The relation between CEO Pay-performance Sensitivity and Firm Performance - the mediating role of Work/Life Benefits: Empirical evidence from the U.S. market

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Abstract

Executive compensation and Work Life Balance have been two topics of much debate. Much discussion has been done about the level, structure and role of CEO compensation in the firm performance, while in the same time there are concerns whether companies should provide employees with the balance of work and family. This balance can be achieved by providing Work Life Benefits to employees in order to help them with many facets of their lives such us their well being and their family. The aim of this study is to investigate the mediator effect of Work Life Benefits on the relationship between firm performance and pay performance sensitivity. To test this theory, the delta of the portfolio of the CEO and the company performance of 404 US companies for the time period 2006 to 2010 has been studied. The results of this study suggest a partial mediator effect of Work Life Benefits on the relationship between Pay performance sensitivity and Company Performance.

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1. Research question and motivation

The research on executive compensation over the last years has increased a lot and it has received much attention in both the press and the academic literature. Special attention in the business press is given to those top executives who are said to enrich themselves at the expense of their own employees, while a top executive such as David Neeleman donated his entire salary to fund scholarships for the children of lower-level employees. Although these are only few examples, the accounts that suggests top executives to have little regard for fairness or being concerned about the welfare of those under them it has been a topic of much discussion (Wade et al 2006).

The level of the executive compensation plays an important role on both organizational and individual level. First, The CEO behavior is strongly linked with the normal processes of organizations like rewards or promotions (Dhar, 2009). Perceptions about the behaviors of CEOs are strongly connected with justice and fairness that can increase or decrease the level of satisfaction of employees. For instance, negative outcomes of organizational politics increase the dissatisfaction of employees as a result to lower the job performance and subsequently create negative feelings on them. (Kacmar & Baron, 1999). Provide or not Work Life Benefits on employees is one of the factors that can influence the level of satisfaction of them about their work.

Work Life Benefits are employer-sponsored benefit programs that can help all employees to balance work life with personal needs. These programs are created in such a way to help employees with several facets of their lives including their personal well-being (eg. healthcare insurance), professional development (eg. Training programs), and family responsibilities (eg. childcare facilities) (Galinsky, Bond, & Friedman, 1996; McShane & VonGlinow, 2000). Therefore, by offering these benefits, organizations reduce the work-life conflict among existing employees and make them more satisfied in order to improve the organizational performance.

Despite the popularity of work life conflict as a topic of much debate, and the plethora of empirical studies and theoretical approaches concerning the CEO compensation and the leadership styles of CEOs, there is not a study that examines the role of Work Life Benefits on

the relation between CEO pay for Performance Sensitivity and Firm performance. This was the most important stimulus for this master thesis.

Hence, this study will attempt to answer the below main research question:

RQ1: Does company concern for Work Life Benefits mediate the relation between Pay for Performance sensitivity and company performance?

In order to investigate this relationship, the following research questions have also been formulated.

RQ2: Has the CEO Pay- Performance sensitivity a positive effect on firm performance?

RQ3: Is the company concern for work life benefits associated positively with firm performance?

This research will contribute to the literature in several ways. First the research on work life benefits is limited while the mediating effect of work life benefits on the relation of company performance and pay performance sensitivity has not been researched yet. Therefore, the results of this thesis should be of relevance of the companies who want to increase their value and the company performance. Indeed, when employees have the perception that their company cares about them, they are trying to reciprocate in a positive manner in order to help the organization performance.

Next, the results of this thesis should be also of relevance to the companies who want to maximize the value of the shareholders. Specifically, all companies have to deal with the conflict between the interest of the shareholders and the interest of the CEO. (Jensen and Murphy, 1990). The main objective of firms is assumed to be creating extra value for the shareholders and maximize the value of the shareholders (Baker, 1992; Holmström, 1979) while the main goal for the CEO is assumed to be maximizing his own utility, which is not in line with the the objectives of the shareholders.

Studying the pay- performance sensitivity which is based on the delta of the portfolio of the executive and the company performance of 404 US companies I will examine the mediating role of Work Life Benefits in the relationship between company performance and pay performance sensitivity. In order to investigate the mediator effect of Work Life Benefits, a four step approach as Baron and Kenny (1986) proposed will be followed. Data on CEO compensation and incentives of top executives are obtained from the Execucomp dataset, while data on Work Life benefits are obtained from the KLD SOCRATES Research and Analytics database.

2. Theory Back ground

2.1 Agency theory

Jensen and Meckling (1976) are the first authors who introduce the agency theory. According to this Theory there are two parties involved in the agency relationship, the principal and the agent. If the principal (the shareholders of the company) compete information related to the CEO s activities and the firm investments opportunities, the principal hires the agent (CEO of the company) by signing a contract in which the agent gets the control rights of the company. This contract indicates the managerial action that should be taken in each state. However, there are actions like the managerial actions and the investments opportunities which are not perfectly observable by shareholders as they do not always know what kind of actions the CEO will take and whether these actions will increase the shareholder wealth. Due to this kind of information asymmetry (the term will be discussed later) the agent will not always take the actions that can maximize the principal's utility (Jensen and Meckling, 1976), as he will try to maximize his own utility. In general, the agent doesn't receive the full benefits of the actions and the effort that he puts in a company as he doesn't have the full ownership of it. Hence, the interest and the objectives of the principal and the agent do not perfectly align with each other and the agent will not always act in the best interest of the principal.

2.2 Agency Problem

The conflict between shareholders and agent as as introduced first by Berle and Means (1932) and later by Jensen and Meckling (1976) is called 'Agent Problem'.

There are three kinds of agency problems:
- Agency Cost of Equity: explains the fact that executives who own less than 100% of the shares of an all-equity firm will not make the same decisions or he will not use the same attention with those who owned 100% of the shares. Executives are usually risk averse and they want to be paid more and take actions that increase their own utility while shareholders are usually risk neutral and they are mainly concerned to provide incentives to executives to take actions that can increase the value of the shares.

- Agency Cost of Free Cash Flow: explain the conflict of interest between executives and financial claimants based on the nature of cash flows in excess of those required to fund all positive net-present-value projects(Jensen, 1986a). Although, the value is maximized by returning free cash flow to shareholders in the form of dividends or repurchases, executives prefer to retain the free cash flow or reinvest in projects that destroy shareholder value.

- Agency Cost of Debt: explains the conflict of interest that exists between a company's shareholders and its debt holders. In general the prefer shareholders prefer riskier investments that can maximize firm value, while debtholders prefer to invest safer than those that would maximize firm value.

2.3 Information asymmetry

In 2.1 section the term of Information asymmetry was introduced. Information asymmetry occurs when one party has information on the nature of a transaction which is not available to the other party. There are two types of information asymmetry, the ex post and the ex ante information asymmetry.

Ex post information asymmetry deals with problems that arise after the contract has been assigned. In this case, the agent behave in such a way that it is unobservable for the principal (Hendrikse, 2003, p. 188) and as a result the principal will not be able to put these actions in some kind of way in the contract that is signed (Holmström, 1979, p. 74). One solution to avoid this type of hidden information is to put better monitoring; but again it will not be easy to monitor everything.

Ex ante information asymmetry deals with problems that arise before the contract has been signed. In contrary with the ex post information asymmetry, one party holds hidden information before the contract is signed. In our case of principal and agent, the principal does not know whether the agent is motivated or not, while the agent know how motivated he is. Akerlof (1970) states two solutions for this problem: signaling and screening. Signaling is the possibility of the agent to signal his characteristics to the principal(e.g reveal the educational level) and screening is when the principal itself will select the agent that he is ideal for him.

2.4 Incentive system

Summarizing all the above, the principal hires the agent by signing a contract in which the agent gets the control rights of the company. However, after this contract is signed the agent is better informed about the actions he will follow. Hence the main instrument used to deal with these asymmetric information problems is an incentive system. More specifically, Shareholders use an executive compensation package to incentivize the CEO to behave in such a way that he maximizes the utility of the shareholders and increase the performance. Therefore, it is necessary to design a compensation package which the objectives of the manager are as much as possible aligned with those of the shareholders.

In most cases the compensation package consists of several parts: a base salary, a bonus part and a part of equity compensation.

- Base salary: is a fixed amount that is been provided to the manager.
- Bonus part: is the part that is dependent on the performance of the company and the manager. The amount of the bonus depends on performance measures that are set at the beginning of period.

A good example in the case of bonus part is an offer of executive compensation with low base salary and a high bonus component designed in such a way that can attract executives who are more eager to put more effort in order to create extra value to the company.

- Equity compensation: another way to align the objectives of the manager and the shareholders. For instance, when a manager has been shown a good performance, he will get compensated in equity next to the base salary and the bonus part.

The existing literature has used two measures to quantify the impact of the compensation structure on the manager's wealth. Pay-performance sensitivity (PPS) measures the impact of a change in equity value on the manager's wealth, and Vega measures the impact of the stock return's standard deviation on the manager's wealth. In this study I will focus on PPS. Prior literature has used the pay-performance sensitivity of the CEO, the change in CEO dollar wealth to a dollar or percentage change in the stock price, as a measure of CEO incentives. Subsequently, shareholders can fix the agency problem, by limiting the amount of the pay given to the CEO and by putting more pressure on the CEO to improve firm performance, which leads to higher CEO pay- performance sensitivity (Hartzell and Starks (2003)); Almazan et al. (2005); Cadman et al. (2010)). McConaughy and Mishra (1996) found that high levels of pay

performance sensitivity are associated with high future performance. Given this framework, a CEO with high pay for performance sensitivity cares more for the company performance.

2.5 Alternative theory

Overall, the linkage of the pay-performance is the main mechanism to the agency problem as expressed by Jensen and Murphy (1990a, p.242) However, there are two other theories of executive's pay that needs to be discussed even if they have received much less attention than the agency theory. These theories are the Managerial Power Theory and the Tournament Theory.

