Executive Pay: What Worked?

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CEO pay is a controversial issue in America, but there was a time, often overlooked today, when chief executives were not paid nearly as much as they are now. From 1940 to the mid-1970s, executive pay was modest by today's standards even though U.S. business was generally thriving. What worked to keep executive pay in check? Economist Thomas Piketty and others credit high marginal income tax rates, leading to calls for a return to a similar tax regime. This Article casts doubt on the impact tax had and also shows that neither the configuration of boards nor shareholder activism played a significant role in constraining executive pay. It emphasizes instead the roles played by strong unions, a different and more circumscribed market for managerial talent, and social norms, explanations that do not easily lend themselves to generating modern policy prescriptions.

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I. INTRODUCTION

There is a substantial consensus that something is seriously amiss with executive pay, as the compensation of top executives of U.S. public companies is widely perceived as scandalously generous.[1] Critics of executive pay can be found even amongst stout defenders of free markets.[2] For instance, Richard Posner, a law and economics pioneer before he became a federal appellate judge, said in 2010 that the proposition that executive pay was excessive was "accepted not only by many leading scholars but by almost the entire nation, including many chief executive officers."[3]

Critics of executive pay often draw upon history for support, noting that the chief executive officers (CEOs) of today are much better paid than their counterparts of a half-century ago.[4] Being a chief executive may be challenging. Still, when the job is basically the same one it was during the mid-20th century, how can it be that CEO pay has increased substantially quicker than gross domestic product (GDP) per capita, total shareholder returns, corporate earnings, and the wages of ordinary employees?[5]

The dramatic growth in executive pay has not occurred in a vacuum. Managerial compensation has generated substantial controversy and criticism for at least a quarter-century,[6] and various reforms have periodically been introduced in response, seemingly to little avail. As the *Wall Street Journal* observed in 2006, "critics tried to slow skyrocketing pay through regulations, legislation and shareholder pressure. Few of their tactics worked. Many backfired."[7] For those perplexed or frustrated that efforts at reform have failed to reverse dramatic increases in executive pay, history may provide valuable lessons. American business enjoyed unparalleled success from the mid-1940s to 1970.[8] Nevertheless, during the middle decades of the 20th century, CEOs of U.S. public companies not only were paid less along various measures than their present-day counterparts, but inflation-adjusted executive compensation remained static and executives lost ground as compared to rank-and-file employees. What "worked" to constrain executive pay? This is the topic we explore in this Article.

Others have identified the shift from (relatively) modest mid-20th century executive compensation to stratospheric CEO pay by the century's closing stages as a topic worth

1. Michael Skapinker, *CEO pay: it is time for one brave leader to ask for less*, FIN. TIMES (May 20, 2015, 10:55 AM), http://www.ft.com/cms/s/0/2aaa6fe8-fe0c-11e4-8efb-00144feabdc0.html#axzz4JaiCE4md.

2. *Id.*

3. Richard A. Posner, *Are American CEOs Overpaid, and, if so, What if Anything Should be Done About It?*, 58 DUKE L.J. 1013, 1013–14 (2009).

4. *See, e.g.*, Robert J. Samuelson, *The CEO backlash*, WASH. POST (June 21, 2015), https://www.washingtonpost.com/opinions/the-ceo-backlash/2015/06/21/8dd31c14-169e-11e5-9ddc-e3353542100c_story.html?utm_term=.e57540dff6dc; *Top US executive pay deserves greater scrutiny*, FIN. TIMES (Aug. 7, 2015), http://www.ft.com/cms/s/0/11acf6fc-3cf3-11e5-8613-07d16aad2152.

5. *See* FIN. TIMES, *supra* note 4 (discussing total shareholder return); MICHAEL B. DORFF, INDISPENSABLE AND OTHER MYTHS: WHY THE CEO EXPERIMENT FAILED AND HOW TO FIX IT 19, 25, 147–48 (2014) (discussing other variables). We provide additional data on historical executive pay trends in Part II of this Article.

6. Troy A. Paredes, *Too Much Pay, Too Much Deference: Behavioral Corporate Finance, CEOs, and Corporate Governance*, 32 FLA. ST. U. L. REV. 673, 702 (2005) ("Executive compensation is one of the most controversial topics in corporate governance."); Paul Taylor, *When the Boss Feels Like a Million Dollars*, FIN. TIMES, Dec. 16, 1991, at 9 (indicating that what had been an interest in what top senior executives were paid was changing to a "fascination").

7. Joann S. Lublin & Scott Thurm, *Behind Soaring Executive Pay, Decades of Failed Restraints*, WALL ST. J. (Oct. 12, 2006, 11:59 PM), http://www.wsj.com/articles/SB116062249630690247.

8. DEREK BOK, THE COST OF TALENT: HOW EXECUTIVES AND PROFESSIONALS ARE PAID AND HOW IT AFFECTS AMERICA 42 (1993).

investigating. Paul Krugman said nearly 15 years ago, "[t]he explosion in C.E.O. pay over the past 30 years is an amazing story in its own right, and an important one."[9] Michael Dorff wrote similarly in 2014 that, "[t]his major shift provides an opportunity to probe the inner workings of CEO pay."[10] Research on point nevertheless is just beginning. Carola Frydman, who has empirically analyzed 20th century executive pay trends in considerable detail,[11] observed in a 2010 survey of CEO pay "the causes of the apparent regime change in CEO compensation . . . remain largely unknown."[12]

Explaining the "regime change" that disrupted mid-20th century CEO pay has important present-day policy ramifications. Thomas Piketty, in his much publicized 2013 tome *Capital in the Twenty-First Century*, detailed historical changes in the concentration of income and wealth and offered policy prescriptions designed to reverse growing inequality on both fronts.[13] In so doing, he argued that imposing high individual marginal income tax rates may be "the only way to stem the observed increase in very high salaries."[14] He suggested that the optimal top marginal tax rate would be above 80%,[15] a policy recommendation that became increasingly contentious as the popularity of his *Capital* book grew.[16] Piketty bolstered his argument with historical evidence, attributing a late 20th century surge in the income of top earners in the United States, including CEOs, to substantial cuts to income tax rates that began in the 1970s and were pronounced in the 1980s.[17] He argued that if the intention is to stop the "stratospheric pay of supermanagers," then "only dissuasive taxation of the sort applied in the United States and Britain before 1980 can do the job."[18]

Piketty's argument is certainly plausible. If, due to high marginal income tax rates, executives keep very little of what they earn, executives might well be prepared to leave substantial money "on the table" because they know that they will only be able to retain a small fraction of what they have earned. This should in turn dampen pressure public companies might otherwise feel to pay management generously. Still, is Piketty's invocation of history appropriate?

We argue no. Tax did not "do the job" with executive pay during the middle decades of the 20th century in the way Piketty implies. Instead, other factors were equally or more important. Powerful unions exerted downward pressure on executive pay. Managerial bargaining power was muted by limited job mobility and by a perception that the

9. Paul Krugman, *For Richer*, N.Y. TIMES (Oct. 20, 2002), https://nytimes.com/2002/10/20/magazine/for-richer.html?pagewanted=all.

10. DORFF, *supra* note 5, at 6.

11. *See, e.g.*, Carola Frydman & Raven E. Saks, *Executive Compensation: A New View from a Long-Term Perspective, 1936–2005*, 23 REV. FIN. STUD. 2099 (2010); Carola Frydman & Raven Molloy, *Pay Cuts for the Boss: Executive Compensation in the 1940s*, 72 J. ECON. HIST. 225 (2012).

12. Carola Frydman & Dirk Jenter, *CEO Compensation*, 2 ANN. REV. FIN. ECON. 75, 96 (2010).

13. *See generally* THOMAS PIKETTY, CAPITAL IN THE TWENTY-FIRST CENTURY (2013).

14. *Id.* at 512.

15. *Id.* at 512, 640 n.50 (stating that the optimal top tax rate would be 82 percent).

16. *See, e.g.*, Holman W. Jenkins, Jr., *Mulally v. Piketty*, WALL ST. J. (Apr. 22, 2014, 7:08 PM), http://www.wsj.com/articles/SB10001424052702303825604579517442982061548 (critiquing Piketty's analysis as "fundamentally trivial"); Robert J. Shiller, *Better Insurance Against Inequality*, N.Y. TIMES (Apr. 12, 2014), http://www.nytimes.com/2014/04/13/business/better-insurance-against-inequality.html ("The book is impressive in its wealth of information but it is short on solutions.").

17. PIKETTY, *supra* note 13, at 508–12.

18. *Id.* at 417, 512.

managerial function was bureaucratic in orientation and correspondingly undeserving of exceptional rewards. Perhaps most crucially, there were norms militating against "moneygrubbing" by top executives that functioned as a potent check on executive pay.

What are the policy implications of our findings? We are not seeking to identify in the past some sort of ideal executive pay model. Instead, our study provides insights regarding tools that could be deployed to restructure executive compensation should the political will develop to limit CEO pay substantially. One might wonder, for instance, if it would be possible to revise perceptions of top management to accord with those prevalent in the 1940s, 1950s, and 1960s or resurrect norms within companies strongly biased against greedy, grasping executives.

Simply turning back the clock, however, is impossible. For instance, to the extent that mid-20th century norms constrained executive pay, these norms were shaped by the economic chaos of the Depression and the challenges of World War II, neither of which we would like to experience again. Moreover, top executives are perceived differently now than they were in the mid-20th century, in the sense that their contribution to corporate success is thought of as being more critical. That means mid-20th century remuneration packages where performance-related pay was largely an afterthought are unlikely to be acceptable today. This in turn has important implications for the *level* of executive pay because a logical trade-off with a managerial compensation scheme where much of the pay is "at risk" is a highly lucrative upside if all goes well.

This Article is organized as follows. Part II provides an overview of the history of executive pay since the 1930s. It focuses primarily on a mid-20th century era of comparatively modest managerial compensation that began to unravel in the 1970s and was displaced fully in the 1980s in a way that set the scene for dramatic increases in executive pay occurring in the 1990s. Part III describes how efforts to respond to executive pay controversies arising over the past quarter century have failed to "work" in the sense that CEO compensation has remained high and criticism of executive pay remains vocal.

The remainder of this Article deals primarily with the middle decades of the 20th century, with the objective being to explain what "did the job" during this era of executive pay moderation. Part IV considers the contribution that tax policy made to managerial compensation trends, focusing particularly on the question of whether the relatively modest executive pay arrangements in place during the mid-20th century were chiefly a product of high marginal tax rates on income in place at that time. Part V analyzes other plausible explanations of what "worked" with executive pay. Some, such as board structure, shareholder intervention, and federal wage controls, had at best a minor role to play. Others—including union power, the market for managerial talent, and corporate culture ("norms")—do help to account for the configuration of executive pay during the middle decades of the 20th century, with the latter two factors being of particular importance. Part VI concludes.

II. THE FACTS OF EXECUTIVE PAY: THE 1930S TO TODAY

To set the scene for analysis of what "worked" with executive pay during the middle decades of the 20th century, we consider now the evolution of executive compensation since the 1930s and do so with particular reference to the period from 1940 to the 1990s. We focus primarily on identifying trends governing overall executive pay, though we also consider how pay was structured. Our summary is not exhaustive; it seeks merely to provide sufficient detail to put our subsequent analysis into proper context.

