Duckworth Industries, Inc.—Incentive Compensation Programs

In early 1992, Mr. John Duckworth, president and controlling shareholder of Duckworth Industries, was considering a change in Duckworth Industries' management incentive compensation systems. If implemented, the new plan for Duckworth management would, it was hoped, align more closely the interests of management and shareholders. Several industrial firms that were pioneers in value-based management had recently adopted similar management compensation systems. Adopting the new system would keep Duckworth in the vanguard of management incentive compensation planning.

Background

Mr. Duckworth was a strong believer in the power of incentives to guide management action. When he was first promoted to a plant management job in the 1950s, Mr. Duckworth took over a plant that had an operating loss of \$2.7 million on sales of \$9.0 million. He implemented what was then a state-of-the-art plan for factory incentives. The plan applied to all supervisors. Achievement of specified goals earned a 15% premium over an individual's base rate of pay. As noted by Mr. Duckworth:

> The more sobering side of the plan consisted of docking supervisors 12% of their base rate when goals were not achieved. Paychecks having a 12% deduction for failure were distributed in bright red envelopes. At that time I was plant manager of the operation, and I got several red pay envelopes. Some 15–18 months after the "12% Club" was profitably and smoothly functioning, the National Labor Relations Board issued a cease and desist order predicated on the fact you cannot tamper with an individual's base pay. Naturally, I complied, but the results were already in—the division was profitable.

Mr. Duckworth founded his own business in 1971. Sales grew from \$400,000 in that year to almost \$125 million in 1992 (Exhibit 1). In 1986 a holding company, Duckworth Industries, was established. It included the original business, Worth Corpo-

Harvard Business School case 293–091.

ration, which was a highly profitable producer of proprietary fasteners and adhesives. In 1986, Hospitality Equipment Service was acquired at a purchase price of $5.5 million. In 1988, Hotel Telecom Services was acquired for about $15.0 million. The two newer acquisitions were service businesses rather than manufacturers and to date had not yet generated satisfactory levels of profitability. In 1992, Duckworth Industries employed 755 people. The structure of the organization is shown in Exhibit 2.

The Duckworth Incentive Plans

Pay for performance was firmly embedded in the corporate culture at Duckworth Industries. In the words of one senior executive, "We put incentives, within reason, behind everything we can."

For plant-level employees, Duckworth had an attendance bonus. A pay incentive of 60¢ per hour was earned for each pay period during which an employee was never more than two minutes late for work.

For plant-level employees up to the shift supervisory level, there was also a quality incentive plan (Exhibits 3 and 4). Quality measures included many variables, such as meeting promised shipment dates and reducing customer complaints of any nature. The quality incentive payment target equaled $100 per employee per month. Performance was often a team effort, and the average employee working under this incentive plan received about $600 per year from it. Employees received a separate check each month for the quality bonus to highlight the importance of quality in the company culture.

All Duckworth employees were participants in a profit-sharing plan. At the level of each business unit, a profit-sharing pool was created. The pool was equal in size to 15% of pre-tax profits after a deduction equal to 10% of the beginning-of-year net worth allocated to the business unit. At the end of each year, the profit-sharing pool was allocated to employees, pro rata, based on their individual share of total wages and salaries in the business unit. At the Worth business unit, profit sharing had grown from about 2% of pay to about 15% of pay in recent years. A plant worker earning $15,000 per year would get $2,250. Information sharing with plant personnel as to profit and margin levels was common at Duckworth, so an estimate of the size of their individual profit-sharing allocation could be made by employees as the year progressed.

The company also had individual incentive plans for all sales and supervisory personnel. These typically afforded an employee the opportunity to earn incentives ranging from 10% to 40% of base pay. The incentive plan targets for a typical customer service representative are included as Exhibit 5.

The Existing Senior Management Incentive Plans

The more senior managers at Duckworth (a group comprised of up to 40 people) all participated in an annual incentive compensation plan. A smaller subset of this group also participated in a long-term incentive program.

The incentive plans (both annual and long-term) for the senior managers had undergone considerable change in the 1983–1992 decade. Prior to 1990, the annual incentive plan would target for each manager a bonus of 20–50% of base salary if certain target levels of performance at the business unit level were reached during the year. Typical measures of performance (depending on the manager's area of responsibility) included at least three of the following:

- Cash flow.
- Sales growth of proprietary products.
- Direct labor variances.
- Inventory turns.
- Accounts receivable (days sales outstanding).
- Gross margins (less purchase price variances).
- Special individual projects.

In 1990, Duckworth abandoned the narrowly defined annual targets and opted to tie the annual bonus to a matrix built around sales growth and profitability goals. Annually, goals for each business unit were set for both sales growth and profitability (Exhibit 6). These were determined with reference to the performance levels achieved by various peer group companies (Exhibit 7). Individual managers were assigned bonus targets (generally ranging from 25% to 50% of base compensation). Depending on the level of sales growth and profitability achieved, a manager could read directly from the matrix the factor by which his or her target bonus would be multiplied to determine the actual bonus he or she would receive. The incentive compensation matrix for the Worth business unit (Exhibit 6) indicated the following: If, in fiscal 1992, a manager working at the Worth business unit had a target bonus of 40%, and the business unit provided a 20% return on assets and 10% sales growth, the manager would receive 1.00 times his or her 40% target bonus. Table A shows the percentages of target bonuses business unit managers at Duckworth received from the annual incentive plan in 1991 and 1992.

While Duckworth's annual incentive plan for senior managers covered several dozen employees by 1992, the long-term incentive plan covered fewer participants, particularly in the early part of the decade from 1983 to 1992. In 1983, Duckworth implemented a 5-year, long-term management incentive plan. The plan covered only two employees, the then vice president and general manager at Worth (now retired) and the then vice president of sales and marketing at Worth (now president of the Hotel Telecom Services operation). The plan made one payment at the end of 5 years; it was a phantom stock plan tied to the increase in book value per share multiplied by a performance factor (Exhibit 8). The performance factor was determined by several measures including (1) the spread separating annual ROE from the sum of the bank prime rate plus two percentage points, and (2) the annual growth in net book value per share.

According to one of the participants, the plan was a horror in complexity, but the fact that a manager could have 1 or 2 bad years and still get a payment was an attractive feature. Because the plan paid only once at the end of 5 years, it was somewhat like a forced savings plan. According to one manager, "The size of the payment at the end made a meaningful difference in what you could do lifestyle-wise.

