Essays on Managerial Pay Structures

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ABSTRACT

This dissertation explores three different aspects of managerial compensation: its tournament structure, its gender differences, and the effect of corporate governance on executives' pay for performance and pay for luck. In the first two essays, I rely on wage records of Czech managerial employees around the time of the Czech Republic's accession to the EU. The third essay employs the U.S. ExecuComp data set to compare executive compensation before and after the passage of the Sarbanes-Oxley Act of 2002.

The topics were inspired by the dramatically changing role of managers in modern firms in the recent years. In the command economy, where the state was the largest owner, managers were not motivated explicitly to pursue a firm's prosperity. However, with the transition to a market economy, managerial contracts have started to be perceived as an important incentive device. In the first chapter, I examine the structure of wages among Czech managers in a representative sample of medium and large firms in the context of tournament theory of compensation. It addresses how managers compete to be promoted at better paid jobs and how pay increases at an increasing rate across hierarchical levels. Consistently with this theory, I find that the managerial pay differential between organizational levels is non-decreasing as managers climb the corporate ladder. Second, the winner's prize in the tournament, i.e., the pay gap at the very top of a firms' hierarchy, increases with the number of competitors for the position of the top manager.

In the second chapter, co-authored with Štěpán Jurajda, we study gender pay differentials among top- and lower-level managerial employees in a large sample of Czech firms. Using the traditional Oaxaca-Blinder technique we find that approximately a third of the raw gender wage gap for both top- and lower-level managers can be explained by gender differences in age and education. This is in contrast to the situation with ordinary employees, where the demographic composition of the workforce is actually more favorable for women and does not explain the pay gap. Using matching decomposition techniques, we find that this "unexplained" wage gap (for men and women that are comparable in terms of demographics and employer type) is about 20% for both two types of managers and for employees.

The motivation for the third chapter comes from the series of corporate scandals in the beginning of 2000 in the United States and the subsequent passage of the Sarbanes-Oxley Act of 2002 on the structure of CEO pay in the largest US corporations. Specifically, I examine whether the improved board oversight guaranteed by the requirement of majority independent (not affiliated to the company) directors reduces CEO pay for luck, i.e., pay for events beyond CEO control and increase pay for performance, i.e., pay for events in CEO control. Using the ExecuComp data, I find that the pay-for-performance link increases after the passage of the Sarbanes-Oxley Act of 2002 only in firms with weak board oversight defined before 2002–that is in firms more affected by SOX stipulations–and pay for luck disappears consistent with improved governance.