Managerial power theory

In contrary with the agency theory, the missing link between executive pay and company performance is the power imbalance between the shareholders and the executives. (Tosi et al., 1999). In other words, the managerial power theory is another pay without performance. In 2004 Bebchuk and Fried identified that the executives of the company with dispersed stock ownership have the power to formulate their own compensation. Indeed, managers with power are able to extract rents and consequently managers with more power are able to extract more rents (Rents is defined as the value in excess of what managers would receive under optimal contracting) (Bebchuk et al. 2002). Hence, the executive compensation in this case is not the mechanism that is used to align the interests between the stockholders and managers.

Tournament theory

An alternative theory which link to the relationship between CEO compensation and company performance is the tournament theory (Lazear and Rosen 1981) which can explain the pay gaps in a corporate compensation system (Ji, & Lee, 2011). In this theory the main instrument of the company performance is not the the level of compensation but the position of the CEO itself. Employers set a compensation policy based on ranking within the organization and this policy provides an incentive to employees to be effectively competitive. In 1986, Rosen predicted that there will be an increasing ratio of pay as the individuals move up along the corporate ladder and the variance in salaries between the hierarchical levels is the most important factor rather than the variation in compensation. This outcome can also be explained by CEOs from large companies who earn more compensation among the years (big companies have more hierarchical levels than small companies).

2.6 The relationship between CEO compensation and firm performance

Several studies have been performed to analyze and provide evidence to identify the relationship between CEO compensation and firm performance. Some of them found a strong relationship, others a weak relationship while few papers found a negative association between these two variables.

Weak Relationship:

Two studies that haven been performed by Jensen and Murphy(1990) found a direct evidence for the pay for performance sensitivity and company performance. In the first study, the authors studied the pay performance sensitivity, analyzing a sample of 1,688 executives from 1,049 U.S. companies in the period of 1974 to 1986 and they identified a weak relationship between Pay for Performance Sensitivity and company performance. Regarding the research methodology, the dependent variable that was used was the change in CEO cash and total compensation and the independent variables were the change in shareholder wealth for the contemporaneous and the lagged relationship. More specifically, they found a weak relationship between pay performance and company productivity, mentioning that a CEO receives an average pay increase of 1.35 cents for each $1,000 increase on shareholder wealth.

The second study indicated again a weak pay for performance sensitivity. This time, they examined the pay-performance sensitivity for 250 U.S. largest companies for the period of 1974-1988. The median CEO in this sample of companies is rewarded with 6.7 cents increase in salary and bonus over the two years for a $1,000 increase in corporate value.

Positive Relationship:

In contrary with the studies of Jensen and Murphy (1990a, 1990b), Hall and Liebman (1998) provided a new evidence related to the pay-performance relationship. More specifically, they examined this relationship in a sample of CEO data from 478 big U.S. public companies for the time period of 1980 to 1994.and they found a strong link between the CEO value and the value of the company that they manage in contrast to the weak relationship that Jensen and Murphy found. Indeed, the results indicated that the CEO wealth changes by millions of

dollars for changes in firm value. Finally, they argued that CEOs are not paid like bureaucrats as the CEO compensation is highly associated to firm performance.

A supporting evidence to the study of Hall and Liebman, provided by Mehran in 1995. The author studied the executive compensation design of 153 U.S. manufacturing companies for the time period of 1979 to1980. The author used as performance variables the Tobin's Q and the return on assets; the results indicated a significant and positive relationship to the executive compensation (an executive compensation based on equity) and also to the equity that held by the managers. In addition, one outcome that has been indicated by this study is that companies that the executive compensation is relative more sensitive to firm performance, used to produce higher returns for their shareholders than companies in which this pay-performance relationship is weaker.

Moreover, in 1999 Core et al. analyzed a sample of 205 traded U.S. companies between 1982 and 1984 using the return on assets and the annual stock return as performance measures. The results showed a positive and not statistically significant relationship between return on assets and CEO compensation, whereas the coefficient of annual stock return shows positive and significant relation with CEO compensation. Finally, this study supports the positive association between executive compensation and prior year's performance.

Recently, a plenty of studies have been performed to analyze the relationship between company performance and CEO compensation with the aim to be differentiated from the old researches.

For instance, in 2006 Gabaix and Landier tried to link the increase in CEO pay with the firm size. Specifically, they state a six fold increase in CEO Pay from 1980-2003 which it was attributed to the six-fold increase in market capitalization of large U.S. companies in that period. Indeed, the authors found that the firm size plays a significant role and can impact the CEO productivity. Besides to that, in 2014 Gabaix et al. find more evidence for the statement that the firm size and the level of talent are reflected by the level of CEO compensation. Actually, they found that the executive compensation follows an identical path compared to the evolution of average firm value. Specifically, the period of 2007-2009 the firm value and

the CEO compensation dropped with 17% and 28% respectively, while the period of 2009-2011 firm value increased with 19% and CEO compensation increased with 22%.

In 2007, Ozkan using a sample of UK companies tried to analyze the relationship between CEO compensation and firm performance by examining the Tobin's Q variable. The findings were in line with Canyon & Murphy (2000) who they found a significant positive effect of stock returns on the total CEO compensation level. However, the author argues that this firm performance as measured by Tobin's Q is not a significant determinant of the CEO compensation level.

In contrary, Grime et al. (2007) investigated the effect of the corporate governance on the CEO pay for a sample of UK companies and their results suggest that the relationship between pay and performance remains weak for their sample of firms over the period 1981-1996. Specifically, they mentioned that the effects of the corporate governance reforms on CEO compensation are discouraging. In addition, Duffhues and Kabir (2008) examined the pay-performance relationship for 135 companies listed at Euronext Amsterdam for the period 1998-2001. The study was based on the compensation of the entire board of directors and as company performance, ROA, ROS and annual stock return have been considered. Finally, they found a significant negative relationship between compensation and company performance.

2.7 Work life benefits

In 1977 Kanter, proposed the idea of work and family in the business world as two different domains that are linked to each other and needs to be treated with the same attention. In this sense, work-life balance is a situation in which the employee behaves and respect both the work and the life with fairness.(Avgar et al., 2011; Kar & Misra, 2013). The main concern of an employer is to design programs that are focusing on the needs of the employees (Iqbal, 2010) and assist them on many facets of their life (Galinsky, Bond, & Friedman, 1996); such programs are the work life benefits.

In general, Work-life benefit programs can be defined as a signal that the company cares about employee's life and well being as a result to strengthen the employer-employee bond and create a desire within employees to reciprocate.

A work-life benefits package is a package that includes benefits from several categories. These categories are:

- child-related (e.g., childcare facilities, financial assistance, and referral, childhood health programs, and maternity/ paternity leave)
- time/schedule (e.g., flex-time, compressed workweek, and job sharing), physical health (e.g., health insurance, medical and fitness centers, and wellness programs)
- psychological well-being (e.g., counseling and employee assistance programs), professional development (e.g., tuition reimbursement and training)
- eldercare (e.g., assistance and referrals).

2.8 Work Life Benefits and Company Performance

Many researches have been performed to investigate whether offering programs that assists workers in balancing work and personal life (programs like the ones that are included in the work life benefits) can improve the company performance. Social exchange theory presented the theoretical justification for expecting work-life benefits to be positively reciprocated by employees in the form of positive attitudes and behaviors (e.g., Lambert, 2000). More precisely, this theory characterizes the employee–employer relationship as an exchange of

valued resources (Blau, 1964). In addition, Balance theory (Heidner, 1958) suggests that individuals must have a balance between their attitudes and behaviors and violations of this balance can create stress and can reduce the dissonance. (Festinger, 1957).

Connecting the social exchange theory (Blau, 1964) and the Balance theory with the work-life benefits it can be claimed that such programs have the potential to create a positive exchange relationship between the employer and employee.

Freeman(2005) claims that the high performance of any company is directly link to the satisfaction of the employees who work in that company. Indeed, more satisfied employees, follow several positive actions which lead to a better company performance and these employees are more loyal and productive when they are satisfied (Hunter and Tietyen,1997). Indeed, Fredrickson's studies (1998, 2001) suggested that sending a message that the organization cares about employees leads to proactive attitudes and behaviors in the workplace which in turn leads to a high company performance. Indeed, Shepard et al. (1996) after collecting information from 36 pharmaceutical companies in the U.S., he found that the use of flexible work hours is associated with an increase of 10% in firm performance.

Moreover, there is an argument that, the consequences of introducing work life practices in the workplace include benefits for both the organization and the employees. Specifically, adding practices to employees work-life appears to increase attitudes like work effort and positive behavior (Pfeffer, 1981).These work life practices can allow organizations to offer lower wages in exchange. For example, Mukerjee, and Sestero (2001) found that offering family sick leave might allow firms to pay lower wages, if workers viewed the leave as compensation for less pay. Finally, Galinsky and Bond(1998) found that almost the 50% of the organisations that follow the work life benefits are claiming a positive return on investment in these practices

In contrary to the above outcomes, several studies have shown that the relationship between work-life benefit practices and employee behaviors is unclear as providing a work life package is not a proof that the employer cares for the well being of the employee (Casper, Lockwood, Bordeaux, & Brinley, 2005; Kossek & Ozeki, 1998; 1999.Indeed, it can be claimed that employers may add the work life practices in the workplace in order to increase

the reputation of the company both internally and externally regardless of employee use or net effect on work-life balance. Consistent with this theory, Konrad, A.M and Mangel, R., (2000) didn't find any clear relationship between the work-life initiatives and productivity. Their sample was included from 658 organisations which provided survey data on firm characteristics and work-life programs while the Productivity data were obtained from 195 public, for-profit firms. In particular, the findings indicated that the relationship between productivity and work life benefits is stronger only for women while for the less skilled employees and for the less high paid employees the benefit in productivity for the usage of work life practices is really small.

Moreover, the extent to which work-life benefits encourage recruitment of all employees, or only those with personal commitments that need the assistance of such work life benefits programs has been a topic of much debate.

On the one hand, there is the statement that companies with work life benefits attract mainly employees who need to have an assistance in the work life balance. For instance, in a study which performed by Kossek and Nichol (1992) examined the effects of an onsite organizational childcare center for employees who use the center and employees who can not use the childcare center as they are in the waiting list. The findings indicated that users of the childcare center have been longer in the organization and held more positive attitudes compared to non users.

