DJIA	NA	7.60%	NA	3.15%	NA	-4.71%
<b>Total Return</b>						
REIT Equity - SNL Index	88.53%	55.90%	31.91%	24.59%	6.48%	3.96%
NAREIT - Equity Index	87.33%	54.78%	31.58%	24.35%	6.38%	3.68%
Homebuilders	179.62%	174.74%	36.21%	34.66%	25.90%	25.58%
<b>By Market Cap</b>						
<b>REIT+REOC</b>						
Real Estate >\$2B	87.29%	60.68%	35.39%	29.44%	7.08%	5.09%
Real Estate >\$1B - \$2B	85.78%	53.32%	30.27%	22.15%	8.25%	5.70%
Real Estate \$500M - \$1B	85.38%	55.13%	34.20%	27.32%	6.88%	4.07%
<b>REIT</b>						
REITs >\$2B	85.37%	54.56%	33.45%	26.50%	6.58%	4.19%
REITs >\$1B - \$2B	88.81%	53.75%	28.30%	19.74%	6.99%	4.20%
REITs \$500M to \$1B	83.88%	49.71%	32.28%	24.94%	6.68%	3.83%
REITs < \$500M	96.62%	60.70%	23.09%	16.26%	2.96%	-0.02%
REITs < \$250M	100.82%	54.31%	16.47%	8.76%	3.68%	0.93%
<b>By Sector Focus - REITs</b>						
Diversified	88.33%	54.67%	32.54%	24.56%	5.68%	3.18%
Healthcare	105.50%	63.68%	22.97%	15.23%	4.30%	0.91%
Hotel	70.76%	52.48%	32.65%	29.95%	2.87%	1.29%
Industrial	103.25%	70.68%	30.65%	24.18%	1.28%	-0.85%
Office	56.37%	27.38%	22.30%	14.96%	7.02%	4.14%
Residential	57.59%	28.27%	32.64%	24.04%	5.50%	2.78%
Multi-Family	59.28%	30.01%	34.58%	26.38%	5.70%	2.97%
Manufactured Homes	32.83%	1.62%	7.88%	-7.04%	1.57%	-0.69%
Retail	151.38%	109.75%	40.76%	33.49%	8.60%	6.24%
Enclosed Mall	181.47%	137.51%	46.46%	38.94%	12.69%	10.40%
Shopping Center	122.64%	84.01%	35.86%	28.94%	5.21%	2.90%
Self Storage	82.54%	56.55%	29.39%	24.06%	13.16%	10.99%
<b>Real Estate Operating Companies</b>						
<b>REOCs</b>						
Hotel	17.55%	16.45%	46.73%	45.45%	5.79%	5.60%
Other	38.29%	40.60%	42.00%	40.24%	21.25%	20.55%

Real Estate = REIT + REOC

Source: The Bradford Group and SNL Financial LC

idends will give way to a period of planning and managing core business growth, opportunities for development, and value-added investments. With increasing foreign investment in real estate (including REITs/REOCs) up 12% in 2004, foreign investment by REITs/REOCs in assets and development (particularly in Europe) and a

baby boom generation focused on retirement and income, the question remains as to whether we will look back on the last few years as a market cycle or one where a new long-term investor following was built. Equally important is whether the past few years have formed lasting change in real estate economics — yields and capital flow.

### The big picture: The link between compensation and performance

For executive compensation in 2004, both the short and longer view of increases in total cash compensation, total compensation and restricted share (or other) versus option awards need to be placed in an appropriate context

with performance. Over time, integrating the overall relationship of compensation and performance will create the essential and powerful governing framework to allow a more systematic rationalization for decisions, the facilitation of effective motivation, retention and the development of REIT/REOC leadership. Linking compensation to performance through the mechanics of incentive design is only a part of the story; the balance is whether a real relationship between the two is developed and effectively managed over time.

With the performance track record over the past few years, and an increasingly loyal following in the marketplace, the ability for REITs/REOCs to both stay under the larger-cap company/industry investment radar screen and to build long-term investor commitment to the sector from its diversification and income advantages may be in conflict. This provides all the more reason for REITs/REOCs to adopt a more strategic approach to management and governing practices of compensation, a framework able to define a

longer-term context of absolute and relative performance and able to more fully integrate with other corporate business objectives and initiatives.

Table 2 and Table 3 examine key statistics related to this framework as of 2004. Table 2 demonstrates that total cash compensation in 2004 and over the past three years has not been out of line with performance. Statistics can vary — particularly examining the change in average compensation or performance compared to the average change in individual growth rates. The

three-year look rightfully steadies the relationship, as the alignment of performance and compensation is a multi-year governance and management process.

For 2004, overall increases in the total cash compensation for the top five executives in the REIT/REOC industry appear to be well within the bounds of associated financial performance. Further, examining the relationship of financial performance (in this case EBITDA) and total cash compensation reflects a strong association in both a

### REIT/REOC M&A and IPO activity since 2000

Year	Companies Merged/Private		REIT/REOC IPOs		Cumulative Net Change
	Companies Per Year	Cumulative Companies	Number of IPOs	Cumulative IPOs	
2000	2	2	1	1	-1
2001	10	12	0	1	-11
2002	12	24	3	4	-20
2003	7	31	6	10	-21
2004	6	37	18	28	-9
2005	4	41	3	31	-10

\* As of 06/30/05

Source: The Bradford Group and SNL Financial LC

Table 2  
Total Cash Compensation vs. Financial Performance - One-Year and Three-Year

Financial Performance				Total Cash Compensation		Relationship
Increase in Average FFO	Average of Individual Company FFO Growth Rate (1)	Increase in Average EBITDA	Average of Individual Company EBITDA Growth Rate (2)	Increase in Average Total Cash Compensation	Average of Individual Co. Total Cash Compensation Growth Rate	Correlation of Total Cash Compensation and EBITDA
<b>One-Year Growth Measures (2003 to 2004)</b>						
1.8%	25.3%	3.4%	49.1%	5.5%	22.7%	0.76
<b>Three-Year Growth Measures (2001 to 2004) (a)</b>						
2.8%	13.5%	1.4%	9.9%	11.6%	17.8%	0.74

(a) All figures are compound annual growth rates - 2001 to 2004.

(1) Median of one-year growth rate = 10.5%

(2) Median of one-year growth rate = 8.3%

All figures for top five executives, across all REITs and REOCs as per proxy.

Source: The Bradford Group and SNL Financial LC

short-term (2004) and long-term (three-year) view. This is the essential foundation for compensation policy, plan design and decision rationale.

Table 3 demonstrates this same result and relationship relative to total compensation and market performance for the top five executives in the REIT/REOC industry. Again, the results of overall statistics reflect a strong association with performance but not an overreach by boards or compensation committees to award market-driven performance.

Over the last three years, REIT/REOC total returns have been approximately 65%, while average total compensation has risen at a rate of 14.8% per year (or 51.3% compounded). The one-year 2004 figures are even more dramatic, with 35% in total return and just under 10% in total compensation. However, growth of average compensation is different than

the average of the growth rates of compensation among the individual companies. For total compensation over the three-year period, the average growth rate was 21%, and for the one-year 2004 period it was nearly 45%.

Utilizing several statistics such as these is the best method to gain a perspective on actual change in both performance and compensation. For aggregate statistics, large and small data, or significant positive or negative changes can balance out to only show only a small difference in an average from year to year. Averaging the range of individual company rates of change is subject to relative variations based on size of company or compensation and magnitude in proportion to any reference year, such as figures demonstrating accelerating IPO growth. However, in either case, each result provides a benchmark of change over a period of measurement, an indicator and not a

definitive or uniquely conclusive answer regarding trend.

What it does tell us, aided by the hindsight of collective results derived from all REIT/REOC proxy filings in 2005, is that industry leaders and their boards have taken a very cautious approach to reward the outstanding performance of the industry. Accounting for both the investment popularity of real estate, its carryover into stock pricing and the hard work of acquiring, divesting and operating to improve financial performance at time of emerging economic growth, compensation committees have mixed the long and short view of past and prospective performance, factoring in market pressures for compensation benchmarks, retention and governing mandates to arrive — without the benefit of aggregate hindsight — at a strong and fair, yet cautious, set of decisions from an overall perspective.