Railways aside, prior to the 20th century, corporations were almost always run either by individuals with large ownership stakes or by their representatives.[19] After a merger wave at the turn of the 20th century started to disperse ownership in major industrial corporations,[20] salaried executives lacking a meaningful ownership interest began taking up top managerial posts with great frequency.[21] Executive pay became a public issue as the 1930s began due to revelations that cast a harsh light on compensation practices during difficult economic times. Lawsuits and congressional hearings revealed that top executives at three major firms, Bethlehem Steel, American Tobacco, and National City Bank, had each been paid more than $1,000,000 a year in 1929 or 1930.[22] These apparently were exceptional cases.[23] Still, in the midst of the Great Depression, the image of a greedy corporate president and his million-dollar pay package became fixed in the public mind with many, if not most, Americans believing executives were paid "too much."[24]

Dissatisfaction with executive pay in the 1930s sparked a series of reform proposals, the most consequential of which required the disclosure of executive pay of publicly listed companies under newly enacted federal securities laws.[25] Evidence compiled from disclosures made to the federal Securities and Exchange Commission (SEC) suggests that, from 1936 to 1940, executive pay increased appreciably even after inflation.[26] This pattern, however, would soon change. During the 1940s, executive compensation saw "the sharpest drop . . . in at least the past 70 years, and possibly even longer."[27] In a 2012 study of compensation at large public manufacturing firms during the decade, Carola Frydman and Raven Saks Malloy found that, in real terms, the average pre-tax compensation for a firm's three highest-paid executives dropped by 11%, and after-tax earnings fell 24%.[28] Correspondingly, the median executive in Frydman and Molloy's sample received in 1949 17 times the pay of the average earner in the economy, compared with 24 in 1940.[29] This was one aspect of a "Great Compression" in wages in the United States at mid-century characterized by a decreasing distance between the wages of lower and higher-paid workers.[30]

19. Harwell Wells, *"No Man Can be Worth $1,000,000 a Year": The Fight Over Executive Compensation in 1930s America*, 44 U. RICH. L. REV. 689, 695–702 (2010).

20. Brian R. Cheffins, *Mergers and Corporate Ownership Structure: The United States and Germany at the Turn of the 20th Century*, 51 AM. J. COMP. L. 473, 474 (2003).

21. ALFRED D. CHANDLER, SCALE AND SCOPE: THE DYNAMICS OF INDUSTRIAL CAPITALISM 85 (1990).

22. Wells, *supra* note 19, at 710–15.

23. JOHN CALHOUN BAKER, EXECUTIVE SALARIES AND BONUS PLANS 261 (1938) (indicating that, as of 1932, the median compensation for a president in a sample of 100 industrial companies was only $41,833, equivalent to less than $750,000 currently).

24. *Fortune Survey Big Salaries*, FORTUNE, Apr. 1936, at 215 (reporting poll indicating that 54.5% of Americans felt this way).

25. *See* Wells, *supra* note 19, at 741–44; Kevin J. Murphy, *Executive Compensation: Where We Are, and How We Got There*, *in* 2A HANDBOOK OF THE ECONOMICS OF FINANCE 211, 251 (George M. Constantinites et al. eds., 2013); Sandra L. Suárez, *Symbolic Politics and the Regulation of Executive Compensation: A Comparison of the Great Depression and the Great Recession*, 42 POL. & SOC'Y 73, 89 (2014).

26. Frydman & Saks, *supra* note 11, at 2107 fig.1.

27. Frydman & Molloy, *supra* note 11, at 225.

28. *Id.* at 239. The authors report the composition of their sample "is similar to that of manufacturing firms traded on the New York Stock Exchange." *Id.* at 229.

29. *Id.* at 227.

30. Claudia Goldin & Robert A. Margo, *The Great Compression: The Wage Structure in the United States*

Executives did somewhat better in the 1950s and 1960s in that their compensation did not shrink in real terms. Still, executive pay barely budged even though this was an era when "U.S. business stood triumphant at home and abroad."[31] According to a 2010 study by Frydman and Saks, which uniquely provides data on executive pay using a uniform methodology for the decades we focus on, between 1950 and 1975, executive compensation only grew after inflation by an average of 0.8% annually.[32] The mid-20th century wage "Great Compression" correspondingly continued. For instance, between 1959 and 1968 the pay of a chief executive of a company with sales of $400 million or more rose 14% as compared with 39% for manufacturing employees overall.[33] Moreover, the one million dollar executive was nowhere to be found. Industry's first "Millionaire Club" only took form in 1977 when the total compensation of the five best paid CEOs in the United States exceeded one million dollars a year.[34]

While overall levels of executive pay barely budged in real terms from 1950 through the 1970s, some changes were occurring with the composition of executives' pay. During the 1940s, executive compensation was overwhelmingly composed of salary and bonuses based on annual targets.[35] Due in large measure to tax changes occurring in 1950,[36] over the next decade, the fraction of executives holding stock options jumped from 10% to 60%, and the grant-date value of stock options awarded rose from 10% to over 20% of total executive compensation.[37] Nevertheless, stock options grants "remained too small to have much of an impact on median pay levels until the late 1970s."[38] Similarly, while deferred compensation—such as pensions—and perquisites—such as expense accounts—became important parts of compensation in the 1950s, the value of such fringe benefits was not substantial enough to change the general conclusion that executive compensation grew anemically during the 1950s and 1960s.[39]

Executive pay stagnation continued into the early 1970s.[40] A 1976 article in the *Harvard Business Review*, citing data indicating executive compensation fell 20% as a multiple of hourly workers' income between 1964 and 1974, referred to a "pinch on executive pay" that was resulting in a "devaluation of the American executive."[41] Matters,

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at Mid-Century, 107 Q. J. ECON. 1, 1–2 (1992).

31. LOUIS GALAMBOS & JOSEPH PRATT, THE RISE OF THE CORPORATE COMMONWEALTH: UNITED STATES BUSINESS AND PUBLIC POLICY IN THE 20TH CENTURY 183 (1988).

32. Frydman & Saks, *supra* note 11, at 2099–100 (discussing the unique nature of Frydman and Saks's data), *id.* at 2106–07 (discussing their 1950–1975 data). The evidence cited relates to pre-tax compensation, but they report broadly similar trends after-tax. *Id.* at 2110. Wilbur Lewellen found that, between 1940 and 1963, average before-tax compensation for senior executives increased 80%. WILBUR LEWELLEN, EXECUTIVE COMPENSATION IN LARGE INDUSTRIAL CORPORATIONS 8 (1968). Frydman and Saks persuasively argue, however, that this greatly overstates growth due to the use of a primitive method for valuing stock options as compensation. Frydman & Saks, *supra* note 11, at 2108–09 n.15.

33. Arch Patton, *Are We Sabotaging Executive Motivation?*, 7 MCKINSEY Q. 52, 55, 57–58 (1970).

34. Donald B. Thompson, *Advent of 7-Figure CEO Prompts Questions*, CHI. TRIB., May 31, 1981, at N1. *Cf. Other Business; The Million Dollar Sure Thing*, N.Y. TIMES, Jan. 24, 1982, at A23 (indicating Henry Ford II became the first million-dollar executive in 1978).

35. Frydman & Saks, *supra* note 11, at 2106–07.

36. *See infra* text accompanying note 142 (discussing executive compensation in the 1950s and 1960s).

37. Murphy, *supra* note 25, at 254.

38. Frydman & Jenter, *supra* note 12, at 81.

39. Frydman & Saks, *supra* note 11, at 2109.

40. *See infra* Figure 1.

41. David Kraus, *The "Devaluation" of the American Executive*, HARV. BUS. REV., May-June 1976, at 84,

however, were in flux. Between 1973 and 1979, the median cash compensation for CEOs in the *Forbes 800* increased by 12.2% each year when annual inflation was 8.5%.[42] By the end of the 1970s, executive pay seemingly had begun a "regime change" from stagnancy to rapid growth.[43] It is impossible to pinpoint the exact moment that executive pay began to increase substantially.[44] Various observers, however, have pegged the second half of the 1970s as the beginning of the acceleration that characterized the rest of the century.[45] A 1977 *McKinsey Quarterly* report substantiates this verdict, as it indicated executive compensation had risen dramatically in 1976 and quoted a *New York Times* story that said, "[t]he restraints are coming off. It is a time to grab" to drive home the point.[46]

Regardless of precisely what happened in the 1970s, in the 1980s, executive compensation increased rapidly. *Newsweek* reported in 1991 that "CEO pay rose dramatically all through the 1980s—212 percent . . . —four times faster than pay for ordinary workers."[47] The *Economist* said in 1992, "chief executives' pay soared throughout the 1980s."[48]

According to financial economists Michael Jensen and Kevin Murphy, all executives were doing in the 1980s was "catching up."[49] In urging public companies to do more to link CEO pay with corporate performance, they argued that, despite headlines to the contrary, top executives were not receiving record salaries and bonuses.[50] To make their point, Jensen and Murphy provided data indicating that, in 1986 dollars, CEOs of larger companies traded on the New York Stock Exchange were paid more in the mid-1930s (an average of $882,000) than they were from 1982 through 1988 ($843,000).[51] Nevertheless, even if Jensen and Murphy were correct that 1980s executives were merely "catching up," the fact that their CEO pay figure for 1982 to 1988 was substantially higher than the equivalent figure for 1974 to 1981 ($642,000) indicated clearly how much things were changing.[52]

Executive pay increases occurring in the 1980s served as a prelude to even more dramatic growth in the 1990s that would drive CEO pay up to unprecedented levels. Carola Frydman and Dirk Jenter found that median compensation for an S&P 500 CEO rose from $2.2 million in 1992 to $7.2 million in 2001.[53] Lucian Bebchuk and Yaniv Grinstein looked at a similar cohort but focused instead on average (mean) CEO compensation and found it "climbed from $3.7[ ]m[illion] in 1993 to $9.1[ ]m[illion] in 2003," a 146% increase.[54]

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42. Murphy, *supra* note 25, at 260.

43. Frydman & Saks, *supra* note 11, at 2101.

44. *See* Detlev Vagts, *Challenges to Executive Compensation: For the Markets or the Courts?*, 8 J. CORP. L. 231, 247 (1983) (describing the difficulty of ascertaining what was going on in the late 1970s).

45. Frydman & Jenter, *supra* note 12, at 83; DORFF, *supra* note 5, at 18, 24.

46. David J. McLaughlin, *Surging Executive Pay: Time to Take Stock*, MCKINSEY Q. 46, 47 (1977) (citing *When the Boss Gets a Raise*, N.Y. TIMES, July 24, 1977, at 12.

47. *The Pay Police*, NEWSWEEK (June 16, 1991), http://www.newsweek.com/pay-police-204464.

48. *Worthy of His Hire?*, ECONOMIST (Feb. 1, 1992), https://www.highbeam.com/doc/1G1-11791136.html.

49. Michael C. Jensen & Kevin J. Murphy, *CEO Incentives—It's Not How Much You Pay, But How*, HARV. BUS. REV. (May–June 1990), https://hbr.org/1990/05/ceo-incentives-its-not-how-much-you-pay-but-how.

