

Imagine if you could sell all the stock you own in a company and get paid a bonus for doing so ? How great would it be if you could just look at a stock in your portfolio and say "I quit. Im tired of owning you. Pull me from the shareholder rosters im out of here ! Oh, by the way. I need to get paid to leave. I want you to cover my losses, and pay me a bonus, and of course, I need access to the company plane."

CEOs can quit. Shareholders cant. CEOs have ridiculous exit packages. Shareholders have nothing but risk exit packages. There is no way on earth that any of the existing pay packages can say they align with shareholders interests when quitting means you hit the lottery.

Thats ridiculous and an insult to shareholders.

So i was pondering the question. What would work with executive pay ? How can an exec's interests even somewhat lie with Shareholders ?

Well first, let me put out there that I am HUGELY bias to dividends. I loved MicroSofts special dividend, I think the huge buyback they just announced is the epitome of stupidity. You dont reward shareholders who sell. You reward shareholders who stay. Buybacks are a sign that the CEO and Board really dont understand shareholder return. Its a sign that they understand pressure from large shareholders who mark the price of their stock to market on a daily basis and what to see it get a bump and want an exit strategy they can sell into.

Dividends on the other hand, do just the opposite.

They send a message to shareholders that you want them to stay as shareholders and are rewarding them for their commitment to your company. Its a reminder to shareholders that the business investments you have made have actually worked and the reward is that cash can be returned to shareholders . That profits are more important to shareholders over the long term than trying to convince wall street to increase your PE.

For boards that believe in the same dividend reward strategy then the solution to executive pay is very easy. Phantom Shares.

Phantom Shares in this case would be the equivalent of an Executive Tracking Stock.

Execs in a public company would be issues non-trading shares that would entitle them to only 2 financial opportunities.

1. They can be paid dividends equal to dividends paid to common shareholders – This way if Im a shareholder and I get paid a nickel per share per year. So does the exec. That is true alignment of interests.
2. The tracking stock is assigned a price equal to the price of the common stock on the day the exec is hired. If the company is sold, the tracking stock is "converted" to a common share and the exec is entitled to any premium in the sale price of the stock above the assignment price on the day of employment.

With this approach, it doesnt matter if the CEO plays games to get the stock price higher, it doesnt help him or her unless the company gets sold. At which point there is certainly risk he or she could play games with the stock and groom the company to sell it. However, given the sale of a company is something that shareholders have to approve far more often than not, it truly can be up to the shareholders to do the deal or not. They can control the financial destiny of their stock, the company and the executives involved compensation.

Its also possible that the board of a company could offer management far more shares of the tracking stock than some may deem reasonable. If the board did give a ridiculous number of tracking shares, they still would have to declare a cash dividend each quarter before the executives could benefit. The cash impact on operations from having to pay out to everyone would hopefully minimize this risk and prevent this from happening. (And yes i know that sleazebags everywhere will find a way to abuse this approach, but what that is, is not obvious to me right now)

So thats my idea to solve executive compensation issues. A phantom or tracking stock issued to execs that only pays them when shareholders are paid a cash dividend or when the company is sold. That is alignment with shareholders IMHO

Would it be difficult to attract top quality executive management to a company with this compensation program ? Hell no. if anything there is an excess of good management talent out there willing to work a job that challenges and interests them.

Its a very simple approach. Its one that would work.

Now whether any boards would do it, thats a completely different question