TABLE A
Annual Incentive Plan Bonuses, 1991 and 1992

	1991	*1992*
Worth Corporation	170%	0%
Hotel Telecom	0	24
Hospitality Equipment	0	0
Duckworth Industries	90	0

TABLE B
Long-Term Incentive Plan Bonuses, 1989–1992

	1989	1990	1991	1992
Worth Corporation	112%	97%	92%	91%
Hotel Telecom	—	40	20	0
Hospitality Equipment	—	—	40	45
Duckworth Industries	85	80	75	73

A check for $150,000 is quite significant when you bring it home. You are willing to make significant personal sacrifices along the way to make it happen."

In 1986 a new long-term management incentive plan was put in place at Duckworth. This plan was broadened to include more managers (15 by 1989) and was designed to begin payments in 1989 after the expiration of the previously described 5-year plan. At the start of each year, beginning in 1986, new targets would be established so that incentive payments could be received annually. The business unit management participants in this plan would be awarded a specified percentage of base salary (generally from 25% to 40%) if a Challenge Earnings level of cumulative earnings before interest and taxes (approved by Duckworth's board of directors) was achieved by their business unit during the period. Lesser levels of earnings achievement would produce a proportionately reduced level of award (as shown in Exhibit 9 for the Worth business unit).

The incentive system established in 1986 continued for 4 years. The last update was put in place in 1989 and covered the 3-year time period ending in 1992. Table B presents the percentages of target bonuses that business unit managers received from the long-term incentive plan between 1989 and 1992.

For the top management team at Duckworth, the target and actual bonus payments (measured as a percentage of base salary) are presented as Exhibit 10.

A Proposed New EVA Incentive System

As fiscal 1992 unfolded, both management and Mr. Duckworth (the controlling shareholder) were looking for ways to more closely align the interests of management and shareholders through the incentive plan for senior management. A number of factors had contributed to dissatisfaction with the existing plans. One major factor had to do with operation of the annual incentive plan of Worth in 1992. In many ways, as Table C shows, Worth's performance in 1992 was improved over that of 1991.

The return on gross performing assets had increased, but sales had declined slightly (versus a 10% goal and a minimum 5% sales growth requirement to achieve any annual incentive plan payment). The sales decline was caused by the loss of a very large

TABLE C
Gross Performing Asset Return and Sales Growth, 1991–1992

	Worth Corporation	
	1991	1992
Return on gross performing assets	23.6%	23.9%
Sales growth	13.9	(2.3)

customer buying a product with commodity-type profit margins. Most of the lost sales in 1992 had been replaced by new customers purchasing proprietary products at higher margins. The change in customer mix was good for enhancing long-run shareholder value, but given the structure of the existing annual incentive plan (Exhibit 6), Worth's management failed to achieve any annual incentive bonus as a result of the change.

Near the close of fiscal 1992, Mr. John Duckworth began reading a book by G. Bennett Stewart entitled *The Quest for Value*. Stewart's book outlined a management incentive plan that promised to link management pay directly to the creation of long-run economic value for shareholders. Implementation of the plan required the services of Stern Stewart & Co., a financial consulting firm.

The economic valued-added (EVA) compensation system developed by Stern Stewart would require (1) considerable data analysis and (2) some reorienting in thinking about how to approach the business going forward for Duckworth's senior management. The EVA system was predicated on the following logic:

1. Economic value for shareholders is created when a firm earns a rate of return on invested capital that exceeds the cost of capital. The economic value-added in a particular year should equal the product of
   a. The average capital employed during the year multiplied by
   b. The spread separating the cost of capital from the return on capital earned during the year.

2. The EVA during a year can be calculated for each business unit. The management of each unit can be directly compensated for its success in adding economic value via a compensation formula that automatically adjusts the baseline for calculating next year's bonus to reflect the actual performance of the prior year.

The Key Drivers of EVA

Exhibit 11 shows a calculation of the EVA by the Worth division of Duckworth Industries from 1988 through 1992. It also shows the forecasted EVA for the period 1993–1997.

The key variables in determining the EVA by a business unit were:

1. Net operating profit after taxes (NOPAT) (Exhibit 11, Line 9).
This excludes corporate overhead, and capitalizes R&D expenses and then amortizes them over 3 years. NOPAT excludes noneconomic, noncash charges.[1]

2. Average capital (Exhibit 11, Line 15).
This excludes construction in progress, and assumes FIFO inventory valuation and the add-back of bad debt reserves. Noneconomic, noncash writeoffs are added back to average capital.[2]

3. Cost of capital (Exhibit 11, Line 17).
This is determined annually for each business unit by using an assumed capital structure and riskiness factor (β value) for peer group firms comparable to each business unit. The formula for calculating capital cost was tied to the yield on 30-year Treasury obligations plus a risk premium.

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1. Items such as the one-time writeoff of a divested business would be a noneconomic, noncash charge. Items such as depreciation or the amortization of debt discount would be economic, noncash charges.

2. This was designed to prevent managers from escaping responsibility for poor prior investment decisions by simply divesting the poorly performing assets.

The Mechanism for Calculating Incentive Compensation

Stern Stewart recommended a mechanism for linking EVA in a business unit during a given year to the incentive compensation paid to management in that year.

First, a bonus target was established. At Worth, this might equal 37% of base pay (Exhibit 12, Line 1). Bonus units (like phantom stock) would be assigned to each manager in an amount such that if the bonus unit was valued at $1.00, the desired level of bonus would be earned by the manager (Exhibit 12, Line 3).

Second, a baseline EVA level was established (Exhibit 12, Line 4). At the end of each year, the baseline EVA for the following year would change by one-half of the difference between the actual EVA achieved and the baseline EVA for the prior year (Exhibit 12, Lines 8–10). This made the system self-adjusting. If EVA performance improved each year, the new base would click up by one-half the amount of the improvement. If EVA performance deteriorated for several years, the base level would decline so that the targets would not be so far away as to be unreachable in ensuing years.

Third, a base unit value was established for each ensuing year (Exhibit 12, Lines 6 and 14). This base unit value defined, to a large degree, how much of the target bonus could be earned by just maintaining the existing level of business performance. If EVA hit exactly the baseline EVA each year, and the base unit value was set at $1.00, then exactly the target bonus would be earned each year. In the case of Worth, after the first year, the base unit value dropped to $.80. This meant that simply repeating the EVA baseline performance after 1993 would produce only 80% of the targeted bonus.