50. *Id.*

51. *Id.*

52. *Id.*

53. Frydman & Jenter, *supra* note 12, at 78 tbl.1.

54. Lucian Bebchuk & Yaniv Grinstein, *The Growth of Executive Pay*, 21 OXF. REV. ECON. POL. 283, 285

The dramatic growth in CEO pay was accompanied by related executive compensation trends. One was that, despite Jensen and Murphy's argument that there was little reason to be concerned about how much executives were paid, sustained and widespread criticism of lucrative CEO pay emerged for the first time since the 1930s. The trend became evident in the 1980s, driven by a takeover boom that meant, at least according to the media, workers were being laid off while dismissed executives were being rewarded with lucrative "golden parachute" severance payments.[55] It crescendoed in the early 1990s with exposés of executive compensation appearing at the same time as articles comparing the compensation of American chief executives to that of their lower-paid, yet ostensibly more successful, foreign counterparts.[56]

A second important trend was greater emphasis on linking pay with performance. The case that Jensen and Murphy made in this regard helped to convert many to the idea that executive pay should be designed to ensure "agents" (i.e., senior executives) had their incentives aligned with those of their "principals" (i.e., shareholders).[57] This reasoning, possibly combined with tax reforms made in 1993 that created incentives for companies to use performance-oriented pay,[58] helped to prompt a reorientation in pay in favor of stock options and later long-term incentive plans with targets related to corporate performance.[59] Only 16% of CEO compensation in S&P 500 companies was performance based in the 1970s, but the proportion grew to 26% in the 1980s and 47% in the 1990s.[60]

The shift toward performance-oriented pay in the 1990s likely helps to explain the substantial increase in aggregate executive compensation.[61] Executives have various reasons to dislike having their pay tied closely to stockholder-related measures of corporate performance, such as share prices and total shareholder return. These include fears that pay will fluctuate dramatically in accordance with changing corporate fortunes, concerns about pay falling substantially due to factors beyond the control of the executives (e.g., general stock market trends), and investment-related apprehension about tying pay to the performance of the company in which they have already tied up virtually all of their human capital.[62]

(2005) (measured ex ante). On the significance of differences between mean/average and median compensation in this particular context, see Frydman & Jenter, *supra* note 12, at 78.

55. *See* Murphy, *supra* note 25, at 267–69.

56. *See, e.g.*, GRAEF CRYSTAL, IN SEARCH OF EXCESS: THE OVERCOMPENSATION OF AMERICAN EXECUTIVES (1991); Peter Passell, *Those Big Executive Salaries May Mask a Bigger Problem*, N.Y. TIMES (Apr. 20, 1992), http://www.nytimes.com/1992/04/20/business/economic-watch-those-big-executive-salaries-may-mask-a-bigger-problem.html?pagewanted=all.

57. On the impact of this reasoning, see, e.g., Simon Holberton, *Why Performance Should be the Most Crucial Element*, FIN. TIMES, May 16, 1990; Charles M. Yablon, *Bonus Questions—Executive Compensation in the Era of Pay for Performance*, 75 NOTRE DAME L. REV. 271, 279 (1999); Frank Dobbin & Dirk Zorn, *Corporate Malfeasance and the Myth of Shareholder Value*, 17 POL. POWER & SOC. THEORY 179, 189 (2005). Jensen was a pioneering proponent of principal/agent theory in the context of the public company, Michael Jensen & William Meckling, *Theory of the Firm: Managerial Behavior, Agency Costs, and Ownership Structure*, 3 J. FIN. ECON. 305 (1976).

58. *See infra* text accompanying notes 84, 91.

59. Murphy, *supra* note 25, at 274–79, 287–88. Murphy offers a multi-causal explanation for the growing use of stock options in the 1990s, including favorable accounting rules and relatively lax disclosure regulation.

60. Frydman & Jenter, *supra* note 12, at 80 tbl.2a.

61. Frydman & Saks, *supra* note 11, at 2103.

62. DORFF, *supra* note 5, at 85–86; BRIAN R. CHEFFINS, COMPANY LAW: THEORY, STRUCTURE AND OPERATION 686–87 (1997).

For companies that want to link pay with performance but also want to assuage managerial doubts about the idea, the obvious solution is to structure executive compensation to provide for a highly lucrative upside if all goes well.[63] Empirical analysis indeed reveals that, between 1980 and 2005, increases in the level of executive pay were driven in large measure by the growing use of performance-oriented managerial compensation.[64] Managerial attitudes aside, the shift toward performance-oriented pay in the 1990s drove executive pay upward because the stock market rose substantially in buoyant economic conditions. As *Time* observed in 1997, "it is that bull market that has turned millions upon millions of stock options into pure CEO gold, in cartloads unforeseen by anyone."[65]

Due to the bursting of a "dot-com" fueled stock market bubble and corporate governance scandals such as Enron and WorldCom, share prices fell substantially in the early 2000s, which coincided with a modest drop in CEO pay.[66] Chief executive compensation rallied in the mid-2000s before falling again in the wake of the 2008 financial crisis.[67] Median pay for an S&P 500 CEO stood at $9.3 million in 2001, dropped to $8.1 million in 2005, and then bounced around, rising to $9.1 million again in 2006 but dropping to $7.4 million in 2009 before recovering to $9 million in 2011.[68] Median CEO pay crossed the $10 million threshold for the first time in history in 2013[69] and rose to a record $10.6 million in 2014.[70]

Even though the dramatic pay increases of the 1990s have not been repeated since 2000, a yawning gap remains between a CEO's pay and that of the average worker. The exact details may vary, but, as many Americans are aware, whereas CEOs used to make not even 20 times what an average worker in their industry made, they now earn roughly 300 times the average worker's wage.[71] The "compression" of executive pay that characterized American public companies during the middle decades of the 20th century

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63. CHEFFINS, *supra* note 62, at 687–88.

64. Frydman & Saks, *supra* note 11, at 2130.

65. Daniel Kadlec & Bernard Baumohl, *Linking the Boss's Check to the Firm's Stock Price Seemed Reasonable Then the Market Went Wild*, TIME, Apr. 28, 1997.

66. Richard A. Lord & Yoshie Saito, *Trends in CEO Compensation and Equity Holdings for S&P 1500 Firms: 1994–2007*, 20 J. APP. FIN. 1, 2, 5, 9 (2010).

67. Martin J. Conyon, *Executive Compensation and Board Governance in US Firms*, 124 ECON. J. F60, F73 (2013).

68. Murphy, *supra* note 25, at 295–96. Frydman and Saks's study, *supra* note 11, ends in 2005 so cannot be referred to for this period.

69. *Median pay for CEOs rises above $10 million in 2013*, L.A. TIMES (May 27, 2014, 6:48 PM), http://www.latimes.com/business/la-fi-ceo-pay-20140527-story.html.

70. *This exec is the highest-paid American CEO*, CBSNEWS (May 26, 2015, 6:00 AM), http://www.cbsnews.com/news/this-exec-is-the-highest-paid-american-ceo.

71. *See* Lawrence Mishel & Alyssa Davis, *Top CEOs Make 300 Times More than Typical Workers*, ECON. POLICY INST. (June 21, 2015), http://www.epi.org/publication/top-ceos-make-300-times-more-than-workers-pay-growth-surpasses-market-gains-and-the-rest-of-the-0-1-percent/ (explaining the EPI number is based on realized, and not estimated, CEO compensation); *see also Anticipating the CEO Pay Ratio—CEO Pay vs Median Income*, EQUILAR (May 20, 2015), http://www.equilar.com/blogs/33-ceo-pay-ratio-median-income.html (finding that CEO pay to median income pay ratio for the S&P 1500 had increased from 83 to 1 in 2007 to 130 to 1 in 2014, and the ratio for S&P 500 companies had grown from 206 to 1 in 2007 to 248 to 1 in 2014); Melanie Trottman, *Top CEOs Make 373 Times the Average U.S. Worker*, WALL ST. J. (May 13, 2015, 12:21 PM), http://blogs.wsj.com/economics/2015/05/13/top-ceos-now-make-373-times-the-average-rank-and-file-worker/ (reporting the results of an AFL-CIO study).

correspondingly, is no more than a dim memory.

III. EXECUTIVE PAY REFORM—MORE MISSES THAN HITS

The dramatic growth in executive compensation over the past four decades has generated significant controversy.[72] A variety of reforms adopted in response are summarized here; to anticipate, none have "worked" to moderate executive pay in the mid-20th century manner. Instead, the dramatic increases occurring in the 1980s and 1990s have remained entrenched because periodic decreases in executive compensation associated with scandals and falling share prices have been more than cancelled out by increases in better times. As a 2015 newspaper editorial said, the effort to reform executive pay practices has been "one of the least-successful movements of the past decade."[73]

Executive pay critics have certainly not been mollified. Instead, they are "angry" and "outraged,"[74] with commentators over the past few years describing CEO pay packages as "gluttonous," "shameful," and "without honor."[75] Hillary Clinton chose to attack executive compensation early in her 2016 Presidential campaign in an apparent attempt to "strik[e] a populist note."[76] Even the former president of the National Association of Manufacturers suggested in 2015 that, "at a time when our economy is sluggish and millions of working Americans are struggling to make ends meet, it is unseemly for the lucky few at the top of the corporate pyramid to be taking conspicuous advantage of their power."[77]

The most ambitious and the most conspicuously unsuccessful efforts at executive pay reform, assuming the objective was to address concerns executives were paid too much, were launched in the early 1990s. Due to a combination of rapidly increasing executive pay and recessionary economic conditions, managerial remuneration became highly controversial and was an issue in the 1992 election campaign.[78] In this context, significant reforms were introduced, impacting the disclosure and taxation of executive pay.

In October 1992, the SEC substantially revamped rules governing disclosure of

72. *Supra* text accompanying note 6.

73. *Editorial, Executive Compensation, Ever Higher, Ever Less Justifiable*, ST. LOUIS POST-DISPATCH (May 26, 2015), http://www.stltoday.com/news/opinion/columns/the-platform/editorial-executive-compensation-ever-higher-ever-less-justifiable/article_9ff743e4-e9fb-507b-93ba-60b969bb4655.html.

74. DORFF, *supra* note 5, at 2; Karen Dillon, *The Coming Battle over Executive Pay*, HARV. BUS. REV. (Sept. 2009), https://hbr.org/2009/09/the-coming-battle-over-executive-pay; Steven Davidoff Solomon, *Outrage Over Wall St. Pay, But Shrugs for Silicon Valley?*, N.Y. TIMES: DEALBOOK (Feb. 18, 2014, 9:12 PM), http://dealbook.nytimes.com/2014/02/18/outrage-over-wall-st-pay-but-shrugs-for-silicon-valley/.

75. Barry Ritholtz, *Executive Pay Gluttony*, BLOOMBERGVIEW (Apr. 30, 2015, 11:36 AM), http://www.bloombergview.com/articles/2015-04-30/executive-pay-transparency-won-t-lead-to-reform; Sheryl Gay Stolberg & Stephen Labaton, *Obama Calls Wall Street Bonuses 'Shameful'*, N.Y. TIMES (Jan. 29, 2009), http://www.nytimes.com/2009/01/30/business/30obama.html?_r=0; Frank Islam & Ed Crego, *Profits Without Honor: The Sad Truth About CEO Compensation*, HUFFINGTON POST, http://www.huffingtonpost.com/frank-islam/profits-without-honor-the_b_7042612.html (last updated June 12, 2015).

76. Caren Bohan et al., *Hillary Clinton surprises with early attack on CEO pay*, REUTERS (Apr. 13, 2015, 7:29 PM), http://www.reuters.com/article/2015/04/13/us-usa-election-clinton-inequality-idUSKBN0N421620150413.

77. Jerry Jasinowski, *Executive Compensation*, HUFFINGTON POST, http://www.huffingtonpost.com/jerry-jasinowski/executive-compensation_b_7459426.html (last updated May 28, 2016).

