Ownership Structure and CEO Pay: Evidence from Member Owned Firms

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Motivation

- Determinants of CEO pay, interaction of explicit and implicit incentives with “career concerns”
- Cooperatives represent and interesting (and new!) place to examine the issue
- We focus on incidence and structure of performance incentives for cooperative CEOs

Theory

- Gibbons and Murphy (1992): Career Concerns
- Baker, Gibbons, Murphy (1994): Explicit+Implicit Incentives.
- Macleod (2003): Subjective Incentives
- Levin (2003): Relational incentives

Empirics

- Murphy and Oyer (2003): Discretion in executive incentive contracts.
- Ederhof (2010): Discretion in wage bonus plans
- Sloof and Sonnemans (2011): Experiments with explicit and implicit incentives
- Johnson, McMillan, and Woodruff (2001): Contract enforcement and economic development

What Makes Cooperatives Different from Other Kinds of Firms?

- Fisher (non)Separation
- Information and incentive environment for board members (principals)
- Board selection and composition (all “outsiders”)

Qualitative Predictions

1. (across) Stock values are a verifiable signal of performance in noncooperative firms => Greater reliance on implicit incentives in co-ops. (strong evidence in support)

2. Career incentives do not exist for late-career workers => Substitute explicit for implicit later in career. (evidence against)

3. Long horizon increases efficacy of implicit incentives => CEOs with long expected horizons in a firm should face more implicit incentives. CEOs with long careers should be able to develop “trusting” relationship. (evidence against).

4. Learning about CEO ability creates an opportunity for better adjusted explicit incentives (evidence in support)

5. Shared beliefs make subjective (implicit) incentives more effective => CEOs hired from within a firm should face more implicit incentives. (evidence against)

Measurement

- Recorded phone interviews with 400+ cooperative CEOs
- Measurement:
  1. Performance incentives.
  2. Implicit vs. Explicit incentives (asked about "formulaic" and "discretionary").
  3. Firm and CEO characteristics:
     i) CEO career profile
     ii) CEO hiring dynamics at firm
     iii) CEO history at firm
     iv) Industry and firm-type controls

Specific Questions

- "Please describe your compensation contract."
- "Do you receive performance incentives?"
- "What portion of your total pay in a typical year is performance incentive?"
- "Of this amount, what portion is discretionary?"

Answers

low powered explicit

high powered explicit

you make the call

low powered implicit

high powered implicit

Implicit/Explicit

- Explicit = 1 if claim there are incentives and nothing is discretionary
- Implicit = 1 if claim incentive with everything discretionary OR claim no incentive
- Mixed = 1 if not Explicit or Implicit