Fourth, a bonus sensitivity factor (Exhibit 12, Lines 7 and 11) was established that could either add to or subtract from the base unit value to create a total unit value. In the Worth example, the bonus sensitivity factor was set at $1,625,000. In any year that EVA varied from the baseline EVA, the amount of the gap was divided by $1,625,000, and the resulting amount (called the performance unit value, Exhibit 12, Lines 12 and 13) was added to the base unit value to determine the total unit value (Exhibit 12, Line 15). In order to earn one times the target bonus solely from the performance unit factor, management of the business unit had to beat the baseline EVA by the amount of the bonus sensitivity factor.

As indicated in Exhibit 12, if Worth hit the forecasted level of EVA in each year, Worth's management would earn the percentage shown in Table D of its target bonus in each of the next 5 years.

TABLE D
Forecasted Earned Target Bonuses, 1993–1997

	% of Target Bonus Earned, Worth Corporation
1993	100%
1994	51
1995	122
1996	170
1997	211[a]

a. Bonuses up to two times the target bonus were paid immediately. One-third of the amount over this maximum was also paid in cash. Remaining amounts were allocated to a "bonus bank" to be paid out in the future. Negative charges for deteriorating performance reduced the bonus bank. Negative charges could even create a negative balance in the bonus bank that would have to be overcome in order to resume bonus payments in future years.

TABLE E
Forecasted Earned Target Bonuses, 1993–1997

	% of Target Bonus Earned	
	Hotel Telecom	**Hospitality Equipment**
1993	45%	79%
1994	99	85
1995	69	71
1996	66	65
1997	62	66

As indicated in Exhibits 13 through 16, if the Hotel Telecom Services and Hospitality Equipment Services business units hit their forecasted levels of EVA in each year, Hotel Telecom's and Hospitality Equipment's managements would earn the percentage shown in Table E of their targeted bonus in each of the next 5 years. (See line 15 in Exhibits 14 and 16.)

According to Bennett Stewart, the beauty of the EVA incentive compensation system was that it was "a self-motivated, self-adjusting corporate governance system that linked capital budgeting and strategic investment decisions to the compensation system."

From John Duckworth's perspective, not only were the interests of management and shareholders aligned, but in addition, the bogeys for determining bonus compensation would not have to be renegotiated each year. What had been two plans (an annual plan and a long-term plan) could be combined into one plan that paid on annual results but was designed to build long-term shareholder value. The system was like a self-winding watch. You set it once, and it might keep going, all by itself, for quite some time.

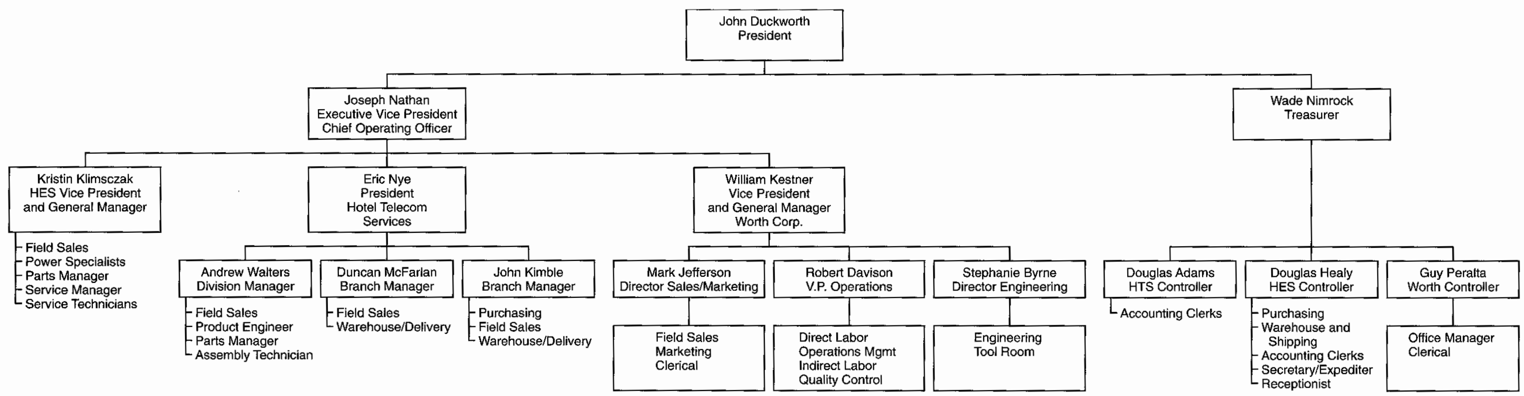
EXHIBIT 1
Consolidated Financial Statements, 1975–1992, Fiscal Years Ended May 31 (millions of dollars)

	1975	1980	1985	1990	1991	1992
Net sales	$5,811	$15,109	$40,793	$116,220	$123,545	$122,570
Cost of goods sold	4,294	11,164	30,142	85,875	89,865	86,720
Selling, gen'l & admin.	1,231	3,199	8,638	24,610	25,080	28,800
Operating income	287	746	2,013	5,735	8,595	7,050
Investment income	68	177	479	1,365	1,375	1,545
Interest expense	129	334	902	2,570	2,390	1,635
Profit sharing expense	55	142	383	1,090	1,595	1,850
Income before taxes	172	447	1,207	3,440	5,985	5,105
Taxes	50	130	351	1,000	1,850	1,565
Net income	122	317	856	2,440	4,135	3,540
Cash & marketable securities[a]	1,067	2,775	7,492	21,345	24,790	26,085
Accounts receivable	578	1,502	4,056	11,555	12,760	13,210
Inventory	572	1,487	4,014	11,435	11,380	12,995
Less: LIFO reserves	51	131	355	1,010	1,111	1,125
Net inventories	522	1,356	3,661	10,430	10,270	11,870
Other current assets	46	119	321	915	960	990
Total current assets	2,212	5,752	15,530	44,245	48,780	52,155
Construction in progress	25	65	176	500	485	3,105
Other net PP&E	799	2,076	5,605	15,970	15,450	14,330
Other assets[b]	290	753	2,032	5,790	5,735	5,685
Total assets	$3,325	$ 8,646	$23,343	$ 66,505	$ 70,450	$ 75,275
Short-term debt	$ 734	$ 1,909	$ 5,154	$ 14,685	$ 17,390	$ 15,910
Other current liabilities	1,048	2,724	7,355	20,955	19,790	23,700
Total current liabilities	1,782	4,633	12,510	35,640	37,180	39,610
Long-term borrowings	496	1,290	3,482	9,920	8,355	7,175
Other liabilities	63	164	444	1,265	1,105	1,140
Net worth	984	2,558	6,908	19,680	23,810	27,350
Total liab. & net worth	$3,325	$ 8,646	$23,343	$ 66,505	$ 70,450	$ 75,275

a. Marketable securities were carried at the lower of cost or market. Market exceeded cost by $4,090 in 1990; $7,870 in 1991; and $10,940 in 1992.

b. Other assets included goodwill of $5,130 in 1990; $4,995 in 1991; and $4,855 in 1992.