On the other hand, Casper and Buffardi (2004) found that the perception of the existence of work life benefits in a company is a psychological mechanism through which such programs influence behavioural intentions. More precisely, they indicated why companies with a concern for work life benefits are more attractive to employees who have less need or no need of work-life practices rather than organizations that do not offer such programs; this can be explained, by the signaling theory. According to this theory, when a contract with incomplete information needs to be signed, decisions for unobservable characteristics need to be made by using observable characteristics (Spence, 1973). For instance, individuals may use the existence of work life benefits as signals for work related characteristics that are important for them like fair treatment.

3. Hypotheses development

As present in the above theory development, I expect a positive relationship between executive compensation and firm performance. This can be predicted by the agency theory. Agency theory supports the concept of pay for performance as a solution to the principal-agent problem. The compensation aligns the interests between the shareholders and the chief executives officers. Shareholders can fix the situation by limiting the amount of the pay given to the CEO and by putting more pressure on the CEO to improve firm performance, which leads to higher CEO pay- performance sensitivity (Hartzell and Starks (2003); Almazan et al. (2005); Cadman et al. (2010)). Indeed, McConaughy and Mishra (1996) found that high levels of pay performance sensitivity are associated with high future performance. Hence it can be claimed that the more incentivized, the more performance for the company you want.

As a result, the following hypothesis is developed:

H1: High pay for performance sensitivity is associated with high company performance

The corresponding <u>null</u> hypothesis is that CEO high pay for performance sensitivity is not associated with high company performance.

In general, Work-life balance for the individual plays a significant role for both individual and organizational actions (Mayerhofer, Schmidt, Hartmann, & Bendl, 2011). For the organization, work-life balance may be a part of good performance, and for the employee work-life balance programs may be a positive factor in deciding to remain in the particular organization (Mayerhofer et al., 2011). First, the programs allow an employer to have a more committed workforce profile. (Wang & Walumbwa, 2007). Employee commitment is a major factor in the success of an organization (Shahid & Azhar, 2013).The major driven for an employee to be committed is to feel safe and be treated fairly.

The top three drivers of employee commitment are employers' care and concern, fairness, and fulfillment (Shahid & Azhar, 2013). For this reason, companies want to provide a nice work environment without risks and hazards. (Howard-Quartey & Buenar-Puplampu, 2012). The work life programs can reduce reduce employee absenteeism, stress, and turnover. (Wang & Walumbwa, 2007).

So from the above it can be claimed that high for performance sensitivity leads to better work life benefits because executives anticipate that this lead to a higher performance.

So, the above argument leads to the following hypothesis:

H2: *Firm performance is positively associated with work life benefits for companies that have a concern on that.*

The corresponding null hypothesis is that firm performance is not associated with Work Life benefits for companies who have a concern.

Subsequently, Social exchange theory provide the theoretical explanation for expecting work-life benefits to be positively reciprocated by employees in the form of positive attitudes and behaviors (Lambert, 2000). more satisfied employees, follow several positive actions which lead to a better company performance and these employees are more loyal and productive when they are satisfied. Indeed, high performance of any company is directly link to the satisfaction of the employees who work in that company (Freeman,2005). For example, Delaney & Huselid, 1996 found that Perceived organizational performance is positively linked to HRM practices and work-family programs, as well as Mangel (2000) found also a positive association between work life programs and firm productivity.

According to, Misener et al., (1996) the employee satisfaction is relevant with the positive employee morale in the work place, the work conditions, the organizational practices and the satisfaction related to pay. Previous research also found that Work life Benefits programs lower turnover rates, promote higher work satisfaction, and subsequently improve the organizational financial performance (Grover and Crooker, 1995; Lobel and Kossek, 1996; Lambert, 2000)

Thus given the above framework, it can be claimed that CEOs with high performance sensitivity want to provide more work life benefits on employees in order to have more satisfied employees and subsequently a better performance.

If so, the bellow Hypothesis is formulated.

H3: *Work Life benefits mediate the relation between Pay for Performance sensitivity and company performance.*

The corresponding <u>null</u> hypothesis is that work life benefits do not mediate the relation between Pay for Performance sensitivity and company performance.

4. Data and Research Methodology

4.1. Sample Description

I study US data from 2006 to 2010 because from 2010 the firm reports use a different format. Specifically, the data for this study have been obtained from two large data sources. First, the data on top executives characteristics and incentives have been collected from Lalitha Naveen website at Temple University[1], while Data for Work Life benefits are obtained from KLD through Wharton Research Data services (WRDS).

Regarding the data for **executives characteristics and incentives** that are available in Lalitha Naveen site, they have been obtained from the Standard & Poor's Execucomp database. Execucomp provides data on salary, bonus, and total compensation for the top five executives (ranked annually by salary and bonus) for firms in the S&P 500, S&P Midcap 400, and S&P Smallcap 600.

The researcher, computed incentives as of fiscal year end based on these data. In general, execucomp provides a separate record for each outstanding option tranche, indicating the number of vested, unvested, and unearned options. For calculation of delta the author used only the vested and unvested shares and options. The unearned awards have not been used because the not available awards that data required to calculate were not available in electronic format in Execucomp for any firm. These unearned shares have been categorised as either shares or options when they are earned, and, the grants that are still held by the executive they included in the delta calculation.

The main variables that has been used for this dataset is the Delta . **Delta or Pay performance sensitivity** is estimated as the sensitivity of CEO wealth to stock price, based on the entire portfolio of stock and options held by the CEO. Specifically, delta is defined as the change in the dollar value of the executive's wealth for a one percentage point change in stock price. Delta has been calculated from Lalitha Naveen using the approach of Core and

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[1] More information for the data on incentives and executives characteristics can be found in the following website of Lalitha Naveen: https://sites.temple.edu/lnaveen/data/

Guay (2002), see Appendix B for more details.

With Regard to **Work life benefits** data, KLD through Wharton Research Data services(WRDS) has been used. KLD is a data set with annual snap-shots of the environmental, social, and governance performance of companies rated by KLD Research & Analytics. KLD started in 1991 rating about 650 companies on issues related to the social responsibility of the firm. The information is gathered from publicly available reports, mandatory filings and supplemental interviews with key personnel at the firms. Currently, KLD ranks over 3000 firms, indicating the firm by name, ticker symbol and CUSIP code.

In general, KLD presents a binary summary of positive and negative Environmental, Social and Governance ratings and is organized by year. If Risk Metrics Group assigned a rating either positive or negative, this is indicated with a 1 in the corresponding cell. If the company did not have a strength or concern in that issue, this is indicated with a 0.It could be that the data for a given category is unavailable indicated with "NR", meaning "Not Rated." In the case that the index membership was not covered, KLD STATS indicates this with "NA", meaning "Not Available."

My sample consists of firms that are covered by KLD, which is for the year 2006-2010. I used the identifiers (GVKEY and COPEROL) to combine the two databases that have been explained above. The initial resulting sample consisted of 1,982 U.S. firms and16664 executives. However after the elimination of all other executives apart from CEOs and selecting firms that have data for both Work Life Benefits and Pay for performance sensitivity, my resulting sample consists of 404 firms for the time period of 2006-2010. The companies that are included in the sample can be found in the Appendix C.

Below is an overview of the main variables that have been used for the data methodology:

Variable Name	Description
GVKEY	unique firm identifier in Execucomp
COPEROL	unique firm executive identifier in Execucomp
YEAR	fiscal year of data from Execucomp
DELTA	Dollar change in wealth associated with a 1% change in the firm's stock price (in $000s)
Work Life Benefits	Work/Life Benefits The company has outstanding employee benefits or other programs addressing work/life concerns, e.g., childcare, elder care, or flextime. In 2005, KLD renamed this strength from Family Benefits Strength.

4.2. Research Methodology

The predictive validity framework ("Libby boxes") presented in the Appendix B show the conceptual relation examined in this thesis will be operationalized in the research design.

For control variables, CEO gender, assets, leverage and number of employees have been taken into consideration. First, researchers have found that age is related to the pay for performance sensitivity. Specifically, the **age** of the CEO is expected to have a positive effect on the pay-for-performance sensitivity. In general, an old CEO has less incentives to work hard and increase his experience as a result the company will try to compensate this loss incentives with a higher compensation package .(Gibbons and Murphy, 1992).

Next, CEO **gender** matters in firm performance. In 2013 Khan and Vieitto found that when the CEO is a female, the firm risk level is smaller than when the CEO is a male. The CEO gender also plays an important role of how the company will concern for the Work life benefits. It is claimed, that women executives are more likely to threat with fairness to his employees than men.((Lambert, 2000).

Leverage has been taken also as control variable. Researchers argue that leverage can help to to reduce two problems. First, this can recuse the Agency problem because debt holders may more closely monitor managerial activities. Second, it can reduce the free cash flow problem as more debt managers pay a future cash flow(Jensen 1986).

Finally, with regard to **firm size** proxy Forbes Global 2000 uses four measures (assets, sales, profits, market cap) to rank the companies around the world, and Fortune 500 uses two measures (sales and profits). On the other hand, Graham, Li, and Qiu (2012) used only the log of assets as firm size proxy, while Hart and Oulton (1996) argue that the number of employees plays also an important role in firm size. In my thesis, I will use two control variables that have an impact on the firm size, the **assets** and the **number of employees**. Assets represents the total assets of a company at a point in time while employees report the number of people employed by the company.

To **proxy performance**, we measure the performance of the concerning firms by return on equity (ROE), Return on asset (ROA) and Tobins Q. These financial performance indicators have been widely used by previous studies, such as those of Zeitun and Tian (2007a and 2007b); Agrawal and Knoeber (1996), Morck et. al (1988) and Lemon et. al (2008). These

three performance estimations will be used as the dependent variables of our models.

