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Misguided Political Attacks on CEO Pay

The best analogy is to pro QBs. Not all become stars, but all are well paid in hopes they will.

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Hostility to corporate CEOs may never entirely subside. Democratic presidential candidate Hillary Clinton, for example, has spoken about the struggles of the average American family "when the average CEO makes about 300 times what the average worker makes." Rolling out her economic program on July 13, Mrs. Clinton promised policies that would be better for "hardworking families, not just for successful CEOs."

Yet much would be gained if the public better understood the logic behind business leaders' seemingly outsize compensation.

When Robert C. Goizueta took over Coca-Colain 1980, the company was worth $4 billion. When he died in October 1997, the company was worth $145 billion. Goizueta transformed a global brand.

A few months before Goizueta died, Steve Jobs returned to run Apple Computer, the company he co-founded in the 1970s. Apple had been a highflier but was hurtling toward bankruptcy, and Jobs was brought in to fix what appeared irretrievably broken. Soon enough the innovations that have defined the modern Apple began to roll out. First was the iMac, followed by the iPod, iPhone and iPad. Jobs died in 2011, and while he did not live to see it, Apple is now worth $746 billion, the most valuable company on earth.

Goizueta died with an estimated net worth of $994 million thanks to his Coca-Cola stock. Jobs's 5.5 million Apple shares were estimated to be worth $2.1 billion when he died.
Were they overpaid? The shareholders of each firm never quibbled with the pay or net worth of these two legendary CEOs.

The achievements of Goizueta and Jobs help explain why CEO pay is so high. Since one man or woman can potentially affect the fortunes of a corporation to the tune of hundreds of billions of dollars, CEO pay mirrors what is possible—even though it is by no means certain.

Professional sports are a similar story. Seattle Seahawks quarterback Russell Wilson will soon receive a pay package reportedly worth $20 million or more. Rare is the quarterback who can lead his team to consecutive Super Bowls—but that is exactly what he did in the past two seasons.

Great CEOs, like champion athletes, are rare. Corporate boards search for transformative CEOs, as personnel directors in sports spend much of their time searching for athletes like Mr. Wilson.

Yet compensation does not always match performance. Exhibit A is former Home Depot CEO Bob Nardelli. Despite $64 million in pay, and a share price that languished during his six years at the top of the retail giant, Mr. Nardelli's forced departure in 2007 came with a $210 million exit package. Mr. Nardelli's compensation was based on his track record at GE, where he worked for Jack Welch. Home Depot bid for his services on the assumption that he would bring with him some of the Welch genius.

Perhaps incoming CEOs should be paid the way company founders are generally compensated. If chief executives were paid mostly in company stock, and comparatively little in annual salary, then the interests of the CEO, the shareholder and the worker will be much better aligned.

If a CEO has a rocky tenure, his departure won't bring much in the way of controversy and his exit will cost shareholders little. But if he makes a great deal of money for shareholders, his pay will reflect that.

The $156 million compensation of this year's highest-paid CEO, Discovery Communications's David Zaslav, is an example of how future CEO pay packages could be structured. Although the amount is eye-popping, equity grants make up more than 95%. The company's market capitalization has quadrupled since Mr. Zaslav took over in 2007.

Many Americans, regardless of their feelings about CEOs, cheer when the founder of a company earns billions for turning an idea into something that saves us money and enriches our lives. Perhaps that reflects their understanding that visionaries might easily have failed, and they should be rewarded for taking risks.

If CEO compensation is about ownership, there will be high rewards for outstanding performance and austere rewards for poor performance. As Coca-Cola and Apple remind us, high but well-earned chief-executive pay is good—and we need more of it.

INSTRUCTIONS: Critique this article within the context of our class discussions on corporate governance and CEO compensation.