EXHIBIT 2
Organization Chart, Duckworth Industries, Inc., June 1, 1992



Supplementary Employment Data, Fiscal Years 1991–1993

	Headcount (fiscal year)		
	1993	**1992**	**1991**
Duckworth Industries	10	10	12
Worth Corporation	500	485	410
HES	135	155	170
Hotel Telecom	110	95	95
Total	755	745	687

EXHIBIT 3
Duckworth Corporation, Quality Incentive Bonus Plan, Fiscal Year 1993

The Quality Incentive bonus plan has been in its current form since FY90 (June of 1989).

As we have improved as a company, it is important that our plan be modified to reflect these changes and more accurately represent what the "real world" reflects in terms of total quality performance. After a thorough review of this year's quality performance, the following changes are being made to the Quality Incentive bonus plan effective June 1, 1992 (FY93). The monthly complaint ratio and bonus payout levels will be as follows:

Complaint Ratio	***Monthly Bonus Payout***
.6% or less	$100.00
More than .6%, less than 2.0%	$ 75.00
More than 2.0, less than 3.5%	$ 50.00

As you can see, the lower limits have been changed and the bottom payout of $25 eliminated, but we have increased the top-level payout by 25% to $100.00. The total potential maximum yearly payout is now $1,200, compared to $900 with the old plan. This year, through the first 11 months, we have paid $800 in incentives to each participant. As you can see from the above, superior performance will be rewarded with high-level bonus payouts.

Duckworth quality performance in FY91 improved dramatically to an average **2.7%** complaint ratio, with the **last six months** of the year averaging **2%**. The revised plan is designed to build on this success and increase our performance to "world-class" levels.

The procedures for analyzing, charging responsibility, and tallying total number of complaints by Richard Sterling all remain the same as in the past. The only additional reporting will be a new category recording invoicing errors, such as billing errors or wrong prices on orders. Complete quality is a total system—from the first customer inquiry to billing of parts and all processes in between.

With constant dedication to teamwork, continuous quality improvement, and satisfying our **customers' requirements**, we are confident that our new goals will be achieved and even surpassed. You are doing it now, and we are counting on you to make Duckworth—**Your Company**—the best quality company possible!

William Kestner
Vice President and General Manager

cc: John Duckworth
Joseph Nathan

EXHIBIT 4
Worth Corporation, Quality Incentive Program, FY93 October Results

No. of shipments	207
No. of chargeable complaints	4
Complaint ratio	1.9%
Quality bonus—October	$ 75
Quality bonus—YTD	$300

With a record number of shipments, this month had the potential of being a great quality month, but we fell short because preventable errors were not caught. Without the large shipment level, the monthly payout would not have been $75.00.

If you look at the customer complaints listed below, you will see that these problems could have been detected by our systems. The key to continued improvement is your using the systems and informing others when the systems do not work.

The XXX and YYY complaints are cases in which the system in place was not followed; the result was a complaint. The AAA and BBB complaints are cases in which people could have come forth to say that the system does not adequately detect these kinds of defects.

The task of improvement needs to be continually addressed by all. We cannot just let things go on and expect good results. Good results are achieved by good people doing the right things at the right time.

Type of Complaint	***Customer***	***Complaint***
Manufacturing process	AAA	Cracked AX47 parts; inventory not rotated
Manufacturing process	BBB	Cracked AX47 parts; inventory not rotated
Color	YYY	Color significantly off standard (yellow)
Label	XXX	Label printed with wrong code

Joy Meadow
Quality Assurance Manager

Thomas Spencer
Production Manager

EXHIBIT 5
Worth Corporation, FY93 Incentive Plan for Customer Service Representatives

	Item Results	% of Bonus	% of Salary
Order Accuracy			
4% maximum potential			
Accuracy equals percentage of	98.0% or higher	40.00%	4.00%
acceptance of orders that have	96.5	30.00	3.00
correct pricing and other	95.0	20.00	2.00
critical information. This	<95.0	0.00	0.00
accuracy is tracked by Director of Sales, with bonus being paid based on overall FY93 results.			
Order Acknowledgment/Turnaround			
3% maximum potential (effective 9/1/92–9-month period)			
Average number of days	2 days or less	30.00%	3.00%
(excluding holidays & weekends)	3 days	15.00	1.50
from order placement until	4 days	5.00	0.50
printing of order acknowledgment	>4 days	0.00	0.00
for all orders received (except those requiring new part numbers). Results to be tracked weekly on late shipments report.			
Sales Growth			
3% maximum potential			
Total net company sales growth	$7,000M	30.00%	3.00%
over FY92 net sales of	$6,000	15.00	1.50
$63.5 million	$3,000	5.00	0.50
	<$3,000	0.00	0.00

Note: Maximum award = 10% of average base salary.

EXHIBIT 6
Duckworth Industries, Inc., Fiscal 1992 Incentive Compensation

Annual Sales Growth (%)

Return on gross assets (%)		4.90	5.00	7.50	10.00	12.50	15.00
					Goal		
25.0		0	1.74	1.81	1.88	1.95	2.03
24.0		0	1.55	1.61	1.67	1.74	1.81
23.0		0	1.37	1.42	1.48	1.55	1.61
22.0		0	1.20	1.25	1.31	1.37	1.42
21.0		0	1.05	1.10	1.15	1.20	1.25
20.0	Goal	0	0.91	0.95	1.00	1.05	1.10
19.0		0	0.78	0.82	0.87	0.91	0.95
18.0		0	0.67	0.71	0.74	0.78	0.82
17.0		0	0.57	0.60	0.63	0.67	0.71
16.0		0	0.48	0.51	0.54	0.57	0.60
15.0		0	0.40	0.42	0.45	0.48	0.51
14.9		0	0	0	0	0	0

Return on gross performing assets will be determined by dividing operational cash flow earnings (OCFE) into average gross performing assets (AGPA).