Table 3  
**Total Compensation vs. Market Performance - One-Year and Three-Year**

Financial Performance				Total Cash Compensation		Relationship
Increase in Average Market Capitalization	Average of Individual Company Market Cap Growth Rate (1)	Average of Individual Company Net Income Growth Rate (2)	Total Return (a)	Increase in Average Total Compensation	Average of Individual Company Total Compensation Growth Rate	Correlation of Total Compensation and Market Capitalization
<b>One-Year Growth Measures (2003 to 2004)</b>						
24.1%	38.9%	69.1%	35.0%	9.7%	41.6%	0.82
<b>Three-Year Growth Measures (2001 to 2004) (b)</b>						
17.9%	33.9%	24.7%	65.0%	14.8%	21.2%	0.85

(a) Combined REIT/REOC Total Return not available - figures are estimated from individual REIT and REOC returns.

(b) All figures are compound annual growth rates - 2001 to 2004.

(1) Median of one-year growth rate = 29.8%

(2) Median of one-year growth rate = 19.5%

All figures for top five executives, across all REITs and REOCs as per proxy.

Source: The Bradford Group and SNL Financial LC

## Part 2

### Compensation Trends

An overview of the compensation and performance results for the industry provides a backdrop for a closer look at the specific aspects of executive compensation and the correlating growth attributes. These statistics will provide indications of the direction and magnitude of compensation change in 2004.

#### Cash and total compensation

Trends in compensation for CEOs and the top five highest-paid executives across all REITs and REOCs are shown

in Table 4, which examines year-to-year change in average total cash and total compensation between 2003 and 2004, as well as the three-year annual growth rate from 2001 to 2004, and the average individual company growth rates in these same compensation components. Growth rates are shown for all 184 companies by investment structure — with 160 REITs and 24 REOCs — by four market-capitalization categories and by eight property sectors. Note that change in both total cash and total compensation for CEOs varies widely between REITs and REOCs, but less so

for all top five executives, indicative of differences in cash and long-term incentive policy and practice, the financial structure of the company and its real estate risks. Variations among market-capitalization strata are more balanced, while differences among property sectors reflect sector economic conditions over the one- and three-year periods.

#### Key positions

Average compensation figures for 2004 are presented in Table 5 for five key positions, along with several statis-

Table 4  
Compensation Trends by REIT/REOC, Market Cap and Property Sector

	No. of Co.'s	Chief Executive Officer						Top 5 Executives (†)					
		Total Cash			Total Compensation			Total Cash			Total Compensation		
		One-Year	Three-Year	Average	One-Year	Three-Year	Average	One-Year	Three-Year	Average	One-Year	Three-Year	Average
		'03 - '04 (a)	'01-'04 (b)	'03 -'04 (c)	'03 - '04 (a)	'01-'04 (b)	'03 -'04 (c)	'03 - '04 (a)	'01-'04 (b)	'03 -'04 (c)	'03 - '04 (a)	'01-'04 (b)	'03 -'04 (c)
<b>REIT + REOC</b>	184	7.0%	7.7%	29.4%	4.4%	12.5%	55.7%	5.5%	11.6%	22.7%	9.7%	14.8%	41.6%
<b>Inv. Structure</b>													
REIT	160	11.4%	9.0%	35.1%	10.9%	15.3%	59.5%	5.5%	11.6%	24.4%	10.2%	15.1%	44.4%
REOC	24	-15.2%	1.7%	16.2%	-31.7%	-3.0%	15.1%	5.1%	12.1%	11.2%	6.8%	13.5%	23.4%
<b>Market Cap (2)</b>													
Over \$5.0B	17	2.7%	4.8%	10.6%	11.9%	8.3%	34.2%	19.2%	14.8%	17.1%	26.7%	18.6%	46.4%
\$1.0B - \$5.0B	67	11.0%	11.4%	31.1%	-5.8%	17.0%	25.3%	2.7%	14.0%	12.1%	-3.9%	17.2%	16.3%
\$500M - \$1.0B	29	25.0%	14.2%	35.9%	131.5%	26.4%	140.1%	20.7%	17.4%	21.9%	83.6%	24.1%	96.4%
Under \$500M	71	16.3%	13.0%	43.1%	20.7%	13.7%	53.4%	8.8%	17.1%	41.6%	24.6%	20.4%	46.2%
<b>Prop. Sector (3)</b>													
Diversified	30	8.2%	4.4%	16.8%	-9.8%	8.9%	28.5%	15.9%	10.0%	11.2%	15.5%	17.7%	25.0%
Health Care	13	-2.3%	2.1%	14.2%	27.6%	-1.9%	31.9%	-8.5%	11.1%	-1.2%	9.1%	5.7%	23.4%
Hotel	30	-12.9%	4.7%	29.9%	-11.5%	3.0%	63.7%	4.7%	13.8%	60.8%	13.5%	13.3%	98.8%
Industrial	10	21.5%	2.7%	33.4%	-19.3%	11.1%	0.2%	13.0%	7.9%	18.0%	-9.4%	15.8%	-0.8%
Multi-Family	25	56.1%	18.4%	89.5%	29.0%	8.7%	81.2%	31.4%	15.9%	54.3%	26.0%	7.0%	71.9%
Office	29	5.8%	16.2%	23.2%	-2.0%	28.6%	28.9%	-8.0%	11.0%	-1.3%	-8.7%	15.9%	0.5%
Retail	37	-2.2%	1.7%	9.8%	14.1%	17.7%	43.1%	1.4%	9.0%	5.0%	15.0%	20.5%	27.6%
Self-Storage	5	19.0%	15.7%	122.3%	72.0%	1.0%	201.3%	55.9%	24.0%	40.2%	51.3%	20.5%	95.0%

(1) Top five executives across all REITs and REOCs as reported in proxy - average of total cash or total compensation for all five reported.

(2) Market Capitalization - Year End 2004

(3) Manufactured Housing sector not shown (5 companies).

(a) Year-to-year change in average compensation.

(b) Compound annual growth rate (CAGR) - Three years of average compensation.

(c) Average of individual company growth rates in compensation component.

Source: The Bradford Group and SNL Financial LC

tics to provide additional perspective. For each position and compensation component, change in average compensation from 2001 to 2004 is only one indicator of increase. The context of interpretation is further developed by the inclusion of the three-year compound annual growth rate — which tends to smooth year-to-year variations and is a strong indicator of trend and an excellent benchmark — and the average of the individual rates of growth among all individual companies. This figure is

generally higher than the rates of change in averages, as the variations in magnitude among individual companies reflect not only a wide range of compensation practices and decisions, but the specific circumstances of retention, recruitment of new employees, internal job changes, special circumstances and, in some cases, awards involving multiple years of performance.

Table 4 also reflects the trends in executive responsibility, with CFOs and chief general counsels (CGC) receiving

considerable additional compensation — particularly in the long term — resulting from the demands of managing the implementation of the requirements of Sarbanes-Oxley and other regulations, as well as COOs who have guided the success of extracting additional FFO growth and tenant relations from existing portfolios.