78. Kevin J. Murphy, *The Politics of Pay: A Legislative History of Executive Compensation*, *in* RESEARCH HANDBOOK ON EXECUTIVE PAY 11, 23 (Randall Thomas & Jennifer Hill, eds., 2012).

executive pay.[79] The most dramatic change was mandating that companies provide, in proxy solicitation documentation circulated to shareholders, a Summary Compensation Table setting out the major components of executive pay the CEO and other highly paid executives had received over the previous three years. The purpose was to provide investors with an easily understood overview of executive pay in a single location.[80] Additional tables describing in much greater detail payment in the form of stock options were also required.[81]

Tax law was also deployed. All compensation has to be "reasonable" to qualify for deduction under the income tax.[82] For corporations, newly-elected President Bill Clinton proposed in 1993 to define all managerial compensation above one million dollars as per se unreasonable, and therefore non-deductible, before backing off so that the deduction would only be denied to pay above this level that was not performance related.[83] As enacted in Section 162(m), amounts paid in excess of one million dollars to the CEO and the other four highest-paid executives of a public corporation were deemed non-deductible unless the pay was based on performance goals that were determined by a compensation committee comprised of independent directors and approved by a vote of shareholders.[84]

Despite the reforms occurring in the early 1990s, executive compensation sky-rocketed for the remainder of the decade.[85] Indeed, the regulatory initiatives may have had the unintended consequence of accelerating the process. For instance, various observers have hypothesized that the toughening of disclosure rules in 1992 helped to foster the dramatic upward spiral of executive pay in the 1990s.[86] Why would this have happened? A 2006 *New York Times* story entitled *Disclosure Won't Tame CEO Pay* captures the logic: "History suggests that whenever [chief executives] discover a fellow CEO is getting something they don't have, they make a grab for it. In other words, as laudable as more disclosure is, there is a real possibility it will make a bad situation worse."[87]

To elaborate, due to disclosure, both managers and board members who set executive pay can find out readily the "market rate" offered by comparable public companies.[88] Executives who become aware they are paid less than their peers will likely seek adjustments. The directors who set their pay will tend to be sympathetic because of a belief the management team is not "below average" and might defect to rivals offering more generous terms.

The $1 million deductibility cap was similarly problematic. It, in effect, may have

79. Executive Compensation Disclosure, 57 Fed. Reg. 48,126 (Oct. 21, 1992) (to be codified at 17 C.F.R. pts. 228, 229, 240, 249); Marlo A. Bakris, Note, *Executive Compensation Disclosure: The SEC's Newest Weapon in its Arsenal Against Executive Compensation Abuse*, 71 U. DET. MERCY L. REV. 105, 110 (1993).

80. CHEFFINS, *supra* note 62, at 677.

81. Murphy, *supra* note 25, at 274.

82. I.R.C. § 162(a)(1) (2014); Aaron S. J. Zelinsky, Comment, *Taxing Unreasonable Compensation: § 162(a)(1) and Managerial Power*, 119 YALE L.J. 637, 638 (2009).

83. Murphy, *supra* note 25, at 277–78; Steven A. Bank, *Devaluing Reform: The Derivatives Market and Executive Compensation*, 7 DEPAUL BUS. L.J. 301, 302 (1995).

84. I.R.C. § 162(m).

85. *Supra* text accompanying notes 53–54.

86. Lublin & Thurm, *supra* note 7; Joseph Nocera, *Disclosure Won't Tame C.E.O Pay*, N.Y. TIMES (Jan. 14, 2006), http://www.nytimes.com/2006/01/14/business/disclosure-wont-tame-ceo-pay.html.

87. Nocera, *supra* note 86.

88. DORFF, *supra* note 5, at 194–95; Brian Cheffins & Randall Thomas, *The Globalization (Americanization?) of Executive Pay*, 1 BERKELEY BUS. L.J. 233, 272 (2004).

been treated as an implicit endorsement of CEO pay of at least $1 million annually, thereby prompting companies paying less to play catch up.[89] Moreover, since performance-related executive pay will tend to correlate with higher aggregate pay,[90] the 1993 tax change, by providing companies with a tax incentive to rely extensively on performance-based pay, may have helped drive the huge compensation numbers in the ensuing years.[91] The fact that many tax-protected bonus payments under Section 162(m) were only weakly tied to performance likely compounded the problem.[92] Even if Section 162(m) was not a catalyst for the rapid growth of executive pay in the 1990s,[93] it does not appear to have done anything to stem the tide.

There was little additional executive pay regulation reform throughout the remainder of the 1990s, but various changes have been made since the early 2000s. None, however, have apparently had a substantial impact on the amount executives are paid nor are likely to do so in the future. For instance, the Sarbanes–Oxley Act in 2002 mandated the "clawback" of performance-based compensation that was paid based on financial information that ultimately proved to be erroneous, while the Dodd–Frank Act of 2010 required companies to implement and enforce policies for recouping such payments made to executives.[94] Executive pay expert Kevin Murphy has said that the Sarbanes–Oxley clawback provision was "notable mostly for its ineffectiveness,"[95] and proposed rules for the implementation of the Dodd–Frank clawback provision, which have yet to be adopted, have generated criticism of their own as commentators question whether companies will undercut the measure by restructuring pay packages or managing earnings in a way to avoid triggering a clawback.[96]

The expansion of the clawback rules was just one feature of Dodd–Frank dealing with executive pay.[97] A much more heavily publicized change was a "say-on-pay" mandate. As Section V.A.2 discusses, for many years there have been requirements that shareholders

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89. Gregg D. Polsky, *Controlling Executive Compensation Through the Tax Code*, 64 WASH. & LEE L. REV. 877, 917–20 (2007); Tod Perry & Marc Zenner, *Pay for Performance? Government Regulation and the Structure of Compensation Contracts*, 62 J. FIN. ECON. 453, 460 (2001).

90. *Supra* text accompanying notes 61–63.

91. Murphy, s*upra* note 25, at 278–79; Joy Sabino Mullane, *Incidence and Accidents: Regulation of Executive Compensation Through the Tax Code*, 13 LEWIS & CLARK L. REV. 485, 524–25 (2009); Meredith R. Conway, *Money for Nothing and the Stocks for Free: Taxing Executive Compensation*, 17 CORNELL J.L. & PUB. POL'Y 383, 410 (2008).

92. LUCIAN BEBCHUK & JESSE FRIED, PAY WITHOUT PERFORMANCE: THE UNFULFILLED PROMISE OF EXECUTIVE COMPENSATION 135 (2004).

93. For studies failing to find much of a causal link see, Brian J. Hall & Jeffrey B. Liebman, *The Taxation of Executive Compensation*, 14 TAX POL'Y & ECON. 1, 3 (2000); Nancy L. Rose & Catherine D. Wolfram, *Regulating Executive Pay: Using the Tax Code to Influence Chief Executive Officer Compensation*, 20 J. LAB. ECON. S138, S166 (2002).

94. Sarbanes–Oxley Act of 2002, Pub. L. No. 107-204, § 304, 116 Stat. 745 (2002); Dodd–Frank Wall Street Reform and Consumer Protection Act (Dodd–Frank Act), Pub. L. No. 111-203, § 954, 124 Stat. 1376, 1904 (2010).

95. Murphy, *supra* note 25, at 289. Voluntary clawback provisions adopted prior to Dodd–Frank were no more effective. Jesse Fried & Nitzan Shilon, *Excess-Pay Clawbacks*, 36 J. CORP. L. 721, 737–42 (2011).

96. Steven A. Bank & George S. Georgiev, *Paying High for Low Performance*, 100 MINN. L. REV. HEADNOTES 14, 23-26 (2016), http://www.minnesotalawreview.org/headnotes/paying-high-performance/; Jesse M. Fried, *Rationalizing the Dodd–Frank Clawback* 33 (EUR. CORP. GOVERNANCE INST., Working Paper No. 314/2016, May 2016),
http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2764409.

97. Dodd–Frank Act, Title IX, subtitle E.

approve specified features of executive compensation. Under Dodd–Frank, shareholders of public companies were given the right for the first time to vote on executive pay policy in its entirety.[98] Corporations, however, were only required to offer a "say-on-pay" vote once every three years, and the outcome of the votes was deemed to be merely advisory.[99] These features may help to explain say-on-pay's modest subsequent impact. In the first five proxy seasons after the say on pay rules went into effect, fewer than three percent of all shareholder say-on-pay votes at Russell 3000 corporations were negative.[100] There is some evidence that the rarity of "no" votes is attributable at least partly to boards modifying compensation plans to head off possible negative recommendations.[101] Such modifications, however, may well have been accompanied by offsetting changes that resulted in higher overall executive pay.[102]

Board structure was another executive compensation topic Dodd–Frank addressed. The Act stipulated that the SEC should require national stock exchanges to provide in their listing rules that public companies must establish compensation committees staffed by independent directors.[103] This was hardly a radical change. As far back as 2000, nearly four out of five S&P 500 companies had a compensation committee comprised entirely of independent directors.[104] Moreover, the New York Stock Exchange has required since 2003 that companies listed for trading have a compensation committee staffed by independent directors.[105]

Dodd–Frank also required expanded disclosure of executive compensation. Most controversially, the Act provided that the SEC should introduce rules requiring an issuer to disclose the ratio between its CEO's total compensation and the median total compensation for all of the company's other employees.[106] With the SEC only having implemented the relevant rules in 2015 and with companies not needing to make the relevant disclosures until 2018,[107] it is too early to gauge the impact of reform. Still, it seems unlikely pay ratio disclosure will substantially change existing practices. As one commentator opined:

> The idea behind publishing the ratio of executive pay to worker pay

98. Dodd–Frank Act § 951.

99. Dodd–Frank Act §§ 951 (a)(3), (c).

100. *See* 2015 SAY ON PAY RESULTS, SEMLER BROSSY (Sept. 28, 2015), http://www.semlerbrossy.com/say-on-pay/seven-additional-companies-fail-say-on-pay/.

101. DORFF, *supra* note 5, at 245.

102. Mathias Kronland & Shastri Sandy, *Does Shareholder Scrutiny Affect Executive Compensation? Evidence from Say-on-Pay Voting* 6 (April 15, 2015), http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2358696.

103. Dodd–Frank Act § 952.

104. Vidhi Chhaochharia & Yaniv Grinstein, *The Changing Structure of US Corporate Boards: 1997–2003*, 15 CORP. GOVERNANCE 1215, 1218, tbl.2 (2007) (finding that 78.5% of all S&P 500 companies had independent compensation committees in 2000).

105. Harvey Gleb, *Corporate Governance and the Independence Myth*, 6 WYO. L. REV. 129, 157 (2006).

106. Dodd–Frank Act § 953(b)(1)(c). Section 953(a) also directed the SEC to enhance rules governing disclosure of the link between pay and performance. In 2015, the SEC issued proposed rules on point, but implementation seems unlikely to have a marked effect on executive pay -- Bank & Georgiev, *supra* note 96, 20.

107. Press Release, SEC Adopts Rule for Pay Ratio Disclosure (Aug. 5, 2015), http://www.sec.gov/news/pressrelease/2015-160.html; Brett F. Busacker, *Dodd–Frank CEO Pay Ratio Disclosure Rules Approved*, NAT'L. L. REV. (Aug. 10, 2015), http://www.natlawreview.com/article/dodd-frank-ceo-pay-ratio-disclosure-rules-approved.