The Return on Equity **(ROE)** is calculated by dividing the Net Income by the book value of equity as stated on the balance sheet while The Return on Assets **(ROA)** is calculated as net income divided by total assets. Finally, **Tobin's Q**, is estimated by dividing the market value of the firm by its total assets.

In order to test all the hypotheses and answer the main research question we will use the model as Baron and Kenny (1986) proposed. Testing for mediation Baron and Kenny (1986) proposed a four step approach in which several regression analyses are conducted. In fact, the tests will show whether or not the work life benefits variable mediate the relationship between company performance and pay for performance sensitivity. This can be visualized as below in Figure 1.

<u>Figure 1</u>

c path

X ——————→ M ——————→ Y

a path   b path
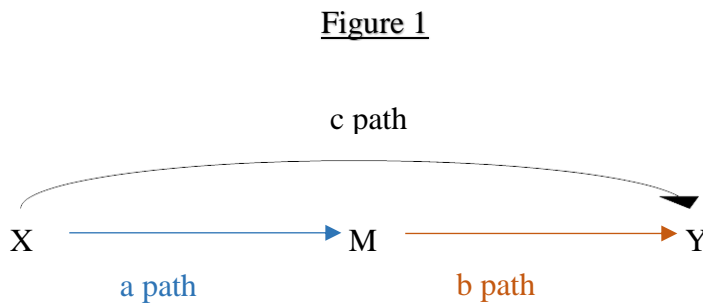
In my thesis, the independent variable(X) is the pay for performance sensitivity and M is the variable suspected of mediating. Y is the dependent variable which indicates the company performance. The paths a and b are called the direct effects. The mediating effect, where X leads to Y via M, is called the indirect effect. The indirect effect is the portion of the effect between X and Y that is mediated by M(Work Life Benefits).

Step	Analysis	Hypothesis testing
1	Use a simple regression analysis with X predicting Y to test for path c, $Y=\beta_0+\beta_1 X+e$	H1
2	Use a simple regression analysis with X predicting M to test for path a alone, $M=\beta_0+\beta_1 X+e$	a path (Figure 1)
3	Use a simple regression analysis with M predicting Y to test for path b, $Y=\beta_0+\beta_1 M+e$	H2
4	Use a multiple regression analysis with X and M predicting Y, $Y=\beta_0+\beta_1 X+ \beta_2 M+e$	H3

Overall, the models that will be tested takes the following form:

STEP 1:

In order to test the H1 hypothesis the below model has been formulated.

FP = βo+ β1*lnα + Ui + εi

Where: **FP**: firm performance, **α**: pay-for-performance sensitivity, **Ui**: set of control variables, **ε$_i$:** error term

Control variables included in the regression analysis include factors that are correlated with pay performance sensitivity, firm performance or both. Such controls are logassets, employee number, CEO age, CEO gender and leverage.

STEP 2:

In order to test the H2 hypothesis the below model has been formulated.

WLB = βo+ β1*lnα + Ui + εi

Where: WLB: work life benefits, **α**: pay-for-performance sensitivity, **Ui**: set of control variables, **ε$_i$:** error term

Control variables included in the analysis include factors that are correlated with pay performance sensitivity, work life benefits or both. Such controls are log assets, employee number, CEO age, CEO gender, leverage, ROA, ROE and Tobins Q.

STEP 3:

FP = βo+ β1*wlb + Ui + εi

Where: FP: firm performance, wlb: Work Life benefits Ui: set of control variables, εi: error term

Control variables included in the regression analysis include factors that are correlated with work life benefits, firm performance or both. Such controls are logassets, employee number, CEO age, CEO gender and leverage

STEP 4:

In order to test the H4 hypothesis the below model has been formulated.

FP = βo+ β1*lna + β2*wlb+ Ui + εi

Where: FP: firm performance, α: pay-for-performance sensitivity, wlb: Work Life benefits Ui: set of control variables, εi: error term

Control variables included in the regression analysis include factors that are correlated with work life benefits, firm performance, pay for performance sensitivity or all three. Such controls are log assets, employee number, CEO age, CEO gender and Leverage.

4.3. Limitations

This study is subject to several limitations. A limitation of my thesis stems from the fact that I focus on companies that are only based in the United States. This fact makes it hard to generalize my findings with respect to all CEO's that run large corporations around the globe. I chose companies form US only mainly due to the fact that the amount of data that are available on US companies is higher than European companies.

The sample period is a 5 years sample, which can result to a lower quality research. In addition, the initial sample was significantly decreased from 1982 firms to 404 firms as a result to affect the quality of the findings. Finally, it should also be taken into account that the data for executive incentives have missing variables as the calculation of the delta couldn't be calculated for each year mainly due to the fact that sometimes the CEO wasn't the CEO in the previous year. It is also advisable to have a better mix of female and male CEOs to avoid gender biases and to be more longitudinal in nature.

With regard to the measure of pay for performance sensitivity (PPS) it can be claimed that it is difficult to be defined. More specifically, each company can have a different measure of firm performance (eg net profit). In my thesis the PPS was based on the delta of portfolio CEO; while there are several ways that can determine the calculation of PPS. Such elements

are base salary, cash bonus, other compensation and equity bonus. Finally, I will only take into account the number of employees and the total assets as firm size proxy.

5. Results - Analysis

To do the analysis of this research a panel data set has been created. As Ceryo and Semadeni (2006) argued the panel data models often experience problems with heteroskedasticity and autocorrelation that can lead to inconsistent results. Therefore, a fixed or a random effects model should be used. In order to decide what kind of effect should be used in our analysis. I did the Hausman specification test on the regressions for its hypothesis and found that fixed effect model is appropriate for my analysis.

However, in my data set there are few firms which they have only one observation and there are only few firms where Work Life Benefits changes over time. Hence, in order to solve the cross observation correlation in variables, I will use the so called clustered standard errors method, which is robust standard errors that are additionally corrected for unwanted correlation.

In the following section, I am going to discuss the descriptive statistics and correlations of the variables used in this study and present the results of the empirical analysis conducted to test the hypotheses.

5.1 Descriptive Statistics and correlations

Table 1 reports the descriptive statistics for the whole sample. Pane A, B, C indicates the descriptive statistics for the main Variables, the Performance Measures, and the Control Variables comprehensively. The sample period is 2006-2010.

<div align="center">

Table 1
Descriptive Statistics

</div>

Variable	Mean	Median	Maximum	Minimum	Std. Dev.	Observations
Panel A: Main Variables						
DELTA	1412.418	200.865	269935	0	12736.31	1206
LOGDELTA	5.338	5.305	12.506	-0.398	1.621	1201
WLB	0.074	0	1	0	0.262	1205
Panel B: Performance Measures						
ROA	0.137		0.886	-0.62	0.129	1145
ROE	0.092	0.101	1.736	-1.803	0.229	1145
TOBINS_Q	1.318	0.953	15.088	0	1.405	1200
Panel C: Control Variables						
ASSETS	15871.89	1465.025	1351520	19.357	80210.29	1200
CEO_AGE	61.368	61	89	38	7.276	1201
CEO_GENDER	0.027	0	1	0	0.163	1206
LEVERAGE	0.53	0.528	4.53	0	0.285	1145
EMPLOYEES	112382.9	32000	3090500	60	251074.8	1200
LOGASSETS	7.579	7.29	14.117	2.963	1.765	1200

The maximum number of observations in my sample of 404 firms in period 2006-2010 is 1206 but there are some missing observations in the variables.

Panel A indicates the main variables of my research. Work life benefits takes value 0 if the company do not have a concern of that or 1 if the company has a strength on that. I can observe from this panel that most companies do not have a strength or concern in Work life Benefits (mean: 0.074 , median: 0), something that can lower my quality of the results. The big standard deviation of log delta (1.621) reflects a large amount of variation in the group that is being studied. The mean of the pay for performance sensitivity (delta) is 1412.418 which means that total compensation of the CEO increases/decreases with approximately 1412.418 dollars for each increase/decrease in firm value of 1.

Panel B indicates the performance measures that is being used in my thesis (ROA, ROE, Tobins Q). The average firm in the sample has a Tobin's Q of 1.318 while ROA and ROE have 0.137 and 0.092 respectively.

Panel C shows that CEOs from our sample are in average 61 years old and are primarily men .High Leverage ratio measure how leveraged a company is and a high ratio means that the company has a lot of debt relative to its assets while a low ratio means that the company is not sensitive to changes in business of interest rates. The mean of leverage in my sample is 0.53.

The average firm size in my sample is large with maximum total assets to be 1351520 and maximum number of employees 3090500. This is not surprising given that our sample is S&P firms.

Table 2 below shows the cross correlation matrix for the dependent and independent variables that might include in the regressions later.

The firm performance metrics ROA, ROE and Tobin's Q show positive strong correlation with the natural logarithm of pay for performance sensitivity. This correlation is in line with the findings of Hartzell and Starks (2003); Almazan et al. (2005) and Cadman et al. (2010) who they claimed that the amount of the pay given to the CEO and by putting more pressure on the CEO to improve firm performance, leads to higher CEO pay- performance sensitivity. This gives a first indication that hypothesis H1 holds.

The Variable Work Life Benefits show different correlation with the firm performance metrics but a positive strong correlation with the logarithm of pay performance sensitivity. This gives a support to the second hypothesis and is also questionable if hypothesis H3 holds.

Moreover, as it was expecting CEO age is positively correlated with pay for performance

sensitivity. More specifically an old CEO has less incentives to work hard and increase his experience as as the company will try to compensate this loss incentives with a higher compensation package. In contrary, it seems that the CEO gender doesn't have any strong impact on firm performance (ROA, ROE and Tobin's Q) while pay for performance sensitivity as it was expected it is highly correlated with Work Life Benefits. Finally, Firm size (log assets and employees) has the strongest correlations with the Work Life Benefits. This correlation is in line with the theory as big companies are more willing to invest in Work Life Benefits.