### Compensation mix

Table 6 presents the percentage mix of REIT/REOC executive compensa-

Table 5  
Compensation Components by Position - 2004 and Trends

	Cash Compensation (a)				Long-Term Compensation (a) (b)				Total Comp.
	Base Salary	Annual Bonus	Bonus as a % of Base	Total Cash Comp.	Restricted Share Award Value	Options Granted	Option Award Value	Other Long-Term	
<b>Chief Executive Officer</b>									
2004	\$439,444	\$562,748	128.1%	\$968,262	\$1,379,199	149,696	\$1,010,497	\$272,934	\$2,214,773
Growth '03/'04	6.4%	6.9%	-	7.0%	-14.5%	-24.6%	22.9%	105.3%	4.4%
Three-Year CAGR	3.2%	8.0%	-	7.7%	28.2%	-4.8%	7.2%	26.2%	12.5%
Avg. Growth Rate '03/'04	13.7%	32.8%	-	32.6%	32.4%	-5.9%	19.7%	63.2%	55.7%
<b>Chief Operating Officer</b>									
2004	\$352,092	\$319,779	90.8%	\$656,306	\$630,417	97,693	\$646,327	N/A	\$1,305,509
Growth '03/'04	4.8%	11.6%	-	5.9%	-29.4%	-9.9%	41.9%	N/A	0.3%
Three-Year CAGR	0.7%	9.5%	-	4.4%	2.3%	-4.8%	6.7%	N/A	-0.3%
Avg. Growth Rate '03/'04	15.9%	32.3%	-	21.3%	55.2%	0.1%	42.6%	N/A	40.4%
<b>Chief Financial Officer</b>									
2004	\$261,412	\$232,229	88.8%	\$493,022	\$526,424	72,516	\$467,118	\$83,107	\$1,047,405
Growth '03/'04	4.5%	17.9%	-	8.4%	-0.3%	-15.1%	35.1%	52.6%	19.2%
Three-Year CAGR	0.7%	10.5%	-	6.0%	7.3%	-0.7%	13.5%	24.4%	8.7%
Avg. Growth Rate '03/'04	20.4%	37.8%	-	20.2%	48.1%	5.0%	38.1%	28.0%	44.9%
<b>Chief Investment Officer</b>									
2004	\$283,426	\$277,923	98.1%	\$572,571	\$600,686	59,710	\$417,878	\$64,603	\$1,167,447
Growth '03/'04	0.2%	32.0%	-	9.1%	8.4%	-35.2%	2.2%	-1.9%	6.4%
Three-Year CAGR	-2.5%	-5.5%	-	-3.5%	0.5%	-25.4%	-6.6%	-15.1%	-3.4%
Avg. Growth Rate '03/'04	8.3%	27.4%	-	15.4%	27.9%	-22.4%	-13.4%	60.4%	24.2%
<b>Chief General Counsel</b>									
2004	\$258,090	\$190,905	74.0%	\$463,484	\$390,210	34,013	\$184,639	\$56,106	\$871,817
Growth '03/'04	11.2%	18.0%	-	16.3%	28.4%	-15.5%	12.2%	109.0%	32.1%
Three-Year CAGR	4.3%	14.8%	-	11.7%	28.9%	-17.0%	-7.2%	55.7%	16.9%
Avg. Growth Rate '03/'04	12.9%	28.4%	-	14.5%	44.2%	0.6%	31.8%	27.7%	44.6%

Note: All compensation figures include both REITs and REOCs, and are growth rates based on the average of the compensation component.

(a) Includes REITs and REOC, and for each position -

- Average compensation for 2004.

- Growth rate of average compensation - '03 to '04.

- Three-year (2001 to 2004) Compound Annual Growth Rate (CAGR) in average compensation.

- Average of individual company growth rates in compensation component.

(b) Option Value is estimated using 20% of grant price times the number of optioned shares.

Source: The Bradford Group and SNL Financial LC

tion components for key positions over the past three years. The relatively steady proportion of total cash compensation shown is created from a declining share related to base salary and an increasing share from annual bonus and other annual cash compensation. These figures are relative to total compensation, which is in turn influenced by the value of restricted-share awards and the method of valuation of option awards. Although the method of option valuation is the same for all periods (the SNL method is 20% of grant price estimate), the rising market value of REIT stocks has no doubt impacted the relative proportion of otherwise rising cash components. Other long-term compensation is an interesting and changing component of compensation. With increasing long-term vehicles including multiple years of performance-based triggers, this category can fluctuate significantly from company to company and over the industry.

### Retention: Is there a "same-store, same-executive" advantage?

Same-store financial and operating statistics are a common benchmark for company performance. But what about the analogy in compensation for REIT/REOC executives who perform with the same company in the same position on an executive team year after year? Would there not be a premium for their loyal commitment and knowledge base of the company, its assets and operations? Thus, we decided to compare the overall trend in executive compensation components where the incumbent executive has been in the same position since at least 2001.

Table 7 presents this analysis, which clearly demonstrates the advantage of longevity and performance over time. For each of the five positions, and for total cash and total compensation — both in 2004 and for the compound growth rate over the last three years — there is a clear advantage in average compensation as measured by the in-

crease received above the overall average. Although the direction of the result was expected, we believe that this is the first systematic estimate of its magnitude. For total cash compensation, this advantage ranges from 3% to 14% and from nearly 5% to nearly 10% in total compensation.

The same pattern emerges for the compound growth rate over the three-year period — except for the general counsel position — an indication perhaps of greater turnover, more-stable compensation levels or the wide range of variations in the utilization of inside versus outside counsel.

### CEOs versus broader market — underpaid?

REIT/REOC CEO compensation trends have been presented in prior tables, but in this section we examine the components of CEO compensation in the industry more closely and compare those elements to the broader market where many such comparative bench-

Table 6  
Allocation Among Total Compensation Components

		Base Salary	Bonus	Total Cash	Restricted Shares	Option Award Value	Other Long-Term Compensation
<b>Chief Executive Officer</b>	2002	13.2%	14.4%	25.9%	33.4%	35.9%	4.7%
	2003	11.9%	15.2%	26.0%	46.4%	23.7%	3.8%
	2004	12.1%	15.5%	26.7%	38.0%	27.8%	7.5%
<b>Chief Operating Officer</b>	2002	19.5%	12.9%	34.0%	32.8%	32.8%	0.4%
	2003	17.1%	14.6%	31.5%	45.4%	23.1%	0.0%
	2004	18.2%	16.5%	34.0%	32.6%	33.4%	0.0%
<b>Chief Financial Officer</b>	2002	21.5%	13.9%	35.7%	32.5%	28.0%	3.8%
	2003	18.1%	14.2%	32.9%	38.2%	25.0%	3.9%
	2004	16.7%	14.8%	31.4%	33.5%	29.8%	5.3%
<b>Chief Investment Officer</b>	2002	18.9%	12.4%	33.0%	30.0%	32.9%	4.1%
	2003	18.2%	13.6%	33.8%	35.7%	26.3%	4.2%
	2004	17.1%	16.8%	34.6%	36.3%	25.2%	3.9%
<b>Chief General Counsel</b>	2002	26.9%	17.8%	45.8%	30.8%	21.4%	2.0%
	2003	26.0%	18.1%	44.6%	34.0%	18.4%	3.0%
	2004	23.6%	17.4%	42.3%	35.7%	16.9%	5.1%

Includes REITs and REOCs

Source: The Bradford Group and SNL Financial LC

marks are available. Table 8 presents average compensation figures for CEOs by REIT and REOC investment structures, market capitalization and property sector. All compensation figures are averages and indicated rates of change are between averages from prior periods. Several compensation components are presented in order to demonstrate trends in the mix of incentives.

Among the many figures and trends within specific sectors are more general conclusions. CEO total compensation on average for REITs/REOCs has risen by 42% over the past three years — a 12.5%-per-year compound annual growth rate. For REITs alone this figure is over 52%, while the REOC figure — which includes 24 companies — reflects a decline in average compensation in 2004 due largely to significant reductions in long-term compensation value in five companies compared to 2003, multiple year awards and the introduction of two REOC IPOs. Additionally, the size and market dominance of REIT/REOC companies of over \$1.0 billion in market capitalization is clear in the compensation of the CEO, while compensation among the property-sector CEOs on the average varies widely in terms of growth in 2004, as well as over the three-year period, and is dominated by the companies in the office and industrial sectors.

### Comparison with non-real estate trends

The comparison of REIT/REOC CEOs with their counterparts in the broader marketplace again demonstrates the conservative nature of REIT/REOC boards in governing compensation for 2004. Table 9 presents selected statistics of average REIT/REOC CEO compensation and mix and compares those with statistics

Table 7  
**Compensation Growth - All vs. Retained Key Executive Team (a)**

	Total Cash Compensation (1)		Total Compensation (2)	
	2004	CAGR 2002 to 2004	2004	CAGR 2002 to 2004
<b>Chief Executive Officer</b>				
CEO - All	\$968,262	10.2%	\$2,214,773	9.2%
CEO - Same	\$1,104,416	16.3%	\$2,378,421	12.4%
Longevity Advantage	14.1%	6.1%	7.4%	3.2%
<b>Chief Operating Officer</b>				
COO - All	\$656,306	7.7%	\$1,305,509	5.0%
COO - Same	\$677,892	11.3%	\$1,424,292	10.3%
Longevity Advantage	3.3%	3.6%	9.1%	5.3%
<b>Chief Financial Officer</b>				
CFO - All	\$493,022	9.9%	\$1,047,405	19.7%
CFO - Same	\$528,973	13.8%	\$1,116,717	20.2%
Longevity Advantage	7.3%	3.9%	6.6%	0.5%
<b>Chief Investment Officer</b>				
CIO - All	\$572,571	11.4%	\$1,167,447	12.4%
CIO - Same	\$621,660	15.8%	\$1,222,599	14.2%
Longevity Advantage	8.6%	4.4%	4.7%	1.8%
<b>Chief General Counsel</b>				
CGC - All	\$463,484	9.8%	\$871,817	19.7%
CGC - Same	\$518,689	7.3%	\$948,606	17.8%
Longevity Advantage	11.9%	-2.5%	8.8%	-1.9%

(a) REITs and REOCs  
 "All" = Incumbents in position from all companies.  
 "Same" = Incumbents who have been in the same position since 2001.  
 CAGR = Compound Annual Growth Rate for the period 2002 - 2004.  
 (1) Average of the sum of Base Salary + Annual Bonus + Other Cash Compensation.  
 (2) Average of Cash Compensation + Long-Term Compensation  
 (Restricted Share Value + Option Award Value + Other Long-Term Compensation.)  
 Source: The Bradford Group and SNL Financial LC

from both other medium-sized U.S. companies, as well as surveys of larger companies and broader-based markets. Base salary increases for medium-sized companies (closest to REIT/REOC size) ranged from 6% to 10% in 2004 — consistent with the real estate industry — while REIT/REOC bonuses were generally significantly less, netting to total cash compensation differences below an overall national average (including much larger companies).