> seems to be that the disparity will embarrass corporate boards and anger investors into cutting back on executive pay. Sounds good. But I don't see that happening. If there was anger and embarrassment over CEO salaries, those salaries already would be cut. As long as CEOs deliver, what is the incentive to cut their pay?[108]

The dramatic acceleration of executive pay that occurred in the 1990s may have ceased. Nevertheless, executive pay has, for the most part, continued to increase since the early 2000s.[109] Correspondingly, it seems fair to say that reform efforts of the past 25 years have yielded many more misses than hits. So the question this Article focuses on naturally arises: why, given the dramatic growth in executive pay as the 20th century drew to a close, was managerial compensation flat for a number of decades prior to that, decades in which American business was performing well? What, in other words, "worked" to compress executive pay? We begin our analysis by considering the role of tax, in large measure because of Thomas Piketty's high- profile recommendation that high marginal tax rates be introduced to bring executive pay under control.[110]

IV. TAXATION AND EXECUTIVE PAY

A. Higher Tax Rates as a Potential Cure for Executives Being Paid "Too Much"

While Thomas Piketty is perhaps the most prominent commentator to have suggested that a solution to unduly lucrative executive pay is to raise income tax rates, he is by no means the only one. As far back as 1993, former Harvard law professor and President Derek Bok made this argument.[111] Judge Richard Posner did likewise in a 2010 law review article on executive pay,[112] as have various academics[113] and media commentators.[114]

These calls to raise top income tax rates to rein in executive pay are implicitly based

108. Paul Sassone, *High CEO pay isn't America's problem*, CHI. TRIB. (Aug. 13, 2015, 11:35 AM), http://www.chicagotribune.com/suburbs/evanston/lifestyles/ct-evr-sassone-ceo-pay-tl-0820-20150813-story.html.

109. *Supra* text accompanying notes 68–70.

110. *Supra* text accompanying notes 14–15.

111. BOK, *supra* note 8, at 275.

112. Posner, *supra* note 3, at 1046.

113. *See, e.g.*, Robert B. Reich, *CEOs Deserve Their Pay*, WALL ST. J., http://www.wsj.com/articles/SB118972669806427090 (last updated Sept. 14, 2007, 12:01 AM) ("[T]he answer . . . is a higher marginal tax rate on the super pay of those in super demand."); Josh Bivens & Lawrence Mishel, *The Pay of Corporate Executives and Financial Professionals as Evidence of Rents in Top 1 Percent Incomes*, 27 J. ECON. PERSP. 57, 74 (2013); Mullane, *supra* note 91, at 551–52; ANTHONY B. ATKINSON, INEQUALITY: WHAT CAN BE DONE? 185 (2015); *see also* David I. Walker, *A Tax Response to the Executive Pay Problem*, 93 B.U. L. REV. 325, 346 (2013) (proposing the combination of an executive pay surtax and investor tax relief).

114. *Frank on Populism: Why Big Paydays Aren't All Bad*, NEWSWEEK (Mar. 30, 2009, 8:00 PM), http://www.newsweek.com/frank-populismwhy-big-paydays-arent-all-bad-75995; Jon Talton, *Changes in public policy could put a lid on executives' excessive pay packages*, SEATTLE TIMES, http://www.seattletimes.com/business/changes-in-public-policy-could-put-a-lid-on-executives-excessive-pay-packages/ (last updated June 26, 2015, 12:04 PM) (proposing a return to the 70% marginal rate of the 1970s); *Cheques Need Balances*, ECONOMIST (June 25, 2016), http://www.economist.com/news/leaders/21701122-right-ways-fix-flawed-system-cheques-need-balances (saying of executive pay, "government meddling in this area tends to have unfortunate unintended consequences . . . . Politicians who want to shift the market's distribution of income have a better tool already at hand: a higher marginal rate of income tax").

on the assumptions that executives take into account the costs and benefits associated with negotiating lucrative compensation and that tax will be a cost that will deter them from taking full advantage of leverage they otherwise have. Piketty refers to the logic involved as a "bargaining power hypothesis."[115] To elaborate, significantly higher marginal tax rates can diminish substantially the after-tax benefits of the additional dollars executives obtain from managerial compensation. As the net benefit decreases, the costs become more salient, and executives theoretically will conclude that the pursuit of additional dollars is not worth whatever social capital has to be expended to obtain those dollars.[116] Executive pay moderation will follow in due course. Developments occurring during the middle of the 20th century provide an opportunity to test whether this theory holds up in practice.

B. Tax and Executive Pay Levels During the Middle of the 20th Century

Proving directly that executives respond to higher tax rates by leaving money on the table is not feasible because few are privy to the deliberations of directors or the negotiations with top management which serve to set executive pay. At least some of those who advocate using tax to solve the executive pay "problem" have correspondingly resorted to citing the historical record as evidence that tax reform would work. In particular, they point to the fact that from the 1940s through the 1970s high income tax rates were in place and that executive pay during this era was modest by present day standards. For instance, Piketty has cited developments in both the United States, where the top marginal tax rate was 91% between 1951 and 1963, and Britain, where the figure was as high as 98% between the 1950s and 1970s.[117] According to Piketty:

> It is always difficult for an executive to truly convince other parties involved in the firm . . . that a large pay raise—say of a million dollars—is truly justified. In the 1950s and 1960s, executives in British and US firms had little reason to fight for such raises, and other interested parties were less inclined to accept them, because 80–90 percent of the increase would in any case go directly to the government.[118]

At first glance, the chronology of the top marginal tax rate in the United States supports Piketty's logic. As Figure 1 indicates, the top marginal tax rate was high from the late 1930s to the 1970s, fell dramatically in the 1980s, and remained low by mid-20th century standards thereafter. Executive pay either fell or increased only modestly in real terms when income tax was high and only began to increase substantially when the top marginal tax rate fell.

Figure 1: Tax Rates and Median Total Compensation, 1936–2005[119]

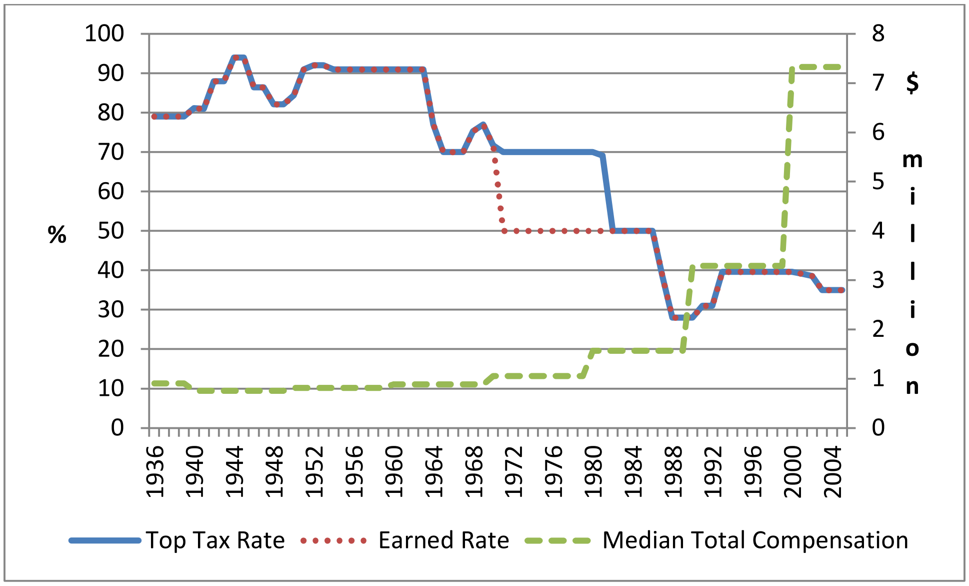
115. PIKETTY, *supra* note 13, at 510.

116. *Id.*; ATKINSON, *supra* note 113, at 186.

117. *See* MARTIN DAUNTON, JUST TAXES: THE POLITICS OF TAXATION IN BRITAIN, 1914–1979, 229 (2007) (describing the UK tax rates).

118. PIKETTY, *supra* note 13, at 509–10. On the British case, see also ATKINSON, *supra* note 113, at 186.

119. *See Historical Individual Income Tax Parameters,* TAX POLICY CENTER, (Feb. 22, 2016), http://www.taxpolicycenter.org/statistics/historical-individual-income-tax-parameters [hereinafter *Historical Individual*]. The data on the "earned rate" reflects the fact that due to the Tax Reform Act of 1969 earned income, such as salary and bonuses, was taxed at a lower rate than income from other sources, such as interest and



But was this merely a coincidence? Or did high marginal income tax rates actually cause executives to leave enough money on the table to explain the relatively modest executive pay arrangements in place from the 1940s through to the 1970s?

C. How Much Did Tax Matter?

During the middle decades of the 20th century, various observers argued that the high marginal tax rates in place put meaningful downward pressure on executive compensation. One practitioner remarked in 1956 that, "the no longer new, but always awe-inspiring, high plateau of progressive individual income taxes upon the take-home pay of high priced key personnel" had made traditional compensation policies "obsole[te]."[120] David Roberts, in a 1959 study of executive compensation, said the income tax regime was "widely credited with partial responsibility for the failure of executive earnings gains to keep pace with those in other occupations. The corporation is allegedly discouraged from making increases which add to its costs and confer little after taxes benefit upon the executive."[121] J. Grant MacDonnell of Northrop Aircraft echoed this sentiment, concluding in 1960 that, "[t]oo often, mere salary increases are meaningless to executives in the higher tax brackets. These executives may retain only 20 to 30 cents (or even less) of each dollar of their increase."[122] Likewise, the *Wall Street Journal* reported in 1969 when General Motors shareholders were debating a proposal to cap the CEO's pay that, "a wife of one top GM executive commented to a friend, 'They don't seem to understand that we give 90% of earnings back

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dividends, from 1971 to 1981. *See infra* text accompanying note 126. On median total executive compensation data presented as averages over five year periods, see Carola Frydman & Raven S. Molloy, *Does Tax Policy Affect Executive Compensation? Evidence from Postwar Tax Reforms*, 95 J. PUB. ECON. 1425, 1426 (2011).

120. Clarence E. Bonnett, Jr., *Compensation Planning for the Executive*, 9 TAX EXECUTIVE 26, 26 (1956).

121. DAVID R. ROBERTS, EXECUTIVE COMPENSATION 155 (1959).

122. J. Grant MacDonnell, *A Struggle to Reward Good Executives*, 2 CAL. MGMT. REV. 25, 25 (1960).

to the government.'"[123]

While high income tax rates plausibly could explain why executive pay was modest in the mid-20th century by present day standards, the only statistically rigorous analysis of the interrelationship between income tax and executive pay over an extended period of time indicates that tax policy was not pivotal. In a 2011 empirical study, Carola Frydman and Raven Saks Molloy examined the salaries, stock options, and post-retirement bonuses paid to a sample of top executives in large corporations between 1946 and 2005 and found there was a correlation in the time-series evidence between tax policy and the level of executive pay.[124] While this seemingly implies tax had a significant role, Frydman and Molloy failed to find any meaningful link between changes in tax rates and changes in pay levels over the short- and long-term.[125] It seems, then, that neither boards nor executives altered their approach to executive pay explicitly in response to the tax regime in place.