Table 2
Correlation Matrix

The sample period is 2006-2010
Leverage, Tobin's Q, ROA and ROE are expressed as ratio

	DELTA	CEOAGE	CEOGENDER	WLB	ROA	ROE	ASSETS	EMPLOYEES	LEV.	TOBINSQ	LOGASSETS	LOGDELTA
DELTA	1											
CEOAGE	0.092	1										
CEOGENDER	-0.014	-0.025	1									
WLB	0.009	0.051	-0.028	1								
ROA	0.052	-0.093	-0.009	-0.018	1							
ROE	0.048	-0.051	0.006	0.014	0.644	1						
ASSETS	0.039	0.043	-0.027	0.405	-0.094	0.012	1					
EMPLOYEES	0.169	0.078	-0.016	0.325	0.018	0.039	0.331	1				
LEVERAGE	0.006	0.134	0.028	0.074	-0.166	-0.071	0.167	0.129	1.00			
TOBINSQ	0.043	-0.177	0.011	-0.044	0.474	0.317	-0.13	-0.099	-0.327	1		
LOGASSETS	0.125	0.159	-0.037	0.407	-0.193	-0.028	0.484	0.455	0.39	-0.424	1	
LOGDELTA	0.321	0.13	-0.058	0.214	0.135	0.178	0.187	0.229	-0.054	0.156	0.365	1

*The **first step*** of the analysis was to test hypothesis H1 which reflect to the relationship between pay for performance sensitivity and firm performance (Hypothesis 1). In order to test this relationship a regression with dependent variable the firm performance as measured by ROA, ROE and Tobin's Q has been tested. For pay for performance sensitivity a natural logarithm of pay for performance sensitivity has been used. I control also for firm size, leverage, CEO age and CEO gender. First, I cluster the standard errors based on firms (Model,2,3) and then I combined the firm fixed effects with the cluster Standard Erros (Model 4,5,6).***Table 3*** present these results of the regression analysis as it is formulated below.

$$\text{Firm Performance}_{it} = \beta o + \beta_1 \log DELTA_{it} + \beta_2 \log ASSETS_{it} + \beta_3 EMPLOYEES_{it} + \beta_4 CEOAGE_{it}$$

$$+ \beta_5 CEOGENDER_{it} + \varepsilon_{it}$$

Table 3
The sample period is 2006-2010
Leverage, Tobin's Q, ROA and ROE are expressed as ratio
Model 1,2,3 Standard Errors clustered at the firm level
Model 4,5,6: combination of Cluster Standard Errors and Firm Fixed Effects
Note: *$p<0.1$, *$p<0.05$, ***$p<0.001$, standard errors in parentheses
The standard errors are displayed between the brackets

Model	1	2	3	4	5	6
Dependent Variable	TOBINSQ	ROA	ROE	TOBINSQ	ROA	ROE
Constant	4,673***	.297***	.164*	74,40***	.233***	-.088
	(.566)	(.063)	(.108)	(,478)	(.046)	(.085)
logDELTA	.293***	.018***	.030***	.319***	.016***	.042***
	(.035)	(.004)	(.007)	(.033)	(.003)	(.007)
logASSETS	-0.429***	-0.022***	-.014*	-,49***	-.021***	-.014***
	(.053)	(.006)	(.007)	(.053)	(.005)	(.007)
EMPLOYEES	4.91**	5.91***	3.84	5,14***	4.34**	1.87
	(1.52)	(1.75)	(3.40)	(1,45)	(1.30)	(2.52)
LEVERAGE	-.472*	-,020	-.012	-.3062	-.006	-.059
	(.236)	(.0428)	(.041)	(.2749)	(.048)	(.041)
CEOAGE	-,024**	-.0014	-.0015	-.0156**	-.004	-.001
	(.008)	(.0008)	(.047)	(.006)	(0.006)	(.0012)
CEOGENDER	.121	-.005	.020	.403	.022	.062
	(.226)	(.022)	(.047)	(.300)	(.046)	(.44)
R^2	0.32	0.04	0.14	0,32	0,09	0,14

Firm Fixed Effects	NO	NO	NO	YES	YES	YES

The results of Model 1,2 and 3 show that as it was expected there is a positive and significant relationship between the log of Pay for performance Sensitivity (log DELTA) and firm performance as measured by Tobin' s Q, ROA and ROE. Specifically, there is a high correlation between the Tobin's Q and the log delta (coefficient of 0.293). Specifically, a 100% increase in Pay performance sensitivity will increase the Tobins Q by 29%. This gives support for Hypothesis 1.

The Firm size as measured by employees have the same direction with the company performance meaning that larger (smaller) firms perform better (worse) while the log assets has a negative but significant effect on the company performance. Moreover, the control variable CEO age is negative and significant when the firm performance is measured by Tobins Q. On the one hand it is surprisingly as one would expect that firms with older CEOs tend to perform better than younger CEOs as an older CEO is more experienced and can lead to better company performance. On the other hand an old CEO has less incentives to work hard and increase his experience as a the company will try to compensate this loss incentives with a higher compensation package With regard to leverage the result of negative and significant impact on company performance is not on line with the findings of Jensen's paper in 1986. However, Leverage is also only significant in the 1st Model with Dependent Variable the Tobin's Q.

In contrary to the paper of Khan and Vieitto (2013) who found a positive and significant effect on CEO gender and company performance, in my analysis I didn't find any significant effect. One possible explanation it might be that in my sample there is big number of men compared to women.

The results for the next three models (Model 4,5 and 6), when introducing Firm fixed effects remain almost the same. However R^2 is higher for the models that firm fixed effects has been included.

The next step was to perform a regression analysis in order to test the relationship between work life benefits and pay for performance sensitivity (step2). As far I know there is not a general way to estimate a Probit model with fixed effects, so I perform a regular OLS regression, the so called Linear Probability model. The Linear Probability Model predicts the probability of an event occurring, and, like other linear models, says that the effects of the independent variables on the probabilities are linear. So, the below model has been formulated and *Table 4* presents the results of this analysis.

$WLB_{it} = \beta o + \beta_1 logDELTA_{it} + + \beta_2 logASSETS_{it} + \beta_3 EMPLOYEES_{it} + \beta_4 LEVERAGE_{it} + \beta_5 CEOAGE_{it} + \beta_6 CEOGENDER_{it} + \varepsilon_{it}$

Table 4

The sample period is 2006-2010
Leverage is expressed as ratio
Model 7: clustered standard errors
Model 8: A combination of clustered standard errors and firm fixed effects
Note: *p<0.1, *p<0.05, ***p<0.001, standard errors in parentheses

Model	7	8
Dependent Variable	WLB	WLB
Constant	-0.27***	-.091*
	(,010)	(,121)
logDELTA	-1,37*	-,004**
	(3,31)	(,002)
logASSETS	,047***	,009
	(,012)	(,016)
EMPLOYEES	1,97	5,94
	(9,68)	(3,98)
LEVERAGE	-,07	,010
	(,032)	(,015)
CEOAGE	,009	,0006
	(,013)	(,0007)
CEOGENDER	-,004	,135
	(,023)	(,127)
R squared	,19	,16
Firm Fixed Effects	NO	YES

The results of the analysis of Model 7 indicates that the log of pay for performance sensitivity (logdelta) is negative and significantly associated with the variable work life benefits. More

specifically, if the number of logdelta decreases by one the probability, the company that has a concern on Work Life benefits increases by 137%. However, when firm fixed effects are included in the model (Model 8) , the coefficient of log delta remains significant but lower (-0.004), indicating that if the number of logdelta decreases by one the probability that the company has a concern on Work Life benefits increases by 0,4%.

Finally, it seems that the firm size as measured by log assets plays a significant effect on the Work Life Benefits only when firm fixed effects are not included in the model. This is in line with the theory of Yamamoto & Matsuura (2012) who found that companies with more work-life practices are the companies who have higher assets and can achieve greater sales growth. The rest variables for both models show a non significant effect on Work Life Benefits.

The 3rd *step* of my analysis is to test hypothesis 2. For this reason, the below general model has been examined with dependent variable the firm performance as measured by Tobin's Q, ROA and ROE. The results are presented in **Table 5**.

Firm Performance$_{it}$= βo+β $_1$ WLB$_{it}$ + β $_2$ logASSETS$_{it}$ + β $_3$LEVERAGE$_{it}$ + β$_4$EMPLOYEES$_{it}$ +β $_5$ CEOAGE$_{it}$ +β 6 CEOGENDER$_{it}$+ ε$_{it}$

Table 5
The sample period is 2006-2010
Leverage, Tobin's Q, ROA and ROE are expressed as ratio
Model 9,10,11 has been tested using cluster standard errors at firm level
Model 12,13,14 combination of Cluster Standard Errors and Firm Fixed Effects
Note: *p<0.1, *p<0.05, ***p<0.001, standard errors in parentheses

Model	9	10	11	12	13	14
Dependent Variable	TOBINSQ	ROA	ROE	TOBINSQ	ROA	ROE
constant	5,401***	.336***	.225**	497,3***	.258***	.160
	(.648)	(.068)	(.118)	(.517)	(.048)	(.093)
wlb	.763***	.0218	.012	.477**	.004*	-.00
	(.188)	(.019)	(.034)	(.203)	(.014)	(.030)
logASSETS	-.35***	-.01***	-.001	-.38***	-.01**	.001
	(.049)	(.005)	(.006)	(.052)	(.005)	(.006)
LEVERAGE	-.79***	-.04	-.05	-.78**	-.03**	-.11**
	(.236)	(.042)	(.037)	(.299)	(.050)	(.044)
EMPLOYEES	4.87***	6.18**	5.31	5.34***	4.69***	4.40
	(1.61)	(1.94)	(3.79)	(1.21)	(1.36)	(2.89)
CEOAGE	-.01*	-.00	-.00	-.00	.000	-.00
	(.008)	(.000)	(.001)	(.006)	(.000)	(.001)
CEOGENDER	.000	-.01	.008	.097	.005	.031
	(.287)	(.020)	(.043)	(.307)	(.012)	(.035)
R squared	,2	0	0	,2424	,05	,07
Firm Fixed Effects	No	No	No	Yes	Yes	Yes

In Model 9,10 and 11 a cluster standard error method has been tested and in models 12,13,14 a combination of cluster standard errors and firm fixed effects has been used. Comparing the two methods, there is not any significant difference. The results give support for Hypothesis 2 which states that *Firm performance is positively associated with a concern of work life benefits*. However, we only found a strong significant effect of firm performance on Work Life Benefits only when measured by Tobins Q. Measuring the firm performance with ROA and ROE doesn't seem to have a significant effect on work life benefits for companies who have a strength on that. Moreover the firm size as measured by both employees and log assets have a significant effect on Tobins Q and ROA.

