

Executive pay critical thinking

[Business](#), [Company](#)



The government has recently considered imposing caps on payments that top executives in top corporations earn. This has been an effort to clear the excessive expenditure by corporations. If this proposition is passed into law, it will have several impacts. First, corporations will adopt new models of expenditure since there will be less money spent on salaries of executives. It may cause a reduction in the cost pass-through effect. This is an effect where executives get pay rises because the shareholders have gotten an increase in earnings. There will also be a reduction in cost per share of executive pay rises. With a capped pay, executives can only earn up to a certain level of salary per share. Lastly, the corporations will be able to compensate or repay the debts obtained from private equity markets.

This scenario can be analyzed using a demand and supply framework whereby corporate will demand less investors' funds to cater for its main needs and remain afloat. Many corporate organizations spend a huge percentage of their revenues and even borrowed money on bonus for their top executives. When salary caps are introduced, these corporate organizations will have reduced expenditures hence they will demand less finances to cater for salaries and general operations. Therefore, demand for funding will reduce drastically while the supply will remain the same. This will reduce the cost of capital thus increasing shareholders' wealth.

Therefore; a law that would cap salaries of top executives in corporate organizations would help them to be in stable financial positions since it reduces expenditures.

On the other hand, if the limit imposed is below the market clearing wages then the labour market may not clear because demand for top executives

will outstrip supply. Top executives are likely to relocate to countries where they will be paid the prevailing market wages. The lower wages are likely to attract low quality executives. This may in turn lead to poor corporate management.

Works Cited

Rezaee, Zabihollah. Corporate Governance Post-Sarbanes-Oxley: Regulations, Requirements, and Integrated Processes. illustrated. New York: John Wiley & Sons, 2007.