Long-term and total compensation was also below the national statistics in two surveys. Pay mix comparisons show

REIT/REOC CEOs with a larger long-term component percentage, a smaller bonus portion and a dominance of restricted-share use in long-term compensation, versus national CEO statistics. It also reveals a significant difference in the decline of REIT/REOC usage of options, as their proportion within the long-term compensation category is generally the opposite of CEOs nationally, compared to restricted shares. Despite these differences, national statistics of CEO pay mix have declined from a high level of 76% options (and a low of 12% re-



Table 9  
**Comparison of REIT/REOC CEO Compensation vs. Selected Broad Market Indicators**

	No. of Co.'s	CEO	CEO	CEO	CEO	CEO	CEO Pay Mix - 2004				
		Base Salary Change '03 - '04	Bonus Change '03 - '04	Total Cash Change '03 - '04	Long-Term Comp. '03 - '04	Change in Total Compensation '03 - '04	Base Salary %	Bonus %	Long-Term Comp. %	Restricted Shares % (of Total Long-Term)	Option Value %
<b>REIT + REOC</b>	184	6.4%	6.9%	7.0%	2.5%	4.4%	12.1%	15.5%	73.3%	51.8%	37.9%
<b>Inv. Structure</b>											
REIT	160	7.7%	11.5%	11.4%	10.6%	10.9%	11.9%	14.6%	73.7%	51.6%	37.7%
REOC	24	-2.0%	-5.2%	-15.2%	-47.7%	-31.7%	15.3%	26.4%	67.2%	56.5%	41.4%
<b>Market Cap (1)</b>											
Over \$5.0 Billion	17	-2.4%	5.5%	2.7%	19.0%	11.9%	10.9%	17.6%	72.4%	52.5%	38.4%
\$1.0 Billion to \$5.0 B	67	13.5%	15.8%	11.0%	-15.3%	-5.8%	12.6%	16.8%	69.7%	54.5%	39.9%
\$0.5 Billion to \$1.0	29	8.4%	31.5%	25.0%	424.5%	131.5%	13.7%	12.1%	75.0%	50.7%	37.1%
Under \$0.5 Billion	71	11.3%	0.8%	16.3%	28.0%	20.7%	20.3%	18.4%	63.0%	60.3%	44.1%
<b>Prop. Sector (2)</b>											
Diversified	30	5.9%	26.3%	8.2%	-21.4%	-9.8%	15.2%	18.6%	68.8%	55.2%	40.4%
Healthcare	13	-4.9%	-12.6%	-2.4%	54.0%	27.6%	12.7%	13.4%	74.1%	51.3%	37.5%
Hotel	30	-3.6%	-9.7%	-12.9%	-9.9%	-11.5%	10.1%	14.5%	77.4%	49.1%	35.9%
Industrial	10	8.7%	16.6%	21.5%	-31.8%	-19.3%	11.2%	18.0%	74.1%	51.3%	37.5%
Multi-Family	25	9.7%	30.5%	56.1%	10.0%	29.0%	12.2%	17.3%	66.2%	57.4%	42.0%
Office	29	10.4%	12.3%	5.8%	-7.8%	-2.0%	11.4%	16.9%	71.2%	53.4%	39.0%
Retail	37	11.9%	2.0%	-2.2%	27.6%	14.1%	12.1%	11.7%	77.9%	48.8%	35.7%
Self-Storage	5	10.5%	-26.8%	19.0%	152.8%	72.0%	15.9%	13.2%	71.6%	53.1%	38.8%
<b>Broad Market Indicators</b>											
<b>Medium-Sized Companies (a)</b>	Low	6.2%	28.0%	N/A		12.0%					
	High	10.4%	36.0%	N/A		31.0%					
	Avg.				66.0%						
<b>2004 National Statistics (b)</b>		3.7%		14.5%	17.1%		15.0%	23.0%	62.0%	<b>Share of Long-Term</b>	
										23.0%	57.0%
<b>2004 National Statistics (c)</b>		N/A	N/A	N/A	N/A	(no option exercise)					
						12.6%					
						(w/ option exercise)					
						40.9%					
<b>CPI</b>		2.7%									
<b>Non-Exempt Employees</b>		3.4%									

(a) From Aon Consulting. Medium sized companies = Revenue from \$100 to \$999 million - 1,509 companies.

(b) From Mercer Human Resources Consulting - sample of 350 companies.

(c) From Pearl Meyer & Partners.

(1) Market Capitalization - Year End 2004

(2) Manufactured Housing sector not shown (5 companies).

Note: All compensation figures are both REITs/REOCs, and are growth rates based on the average of the compensation component.

Source: The Bradford Group and SNL Financial LC

compensation for CEOs, with the sum of salary and bonus averaging \$2.5 million, versus a REIT/REOC average of approximately \$975,000 — a reflection of company size. Cross-industry statistics for CEOs showed total compensation of nearly \$6.0 million in 2004 — including proceeds from the exercise of stock options — on significantly lower

overall market performance than REITs/REOCs, as well as a strong showing in financial performance, with profits up 23%. The option exercise value was up 40.9%, compared to a REIT/REOC increase of 51.6%.

But here is an even more startling point of reference: hedge fund compensation. The CEO of ESL Invest-

ments, a major hedge fund, hit \$1.0 billion in compensation value in 2004. Although more short-term in perspective, there may actually be some comparison of hedge funds to REITs/REOCs — a leveraged portfolio of assets with independent risk profiles able to be managed bought and sold somewhat independently. But the typ-

ical hedge fund "2 and 20" compensation structure — 2% of asset value in fees and 20% annual share of market gains — offers a huge distinction and a huge incentive.

So how would this formula have worked out for REITs/REOCs? In the case above, it was the first time an individual hedge fund CEO's share of the 20% gain reached an annual compensation value of \$1.0 billion. If we applied the 20% of increase in market value as compensation for REITs/REOCs — all executives, not just the CEO — how many companies would reach the \$1.0 billion mark? Although there was no situation clearly over \$1.0 billion for REITs/REOCs — though a few came close — a look at year-end 2004 market-capitalization growth including common shares, when only compared to year-end 2003, found the following summary of companies in several strata of the 20% portion of the "compensation formula:"

In the search for methods and perspective on appropriate value and compensation of CEOs and senior management, another relative measure of compensation is the relationship of a company's net income to aggregate total compensation value for its top five executives. Taken in rolling five-year periods, this figure has been rising for many years for a broad range of national companies, large- and medium-size combined. In the 1993 to 1997 period, this figure was 5.7% and had risen to approximately 10.5% in the 2000 to 2004 period. Although there may be technical arguments related to comparison of the financial statements of

REITs/REOCs on this platform/measurement ratio, a review of the 2000 to 2004 ratio of all REITs/REOCs shows the net income to aggregate total compensation value of the top five reported executives at approximately 7.5%. Lagging or logical, more analysis is likely needed to validate this method of perspective on executive compensation.

Private versus public, industry type, financial structure, operations, risk — there are many ways to analyze compensation, but whether REIT/REOC CEOs are overpaid or underpaid remains for interpretation by many before it can be conclusive.