OCFE is net profit adjusted to add depreciation and to eliminate (a) interest expense, (b) acquisition expenses, (c) net investment income, (d) expense or profit relating to LIFO, and (e) gains or losses from the disposition of depreciable assets. All adjustments will be made on an after-tax basis, using Worth Corporation's effective tax rate.

AGPA is a 13-month average of the company's gross book assets, with cumulative depreciation and the LIFO reserve added back, but investment securities and intercompany receivables eliminated.

The Board of Directors reserves the right to adjust the formula and its components, even after the fact, in any way it determines to be appropriate in order to better effectuate the plan and its purposes.

EXHIBIT 7
ROA/Growth Matrix for Worth Peer Group

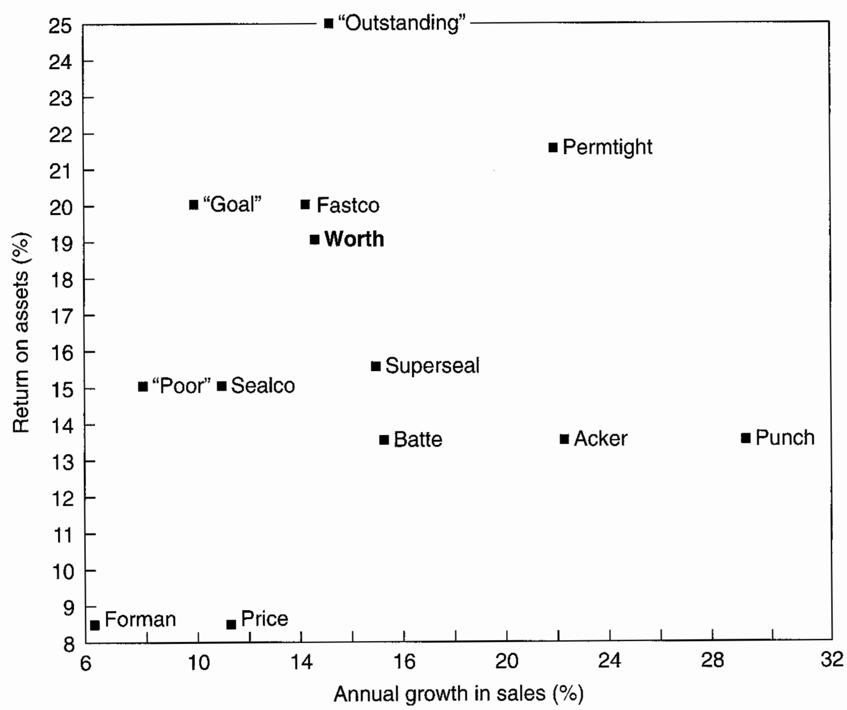


EXHIBIT 8
Worth Corporation, Inc., Executive Long-Term Incentive Plan

Summary	*May 31, 1983*	*May 31, 1988*	*5–Year Change*
Total shareholder's equity at year-end	$8,616,500	$16,379,000	
Per share, using standard of 500,000 shares	$ 17.23	$ 32.76	
Value-weighting "performance factor"	0.50	1.70	
Weighted share price .... (= Equity per share × Performance factor)	$ 8.62	$ 55.69	$47.07
Per participant .... $47.07 × 3000 shares	=	$141,210	
In total .... × 2 participants	=	$282,420	

EXHIBIT 9
Worth Division of Duckworth Industries, Management Long-Term Plan: Targets Established for Successive 3-Year Plans versus Results Achieved

Plan Years	*Challenge Earnings Levels (3-yr. cumulative EBIT)*	*% of Target Award Earned*	*Actual Results during Period*
1986–1989	$12.0 million	100%	$13.4 million and 112%
	10.0	50	
	7.5	10	
	< 7.5	0	
1987–1990	$20.0	100	$19.3 million and 97%
	12.5	10	
	<12.5	0	
1988–1991	$28.75	100	$26.1 million and 92%
	20.0	10	
	<20.0	0	
1989–1992	$33.0	100	$30.1 million and 91%
	25.0	10	
	<25.0	0	

Award Determination

Each participant will, at the start of a performance period, be assigned a target award expressed as a percentage of the participant's average annual base salary to be paid during the performance period. The percent of the target award earned by each participant will be based upon the relationship of performance period earnings to various challenge earnings levels specified by the board for such performance period.

The percent of target award earned will awarded on a pro rata basis if the actual results fall between specified challenge earnings levels. If a participant significantly changes responsibility or positions during the performance period, the board will consider the propriety of an equitable adjustment in the target award assigned.

A participant's award is subject to organizational and environmental constraints affecting performance period earnings. Unforeseen problems (other than those referred to in the next paragraph) or opportunities, as well as peer group performance, will be taken into account during the evaluation process. As soon as practicable after the end of a performance period, the board will determine how successfully objectives were met. The board will evaluate how unforeseen difficulties, as well as unexpected opportunities, were addressed. To allow recognition for quality of results and level of effort, award amounts may be adjusted (to a maximum of plus or minus 25% of the award) by the board.

The plan also recognizes that actions of participants may be negated or overstated due to the occurrence of certain extraordinary events. Examples of extraordinary events include, but are not limited to, "acts of God," financial difficulty of a major supplier or customer, unexpected tax law changes and acquisitions, divestitures, mergers, or significant structural changes. Should such extraordinary occurrences take place, the board may adjust the incentive awards (or the various formula components thereof) in any manner reasonably intended to reflect the impact of the extraordinary occurrence.

EXHIBIT 10
Target and Actual Payments for Annual and Long-Term Incentive Compensation Plans (as a % of base salary)