Contrary to what I was expected the CEO age and CEO gender do not have any significant effect on all models. After introducing firm fixed effects in the model the leverage shows a negative and significant relationship with the company performance as measure by ROA ROE and Tobin's Q. This negative relationship between financial leverage and firm performance is in line with the papers of (Onaolapo and Kajola, 2010) .

Taking into account that there are significant relationships from Step 1-3, we can proceed to step *4. In Step 4*, the main hypothesis is examined (H3). I conducted a multiple regression analysis with pay for performance sensitivity and Work life benefits predicting company performance. Examining for Company performance as measured by Tobin's Q, ROE, and ROA (for ROE and ROA I found a not significant relationship with Work life benefits for companies who have a concern on that in Step 3), the below general models have been formulated

$$TobinsQ = \beta o + \beta_1 WLB_{it} + \beta_2 logdelta_{it} + \ldots + \varepsilon_{it}$$
$$ROA = \beta o + \beta_1 WLB_{it} + \beta_2 logdelta_{it} + \ldots + \varepsilon_{it}$$
$$ROE = \beta o + \beta_1 WLB_{it} + \beta_2 logdelta_{it} + \ldots + \varepsilon_{it}$$

Using again the method of cluster standard errors at firm level and then the combination of cluster standard errors and firm fixed effects I examined the above models. The findings are presented in Table 6.

Table 6

The sample period is 2006-2010

Leverage, Tobin's Q, ROA and ROE are expressed as ratio

Model 15,16,17 has been tested using cluster standard errors based on firm

Model 18,19,20 used combination of Cluster Standard Errors and Firm Fixed Effects

Note: *p<0.1, *p<0.05, ***p<0.001, standard errors in parentheses

Model	15	16	17	18	19	20
Dependent Variable	TOBINSQ	ROA	ROE	TOBINSQ	ROA	ROE
Constant	4,484***	,23***	.085	7,81***	.17	-.18
	(.472)	(.046)	(.0855)	(1,43)	(.115)	(.310)
logdelta		.0166***	.0430***		.015**	.066
	.319***			.345***		
	(.032)	(.003)	(.007)	(.045)	(.004)	(.012)
wlb	.489**	.007	-.012	.122*	-.013	-.052
	(.192)	(.014)	(.028)	(2,16)	.017	(.042)
logASSETS	-.511***	-.021***	-.013*	-1,09***	-.022	.055
	(.054)	(.006)	(.007)	(.180)	(.015)	(.038)
EMPLOYEES	4.05***	4.17**	2.13	-1.86***	-3.41	-3.8
	(1.55)	(1.28)	(2.52)	(3.88)	1.01	(2.37)
LEVERAGE	-.294	-.005	-.059	-.381	-.027	-.250
	(.267)	(.048)	(.041)	(.519)	(.095)	(.205)
CEOAGE	.015**	-.0004	-.001	.001*	.001	.0003
	(.006)	(.048)	(.0012)	(.009)	(.0007)	(.002)
CEOGENDER	.377	.021	.06	1.09*	.047**	.224
	(.295)	(.014)	(.044)	(.434)	(.017)	(.126)
R2	0.33	.10	.045	0.33	,058	,003
Firm Fixed Effects	No	No	No	Yes	Yes	Yes

The effect of Work life benefits is still significant after adding in the regression analysis the variable of the logarithm of Pay for Performance sensitivity. So, the finding supports for a partial mediation. In general, comparing the coefficients on Log Delta of Table 3 and Table 6 we can see that the coefficients are about the same, indicating that the effect of Log Delta is more or less independent from Work Life Benefits. Specifically, after adding the Work Life benefits in the regression analysis (Table 6) the coefficients are slightly higher and still significant.

However, it is worth mentioning that when work life benefits is included as control variable CEO age plays a significant role in the relationship between company performance (as measured by Tobins Q) and pay performance sensitivity (when the work life benefits is included as control variable. Moreover, CEO gender became highly significant when firm fixed effects have been added in the model 19. This indicated that firm fixed effects play a significant role in the relationship of CEO Gender and company performance.

5.3 Conclusion

Summarizing the above results, the below table has been formulated to understand better the findings.

Step	Analysis	Hypothesis testing	Finding	Support Hypothesis
1	Conduct a simple regression analysis with pay for performance sensitivity predicting company performance	**H1:** High Pay for performance sensitivity is associated with high company performance	Positive and significant effect on company performance as measured by ROA, ROE and Tobin's Q	Support for H1
2	Conduct a simple regression analysis with pay for performance sensitivity predicting Work Life benefits	**a path**	Negative and significant effect on Work Life Benefits	
3	Conduct a linear propabilty regression regression analysis with Work life benefits predicting company performance.	**H2:**High firm performance is associated with a concern of work life benefits	Positive and significant effect on company performance when measured by Tobin's Q.	Support for H2 only when the firm performance is measured by Tobins Q
4	Conduct a multiple regression analysis with Pay for performance sensitivity and WLB(for companies who have a concern) predicting Company performance	**H3**: A concern of work life benefits mediate the relation between Pay for Performance sensitivity and company performance.	Positive and significant effect for both Pay for performance sensitivity and WLB(for companies who have a concern) benefits on company performance(Tobin's q)	Partial support for H3

6. Discussion

Executive compensation has been a topic of much discussion among the researchers for a long period of time. Continuous debates among the press about the level, structure and role of CEO compensation take place in most countries (Duffhues and Kabir 2008) while in the same time there were concerns whether companies should provide employees with the balance of work and family. That balance can be succeeded by offering work life benefits to employees.

The purpose of this study was to investigate the mediator role of Work life benefits (when companies have a concern on that) on the Pay for performance sensitivity and Company Performance. In order to test this main research question three hypothesis have been formulated and the model of Baron and Kenny (1986) has been followed proposing a four step approach in which several regression analyses are conducted.

Our findings indicated support for the first Hypothesis which is stated as 'High Pay for performance sensitivity is associated with high company performance'. More specifically, the results indicated a positive and significant association with company performance and pay for performance sensitivity as it was expected. To proxy for firm performance we used the Tobin's q, the ROA and the ROE. This is in line with the authors McConaughy and Mishra (1996) who found that high levels of pay performance sensitivity are associated with high future company performance.

For Hypothesis 2 which is stated as 'firm performance is positively associated with a concern of work life benefits' we found support with the results indicating company concerns of work life benefits to have a positive and significant effect on company performance only when measured by Tobin's Q and an insignificant effect when measured by ROE and ROA.

As it has been already mentioned it seems that it depends to what kinds of work life benefits are provided to employees. It, should be that work-life practice cannot be effective and employees will not be willing to take advantage of these programs if they believe it might end soon and this is not part of the organizational culture. (Chinchilla, Poelmans & Leon, 2003). On the other hand it can be claimed that offering specific benefits to employees entails such a high investment for the company that any increase in firm performance would be offset by its cost (Meyer et al, 2001; Dex & Smith, 2002). Finally, as Meyer et al (2001) also observed that companies who implement work life benefits were actually reducing labor cost which in turn reduce the company performance.

Our main hypothesis stated as 'A concern of work life benefits mediate the relation between Pay for Performance sensitivity and company performance'. We found evidence of partial mediation as we predicted a significant role for both Pay for performance sensitivity and WLB in the Company performance (as measured by Tobin's Q). A possible explanation for this is that the concern of Work life benefits is not the main factor that can mediate the relationship between the company performance and pay for performance sensitivity. Moreover, the effect of Log Delta is independent from Work Life Benefits and whether the companies have a strength on that.

Considering the findings, it should be mentioned that even if we found support and the estimates move in the same or the opposite direction this doesn't mean the we have causation. It could be that there is another factor that can have an impact on the firm performance the work life benefits and the pay for performance sensitivity. This could also be explained from the sample which is not representative.

Taking into account the causation issue and the limitations that have been presented in an earlier section, a future research can be addressed these. It would be interesting though to examine the mediator role of work life benefits in different kind of industries and control for variables like marital status of CEO. Finally, future research on CEO incentives and employee satisfaction would also provide a valuable contribution. For example, it could be a good idea to examine whether employees in firms with more incentivized CEOs are more or less happy about how they are treated. CEOs with high-powered incentives might reduce wages costs or realize that employee morale is important for firm performance and hence treat employees very well.

Finally, the findings from the current study are important to both employees and employers in terms of a better understanding of Work Life Benefits and its effects on people's wellbeing and company performance. Indeed, from the theory that it has been developed above, work-life balance practices, as promoted by many organizations, rests on attracting better applicants and reducing work-life conflict among existing employees in order to help company performance. However, even if we found a partial mediator effect of Work Life benefits on Pay performance sensitivity and organizational Performance, this thesis can still be considered as a base for companies who want to increase their value.

Appendix A

The value and the delta of the stock options possessed by the executives are calculated using the adjusted Merton-Black-Scholes option valuation method. For the calculation of the pay-for-performance sensitivity the existing portfolio of the executive will be taken.

The adjusted formula of Merton (1973) is: Option value = N [Pe-dTΦ(Z) – Xe-rTΦ(Z - σ√T)]

Where:

Z = [ln(P/X) + T(r – d + σ2/2)] / σ√T N = number of options   P = price of underlying stock   X = exercise price of the option

T = time to expiration   d = expected dividend rate   r = risk-free interest rate σ = expected standard deviation of stock return   Φ (x) = cumulative probability function for normal distribution

The delta of the option s is calculated by taking the cumulative probability function for normal distribution of Z: Φ(Z).