Descriptive Statistics

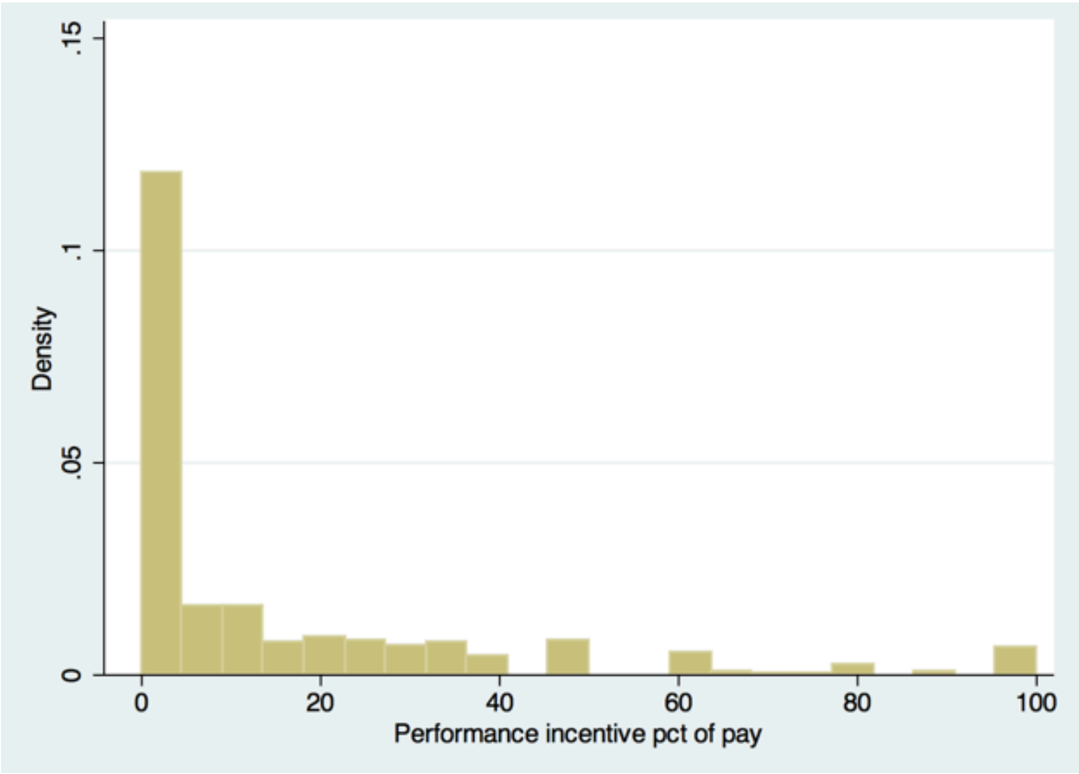
Variable	Obs	Mean	Std. Dev.	Min	Max
CEOAge	465	54.02366	8.0669	23	85
YrsAtFrm	475	16.43579	11.47928	0	52
NumCEOs	469	2.515991	1.668672	0	16
NumMem	484	14131.08	124771.2	0	2500000
CoopType					
2	485	.4701031	.4996207	0	1
3	485	.0948454	.2933038	0	1
Sector					
1	485	.0742268	.2624103	0	1
2	485	.0783505	.2689998	0	1
3	485	.1278351	.3342508	0	1
4	485	.0268041	.1616773	0	1
5	485	.1278351	.3342508	0	1
6	485	.1092784	.3123103	0	1
implicit	485	.5979381	.4908206	0	1
explicit	485	.2515464	.4343499	0	1
mixed	485	.1505155	.3579452	0	1