		1990		1991		1992	
		Target	***Actual***	***Target***	***Actual***	***Target***	***Actual***
Manager A	Annual bonus	—	—	40[a]	68	40[a]	0
	Long-term incentive	—	—	35[a]	32	35[a]	32
Manager B	Annual bonus	—	—	25[a]	35	25[a]	0
	Long-term incentive	—	—	25[a]	23	25[a]	23
Manager C	Annual bonus	50[a]	50	50[a]	85	50[b]	0
	Long-term incentive	40[a]	39	40[a]	37	40[b]	0
Manager D	Annual bonus	25[a]	25	40[a]	35	25[a]	0
	Long-term incentive	25[a]	24	40[a]	37	40[a]	36
Manager E	Annual bonus	40[a]	40	40[a]	68	40[a]	0
	Long-term incentive	40[a]	39	35[a]	32	35[a]	32
Manager F	Annual bonus	—	—	25[b]	0	25[b]	6
	Long-term incentive	—	—	25[b]	5	25[b]	0
Manager G	Annual bonus	40[a]	40	50[b]	0	50[b]	12
	Long-term incentive	40[a]	39	40[b]	8	40[b]	0
Manager H	Annual bonus	—	—	25[b]	0	25[b]	6
	Long-term incentive	—	—	25[b]	5	25[b]	0
Manager I	Annual bonus	25[a]	25	50[d]	46	50[d]	0
	Long-term incentive	25[a]	25	25[c]	10	60[d]	44
Manager J	Annual bonus	—	—	—	—	25[c]	0
	Long-term incentive	—	—	—	—	—	—
Manager K	Annual bonus	30[c]	0	30[c]	0	30[c]	0
	Long-term incentive	30[c]	0	30[c]	12	30[c]	14
Manager L	Annual bonus	40[c]	0	40[c]	0	50[c]	0
	Long-term incentive	35[c]	0	35[c]	14	35[c]	16
Manager M	Annual bonus	50[c]	0	50[c]	0	50[c]	0
	Long-term incentive	50[c]	0	50[c]	20	50[c]	46
Manager N	Annual bonus	—	—	35[a]	60	35[a]	0
	Long-term incentive	40[a]	39	40[a]	37	40[a]	36
Manager O	Annual bonus	40[a]	40	40[a]	68	40[a]	0
	Long-term incentive	25[a]	24	25[a]	23	25[a]	23
Manager P	Annual bonus	20[a]	20	20[a]	34	20[a]	0
	Long-term incentive	20[a]	19	20[a]	18	20[a]	18

a. Worth.
b. Hotel Telecom Services.
c. Hospitality Equipment Services.
d. Duckworth Industries.

EXHIBIT 11
Worth Corporation, Summary of Historical and Projected Operating Performance (millions of dollars)

		History					Forecast				
Line #		*1988*	*1989*	*1990*	*1991*	*1992*	*1993*	*1994*	*1995*	*1996*	*1997*
	Operating results										
1	Revenue	$47,255	$54,615	$57,125	$65,035	$63,565	$69,500	$76,100	$83,330	$91,250	$99,915
2	% Growth	15.0%	15.6%	4.6%	13.9%	(2.3%)	9.3%	9.5%	9.5%	9.5%	9.5%
3	– Cost of sales	34,985	40,305	41,760	46,020	42,025	47,355	51,950	56,915	62,415	68,445
4	% Sales	74.0%	73.8%	73.1%	70.8%	66.1%	68.1%	68.3%	68.3%	68.4%	68.5%
5	– SG&A	6,620	6,700	6,905	6,905	8,585	9,695	10,865	11,715	12,680	13,585
6	% Sales	14.0%	12.3%	12.1%	10.6%	13.5%	13.9%	14.3%	14.1%	13.9%	13.6%
7	– Cash taxes	$ 2,280	$ 1,965	$ 2,615	$ 3,500	$ 3,650	$ 4,225	$ 4,855	$ 5,310	$ 5,785	$ 6,215
8	% Operating income	40.4%	25.8%	30.9%	28.9%	28.2%	33.9%	36.5%	36.1%	35.8%	34.8%
9	**NOPAT**	**$ 3,370**	**$ 5,645**	**$ 5,840**	**$ 8,615**	**$ 9,305**	**$ 8,225**	**$ 8,430**	**$ 9,390**	**$10,370**	**$11,670**
	Capital										
10	Net accounts receivable	$ 5,310	$ 4,855	$ 5,460	$ 5,525	$ 6,060	$ 6,185	$ 6,760	$ 7,395	$ 8,090	$ 8,850
11	Inventory	2,865	2,965	3,360	3,865	4,020	4,030	4,260	4,585	4,945	5,325
12	PP&E	5,540	9,415	13,775	13,505	12,180	19,465	21,555	21,825	20,915	21,200
13	Other assets	620	350	1,455	1,565	3,765	3,210	2,450	1,800	1,245	1,185
14	– NIBCL's[a]	(10,775)	(9,790)	(11,545)	(10,025)	(13,125)	(9,940)	(10,860)	(12,040)	(13,360)	(14,725)
15	**Capital**	**$ 3,555**	**$ 7,795**	**$12,505**	**$14,440**	**$12,900**	**$22,945**	**$24,165**	**$23,560**	**$21,830**	**$21,835**
	Operating analysis										
16	NOPAT/Avg cap (r)	51.4%	99.5%	57.5%	63.9%	68.1%	45.9%	35.8%	39.3%	45.7%	53.5%
17	– Cost of capital (c)	13.0%	12.6%	12.7%	12.4%	12.2%	12.2%	12.2%	12.2%	12.2%	12.2%
18	Spread (r – c)	38.4%	86.9%	44.8%	51.5%	55.9%	33.7%	23.6%	27.2%	33.5%	41.3%
19	× Average capital	$ 6,550	$ 5,675	$10,150	$13,470	$13,670	$17,925	$23,555	$23,865	$22,695	$21,830
20	**Economic value added**	**$ 2,515**	**$ 4,935**	**$ 4,550**	**$ 6,945**	**$ 7,640**	**$ 6,045**	**$ 5,565**	**$ 6,485**	**$ 7,605**	**$ 9,010**

a. Non-interest-bearing current liabilities.

EXHIBIT 12
Worth Corporation

A. Input Table

Line #		*1993*	*1994*	*1995*	*1996*	*1997*
	Bonus Pool Characteristics					
1	Target bonus	37%	37%	37%	37%	37%
2	Base salary (000)	$1,710	$1,795	$1,885	$1,980	$2,075
3	Number of units (000)	630	660	695	730	765
	Bonus Calculation Framework					
4	Baseline EVA (000)	$6,045				
5	Annual target adjustment factor	50%				
6	Base unit value	$ 1.00	$ 0.80	$ 0.80	$ 0.80	$ 0.80
	EVA Bonus Sensitivity Factor					
7	EVA bonus sensitivity factor (000)	$1,625				