**REITs/REOCs on level with 20% portion of "compensation formula"**

<b>20% of 2003/2004 Market Cap Growth =</b>	<b>REITs</b>	<b>REOCs</b>
\$10M to \$100M	66	6
\$100M to \$950M	35	3
\$Over \$950M	1	1

Source: The Bradford Group and SNL Financial LC

## Part 3

### Performance Expands the Group of Big Winners

Again in 2004, both rising share prices and compensation awards have expanded the ranks of REIT/REOC executives who received "large" compensation packages compared to 2003. Table 10 shows increasing annual membership among the top five executives at REIT/REOCs since 2001 in the "club" of those who receive more than \$1.0 million in annual total cash compensation — a group that expanded nearly 43% in 2004 — and/or receive more than \$3.0 million in annual total compensation — a group that increased more than 27% in 2004. Again reflective of board caution not to overextend in compensation awards, the growth in the group earning more than \$3.0 million in total compensation value declined to 27% in 2004 compared to the 52% increase in 2003, despite nearly equal annual total re-

turns and improving financial performance.

The rise in REIT values has also led to the opportunity for executives to convert value from vested options into cash. Table 11 shows the biggest option exercise conversions of 2004 (top five executives by company) — a rise of only 1.7%, despite a second year of nearly equal total return in 2004. These, however, are not just rewards captured from a period of rising market value; they also reflect the long-term achievements of building public real estate into a strong and disciplined investment sector. The hard work of building and executing effective operational policy and procedures and the discipline of sound asset and corporate financial structure is a part of why investors — including those in the international community to a much greater degree — continue to stick with REITs, and why the sector continues to build

a reliable reputation from portfolio diversification and income attributes.

REIT management/leadership has established an investment market niche over the past few years, in particular, and the opportunity to reap the financial rewards from success is well deserved. Expectedly, realizing value from options is not the domain of the largest REIT/REOCs or annually the most well-paid executives. As illustrated in Table 11, although annual and three-year total returns for the top 10 companies where the top five executives realized the most in option exercise value were generally well above the SNL REIT Equity Index, ranking of total compensation paid to these executives varied far beyond top 10, to as high as No. 64, and in 2004 included only three of 11 companies with greater than \$8.0 billion market cap.

Increases in compensation for the top 10 executives across all

Table 10  
Expanding Size of Highly Paid REIT/REOC Executives

Total Cash Compensation for REIT/REOC Executives Receiving Greater than \$1.0 million						
	2001	2002	2003	2004	Period % Change	Three-Year CAGR
Chief Executive Officer	24	28	40	56	133.3%	32.6%
Chief Operating Officer	6	5	9	13	116.7%	29.4%
Chief Financial Officer	4	3	5	9	125.0%	31.0%
Top 5 Executives	46	50	68	97	110.9%	28.2%
Annual % Increase		8.7%	36.0%	42.6%		
Total Compensation (w/Option Award Value) for REIT/REOC Executives Receiving Greater than \$3.0 million						
	2001	2002	2003	2004	Period % Change	Three-Year CAGR
Chief Executive Officer	12	20	31	37	208.3%	45.5%
Chief Operating Officer	3	3	1	5	66.7%	18.6%
Chief Financial Officer	1	2	5	4	300.0%	58.7%
Top 5 Executives	21	29	44	56	166.7%	38.7%
Annual % Increase		38.1%	51.7%	27.3%		

Source: The Bradford Group and SNL Financial LC

Table 11  
**REITs/REOCs With Most Realized Option Exercise Value - Top 5 Executives in 2004**

Company	Ticker	Property Type	2004	2004	2004	2004	2004	Three-Year
			Total Option \$ Value Realized	Compensation Paid \$ (1)	Comp. Rank (2)	Market Cap. (\$B)	Total Return	Total Return
Boston Properties Inc.	BXP	Office	47,681,289	12,796,468	12	\$7.1	40.6%	101.0%
Starwood Hotels & Resorts Worldwide Inc.	HOT	Hotel	37,271,041	32,880,970	1	\$12.2	64.7%	110.3%
St. Joe Company	JOE	Mixed Use	36,842,103	6,007,999	58	\$4.9	74.2%	137.1%
SL Green Realty Corporation	SLG	Office	31,624,458	23,667,402	4	\$2.5	53.5%	128.4%
Hilton Hotels	HLT	Hotel	28,194,513	11,352,625	16	\$8.9	33.3%	111.7%
Camden Property Trust	CPT	Multi-Family	26,079,356	5,785,436	64	\$2.5	21.6%	68.9%
Marriott International Inc.	MAR	Hotel	26,067,855	19,794,537	5	\$14.3	37.2%	58.4%
Developers Diversified Realty Trust	DDR	Retail	18,145,086	10,572,310	22	\$4.8	38.9%	177.7%
Kimco Realty Corporation	KIM	Retail	14,570,090	9,527,822	31	\$6.5	35.6%	109.4%
Arden Realty Inc.	ARI	Office	12,713,000	8,362,430	39	\$2.5	32.3%	77.0%
<b>Total - 2004</b>			279,188,791	140,747,999	SNL REIT Index		31.9%	88.5%
<b>Total - 2003</b>			274,442,619	126,454,210				
<b>% Change '03-'04</b>			1.7%	11.3%				

(1) Total compensation, including option award value.

(2) Company rank among approximately 155 REITs and REOCs.

Source: The Bradford Group and SNL Financial LC

REIT/REOCs for 2004 — illustrated in three categories in Table 12, versus 2003 — showed a significant 24% increase in total cash compensation, a 9.0% decline in total compensation excluding option value and no change in total compensation. These statistics tend relate to an increase in financial fundamentals and cash compensation, as well as relative restraint by boards and compensation committees in awarding long-term compensation.

### The shift to restricted shares continues

Figures for the past two years demonstrate the trend in increased use of restricted-share equity awards and variations related performance units/shares and operating partnership (OP) units, as well as the corresponding decline in the use of stock options. Table 13 and Table 14 show the steep decline in the grant of stock options for long-term compensation awards, a reaction to the emerging regulatory re-

quirements for expensing options, general public concern over executive stock options and the trend in diversification into other vehicles for long-term compensation incentive to better align with shareholders. Given the magnitude of REIT share price increases, the decline in number of options granted in 2004 was countered by increases in estimated fair market value. Table 14 documents the corresponding dramatic rise in the award of restricted shares to REIT executives through 2003 and demonstrates again the board discipline/constraint not to overextend compensation awards, reflected in a small decline in 2004.

### Building "pay-for-performance" relationships

Perhaps the most discussed question by media, management and boards in the executive compensation "conversation" is its relationship to company performance. The media often finds several companies with highly paid execu-

tives and poor performance in a particular year, and touts them as examples of "the problem." Perhaps making an easy point, they do much more disservice to all, unable to see the larger but more complex issue. Incentive-compensation decisions should be related to both market and performance, but putting performance into the right context isn't simple.

Even though there are benchmarks of market competitive compensation in any single year, and there is increasing design of performance contingent executive compensation plans, the overall alignment of performance and compensation is a missing piece of most compensation committee proxy reports. Doing more in this category is emerging as significant and essential to the context of board of director and compensation committee decisions, and can only be understood from examining multiple years of evidence. Time and the assessment of compensation and performance over time pro-

Table 12a

**Rankings of Top Executive Compensation - REITs and REOCs - 2004**

Top 10 Executives - Total Compensation, including Options - 2004

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

Ticker	Company	Title	Executive	2004 (\$)	2003 (\$)	% Change '03 to '04	2004 Total Return	Three-Year '01-04 Total Return
HOT	Starwood Hotels & Resorts Inc.	Chairman	Barry S. Sternlicht	24,793,341	6,419,252	286.23%	64.7%	110.3%
SLG	SL Green Realty Corp.	President	Marc Holliday	17,453,712	2,536,960	587.98%	53.5%	128.4%
PLD	Prologis	Chairman	K. Dane Brooksher	10,334,658	8,708,539	18.67%	41.0%	135.8%
REG	Regency Centers Corp.	Chairman	Martin E. Stein Jr.	9,497,658	4,611,326	105.96%	46.2%	138.7%
HTG	Heritage Prop. Inv. Trust Inc.	President	Thomas C. Prendergast	8,814,821	8,710,917	1.19%	21.0%	57.4%
VNO	Vornado Realty Trust	Executive VP	Sandeep Mathrani	7,767,777	1,212,161	540.82%	46.5%	120.4%
CEI	Crescent Real Estate Equities Co.	CEO	John C. Goff	7,345,699	2,977,229	146.73%	16.8%	32.9%
AFR	American Financial Realty Trust	President	Nicholas S. Schorsch	7,179,878	10,820,318	-33.64%	1.4%	42.8%
ARC	Affordable Res. Communities Inc.	Chairman	Scott D. Jackson	6,846,284	502,514	1262.41%	-19.2%	-19.2%
BRE	BRE Properties Inc.	Vice Chairman	Frank C. McDowell	6,370,327	2,094,808	204.10%	27.3%	55.2%
Average of Top 10 - 2004				10,640,416	4,859,402	312.05%	29.9%	80.3%
Average of Top 10 - 2003				10,640,253		207.70%	37.1%	
% Change '03 to '04						0.0%		

(1) Options awarded times share price at option grant date, divided by five.