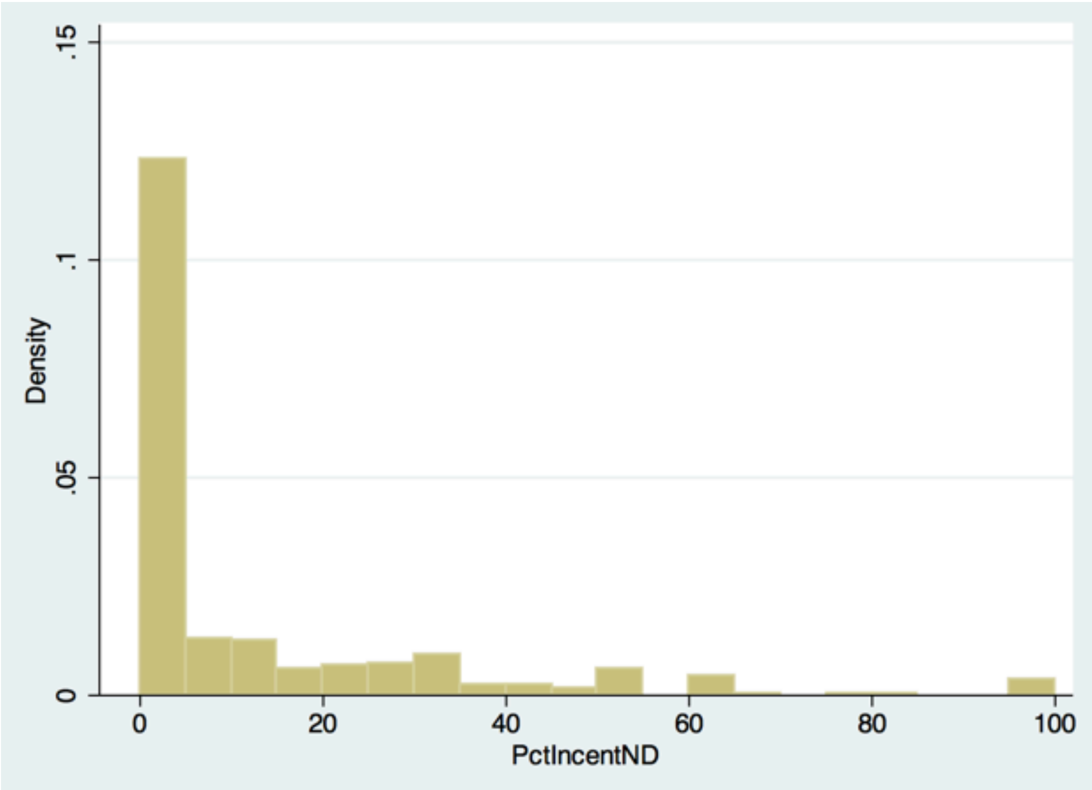
“Across” Evidence

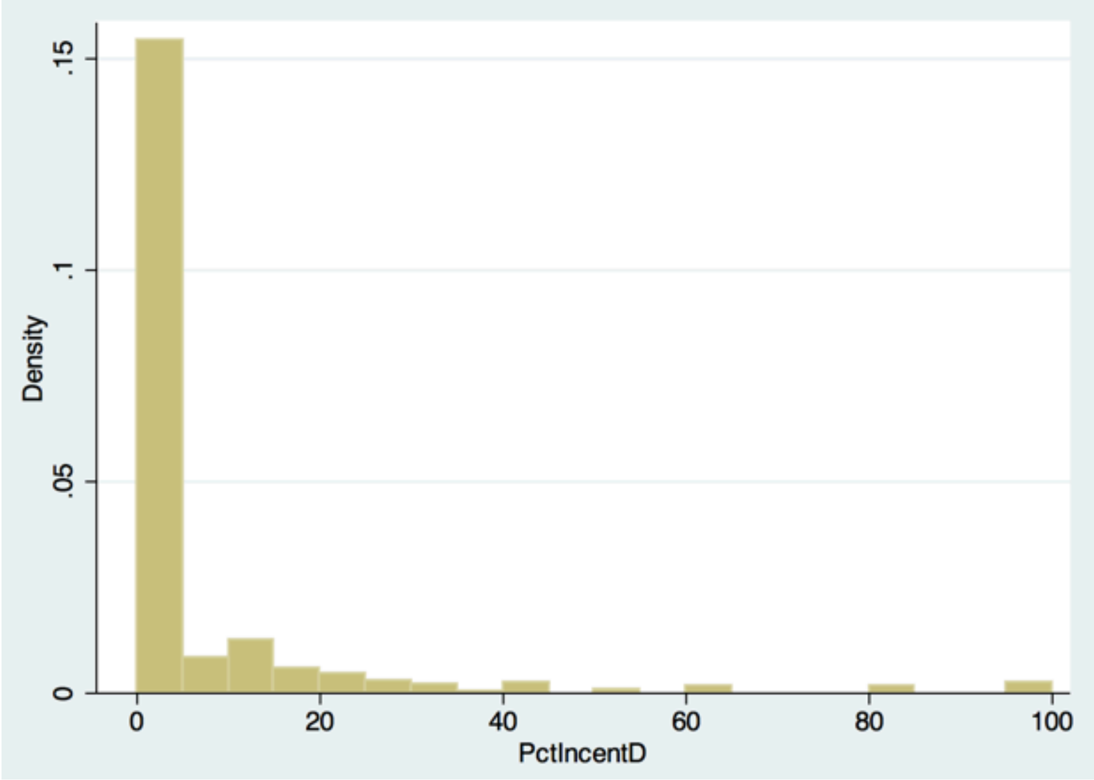
	Public	Co-op
Tenure (yrs)	5	10
PBP % of total pay	80	20
% Hired from inside	70	95