B. Current Bonus Calculation

Line #		*1993*	*1994*	*1995*	*1996*	*1997*	*Average*
	Performance Unit Value						
8	EVA (000)	$6,045	$5,565	$6,485	$7,605	$9,010	$6,940
9	– Baseline EVA (000)	$6,045	$6,045	$5,805	$6,145	$6,875	$6,180
10	= EVA vs baseline EVA (000)	$ 0	($ 480)	$ 680	$1,460	$2,135	$ 760
11	/ EVA bonus sensitivity factor (000)	$1,625	$1,625	$1,625	$1,625	$1,625	$1,625
12	= Performance unit value	$ 0.00	($ 0.29)	$ 0.42	$ 0.90	$ 1.31	$ 0.47
	Total Unit Value						
13	Performance unit value	$ 0.00	($ 0.29)	$ 0.42	$ 0.90	$ 1.31	$ 0.47
14	+ Base unit value	$ 1.00	$ 0.80	$ 0.80	$ 0.80	$ 0.80	$ 0.84
15	= Total unit value	$ 1.00	$ 0.51	$ 1.22	$ 1.70	$ 2.11	$ 1.31
	Current Bonus						
16	Total unit value	$ 1.00	$ 0.51	$ 1.22	$ 1.70	$ 2.11	$ 1.31
17	Number of units (000)	630	660	695	730	765	695
18	Current bonus earned (000)	$ 630	$ 335	$ 850	$1,240	$1,620	$ 935

C. Past Bonus If System Had Been In Place Prior 5 Years

Line #		*1988*	*1989*	*1990*	*1991*	*1992*	*Average*
	Current Bonus						
19	Total unit value	$ 1.00	$ 2.29	$ 1.31	$ 2.53	$ 2.09	$ 1.84
20	Number of units (000)	695	720	720	740	530	680
21	Current bonus earned (000)	$ 695	$1,645	$ 945	$1,875	$1,115	$1,255

EXHIBIT 15
Hospitality Equipment Service Co., Summary of Historical and Projected Operating Performance (millions of dollars)

		History					Forecast				
Line #		***1988***	***1989***	***1990***	***1991***	***1992***	***1993***	***1994***	***1995***	***1996***	***1997***
	Operating results										
1	Revenue	$24,770	$28,670	$26,555	$28,525	$26,720	$29,220	$31,410	$33,765	$36,300	$39,020
2	% Growth	49.2%	15.8%	(7.4%)	7.4%	(6.3%)	9.4%	7.5%	7.5%	7.5%	7.5%
3	– Cost of sales	18,560	21,545	19,545	20,955	14,305	21,190	22,500	24,170	25,965	27,895
4	% Sales	74.9%	75.1%	73.6%	73.5%	72.2%	72.5%	71.6%	71.6%	71.5%	71.5%
5	– SG&A	5,765	6,100	7,240	6,495	7,135	7,065	7,480	7,950	8,455	8,985
6	% Sales	23.3%	21.3%	27.3%	22.8%	26.7%	24.2%	23.8%	23.5%	23.3%	23.0%
7	– Cash taxes	$ 275	$ 440	$ 55	$ 420	$ 320	$ 420	$ 545	$ 615	$ 690	$ 780
8	% Operating income	62.0%	43.0%	(23.7%)	38.8%	113.3%	43.6%	38.0%	37.2%	36.7%	36.4%
9	**NOPAT**	**$ 170**	**$ 585**	**($ 290)**	**$ 660**	**($ 35)**	**$ 545**	**$ 885**	**$ 1,035**	**$ 1,190**	**$ 1,365**
	Capital										
10	Net accounts receivable	$ 2,655	$ 3,775	$ 3,075	$ 3,525	$ 3,010	$ 3,660	$ 6,288	$ 4,220	$ 4,530	$ 4,865
11	Inventory	2,830	3,420	4,115	3,205	3,105	3,365	3,560	3,815	4,085	4,380
12	PP&E	545	965	815	515	360	950	1,160	1,370	1,580	1,790
13	Other assets	535	355	335	835	850	675	770	805	805	810
14	– NIBCL's[a]	(4,295)	(4,845)	(4,095)	(3,250)	(4,045)	(3,295)	(3,520)	(3,805)	(4,110)	(4,440)
15	**Capital**	**$ 2,270**	**$ 3,675**	**$ 4,250**	**$ 4,825**	**$ 3,280**	**$ 5,355**	**$ 5,900**	**$ 6,405**	**$ 6,890**	**$ 7,400**
	Operating Analysis										
16	NOPAT/Avg cap (r)	7.8%	19.7%	(7.3%)	14.5%	(0.9%)	12.6%	15.7%	16.8%	17.9%	19.1%
17	– Cost of capital (c*)	13.4%	13.4%	13.4%	13.4%	13.4%	13.5%	13.5%	13.5%	13.5%	13.5%
18	Spread (r – c*)	(5.6%)	6.3%	(20.7%)	1.1%	(14.3%)	(1.0%)	2.2%	3.3%	4.4%	5.5%
19	× Average capital	$ 2,155	$ 2,970	$ 3,960	$ 4,535	$ 4,055	$ 4,315	$ 5,625	$ 6,150	$ 6,645	$ 7,145
20	**Economic value added**	**($ 120)**	**$ 185**	**($ 820)**	**$ 50**	**($ 580)**	**($ 40)**	**$ 125**	**$ 205**	**$ 290**	**$ 395**

a. Non-interest-bearing current liabilities.

EXHIBIT 14
Hotel Telecom Services

A. Input Table

Line #		1993	1994	1995	1996	1997
	Bonus Pool Characteristics					
1	Target bonus	38%	38%	38%	38%	38%
2	Base salary (000)	$905	$950	$1,000	$1,050	$1,100
3	Number of units (000)	345	360	380	400	420
	Bonus Calculation Framework					
4	Baseline EVA (000)	($140)				
5	Annual target adjustment factor	50%				
6	Base unit value	$0.25	$0.25	$0.25	$0.25	$0.25
	EVA Bonus Sensitivity Factor					
7	= EVA bonus sensitivity factor (000)	$700				

B. Current Bonus Calculation

Line #		1993	1994	1995	1996	1997	Average
	Performance Unit Value						
8	EVA (000)	$ 0	$450	$495	$630	$745	$465
9	– Baseline EVA (000)	($140)	($70)	$190	$340	$485	$160
10	= EVA vs baseline EVA (000)	$140	$520	$305	$290	$255	$300
11	/ EVA bonus sensitivity factor (000)	$700	$700	$700	$700	$700	$700
12	= Performance unit value	$0.20	$0.74	$0.44	$0.41	$0.37	$0.43
	Total Unit Value						
13	Performance unit value	$0.20	$0.74	$0.44	$0.41	$0.37	$0.43
14	+ Base unit value	$0.25	$0.25	$0.25	$0.25	$0.25	$0.25
15	= Total unit value	$0.45	$0.99	$0.69	$0.66	$0.62	$0.68
	Current Bonus						
16	Total unit value	$0.45	$0.99	$0.69	$0.66	$0.62	$0.68
17	Number of units (000)	345	360	380	400	420	380
18	Current bonus earned (000)	$155	$360	$260	$265	$260	$260