Source: The Bradford Group and SNL Financial LC

Table 12b

**Rankings of Top Executive Compensation - REITs and REOCs - 2004**

Top 10 Executives - Total Compensation, excluding Options - 2004

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

Ticker	Company	Title	Executive	2004 (\$)	2003 (\$)	% Change '03 to '04	2004 Total Return	Three-Year '01-04 Total Return
HOT	Starwood Hotels & Resorts Inc.	Chairman	Barry S. Sternlicht	18,902,487	5,962,952	217.0%	64.7%	110.3%
SLG	SL Green Realty Corp.	President	Marc Holliday	17,453,712	2,536,960	588.0%	53.5%	128.4%
HTG	Heritage Prop. Inv. Trust Inc.	President	Thomas C. Prendergast	8,814,821	7,913,757	11.4%	21.0%	57.4%
PLD	Prologis	Chairman	K. Dane Brooksher	8,239,158	6,908,539	19.3%	41.0%	135.8%
CEI	Crescent Real Estate Equities Co.	CEO	John C. Goff	7,345,699	2,977,229	146.7%	16.8%	32.9%
AFR	American Financial Realty Trust	President	Nicholas S. Schorsch	7,179,878	10,820,318	-33.6%	1.4%	42.8%
ARC	Affordable Res. Communities Inc.	Chairman	Scott D. Jackson	6,846,284	502,514	1262.4%	-19.2%	-19.2%
MHX	MeriStar Hospitality	Chairman	Paul W. Whetsell	6,213,796	1,043,633	495.4%	28.3%	41.0%
VNO	Vornado Realty Trust	Div. President	David R. Greenbaum	5,786,680	1,261,113	358.9%	46.5%	120.4%
AIV	Apartment Investment & Mgmt Co.	Executive VP	David R. Robertson	5,491,973	1,046,125	425.0%	20.3%	6.7%
Average of Top 10 - 2004				9,227,449	4,097,314	349.0%	28.7%	65.6%
Average of Top 10 - 2003				10,138,608		313.8%	35.5%	
% Change '03 to '04						-9.0%		

(1) Options awarded times share price at option grant date, divided by five.

Source: The Bradford Group and SNL Financial LC

Table 12c

**Rankings of Top Executive Compensation - REITs and REOCs - 2004**

**Top 10 Executives - Total Cash Compensation - 2004**

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

Ticker	Company	Title	Executive	2004 (\$)	2003 (\$)	% Change '03 to '04	2004 Total Return	Three-Year '01-04 Total Return
SLG	SL Green Realty Corp.	CEO	Marc Holliday	6,332,852	2,532,960	150.0%	53.5%	128.4%
HOT	Starwood Hotels & Resorts Inc.	Chairman	Barry S. Sternlicht	6,022,507	3,782,146	59.2%	64.7%	110.3%
VNO	Vornado Realty Trust	Div. President	David R. Greenbaum	5,575,000	940,000	493.1%	46.5%	120.4%
MLS	Mills Corporation	Chairman	Laurence C. Siegal	3,291,703	4,872,000	-32.4%	52.4%	192.3%
HLT	Hilton Hotels Corp.	President	Stephen F. Bollenbach	3,251,024	3,000,000	8.4%	33.3%	111.7%
VNO	Vornado Realty Trust	Chairman	Steven Roth	3,000,000	2,000,000	50.0%	46.5%	120.4%
VNO	Vornado Realty Trust	President	Michael D. Fascitelli	3,000,000	1,900,000	57.9%	46.5%	120.4%
BRE	BRE Properties Inc.	Vice Chairman	Frank C. McDowell	2,894,872	800,390	261.7%	27.3%	55.2%
TRZ	Trizec Properties Inc.	Former EVP	Casey Wold	2,712,603	1,700,000	59.6%	28.8%	40.4%
JOE	St. Joe Corporation	Chairman	Peter S. Rummell	2,626,753	1,945,754	35.0%	74.2%	137.1%
Average of Top 10 - 2004				3,870,731	2,347,325	64.9%	47.4%	113.7%
Average of Top 10 - 2003				3,122,105		98.2%	55.5%	
% Change '03 to '04						24.0%		

(1) Options awarded times share price at option grant date, divided by five.

Source: The Bradford Group and SNL Financial LC

Table 13

**REIT/REOC Option Grant (vs. Common Shares) Trend  
- Top Five Executives 2001 to 2004 (figures in millions)**

	2001		2002		2003		2004		Period % Change		CAGR Value
	Options	Option Value (a)	Options	Option Value (a)							
REITs + REOCs	25.7	\$115.8	31.7	\$142.4	25.2	\$102.0	18.3	\$120.6	-28.8%	4.1%	1.4%
% Change/Yr.			23.3%	23.0%	-20.5%	-28.4%	-27.4%	18.2%			
Health Care	4.1	\$7.9	1.0	\$3.7	1.2	\$4.8	1.2	\$6.2	-70.7%	-21.5%	-7.8%
Hotel	0.6	\$1.4	4.7	\$21.8	5.5	\$12.9	2.5	\$17.3	316.7%	1135.7%	131.2%
Industrial	2.6	\$12.7	2.8	\$14.0	2.4	\$13.7	2.1	\$15.0	-19.2%	18.1%	5.7%
Diversified	3.4	\$20.9	2.4	\$13.0	3.8	\$11.2	2.2	\$15.9	-35.3%	-23.9%	-8.7%
Multi-Family	6.4	\$35.2	4.0	\$23.3	3.6	\$18.9	3.0	\$20.1	-53.2%	-42.9%	-17.0%
Office	3.2	\$16.3	11.6	\$42.1	4.3	\$16.3	1.4	\$8.5	-56.3%	-47.9%	-19.5%
Retail	5.1	\$20.1	4.8	\$21.7	4.1	\$22.1	4.9	\$31.5	-3.9%	56.7%	16.2%
Self-Storage	0.3	\$1.3	0.5	\$2.8	0.3	\$2.1	1.0	\$6.1	233.3%	369.2%	67.4%

(a) Option value = options awarded times share price at grant date divided by five.

CAGR = Compound Annual Growth Rate 2001 - 2004

Source: The Bradford Group and SNL Financial LC

vide this context. This has been missing from REIT assessments of compensation, and given the discipline and diligence of REIT/REOC board rationale, offers a compelling platform to enhance already leading governance.

So, let's take a further look at REIT/REOC pay and performance, and examine the underlying relationship between compensation and performance over the past few years. As previously indicated, statistical similarity in direction and magnitude of change in performance and compensation (as in Table 2 and Table 3) is only a point of departure in the often complex conversation of good judgment in executive pay. The heart of the issue would be the establishment of clear underlying relationships over time, overall and among property types, which would begin to build a more comprehensive and strategic framework for compensation decisions by both management and board committees.

Again this year for the REIT/REOC compensation review, we examined financial performance indicators versus total cash compensation and market indicators compared to total compensation value over both a one-year period (Table 15) and a three-year period (Table 16). From 2002 to 2004, strong and statistically significant relationships exist between EBITDA and FFO compared to total cash compensation, as well as between market capitalization and total compensation, as indicated by the correlations shown.