Even with Frydman and Molloy's time series evidence, the correlation between tax policy and executive pay did not hold at all times. At the beginning of the 1970s, the top rate of marginal income tax on earned income was reduced from 70% to 50% while income from other sources, such as interest and dividends, continued to be taxed at a top rate of 70% (Fig. 1).[126] Paul Samuelson, a well-known economist, described the change as "the greatest thing that ever happened to executives."[127] CEO compensation nevertheless increased only modestly in real terms in the decade following,[128] even if there are some indications an executive pay "regime change" began in the second half of the 1970s.[129]

Why didn't tax affect executive pay as much as has been theorized? One possibility was that with top marginal tax rates only kicking in at very high levels of pay, the tax "hit" was not substantial enough to mean senior executives were indifferent about their pre-tax pay. For instance, the highest tax bracket was only applicable to income over $200,000 between 1942 and 1947 and over $400,000—well over $3 million in today's money[130]—between 1948 and 1964.[131] A 1963 study by Leonard Burgess of the executive pay of the three highest-paid executives in each of the 25 largest manufacturing companies indicates that, as of 1958, these executives were paid on average $268,000 annually.[132] The top rate of income tax correspondingly was irrelevant for many top executives. Roberts affirmed the point in his 1959 study, conceding that it was widely thought that tax had impacted upon levels of executive pay but saying, "except in periods of emergency the rate has not been that high."[133]

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123. *About 19% of GM Holders Back Lid on Executive Pay*, WALL ST. J., May 26, 1969, at 5. This comment of course reflects a misunderstanding of marginal income tax rates.

124. Frydman & Molloy, *supra* note 119, 1426.

125. *Id.*

126. GRAEF S. CRYSTAL, FINANCIAL MOTIVATION FOR EXECUTIVES 185 (1970).

127. *Executive Compensation: Getting Richer in '73*, BUS. WK., May 4, 1974, at 58.

128. Frydman & Molloy, *supra* note 119, at 1427. This does not mean tax had no effect on compensation packages during this era. Instead, it may well have helped to change the mix of compensation, rather than the overall amount. *See* Anthony M. Vernava, *"Cash Now"—The Attractions of Current Compensation after the Tax Reform Act*, 17 WAYNE L. REV. 1055, 1059–60 (1971); *infra* note 146 and accompanying text.

129. *Supra* note 45 and accompanying text.

130. To be more precise, $3.6 million using 1955 as the base year. US INFLATION CALCULATOR, http://www.usinflationcalculator.com/ (calculated Aug. 29, 2015).

131. *Historical Individual*, *supra* note 119.

132. LEONARD RANDOLPH BURGESS, TOP EXECUTIVE PAY PACKAGE 114 (1963).

133. ROBERTS, *supra* note 121, at 155–56.

Other data Burgess compiled confirms that the after-tax income of top executives was far from negligible during the middle decades of the 20th century. He estimated using his 1958 data the percentage of the total pay package of the three highest paid executives that would have been paid as tax if progressive rates used for income applied to all forms of executive compensation. Even in this worst case scenario for executives, the potential tax "take" varied from just over 40% for top management of International Harvester, where the pay of the top three executives taken together was $317,000 before taxes and would have been $194,000 after, to just over 60% for the executives of Bethlehem Steel, with the equivalent figures for its top three executives being nearly $1.6 million and $655,000.[134] Hence, even though a top marginal tax rate of 91% might have reduced the incentive to fight for the last dollar, executives could still benefit materially from lucrative aggregate pay.

There were other reasons why tax policy might not have led to marked reductions in pre-tax compensation. A *Business Week* columnist observed in 1956 after noting that, in the magazine's most recent annual survey of executive pay, General Motors president Harlow Curtice had been paid the highest figure ever reported by the magazine ($776,000), "A figure like this prompts some people to raise the general question: Why do companies pay their top men so much; after all, they keep a relatively small amount of it after taxes."[135] One explanation the columnist offered was that pay increases for top executives made sense because what they were paid served as a benchmark for other executive salaries in the company, and too much "compression" at the top created problems with setting the pay of less senior executives faced with a less onerous tax situation, reasoning similar to that offered by some academics at the time.[136] Another possibility the columnist identified was that levels of pre-tax pay mattered because of "an emotional reaction"—a typical top executive had "the desire to be recognized for his ability or status in terms of pay figures."[137] Graef Crystal, writing in 1970 when he was a senior official at a firm specializing in providing executive compensation advice, concurred, saying, "most executives place primary emphasis on their pretax compensation and not their after-tax yield. To them, their pretax compensation represents a form of recognition."[138] Given this, even if the high income tax rates in place during the mid-20th century were prompting executives to leave some money on the table, their pride meant they were not about to leave all, or perhaps even most, of it.

Tax mitigation strategies may have also lessened the effects of high marginal tax rates. For instance, the *Business Week* columnist, in his 1956 analysis of why companies continued to pay senior management well despite "the big tax bite," said, "many companies

134. BURGESS, *supra* note 132, at 135, 159.

135. *Ideas Shift on Executive Pay*, BUS. WK., June 16, 1956, at 85 [hereinafter *Ideas Shift]*.

136. Notably, well-known economist Herbert Simon argued in 1956 that, in large-scale organizations, individuals at each managerial level would demand to be paid more than their immediate subordinates, "measured not in absolute terms but as a ratio," which he calculated as between 1.25 and 2. Herbert A. Simon, *The Compensation of Executives*, 20 SOCIOMETRY 32, 32–33 (1957). Given that entry-level salaries would be set by the market, Simon argued this pattern would foster high compensation for top executives at firms with multiple layers of management. *Id.* at 35.

137. *Ideas Shift*, *supra* note 135. A third factor identified, the market for managerial talent, will be discussed in Section V.B.5.

138. CRYSTAL, *supra* note 126, at 19.

[were] changing their ideas of how an executive might be paid."[139] The nature of the change was described by an adviser on compensation in 1954:

> It is no longer enough merely to increase the salary or bonus or to write a share of the profits into the executive's contract. High income tax rates leave him very little of any additional compensation . . . . These conditions result in a great deal of pressure being exerted on employers to work out new methods of compensating executives which will prove attractive tax-wise.[140]

An in-house lawyer at E. I. duPont de Nemours and Company echoed this sentiment, observing that, "[t]ax planners have devoted much time to devising a plan for compensating executives which will alleviate the effect of the high individual surtax."[141] Companies in the 1950s and 1960s indeed increasingly paid executives using tax-favored deferred compensation schemes,[142] such as tax advantaged "restricted" stock option plans provided for under the Revenue Act of 1950.[143] Restricted stock plans in turn became "the new rage" after stock option rules were tightened in 1964.[144] Fringe benefits not subject to tax in the same way as income were also used liberally, including life and health insurance, dining and country club memberships, recreational facility fees, interest-free loans, and the free use of personal residences, cars, and planes.[145]

Some observers suggested that with managerial compensation deployment of tax planning strategies largely cancelled out the effect of high marginal rates. According to a 1958 law review article on executive pay, "[t]he argument that the current high rate of

139. *Ideas Shift*, *supra* note 135.

140. William C. Childs, *Deferred-Compensation Plans for Executives*, 1954 INS. L.J. 25, 25 (1954).

141. Roy A. Wentz, *Remedying the Effect of Taxation on Management Ownership of Corporate Stock*, 48 NW. U. L. REV. 442, 443 (1953).

142. J.K. Lasser & V. Henry Rothschild, *Deferred Compensation for Executives*, HARV. BUS. REV., Jan.–Feb. 1955, at 91; Raymond A. Hoffman, *Executives' Compensation*, 3 LAB. L.J. 97, 101 (1952); GEORGE THOMAS WASHINGTON & V. HENRY ROTHSCHILD, COMPENSATING THE CORPORATE EXECUTIVE 168, 170 (2d ed., 1951) [hereafter WASHINGTON 1951]; Louis Eisenstein, *A Case of Deferred Compensation*, 4 TAX L. REV. 391, 416 (1949).

143. Revenue Act of 1950, Pub. L. 81-814, § 130A, 64 Stat. 906, 942 (1950). This provision reversed a decision of the Supreme Court from 1945 that was inhospitable to stock options and created a class of "restricted stock options" that one contemporary compensation consultant claimed "[gave] the stock option a new lease on life as an executive incentive": Arch Patton, *Incentive Compensation for Executives*, HARV. BUS. REV., Sept. 1951 at 35, 43. See also Frydman & Saks, *supra* note 11, at 2099, 2107. "Restricted stock options" were replaced with "qualified stock options" in the Revenue Act of 1964, which, among other things, required that, to qualify for favorable tax treatment, the options had to be awarded "at the money." Revenue Act of 1964, Pub. L. 88-272, § 221, 78 Stat. 63 (1964). Doubts were expressed as to whether the additional requirements in fact reduced markedly the attraction of stock options. *See* Charles L. B. Lowndes, *The Revenue Act of 1964: A Critical Analysis*, 1964 DUKE L.J. 667, 684–85.

144. Walter J. Blum, *Restricted Stock Arrangements Reconsidered*, 46 TAXES 598, 598 (1968); *see* also George W. Hettenhouse & Wilbur G. Lewellen, *The Taxation of Restricted Stock Compensation Plans*, 22 NAT'L TAX J. 368, 368 (1969); Ronald Hindin, *Internal Revenue Code Section 83 Restricted Stock Plans*, 59 CORNELL L. REV. 298, 300–02 (1974). The enactment of Section 83 in the Tax Reform Act of 1969 was designed to rein in some of the benefits of restricted stock plans. Hindin, *id.* at 303.

145. *See* William H. Hoffman, Jr., *Tax Influences in Shaping the Executive Pay Package*, 40 TAXES 386, 390 (1962) ; Henry W. Trimble, Jr., *Executive Compensation–Corporate Considerations*, 13 TAX EXEC. 7, 9 (Oct. 1960); Leslie Mills, *Recent Developments in the Taxation of Executive Compensation*, 34 TAXES 882, 883 (1956).

individual tax in the upper income brackets provides a built-in safeguard against managerial desire for increased compensation has little factual basis . . . . [T]axation does not limit total compensation; it merely changes the techniques of reward."[146] Tax planning, however, does not explain fully why tax failed to constrain executive pay to the extent that might have been anticipated. This is because most of the pay top executives received was in fact fully taxable.

Burgess, in his study of executive pay in the 25 largest companies in the United States as of 1958, reported on the tax-oriented executive pay "savings" for each of the 25 companies, this being the difference between the tax their three most highly paid executives would have paid if their compensation was taxed fully at the rates applicable to income and actual tax paid, adjusted for favorable tax treatment afforded to other types of compensation. Ford had the greatest savings with a differential of 26% between 35% of pre-tax aggregate compensation actually paid as tax and a possible tax "hit" of 61%.[147] With most of the 25 companies, however, the tax savings were 10% or less. This indicates that not only did top executives fail, as the wife of the senior GM executive suggested in 1969,[148] to hand over most of their compensation to the government, but that tax mitigation strategies played only a supporting role in protecting them from a damaging tax "hit." None of this is to claim that high marginal tax rates had no role in suppressing mid-century executive compensation nor that it is impossible in theory for tax to put substantial downward pressure on executive pay.[149] Nevertheless, mid-20th century income tax rates were not the "smoking gun" explanation for modest managerial compensation claimed by modern proponents of a tax-based solution to the problem of executive pay.

So we are left with a puzzle. If high tax rates do relatively little, on their own, to explain the stagnation of executive pay in the United States during the middle decades of the 20th century, then what does? We consider various possibilities next.