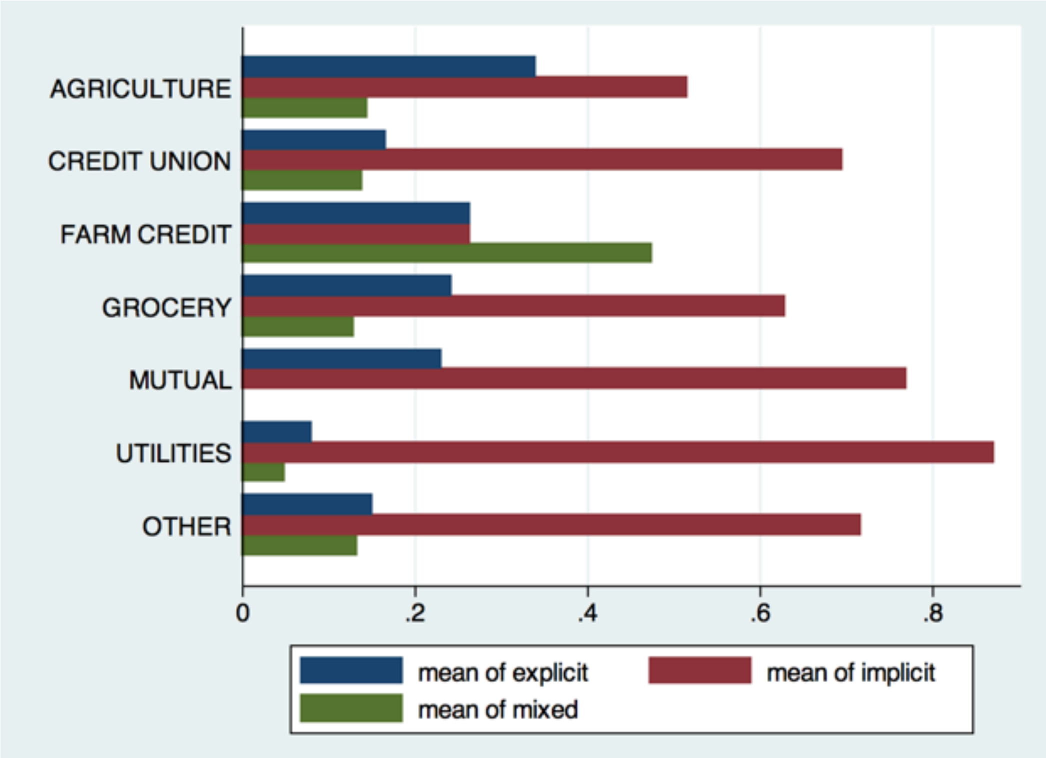
=> Implicit incentives are used as a substitute for explicit incentives. Lack of performance measure creates incentive to invest in relationship. Less “employment liquidity”

Lots of “within” variation to explain









Results

	(1)	(2)	(3)
	implicit	explicit	mixed
main			
YoungCEO==1	-0.447^{*}	0.596^{*}	0.101
	(-2.13)	(2.16)	(0.26)
LnNumMem	-1.163^{***}	0.618^{*}	1.770^{***}
	(-4.56)	(2.04)	(3.80)
CoopType==2	-1.206^{***}	1.380^{***}	0.573
	(-5.00)	(4.52)	(1.34)
CoopType==3	-1.033^{***}	0.779^{*}	1.181^{**}
	(-4.17)	(2.56)	(2.81)
Observations	462	462	462

Standardized beta coefficients; *t* statistics in parentheses

* $p < 0.05$, ** $p < 0.01$, *** $p < 0.001$

Results

	(1)	(2)	(3)
	implicit	explicit	mixed
main			
LowTurnover==1	-0.464	0.426	0.582
	(-1.75)	(1.21)	(1.00)
LnNumMem	-1.068***	0.574	1.595***
	(-4.25)	(1.93)	(3.48)
CoopType==2	-1.113***	1.309***	0.427
	(-4.64)	(4.34)	(0.99)
CoopType==3	-0.991***	0.737*	1.123**
	(-3.99)	(2.45)	(2.68)
Observations	467	467	467