Many executives ask, "Okay, so why is this so important?" It is important because these relationships are a framework to define the strategic position of company compensation levels and programs compared to its property sector and peer group. The relationships allow a "dynamic benchmarking" of com-

Table 14  
**REIT/REOC Restricted Share Award Trend**  
**- Top Five Executives 2001 to 2004 (figures in millions)**

	2001	2002	2003	2004	Period % Change	
	Award Value \$ (a)	CAGR Value				
REITs + REOCs	\$92.6	\$183.2	\$289.2	\$277.0	199.1%	44.1%
% Change/Yr.		97.8%	57.9%	-4.2%		
Health Care	\$8.2	\$14.1	\$13.4	\$9.4	14.6%	4.7%
Hotel	\$8.4	\$21.6	\$48.1	\$45.9	446.4%	76.1%
Industrial	\$7.7	\$14.0	\$39.4	\$25.9	236.4%	49.8%
Diversified	\$4.1	\$34.6	\$34.9	\$25.5	522.0%	83.9%
Multi-Family	\$22.3	\$20.6	\$28.0	\$52.2	134.1%	32.8%
Office	\$18.5	\$36.8	\$70.1	\$61.2	230.8%	49.0%
Retail	\$20.8	\$40.2	\$51.7	\$54.4	161.5%	37.8%
Self-Storage	\$2.6	\$1.3	\$3.6	\$2.5	-3.8%	-1.3%

(a) Restricted share value = number of shares awarded times share price at time of award.  
CAGR = Compound Annual Growth Rate 2001 - 2004  
Source: The Bradford Group and SNL Financial LC

penetration that is able to directly move with company size and anticipated growth, allowing the option to avoid the issues of conventional methods. Because the relationship of performance and compensation is not linear, when traditional benchmarking — averages and percentiles — collapse data without seeing the underlying relationship, it penalizes high performers more than rewarding low performers. The overall relationships are built on macro-level data and are the reference point for more specific relative performance measures (per share and compared to peers and indexes) most often used by companies to define performance.

Relative performance is extremely important, but direct application of relative measures can often mask the degree of difficulty to perform based on company size or other factors; for example, a 10% increase in FFO per share may well be much more difficult for a larger company than for a smaller one even in the same peer group. By first es-

establishing the macro relationships of compensation and performance — using EBITDA or market capitalization for example — the foundation is built for greater context and clarity in the compensation decisions made by management and board committees.

Time is the most important element in the establishment of compensation/performance relationships, allowing the many annual market, company and individual factors in compensation decisions to settle. Note that the single-year relationships (Table 15, for 2004) are often weaker than the three-year (Table 16), also reflecting the longer-term nature of compensation issues and decisions relative to performance. In the last two years, the attention and capital flow into REITs/REOCs has generated nearly as strong a one-year relationship between compensation and performance as a three-year relationship, compared to those found in similar analysis in the late 1990s through 2002.

Table 15

**One-Year Compensation and Performance - Growth Rates and Relationships (1)**

	No. of Co.'s	Total Cash Growth (a)	Financial Performance Measures					One-Year Correlation with Total Comp. (b)	Total Comp. Growth (c)	Market Performance Measures			
			Growth of Avg. FFO	Avg. of Ind. Co. FFO Growth Rate	Growth of Avg. FFOPS	Growth of Avg. EBITDA	Average of Ind. Co. EBITDA Growth Rate			Total Return	Growth of Avg. Market Cap	Average of Ind. Co. Market Cap Growth	One-Year Correlation with Total Comp. (d)
<b>REIT + REOC</b>	184	5.5%	1.8%	25.3%	0.3%	3.4%	49.1%	0.76	9.7%	35.0%	24.1%	38.9%	0.82
<b>Inv. Structure</b>													
REIT	160	5.5%	0.3%	25.4%	-1.3%	1.7%	53.8%	0.75	10.2%	31.9%	21.4%	32.7%	0.81
REOC	24	5.1%	220.7%	8.9%	212.9%	15.5%	18.8%	0.81	6.8%	44.5%	40.4%	76.5%	0.90
<b>Prop. Sector (2)</b>													
Diversified	30	15.9%	-3.0%	109.5%	-16.1%	7.3%	87.4%	0.89	15.5%	32.5%	22.8%	24.2%	0.78
Healthcare	13	-8.5%	-0.3%	11.0%	-5.4%	1.9%	16.2%	0.90	9.1%	23.0%	18.6%	28.9%	0.85
Hotel	30	4.7%	361.6%	99.2%	362.3%	14.0%	66.3%	0.88	13.5%	32.7%	29.4%	87.3%	0.83
Industrial	10	13.0%	-7.8%	8.8%	-6.2%	3.8%	50.4%	0.86	-9.4%	30.7%	29.6%	32.5%	0.96
Multi-Family	25	31.4%	-6.2%	5.3%	-1.7%	-3.9%	2.4%	0.72	26.0%	34.6%	22.5%	30.3%	0.87
Office	29	-8.0%	-7.3%	8.2%	-6.8%	1.6%	47.0%	0.63	-8.7%	22.3%	21.7%	28.4%	0.81
Retail	37	1.4%	15.2%	8.6%	16.2%	17.1%	61.0%	0.89	15.0%	40.8%	35.9%	39.1%	0.81
Self-Storage	5	55.9%	-22.2%	8.5%	-32.2%	-33.2%	14.3%	0.94	51.3%	29.4%	-15.3%	25.4%	0.83

Table 16

**Three-Year Compensation and Performance - Growth Rates and Relationships (1)**

	No. of Co.'s	Total Cash Growth (a)	Financial Performance Measures					Three-Year Correlation with Total Comp. (b)	Total Comp. Growth (c)	Market Performance Measures			
			Growth of Avg. FFO	Avg. of Ind. Co. FFO Growth Rate	Growth of Avg. FFOPS	Growth of Avg. EBITDA	Average of Ind. Co. EBITDA Growth Rate			Total Return	Growth of Avg. Market Cap	Average of Ind. Co. Market Cap Growth	Three-Year Correlation with Total Comp. (d)
<b>REIT + REOC</b>	184	11.6%	2.8%	13.5%	-2.6%	1.4%	9.9%	0.74	14.8%	65.0%	17.9%	33.9%	0.85
<b>Inv. Structure</b>													
REIT	160	11.6%	1.5%	13.5%	-3.7%	2.0%	10.6%	0.76	15.1%	88.5%	17.6%	30.2%	0.88
REOC	24	12.1%	101.9%	20.6%	71.3%	-2.4%	5.6%	0.74	13.5%	35.8%	20.4%	55.1%	0.83
<b>Prop. Sector (2)</b>													
Diversified	30	10.0%	9.1%	8.2%	-2.6%	3.8%	13.4%	0.93	17.7%	88.3%	14.7%	17.5%	0.91
Healthcare	13	11.1%	6.9%	26.6%	2.2%	6.1%	13.4%	0.95	5.7%	105.5%	23.1%	31.2%	0.96
Hotel	30	13.8%	-15.7%	-4.5%	-18.0%	-4.9%	8.1%	0.72	13.3%	70.8%	16.9%	59.3%	0.88
Industrial	10	7.9%	0.5%	14.9%	1.7%	0.2%	10.4%	0.93	15.8%	103.3%	19.3%	29.4%	0.98
Multi-Family	25	15.9%	-5.6%	-6.1%	-5.7%	-8.2%	-3.6%	0.92	7.0%	56.4%	10.5%	18.1%	0.89
Office	29	11.0%	-1.0%	6.0%	-4.2%	2.1%	6.3%	0.64	15.9%	59.3%	12.5%	20.1%	0.80
Retail	37	9.0%	19.4%	36.7%	5.3%	15.9%	19.5%	0.71	20.5%	151.4%	36.5%	53.0%	0.86
Self-Storage	5	24.0%	-5.1%	9.2%	-12.6%	-10.8%	7.8%	NA	20.5%	82.5%	6.1%	22.1%	NA

(1) Three-year period - Year End 2001 to Year End 2004.

(2) Manufactured Housing sector not shown (5 companies).

All Growth figures are compound annual growth rates (Three- year '01 to '04).

NA = Insufficient Data

(a) Total Cash Compensation = Base Salary + Annual Bonus + Other Annual Compensation - Aggregate of Top Five (5) Executives.

(b) Relationship between Total Cash and EBITDA.

(c) Total Cash Compensation + Value of Equity Award (including option award value) - Aggregate of Top Five (5) Executives.

(d) Relationship between Total Compensation and Market Cap.

Source: The Bradford Group and SNL Financial LC

## Part 4

### Future compensation trends — a new era?

Many industry forecasters have indicated that we are about to experience a shift in the market and a new era for REIT/REOC investment. Short-term interest rates are rising, but long-term rates have yet to follow. The economy has created jobs and is on a growing trend. Real estate fundamentals are better. But will investors continue to focus on yield? As the industry matures, so does its compensation practices. Prediction is one thing; preparation is another. Many trends and changes in compensation 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:

- REITs/REOCs are ahead of the curve in structuring performance-based incentives, particularly long-term vehicles. However, larger companies in the broader market and other industries are catching up fast and will be setting many precedents and trends. Though performance contingent long-term equity awards are indeed the trend, REITs and REOCs cannot rest on past reputation or rely on current structures; they must continue to examine performance compensation structures and adapt to a changing world.