V. IF NOT TAX, THEN WHAT "WORKED?"

Having identified the middle decades of the 20th century as an era when executive pay was modest in comparison with the decades to follow and set aside tax as the decisive explanatory variable, we consider which other factors "worked" to compress executive pay. We will begin with variables that can be thought of as "internal" in the sense that they were intrinsic features of the public companies that were paying the executives. We then turn to potential "external" determinants of managerial remuneration.[150]

146. Robert B. Mautz & Gerald W. Rock, *The Wages of Management*, 11 U. FLA. L. REV. 474, 482 (1958).

147. BURGESS, *supra* note 132, at 160.

148. *Supra* note 123 and accompanying text.

149. It is possible, for instance, that this occurred in Britain with respect to cash salaries and bonuses in the decades following World War II. *See* CHEFFINS, *supra* note 62, at 704; Brian R. Cheffins & Steven A. Bank, *Corporate Ownership and Control in the UK: The Tax Dimension*, 70 MOD. L. REV. 778, 796 (2007).

150. On the distinction between "internal" and "external" factors influencing on management, see James P. Walsh & James K. Seward, *On the Efficiency of Internal and External Corporate Control Mechanisms*, 15 ACAD. MGMT. REV. 421, 422–24, 434–35, 445 (1990); Brian R. Cheffins, *Corporate Governance Since the Managerial Capitalism Era*, 89 BUS. HIST. REV. 717, 728–30 (2015).

A. Internal Variables

1. Boards of Directors

State corporate statutes vest the board of directors with the authority to manage the corporation, and it has long been understood that the setting of executive pay falls within the ambit of this grant of managerial power.[151] Hence, historically, boards of public companies have been formally responsible for fixing the compensation of the officers.[152] A correct but ultimately uninformative answer can correspondingly be provided to the question of why executive pay was "compressed" during the middle decades of the 20th century: boards of directors fixed managerial compensation that way. That begs the more challenging but more interesting question: why? Were boards structured in a manner that tilted them towards moderation in a manner that boards have not been more recently? As we will see now, the answer is no, which indicates that the manner in which boards were organized does not explain the executive pay moderation of the mid-20th century.

Given that boards of public companies are formally responsible for setting managerial compensation, critics of executive pay have not surprisingly identified the board as a prime culprit when diagnosing what has gone "wrong." Those espousing what has been referred to as the "managerial power" approach to executive pay assert that managerial compensation reached unjustified levels in recent decades largely because powerful executives benefitted from favors weak boards bestowed.[153] Critics who blame the board acknowledge that, even before Dodd–Frank required U.S. public companies to set up a compensation committee comprised of "independent" directors, most public companies had such committees in place.[154] The critics have argued, however, that due to CEOs exercising significant influence over the director nomination process and board dynamics that mean independent directors will be supportive of the management team absent a crisis ("support or fire"), compensation committees are counter-productively management friendly.[155]

Following the logic of those who blame boards for executive pay reaching unsatisfactory levels in recent decades, it would seem that boardroom procedures must have been more robust during the middle decades of the 20th century than they were in ensuing decades. As various critics of managerial power theory have argued, the situation in fact was quite different.[156] Boards, even if they did not function optimally as the 20th

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151. Linda J. Barris, *The Overcompensation Problem: A Collective Approach to Controlling Executive Pay*, 68 IND. L.J. 59, 74 (1992).

152. FRANKLIN G. MOORE, MANAGEMENT: ORGANIZATION AND PRACTICE 59 (1964); J.M. JURAN & J. KEITH LOUDEN, THE CORPORATE DIRECTOR 65–68 (1966); Lucian Arye Bebchuk et al., *Managerial Power and Rent Extraction in the Design of Executive Compensation*, 69 U. CHI. L. REV. 751, 765 (2002).

153. Bebchuk et al., *supra* note 152, at 754; BEBCHUK & FRIED, *supra* note 92, at 2; *see* Randall Thomas, *Explaining The International CEO Pay Gap: Board Capture or Market Driven*, 57 VAND. L. REV. 1171, 1174 (2004) (summarizing "board capture theory"). *Cf.* DORFF, *supra* note 5, at 116 ("[T]he existing evidence is a far cry from persuasive proof that managerial power is the primary cause of the inefficiencies Bebchuk and Fried catalog so aptly.").

154. Text accompanying *supra* note 104; Bebchuk et al., *supra* note 152, at 765.

155. Bebchuk et al., *supra* note 152, at 767–68; Charles M. Elson, *Executive Overcompensation—A Board-Based Solution*, 34 B.C. L. REV. 937, 974–80 (1993).

156. Thomas, *supra* note 153, at 1175; Marianne Bertrand, *CEOs*, 1 ANN. REV. ECON. 121, 134 (2009); Steven Kaplan, *Executive Compensation and Corporate Governance in the U.S.* 5 (Nat'l Bureau of Econ., Research Paper No. 18395, 2012), ssrn.com/abstract=2134208 (discussing and analyzing perceptions of CEO

century drew to a close, nevertheless were structured to operate more effectively as detached scrutineers of managerial behavior than had been the case previously. Of particular relevance in the present context, independent directors, who might have been expected to enhance the objectivity of the process by which executive pay was set, moved to the forefront just as managerial compensation began to escalate rapidly. Hence, "if managerial power is the principal explanatory variable for escalating pay, the timing is odd."[157]

A 2007 study by Jeffrey Gordon of the growing prominence of independent directors over time is instructive on trends concerning board structure. He says that, as of 1950, the consensus was "that boards should consist of the firm's senior officers, some outsiders with deep connections with the firm . . . and a few directors who were nominally independent but handpicked by the CEO."[158] Hence, while only 15% of directors in large public companies were executives of the same firm as 2005,[159] the equivalent figure was approximately half in industrial companies both in the mid-1930s and at the start of the 1950s.[160] Boards correspondingly were less well-positioned to deal with executive pay in a detached manner than they would be subsequently.

The proportion of directors who were executives of the same company was considerably smaller with railways and utility companies at mid-century than was the case in industrial companies.[161] Even with companies where executives were outnumbered on the board, however, boards seemingly were not well-positioned to engage in arm's-length negotiations over executive pay. A 1945 study of business leadership in large corporations indicated that boards of the time were "passive" and said that outside directors "function[ed], if at all, primarily as financial and business advisers."[162] According to a 1958 law review article on executive pay, boards were "frequently either inactive and mere formalities or they [we]re officer dominated."[163] A 1964 text on management organization suggested similarly that "most boards don't review the executives' stewardship very critically. Outside directors are only part-time men and are sometimes beholden to the president (chief executive officer) and hold their jobs at his sufferance."[164]

There was awareness during the mid-20th century that the manner in which boards were structured and functioned was problematic from an executive pay perspective. The 1958 law review article on executive pay that characterized boards as inactive or officer

compensation and corporate governance).

157. Jeffrey N. Gordon, *Executive Compensation: If There's a Problem What's the Remedy? The Case for "Compensation Discussion and Analysis"*, 30 J. CORP. L. 675, 683 (2005).

158. Jeffrey N. Gordon, *The Rise of Independent Directors in the United States, 1950–2005: Of Shareholder Value and Stock Market Prices*, 59 STAN. L. REV. 1465, 1468 (2007).

159. *Id.* at 1565.

160. *Id.* at 1565 (citing Lehn et al., *Determinants of the Size and Composition of US Boards: 1935–2000*, 38 FIN. MGMT. 747, 758 tbl. 1 (2009)). On the mid-1930s, see also ROBERT A. GORDON, BUSINESS LEADERSHIP IN THE LARGE CORPORATION 122 (1945) (indicating that, with 25 selected large industrial corporations, 191 of the 372 directors were officers).

161. GORDON, *supra* note 16060, at 123 (stating that with ten large utilities and railways as of 1935, officers held 35 of 154 directorships); MABEL NEWCOMER, THE BIG BUSINESS EXECUTIVE: THE FACTORS THAT MADE HIM 1900–1950 27 (1955) (indicating that as of 1952 executives were in the minority on the boards of all railway companies and nearly 90% of utilities).

162. GORDON, *supra* note 16060, at 144, 145.

163. Mautz & Rock, *supra* note 146, at 490.

164. MOORE, *supra* note 152, at 61.

dominated spelt out the implications: "Who controls the wages of management? It is accurate to say that it is usually management. There is the possibility of danger in such a situation . . . ."[165] An executive compensation expert noted similarly in a 1943 *Harvard Business Review* article: "in most companies executives have control over their own compensation; herein lie both temptation and opportunity to profit personally from compensation policies."[166] The authors of a 1975 study that found little relation between executive pay and standard measures of corporate performance thought it was relevant that "[f]riendly boards, usually chosen by the chief executive . . . make the compensation process a congenial give-and-take affair."[167]

During the decades immediately following World War II, delegation to board committees was emerging as a response to the potential conflict of interest that existed in the executive pay realm due to managerial influence in the boardroom. A 1955 empirical investigation of "big business" executives indicated that, when boards set up committees to deal with managerial salaries, it was customary for the committee to be staffed exclusively by outside directors.[168] By 1967, nearly three out of five larger public companies had established a compensation committee.[169] Due to the fact that it was "indelicate and improper for inside officer-directors to sit in judgment on their own salaries and incentive compensation," such committees "increasingly [were] . . . made up exclusively of outside directors who may make final decisions in this important area."[170] Doubts existed, however, about the objectivity and autonomy of these committees, in part because the recipients of the compensation usually had considerable influence over the composition of the committees.[171] Also, the compensation committees typically did not get "to upset established patterns. Big changes . . . [were] full board actions."[172]

With most large public companies having a compensation committee staffed by independent directors by 2000,[173] the procedure public companies were using to set executive pay therefore apparently was more objective and robust as the 20th century drew to a close than it was during the middle decades of the 20th century. Executive pay thus seemingly grew dramatically in tandem with better corporate governance. Ironically, if conjectures by Arch Patton, a highly influential McKinsey-based commentator on executive pay,[174] are correct, the changes that should have enhanced objectivity with respect to the setting of executive pay may have accelerated the growth of managerial compensation.

Patton, in a 1985 *Harvard Business Review* article, sought to explain why there had

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165. Mautz & Rock, *supra* note 146, at 500.

166. John C. Baker, *A "Just Gauge" for Executive Compensation*, HARV. BUS. REV. Autumn 1943, #1 at 75, 76,. Baker was the author of a 1938 book on executive pay. BAKER, *supra* note 23, at 261.

167. K.R. Srinivasa Murthy & Malcolm S. Salter, *Should CEO Pay be Linked to Results?*, HARV. BUS. REV. May–June 1975, at 66, 71.

168. NEWCOMER, *supra* note 161, at 127.

169. Marshall L. Small, *The Evolving Role of the Director in Corporate Governance*, 30 HASTINGS L.J. 1353, 1358 (1979) (citing data compiled by the Conference Board).

170. HAROLD KOONTZ, THE BOARD OF DIRECTORS AND EFFECTIVE MANAGEMENT 179, 180 (1967).

171. NEWCOMER, *supra* note 161, at 127; Erwin N. Griswold, *Are Stock Options Getting Out of Hand?*, HARV. BUS. REV., Nov.–Dec. 1960, at 47, 55; EDWARD MCSWEENEY, MANAGING THE MANAGERS 89–91 (1978).

172. MOORE, *supra* note 152, at 592.

173. *Supra* text accompanying note 104.