C. Past Bonus If System Had Been In Place Prior 4 Years

Line #		1989	1990	1991	1992	Average
	Current Bonus					
19	Total unit value	$1.27	$0.39	($0.68)	($.60)	$0.08
20	Number of units (000)	50	150	325	340	215
21	Current bonus earned (000)	$ 60	$ 60	($225)	($205)	($ 78)

EXHIBIT 15
Hospitality Equipment Service Co., Summary of Historical and Projected Operating Performance (millions of dollars)

Line #		History					Forecast				
		1988	1989	1990	1991	1992	1993	1994	1995	1996	1997
	Operating results										
1	Revenue	$24,770	$28,670	$26,555	$28,525	$26,720	$29,220	$31,410	$33,765	$36,300	$39,020
2	% Growth	49.2%	15.8%	(7.4%)	7.4%	(6.3%)	9.4%	7.5%	7.5%	7.5%	7.5%
3	– Cost of sales	18,560	21,545	19,545	20,955	14,305	21,190	22,500	24,170	25,965	27,895
4	% Sales	74.9%	75.1%	73.6%	73.5%	72.2%	72.5%	71.6%	71.6%	71.5%	71.5%
5	– SG&A	5,765	6,100	7,240	6,495	7,135	7,065	7,480	7,950	8,455	8,985
6	% Sales	23.3%	21.3%	27.3%	22.8%	26.7%	24.2%	23.8%	23.5%	23.3%	23.0%
7	– Cash taxes	$ 275	$ 440	$ 55	$ 420	$ 320	$ 420	$ 545	$ 615	$ 690	$ 780
8	% Operating income	62.0%	43.0%	(23.7%)	38.8%	113.3%	43.6%	38.0%	37.2%	36.7%	36.4%
9	**NOPAT**	**$ 170**	**$ 585**	**($ 290)**	**$ 660**	**($ 35)**	**$ 545**	**$ 885**	**$ 1,035**	**$ 1,190**	**$ 1,365**
	Capital										
10	Net accounts receivable	$ 2,655	$ 3,775	$ 3,075	$ 3,525	$ 3,010	$ 3,660	$ 6,288	$ 4,220	$ 4,530	$ 4,865
11	Inventory	2,830	3,420	4,115	3,205	3,105	3,365	3,560	3,815	4,085	4,380
12	PP&E	545	965	815	515	360	950	1,160	1,370	1,580	1,790
13	Other assets	535	355	335	835	850	675	770	805	805	810
14	– NIBCL's[a]	(4,295)	(4,845)	(4,095)	(3,250)	(4,045)	(3,295)	(3,520)	(3,805)	(4,110)	(4,440)
15	**Capital**	**$ 2,270**	**$ 3,675**	**$ 4,250**	**$ 4,825**	**$ 3,280**	**$ 5,355**	**$ 5,900**	**$ 6,405**	**$ 6,890**	**$ 7,400**
	Operating Analysis										
16	NOPAT/Avg cap (r)	7.8%	19.7%	(7.3%)	14.5%	(0.9%)	12.6%	15.7%	16.8%	17.9%	19.1%
17	– Cost of capital (c*)	13.4%	13.4%	13.4%	13.4%	13.4%	13.5%	13.5%	13.5%	13.5%	13.5%
18	Spread (r – c*)	(5.6%)	6.3%	(20.7%)	1.1%	(14.3%)	(1.0%)	2.2%	3.3%	4.4%	5.5%
19	× Average capital	$ 2,155	$ 2,970	$ 3,960	$ 4,535	$ 4,055	$ 4,315	$ 5,625	$ 6,150	$ 6,645	$ 7,145
20	**Economic value added**	**($ 120)**	**$ 185**	**($ 820)**	**$ 50**	**($ 580)**	**($ 40)**	**$ 125**	**$ 205**	**$ 290**	**$ 395**

a. Non-interest-bearing current liabilities.

EXHIBIT 16
Hospitality Equipment Service Co.

A. Input Table

Line #		1993	1994	1995	1996	1997
	Bonus Pool Characteristics					
1	Target bonus	42%	42%	42%	42%	42%
2	Base salary (000)	$705	$740	$775	$815	$855
3	Number of units (000)	300	315	330	345	365
	Bonus Calculation Framework					
4	Baseline EVA (000)	($310)				
5	Annual target adjustment factor	50%				
6	Base unit value	$0.25	$0.25	$0.25	$0.25	$0.25
	EVA Bonus Sensitivity Factor					
7	= EVA bonus sensitivity factor (000)	$500				

B. Current Bonus Calculation

Line #		1993	1994	1995	1996	1997	Average
	Performance Unit Value						
8	EVA (000)	($40)	$125	$205	$290	$395	$195
9	– Baseline EVA (000)	($310)	($175)	($25)	$90	$190	($45)
10	= EVA vs baseline EVA (000)	$270	$300	$230	$200	$205	$240
11	/ EVA bonus sensitivity factor (000)	$500	$500	$500	$500	$500	$500
12	= Performance unit value	$0.54	$0.60	$0.46	$0.40	$0.41	$0.48
	Total Unit Value						
13	Performance unit value	$0.54	$0.60	$0.46	$0.40	$0.41	$0.48
14	+ Base unit value	$0.25	$0.25	$0.25	$0.25	$0.25	$0.25
15	= Total unit value	$0.79	$0.85	$0.71	$0.65	$0.66	$0.73
	Current Bonus						
16	Total unit value	$0.79	$0.85	$0.71	$0.65	$0.66	$0.73
17	Number of units (000)	300	315	330	345	365	330
18	Current bonus earned (000)	$235	$265	$235	$225	$240	$240

C. Past Bonus If System Had Been In Place Prior 5 Years

Line #		1988	1989	1990	1991	1992	Average
	Current Bonus						
19	Total unit value	$0.71	$1.10	($1.34)	$1.20	($0.54)	$0.22
20	Number of units (000)	285	525	315	335	255	345
21	Current bonus earned (000)	$205	$575	($425)	$405	($140)	$125