- Boards and compensation committees will be adding more and tougher performance measures linked to incentive compensation and award criteria.

- CEO and senior executive-level base salary adjustment is moving away from serial annual market adjustment to multi-year structures, shifting compensation emphasis even more toward performance and risk-based components.

- Less emphasis on strictly annual bonus structures allow for multiyear performance criteria and using rollover, deferral and multiple payout opportunities designed for a better alignment with the range of time frames and risks in real estate development, investment, financial and operating activities.

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

- With the pool of real estate executive talent declining, pressure continues for increased "market" compensation; with strong market performance comes pressure to recognize and gain the commitment of key management with more long-term compensation.

- Although delayed, FASB 123(R) policy regarding share-based payments is now transitioning into practice for the full year 2006, changing the accounting treatment of long-term compensation awards and option-pricing methods, creating greater parity among vehicles, opportunities for creative structuring and unique consideration for methods beyond time vesting. Most firms will make revisions to incentive compensation plans in light of these new policies.

- Although much is underway in many firms, the new FASB regulations will require greater analytical resources for modeling equity values, tracking executive exercise behavior, testing the financial impact of incentive vehicles and incorporating equity plan status into quarterly/annual financial guidance.

- Also a result of the new FASB regulations, companies are examining and changing the eligibility criteria, design parameters and size of long-term awards to better align with performance and to narrow the participation in long-term award incentives to key

executives. Thirty-five percent of companies are putting more limits on the number of employees in long-term plans. For real estate, this comes precisely at a time when market performance is encouraging more desire for long-term equity based compensation at more management levels.

- The rate of shift from options to restricted shares — including performance units/shares — will slow and a balance in the type and structure of long-term vehicles will be the cause of a wider range of incentive offerings.

- Executive ownership guidelines/criteria for company executives will be increasingly adopted to better align with shareholders. These programs will also influence the structure of long-term plans as timing, vesting and reporting issues will affect conversion and proceeds.

- REIT/REOC compensation review and decisions by boards and compensation committees will reduce the extent of reliance on peer and market-mirrored "bottom-up" assessment of individual compensation components and will also develop and utilize an assessment strategy from the "top down," emphasizing total compensation comparisons/targets.

- Executive retirement accounts are the next topic for media discussion of the problems of excess executive compensation. Retirement programs were intended to replace income, not build wealth, and some abuse of this objective is apparent. This area of compensation has limited disclosure and is ripe for regulatory change.

- Pressure for greater disclosure and greater clarity in disclosure as part of the response to public company issues of executive compensation. Companies and 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 presentation, emphasizing not just compensation value but, more so, the value of compensation.

### Sarbanes-Oxley and compensation

The impact of the Sarbanes-Oxley legislation has rippled through American business for more than two years. Understanding the regulations, interpreting the requirements, implementing the necessary changes and keeping up with emerging opinion on the breadth of the implications of the law have become another full-time job for public companies.

The cost has been particularly heavy for small and medium-sized companies like REITs/REOCs. A recent study of the cost of Sarbanes-Oxley found that for companies with under \$1.0 billion in revenue, which includes most REITs/REOCs, as only 16 companies — 8.7% — had revenue greater than \$1.0 billion in 2004, the overall cost of being a public company increased 33% in 2004 — an average of \$850,000 — and from the Sarbanes-Oxley Act alone increased 223% since 2003. For companies with more than \$1.0 billion in revenue, the costs of being a public company increased by 45% in 2004.

These figures are important to REIT/REOC compensation of both management and directors. Despite the call for change, the Sarbanes-Oxley law is likely here to stay, regardless of its flaws. For CEOs and directors, the implications are significant relative to financial reporting and control. For COOs, CFOs and CGCs who are the most responsible for the implementation and management of its requirements, there has been considerable ad-

ditional burden placed on their jobs. The review of compensation for 2004 reflects this change, the successful completion of much of the transition and the rewards in recognition of the effort.

### Director-compensation trends

Executive-compensation decisions and trends relate directly to compensation committees and boards of directors, and although the usual focus is on the pay awarded to management, an important aspect of the broad subject of "executive compensation" includes the compensation of outside directors. Director compensation has been rising over the past few years in line with the dramatic increase in time requirements, responsibility and liability. In 2004, director compensation rose 4.5% in the manufacturing sector, 21.8% in the financial sector and 16.7% in the service sector. REIT/REOC director pay has also been rising, but on average not at the high end of these annual average figures.

Director compensation at larger REITs/REOCs has risen substantially, but the number of smaller REITs/REOCs (comprising over 54% of the industry, as approximately 100 are under \$500 million in market capitalization) dilute the average figures. There is continuing regulatory pressure for director independence, and a NYSE review of 2005 proxy filings has opened the possibility of further modification and clarification to the determination "tests" of independence and the full disclosure of information relating to director independence. Guidance and regulation related to director status and compensation governance, among many categories, is unlikely to subside soon.

REITs/REOCs boards continue to be challenged in establishing appropriate outside director compensation plans

which are competitive, have the appropriate balance of cash, equity and benefits, are oriented to the overall role and responsibility of a director — rather a menu of activities and fees — recognize the additional contributions of leadership of committee chairs and executive director positions and, most importantly, align directors with shareholders.

### Vision and leadership — stepping into the conversation of competitiveness

With five-and-a-half years of leading market performance, there have been considerable rewards to REIT/REOC CEOs and management for building a long-term public market platform for commercial real estate. A part of the success and recognition of this industry as a mainstream investment vehicle and a recognized component of a balanced portfolio is the opportunity to assume business leadership at a higher level. Sustaining and improving American competitiveness is one of the most important topics relative to the future of our economy and the lifeblood of our business and personal lives. Acting to improve the United States' competitive position in the world economy is needed in the changing era of global economic leadership, where our historical position is potentially being threatened or diluted every day. REITs/REOCs have been recognized (e.g., ISS Governance Index) as one of the outstanding industries relative to governance. This is recognition of leadership and perhaps now is the time to step up to an even more important platform — transitioning from industry leadership to industry statesmanship.

The real estate industry is at the heart of the American economy, more so than many. Every business that utilizes space, every consumer who eats

and shops, every employee and family who rent or own a home, every household that requires medical services or extra space and every business and personal trip for work or pleasure — all are partially driven by real estate. Long in the tendency to be closed and self-protected, the real estate industry now must transform to sustain its position in the market, and build a legacy of contribution to the fulfillment of the American economy. Leaving public policy just to politicians is too risky. We certainly have the talent in our leaders, its CEOs are some of the most capable financial and value-creation-oriented executives in the world and have proven their capacity for building a stable public industry, and now must be willing to take the next step in leadership.

The cautious and conservative decisions by compensation committees and boards of directors regarding REIT/REOC compensation in 2004 will prove to be sound judgment. Winds of change are still in the background and the REIT/REOC years of strong outperformance may subside, giving way to more broadly balanced

investment market returns. Much abounds that is able to change the industry or break the investment momentum quickly — interest rates may continue to rise and long-term rates will eventually follow (good or bad for real estate), a burst in the housing bubble could create a substantial "negative wealth" effect impacting consumer spending, the whispers of major tax reform (national sales, value-added and/or consumed income) — all have substantial potential impact on REIT/REOC economics overall as well as in certain property sectors, not to mention an SEC change in the definition of FFO or other new regulatory requirements and the ability of the U.S. economy to grow and remain competitive.

As in 2003, the year 2004 was good for REITs and REOCs and their executives. The market performance record is remarkable, now backed up with stronger financial results. REIT/REOC board caution not to create an issue related to compensation is wise — a careful and complex balancing act. Retaining and motivating REIT/REOC leadership is a result of sound compensation

policy and strategy and is why effective assessment methods are critical to both management and boards. Change in the economic conditions for REITs/REOCs is inevitable, as is the preparation for change. The doctrine is one of a clearer linkage between compensation and performance, not just in design mechanisms, but in its ability to form a strategic foundation for compensation governance. For executive compensation, both the art and the science of decisions and governance will continue to evolve, and effective and defensible methods to demonstrate pay and performance relationships over time will remain a near-term strategic challenge.

*Contact guest author James Wright at The Bradford Group: (310) 575-0250 or <http://www.bradfordgroup1.com>.*

*Data used in this article was compiled by SNL Financial and is available in the 2005 SNL Real Estate Executive Compensation Review. For more information, please call (434) 977-1600 and ask for the Sales Department, or visit <http://www.snl.com>.*

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