Standardized beta coefficients; *t* statistics in parentheses

* $p < 0.05$, ** $p < 0.01$, *** $p < 0.001$

Results

(1)		(2)		(3)
	implicit		explicit	mixed
main				
RecentHire==1	0.459		-0.561	-0.324
	(1.93)		(-1.67)	(-0.75)
LnNumMem	-1.203***		0.639*	1.895***
	(-4.72)		(2.11)	(3.97)
CoopType==2	-1.247***		1.357***	0.713
	(-5.17)		(4.50)	(1.62)
CoopType==3	-1.161***		0.845**	1.410***
	(-4.69)		(2.81)	(3.31)
Observations	471		471	471

Standardized beta coefficients; *t* statistics in parentheses

* $p < 0.05$, ** $p < 0.01$, *** $p < 0.001$

Results

	(1)	(2)	(3)
	implicit	explicit	mixed
main			
PrevCoop==1	-0.418	0.186	0.754
	(-1.96)	(0.70)	(1.89)
CEO: years at current firm	-0.136	-0.116	0.585
	(-0.64)	(-0.44)	(1.47)
LnNumMem	-1.097***	0.569	1.754***
	(-4.24)	(1.86)	(3.63)
CoopType==2	-1.187***	1.319***	0.626
	(-4.87)	(4.33)	(1.41)
CoopType==3	-1.142***	0.780**	1.478***
	(-4.55)	(2.59)	(3.41)
Observations	466	466	466

Standardized beta coefficients; *t* statistics in parentheses

* $p < 0.05$, ** $p < 0.01$, *** $p < 0.001$

Results

	(1)	(2)	(3)
	implicit	explicit	mixed
main			
YoungCEO==1	-0.445*	0.517	0.189
	(-2.06)	(1.89)	(0.47)
RecentHire==1	-0.368	-6.021	1.060
	(-0.62)	(-0.02)	(1.26)
YoungCEO==1 & RecentHire==1	0.832	5.162	-1.454
	(1.37)	(0.02)	(-1.58)
LowTurnover==1	-0.443	0.390	0.570
	(-1.65)	(1.09)	(0.95)
PrevCoop==1	-0.411	0.266	0.550
	(-1.94)	(1.02)	(1.41)
LnNumMem	-0.999***	0.405	1.803***
	(-3.76)	(1.29)	(3.57)
CoopType==2	-1.095***	1.165***	0.619
	(-4.33)	(3.74)	(1.35)
CoopType==3	-1.018***	0.673*	1.360**
	(-3.95)	(2.14)	(3.00)
Observations	441	441	441

Standardized beta coefficients; *t* statistics in parentheses

* $p < 0.05$, ** $p < 0.01$, *** $p < 0.001$

Summary

- Explicit incentives are more likely employed with younger CEOs who have established tenure in firms with relatively low turnover.
  - More explicit incentives early in career contrary to career concerns model
  - Explicit incentives after establishing some tenure is consistent with learning model
  - Low-turnover firms using explicit incentives inconsistent with relational contracting.
- Explicit incentives are an *investment* that firms make. Firms that are organized (low turnover) make the investment after a period of time for CEOs who have a long career in front.
- Evidence is weak; use of explicit incentives seems largely explained by firm size and type...
- "Across" evidence is strong; availability of performance measures reduces use of implicit incentives... and this leads to long-term employment duration.

Future Directions

- Common agency and contract design
  - Arguably no shared objective (esp. in consumer cooperatives)
- Firm size and performance incentives
  - Cooperatives are much smaller than public companies. Our results seem to contradict existing evidence (less PBP with larger firms)
- Monitoring and incentives: substitutes or compliments?
  - Owner direct interaction with firm (in addition to board participation). Haven't looked at any of the governance variables.
- Incentives, governance, and performance; RDC data.