Appendix B: Predictive validity framework

Independent variable (X)   Dependent variable (Y)

Conceptual

| Pay for Performance Sensitivity | → | Work Life benefits | → | Company Performance |

Operational

| Lna

a: pay for performance sensitivity | → | **Company concern of Work Life benefits** | → | Return on Assets, Tobins Q, Return on Equity |

Control Variables:

CEO age
CEO gender
Employee number, log assets, leverage
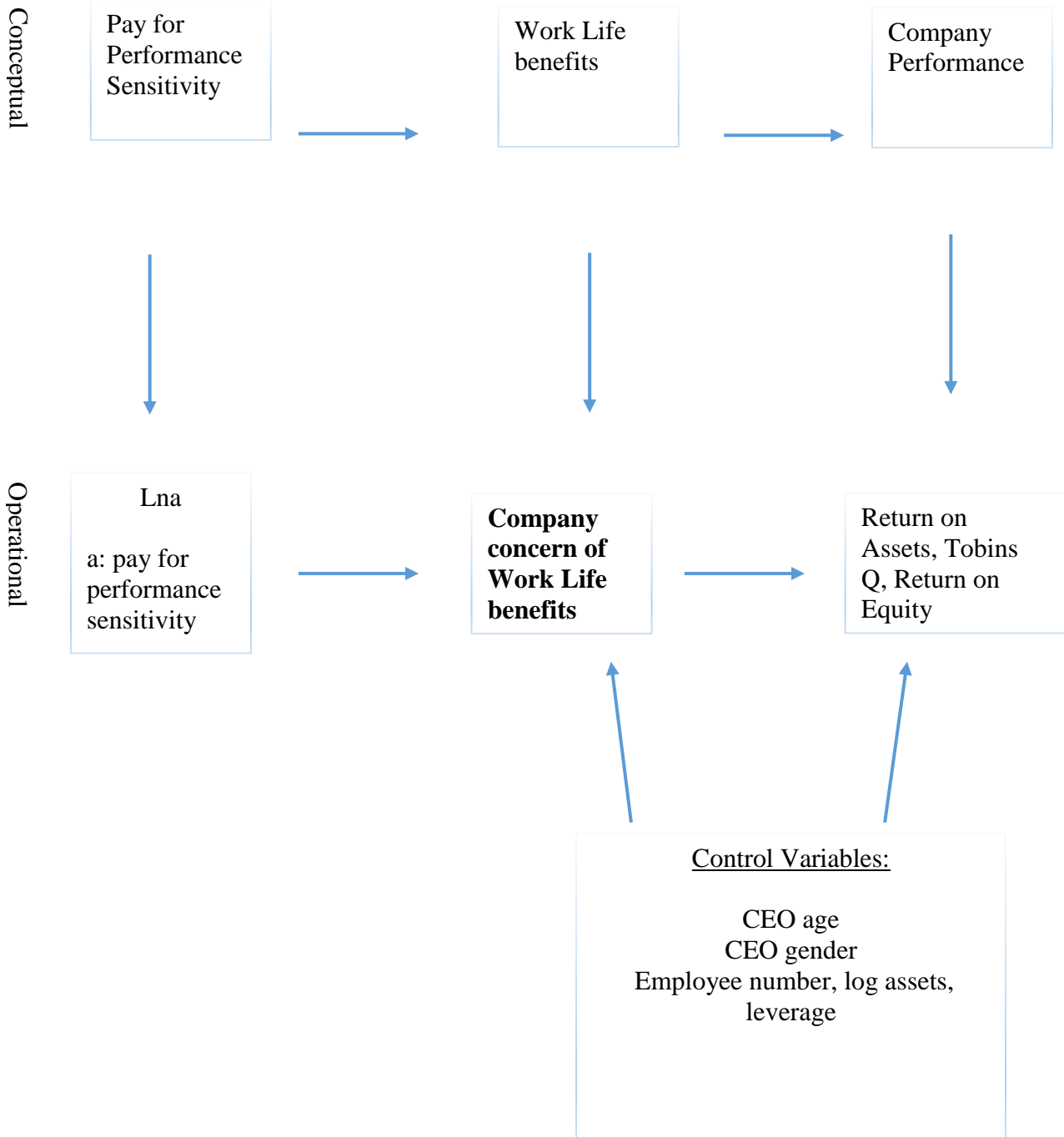
Appendix C: Companies included in the sample

#	Companies	#	Companies
1	HESS CORP	41	DOMINION RESOURCES INC
2	VERIZON COMMUNICATIONS INC	42	FREEPORT-MCMORAN INC
3	JPMORGAN CHASE & CO	43	EOG RESOURCES INC
4	COMCAST CORP	44	OSI RESTAURANT PARTNERS INC
5	CA INC	45	CENTERPOINT ENERGY INC
6	MOLSON COORS BREWING CO	46	POLYONE CORP
7	FEDEX CORP	47	TITAN INTERNATIONAL INC
8	MELLON FINANCIAL CORP	48	PMI GROUP INC
9	AT&T INC	49	M & T BANK CORP
10	UNITEDHEALTH GROUP INC	50	EPICOR SOFTWARE CORP -OLD
11	ORACLE CORP	51	COSTCO WHOLESALE CORP
12	KB HOME	52	WGL HOLDINGS INC
13	REGIONS FINANCIAL CORP	53	PRICE (T. ROWE) GROUP
14	VECTREN CORP	54	AES CORP
15	PNM RESOURCES INC	55	ALLEGHENY TECHNOLOGIES INC
16	SCANA CORP	56	DIAMOND OFFSHRE DRILLING INC
17	SEALED AIR CORP	57	MBIA INC
18	SENSIENT TECHNOLOGIES CORP	58	ENERGY EAST CORP
19	AQUILA INC	59	CIBER INC
20	VARIAN MEDICAL SYSTEMS INC	60	LANDRYS RESTAURANTS INC
21	PPL CORP	61	LABORATORY CP OF AMER HLDGS
22	CONOCOPHILLIPS	62	MCKESSON CORP
23	CH ENERGY GROUP INC	63	CONSTELLATION BRANDS -CL A
24	CHEMED CORP	64	BJ'S WHOLESALE CLUB INC
25	ENERGEN CORP	65	ACTUANT CORP -CL A
26	INSTEEL INDUSTRIES	66	ALTRIA GROUP INC
27	JO-ANN STORES INC	67	CAPITAL ONE FINANCIAL CORP
28	XCEL ENERGY INC	68	VALERO ENERGY CORP
29	AQUA AMERICA INC	69	HEALTH NET INC
30	AGILYSYS INC	70	SUNOCO INC
31	CASH AMERICA INTL INC	71	SVB FINANCIAL GROUP
32	SAKS INC	72	PSS WORLD MEDICAL INC
33	AMCOL INTERNATIONAL CORP	73	MAF BANCORP INC
34	DEVON ENERGY CORP	74	MANPOWERGROUP
35	TETRA TECHNOLOGIES INC/DE	75	ENTERGY CORP
36	BENCHMARK ELECTRONICS INC	76	INSIGHT ENTERPRISES INC
37	REGENERON PHARMACEUTICALS	77	RTI INTL METALS INC
38	PANERA BREAD CO	78	ADTRAN INC
39	VERTEX PHARMACEUTICALS INC	79	MONACO COACH CORP
40	XTO ENERGY INC	80	INVESTMENT TECHNOLOGY GP INC

81	DENNYS CORP	121	EXELON CORP
82	CARDINAL HEALTH INC	122	CLECO CORP
83	POLYCOM INC	123	FLOWSERVE CORP
84	HELIX ENERGY SOLUTIONS GROUP	124	PEPSIAMERICAS INC
85	SCPIE HOLDINGS INC	125	WASTE MANAGEMENT INC
86	PG&E CORP	126	ITT EDUCATIONAL SERVICES INC
87	PRAXAIR INC	127	ARBITRON INC
88	EXTREME NETWORKS INC	128	ATMI INC
89	AKAMAI TECHNOLOGIES INC	129	TRIAD HOSPITALS INC
90	JUNIPER NETWORKS INC	130	LIFEPOINT HEALTH INC
91	SANDISK CORP	131	NAVIGANT CONSULTING INC
92	GRACE (W R) & CO	132	FEI CO
93	UNUM GROUP	133	PMC-SIERRA INC
94	AVID TECHNOLOGY INC	134	GLOBAL PAYMENTS INC
95	NVIDIA CORP	135	MOBILE MINI INC
96	QUEST DIAGNOSTICS INC	136	EMCOR GROUP INC
97	AVISTA CORP	137	SUNRISE SENIOR LIVING INC
98	ARCH CHEMICALS INC	138	AGERE SYSTEMS INC
99	NVR INC	139	MONSANTO CO
100	POOL CORP	140	ZIMMER BIOMET HOLDINGS INC
		141	STARWOOD HOTELS&RESORTS WRLD
101	VERTRUE INC	142	INCYTE CORP
102	VIASAT INC	143	GRANT PRIDECO INC
103	WESTAR ENERGY INC	144	IDEXX LABS INC
104	CAMERON INTERNATIONAL CORP	145	STILLWATER MINING CO
105	DSP GROUP INC	146	VIASYS HEALTHCARE INC
106	TD BANKNORTH INC	147	SKYWORKS SOLUTIONS INC
107	SPSS INC	148	TRIQUINT SEMICONDUCTOR INC
108	HYPERION SOLUTIONS CORP	149	VALEANT PHARMACEUTICALS - OLD
109	EAST WEST BANCORP INC	150	PDL BIOPHARMA INC
110	RADIANT SYSTEMS INC	151	ODYSSEY HEALTHCARE INC
111	P F CHANGS CHINA BISTRO INC	152	PRINCIPAL FINANCIAL GRP INC
112	BALLY TOTAL FITNESS HLDG CP	153	SAVIENT PHARMACEUTICALS INC
113	UCBH HOLDINGS INC	154	BROOKLINE BANCORP INC
114	IDEX CORP	155	DRS TECHNOLOGIES INC
115	AUTONATION INC	156	KEYSPAN CORP
116	ADOBE SYSTEMS INC	157	3M CO
117	DAVITA HEALTHCARE PARTNERS	158	FRONTIER OIL CORP
118	NISOURCE INC	159	ANSYS INC
119	AETNA INC	160	FMC TECHNOLOGIES INC
120	METLIFE INC		

161	JDA SOFTWARE GROUP INC	201	SCIENTIFIC GAMES CORP
162	AMERIGROUP CORP	202	STARTEK INC
163	MERITAGE HOMES CORP	203	TRADESTATION GROUP INC
164	AMERICAN MEDICAL SYSTMS HLDS	204	AFFYMETRIX INC
165	SELECT COMFORT CORP	205	CONSOL ENERGY INC
166	EXXON MOBIL CORP	206	FIRST INDIANA CORP
167	NAUTILUS INC	207	KENDLE INTERNATIONAL INC
168	WINTRUST FINANCIAL CORP	208	KEYSTONE AUTOMOTIVE INDS INC
169	INTERNAP CORP	209	SAFETY INSURANCE GROUP INC
170	EFUNDS CORP	210	WILSHIRE BANCORP INC
171	BIOGEN INC	211	PSYCHIATRIC SOLUTIONS INC
172	EL PASO CORP	212	BLUE COAT SYSTEMS INC
173	ICU MEDICAL INC	213	NEOWARE INC
174	LAIDLAW INTERNATIONAL INC	214	FIDELITY NATIONAL INFO SVCS
175	TD AMERITRADE HOLDING CORP	215	ACUITY BRANDS INC
176	SWS GROUP INC	216	CALIFORNIA PIZZA KITCHEN INC
177	TIBCO SOFTWARE INC	217	VENTANA MEDICAL SYSTEM INC
178	OFFICEMAX INC	218	GOLDMAN SACHS GROUP INC
179	JANUS CAPITAL GROUP INC	219	HOST HOTELS & RESORTS INC
180	PRIDE INTERNATIONAL INC	220	ASSURANT INC
181	INFINITY PROPERTY & CAS CORP	221	MKS INSTRUMENTS INC
182	ADVANCE AUTO PARTS INC	222	NETFLIX INC
183	MEDCO HEALTH SOLUTIONS INC	223	99 CENTS ONLY STORES
184	ADVANCED MEDICAL OPTICS INC	224	ENCORE ACQUISITION CO
185	STAGE STORES INC	225	WELLCARE HEALTH PLANS INC
186	DITECH NETWORKS INC	226	BLUE NILE INC
187	NETGEAR INC	227	BLACKBAUD INC
188	PROASSURANCE CORP	228	NEUSTAR INC
189	RED ROBIN GOURMET BURGERS	229	ADESA INC
190	USANA HEALTH SCIENCES INC	230	GENESIS HEALTHCARE CORP
191	GAMESTOP CORP	231	WEBEX COMMUNICATIONS INC
192	GEN-PROBE INC	232	LIFE TIME FITNESS INC
193	M/I HOMES INC	233	CYBERSOURCE CORP
194	D R HORTON INC	234	FOUNDRY NETWORKS INC
195	GLACIER BANCORP INC	235	INFORMATICA CORP
196	GENWORTH FINANCIAL INC	236	JONES LANG LASALLE INC
197	FIRST NIAGARA FINANCIAL GRP	237	KBR INC
198	QUICKSILVER RESOURCES INC	238	LHC GROUP INC
199	VIACOM INC	239	MOLINA HEALTHCARE INC
200	PLAYTEX PRODUCTS INC	240	OMNICELL INC

241	NATCO GROUP INC	281	EMERGENT BIOSOLUTIONS INC
242	PERFICIENT INC	282	EXPONENT INC
243	SI INTERNATIONAL INC	283	NETSCOUT SYSTEMS INC
244	RANGE RESOURCES CORP	284	PINNACLE FINL PARTNERS INC
245	DIGITAL RIVER INC	285	QUEST SOFTWARE INC
246	PHASE FORWARD INC	286	CISCO SYSTEMS INC
247	MARVEL ENTERTAINMENT INC	287	MACY'S INC
248	DREAMWORKS ANIMATION INC	288	COLLECTIVE BRANDS INC
249	NUTRISYSTEM INC	289	APPLIED INDUSTRIAL TECH INC
250	MASTERCARD INC	290	QUIKSILVER INC
251	AMERIPRISE FINANCIAL INC	291	AGILENT TECHNOLOGIES INC
252	WYNDHAM WORLDWIDE CORP	292	C H ROBINSON WORLDWIDE INC
253	AIRTRAN HOLDINGS INC	293	CABOT MICROELECTRONICS CORP
254	RENT-A-CENTER INC	294	TRUEBLUE INC
255	CENTENE CORP	295	TETRA TECH INC
256	EMS TECHNOLOGIES INC	296	INTERSIL CORP -CL A
257	ENPRO INDUSTRIES INC	297	HEADWATERS INC
258	EPIQ SYSTEMS INC	298	ARIBA INC
259	GENTIVA HEALTH SERVICES INC	299	BLACKROCK INC
260	HEARTLAND PAYMENT SYSTEMS	300	CME GROUP INC
261	NATIONAL FINANCIAL PRTNRS CP	301	APPLIED MICRO CIRCUITS CORP
262	OLYMPIC STEEL INC	302	SRA INTERNATIONAL INC
263	PARKWAY PROPERTIES INC	303	MEDCATH CORP
264	SONIC AUTOMOTIVE INC -CL A	304	SYNNEX CORP
265	SUPERIOR WELL SERVICES INC	305	BIG 5 SPORTING GOODS CORP
266	TALEO CORP	306	BILL BARRETT CORP
267	TREEHOUSE FOODS INC	307	HMS HOLDINGS CORP
268	TRUE RELIGION APPAREL INC	308	FIRST FINL BANKSHARES INC
269	TTM TECHNOLOGIES INC	309	HEALTHSPRING INC
270	VIAD CORP	310	TERADATA CORP
271	BANKUNITED FINANCIAL CORP	311	BROADRIDGE FINANCIAL SOLUTNS
272	DJO INC	312	J CREW GROUP INC
273	SYNAPTICS INC	313	INTEGRAL SYSTEMS INC
274	MARINER ENERGY INC	314	LANDAUER INC
275	HITTITE MICROWAVE CORP	315	MWI VETERINARY SUPPLY
276	SALESFORCE.COM INC	316	PHARMERICA CORP
277	UNITED THERAPEUTICS CORP	317	SOLERA HOLDINGS INC
278	EAGLE MATERIALS INC	318	COMPELLENT TECHNOLOGIES INC
279	BJ'S RESTAURANTS INC	319	ALLEGIANT TRAVEL CO
280	DTS INC	320	BALLY TECHNOLOGIES INC
321	ERESEARCHTECHNOLOGY INC	365	PCTEL INC
322	CIRCOR INTL INC	366	FRONTIER COMMUNICATIONS CORP
323	HEWITT ASSOCIATES INC	367	PRGX GLOBAL INC

324	AECOM INC	368	CATALYST HEALTH SOLUTIONS
325	SYNIVERSE HOLDINGS INC	369	ATC TECHNOLOGY CORP
326	VOLCOM INC	370	AMERICAN CAPITAL LTD
327	AMERISAFE INC	371	LIFE TECHNOLOGIES CORP
328	EHEALTH INC	372	ZEP INC
329	COMSCORE INC	373	TICKETMASTER ENTERTNMNT INC
330	MSCI INC	374	VISA INC
331	AMERICAN PUBLIC EDUCATION	375	GENOPTIX INC
332	COGENT INC	376	TW TELECOM INC
333	MICRUS ENDOVASCULAR CORP	377	DISCOVERY COMMUNICATIONS INC
334	SOURCEFIRE INC	378	NCI INC
335	INTERACTIVE BROKERS GROUP	379	DOLAN CO
336	ENSIGN GROUP INC	380	ORION MARINE GROUP INC
337	OPLINK COMMUNICATIONS INC	381	ALLSCRIPTS HEALTHCARE SOLTNS
338	LIQUIDITY SERVICES INC	382	SUPER MICRO COMPUTER INC
339	CABLEVISION SYS CORP -CL A	383	KAPSTONE PAPER & PACKAGING
340	CONTANGO OIL & GAS CO	384	QUESTCOR PHARMACEUTICALS INC
341	IGATE CORP	385	B&G FOODS INC
342	PROVIDENT FINANCIAL SVCS INC	386	VIRTUSA CORP
343	TEXAS CAPITAL BANCSHARES INC	387	MEDNAX INC
344	COMPASS MINERALS INTL INC	388	EQT CORP
345	RIGHTNOW TECHNOLOGIES INC	389	BLYTH INC
346	SYNCHRONOSS TECHNOLOGIES	390	MERCK & CO
347	MEADOWBROOK INS GROUP INC	391	RRI ENERGY INC
348	PRESTIGE BRANDS HOLDINGS	392	KID BRANDS INC
349	CALAMOS ASSET MANAGEMENT INC	393	CLEARWATER PAPER CORP
350	KOPPERS HOLDINGS INC	394	TIME WARNER CABLE INC
351	MONOTYPE IMAGING HOLDINGS	395	IPC HEALTHCARE INC
352	SONOSITE INC	396	INTREPID POTASH INC
353	ALPHA NATURAL RESOURCES INC	397	HI TECH PHARMACAL CO INC
354	VERIFONE SYSTEMS INC	398	MEDIFAST INC
355	APPROACH RESOURCES INC	399	CORELOGIC INC
356	CLIFFS NATURAL RESOURCES INC	400	MAXIM INTEGRATED PRODUCTS
357	CRACKER BARREL OLD CTRY STOR	401	JONES GROUP INC
358	IAC/INTERACTIVECORP	402	O'REILLY AUTOMOTIVE INC
359	ZIX CORP	403	CAREFUSION CORP
360	NETAPP INC	404	QEP RESOURCES INC
361	HANGER INC		
362	AXT INC		
363	DISH NETWORK CORP		
364	NV ENERGY INC		

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