174. Stephen F. O'Byrne & Mark Gressle, *How "Competitive Pay" Undermines Pay for Performance (and What Companies Can Do to Avoid That)*, 25 J. APPLIED CORP. FIN. 2, 26–27 (2013).

been "an explosion in top management compensation"[175] over the previous decade and identified changes in the boardroom as one cause. During the middle decades of the 20th century, it was common for chief executives, having spent lengthy stints in their company's managerial ranks before taking over the top job, to step down a few years later but then remain on the board for a few more years thereafter.[176] Patton likely was mindful of the continuity this arrangement fostered when he said that, "not long ago" board members "spent the company's money carefully," citing specifically chief executives who would, upon retirement, become chairman of the board.[177] According to Patton, as it became more common for directors of public companies to be independent from management, these directors, who were often chief executives of other companies, had considerably less direct contact with employees and customers than their executive director counterparts from previous decades.[178] Boards correspondingly became increasingly "executive-protective" rather than "company protective." Executive pay, Patton reasoned, increased accordingly.

Data from the early 1950s and early 1980s indicating that boards with substantial executive representation were less generous than outsider-dominated boards lends credence to Patton's conjectures.[179] Other empirical research on the impact of board composition on executive pay yielded mixed results.[180] Correspondingly, it remains an open question whether ostensible improvements to boardroom governance counter-intuitively prompted increases in executive pay in the manner Patton conjectured. Regardless, it is clear that explaining the executive pay arrangements in place during the middle decades of the 20th century requires investigating variables other than the manner in which boards were structured.

2. Shareholders

Policymakers have recently shown considerable faith in shareholders as a check on runaway executive pay, as evidenced by the introduction of "say-on-pay" votes in the 2010 Dodd–Frank Act.[181] It is open to question whether shareholders are ever likely to use powers available to them to reform executive pay in the way critics who argue that executives are paid "too much" hope or expect.[182] Regardless, shareholders were pretty much entirely peripheral to the moderation in executive compensation occurring between the 1940s and the 1970s. While shareholders had (and have) a variety of legal tools at their disposal that could be used to influence compensation decisions, shareholder challenges to

175. Arch Patton, *Those Million-Dollar-a-Year Executives*, HARV. BUS. REV., Jan.–Feb. 1985, at 56.

176. ROY C. SMITH & INGO WALTER, GOVERNING THE MODERN CORPORATION: CAPITAL MARKETS, CORPORATE CONTROL, AND ECONOMIC PERFORMANCE 102 (2006); Myles L. Mace, *Should the Retiring CEO Stay on the Board*, HARV. BUS. REV., May–June 1978, at 16.

177. Patton, *supra* note 175, at 60.

178. *Id.*

179. NEWCOMER, *supra* note 161, at 128 (using 1952 data); John E. Core et al., *Corporate Governance, Chief Executive Officer Compensation, and Firm Performance*, 51 J. FIN. ECON. 371, 386–88 (1999) (using data from 1982–84).

180. *See* Core et al., *supra* note 179, at 373 ("[T]he empirical evidence to date is mixed . . . ."); Vagts, *supra* note 44, at 251 (summarizing the empirical evidence); Frydman & Saks, *supra* note 11, at 2129 (finding, based on the insider/outsider proportion on boards as of 1936, 1950, 1970, and 1990, that board structure did not have a measurable effect on executive pay).

181. *Supra* text accompanying note 98.

182. *See* Bank & Georgiev, *supra* note 96, at 22 (highlighting "shareholders' limited interest in challenging executive compensation").

executive pay were uncommon and usually unsuccessful.

Though a "say-on-pay" vote was decades in the future, shareholders acting collectively theoretically could have substantially influenced the setting of executive pay during the middle of the 20th century. The powers available to them, however, turned out to be of little practical importance. One way that shareholders potentially could have dictated the approach companies took to executive pay was by selecting directors who would implement desired policies when exercising control over the setting of managerial compensation. During the middle decades of the 20th century, however, boards themselves controlled the director nomination process and usually put forward a slate listing as many individuals as there were open seats on the board, whom shareholders would then duly elect.[183] The only time shareholders were given a real choice with director selection was during a proxy fight, which frequently involved an attempted takeover of the corporation. Proxy contests for board control in public companies were not particularly common, however, with the number attracting press coverage averaging just over 13 per year between 1945 and 1965.[184]

Board elections aside, shareholders were given in some instances a veto over particular aspects of executive pay. Though it was thought to be good practice for companies to seek shareholder approval when they introduced new executive compensation bonus and stock option plans, particularly if there was a shadow of self-dealing, this was never required in any general way.[185] On the other hand, some states, including New York, mandated shareholder approval in circumstances where a corporation was establishing a plan involving the issuance of stock to employees, including executive stock option plans.[186] Shareholder approval would also typically become necessary under state corporate law if implementing a stock option plan required a corporation to increase its share capital or if existing shareholders were vested with pre-emptive rights.[187] The New York Stock Exchange additionally required all listed companies to seek shareholder approval of issuances of stock options to senior executives.[188] Despite all this, it was virtually unknown for shareholders to use their powers to block proposed changes to managerial compensation.[189]

It is not surprising that shareholders, acting together, failed to curb executive pay

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183. J.A. LIVINGSTON, THE AMERICAN STOCKHOLDER 43–46 (1958).

184. Derived from data generated for John Armour & Brian Cheffins, *Stock Market Prices and the Market for Corporate Control*, 2016 U. ILL. L. REV. 761, 783, fig.3.

185. *See* 2 GEORGE THOMAS WASHINGTON & V. HENRY ROTHSCHILD, COMPENSATING THE CORPORATE EXECUTIVE 27 (1962) [hereinafter WASHINGTON 1962] ("[M]anagement will, as a matter of good practice today, and even though not required by law or regulation, submit a plan for its own compensation to stockholders for their approval."); *id.* at 228 ("Not only may submission to stockholders help clear up questions of the directors' power: it may also be helpful in resolving doubts as to the manner of the exercise of that power.").

186. *Id.* at 251–54, n.223 (citing NY STOCK CORP. LAW § 14 (1951)). The Model Business Corporation Act had an optional provision requiring shareholder approval. *Id.*

187. Anthony M. Vernava, *Stock Options: Corporate, Regulatory and Related Tax Aspects*, 30 U. PITT. L. REV. 197, 229–30 (1968).

188. WASHINGTON 1962, *supra* note 185, at 824.

189. In the leading work on the law on executive compensation, no case was discussed where shareholders voted to reject a stock option plan. See *id.* at 223–28, 252–54; *see also* Note, *Shareholder Attack Against Stock Options For Corporate Executives*, 62 YALE L.J. 84, 90 (1952) (saying in the context of potential shareholder opposition to stock options "ratification is often an empty formality"). For an instance where shareholders did defeat a management-sponsored stock option plan, see Robert Metz, *Criticism Voiced on Stock Options*, N.Y. TIMES, Apr. 28, 1963, at 147 (discussing General Baking Co.).

during the middle decades of the 20th century. The retail investors who collectively owned most of the shares in public companies during this era lacked both the appetite and aptitude to intervene in corporate affairs.[190] The fact that institutional investors, which held at this time only a small percentage of corporate equities despite an emerging trend in favor of institutional ownership,[191] would not actively oppose proposals management put forward at shareholder meetings helped to give companies full freedom in setting executive compensation.[192] The upshot, as the AFL–CIO said in a 1959 report critical of stock options, was that "management is in the driver's seat. With its control over proxies it is able to do pretty much as it pleases."[193]

Given that it was unlikely that shareholders would exercise power collectively to influence executive pay, shareholder influence was restricted to individual investors prepared either to agitate publicly for change or to litigate to challenge particular features of managerial compensation. During the middle decades of the 20th century, shareholder agitation was the province of the "gadflies," self-appointed spokespersons for stockholders who lobbied for shareholder rights, with the most visible being Lewis and John Gilbert and Wilma Soss.[194] Executive compensation was one of the gadflies' perennial targets. Lewis Gilbert, for example, used shareholder proposals, speeches, and media interviews to denounce executive salaries (he thought many too high) and to call for reform of stock option plans (he wanted longer holding periods before options could be exercised) and pension schemes (he wanted annual pensions capped at $25,000).[195]

The media found something appealing in the gadflies' quest to force managers to listen to shareholders,[196] which meant that the gadflies could garner considerable publicity. However, because few shareholders were prepared to offer active support, the gadflies did not wield real power.[197] This was as much the case with executive pay as with other issues. Graef Crystal, writing in 1970, said that, while "some companies rationalize their failure to pay meaningful incentive awards by citing the specter of adverse stockholder reaction," most shareholders "were unlikely to begrudge a company's $5 million in bonus funds, if the funds are paid only when they receive $25 million in additional earnings."[198] Given such attitudes, the gadflies' shareholder proposals relating to executive pay not only never passed, but were usually overwhelmingly rejected in shareholder votes.[199]

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190. Brian R. Cheffins, *Introduction*, *in* THE HISTORY OF MODERN U.S. CORPORATE GOVERNANCE ix, xix (Brian R. Cheffins ed., 2011).

191. In 1950, mutual funds and private and public retirement funds held 4% of corporate equities; in 1970, less than 15%. JAMES P. HAWLEY & ANDREW T. WILLIAMS, THE RISE OF FIDUCIARY CAPITALISM 53 (2000).

192. J.A. Livingston, *Investors Could Curb Executive Excesses*, WASH. POST, Apr. 11, 1958, at C24.

193. Industrial Union Department, AFL–CIO Research Section, *The Stock Option Scandal*, unpublished, Aug. 1959.

194. Harwell Wells, *A Long View of Shareholder Power: From the Antebellum Corporation to the Twenty-First Century*, 67 FLA. L. REV. 1033, 1079–81 (2015).

195. LIVINGSTON, *supra* note 183, at 88–89; LEWIS D. & JOHN J. GILBERT, NINETEENTH ANNUAL REPORT OF STOCKHOLDER ACTIVITIES AT CORPORATE MEETINGS DURING 1958 122 (1959).

196. *See, e.g.*, Andy Logan, *Hoboken Must Go!*, NEW YORKER, Mar. 17, 1951, at 34; John Bainbridge, *The Talking Stockholder—I*, NEW YORKER, Dec. 11, 1948, at 40.

197. *See* John E. Balkcom, *Executive Compensation: A History of Imbalance in Public Controls, Shareholder Interests and Executive Rewards*, DIRECTORS & BOARDS, Spring 1977, 4, 7 (suggesting that a roundly rejected 1938 Gilbert proposal that the highly paid CEO of Bethlehem Steel be demoted to a less lucrative post may nevertheless have prompted the company to pay that CEO less).

198. CRYSTAL, *supra* note 126, at 32.

199. Metz, *supra* note 189 (stating in an article on executive pay that Lewis Gilbert's "resolutions are usually

On the litigation front, lawsuits have been launched with some regularity over time by shareholders who believe executives have been overpaid.[200] The trend was the same during the middle decades of the 20th century, but it is unlikely that litigation was any more effective as a check on executive pay than was agitation by gadflies. In the early 1930s, in *Rogers v. Hill*,[201] a shareholder successfully challenged "excessive" compensation paid through a bonus plan at American Tobacco, briefly igniting hope that courts would seriously scrutinize executive pay packages and strike down those that were "excessive." Over the rest of the decade, though, such hopes dwindled as courts declared themselves incompetent to decide what was a "fair" amount of compensation and consistently rejected shareholder suits challenging big pay packages as a "waste" of corporate assets.[202] After 1945, shareholder suits solely challenging the amount of compensation public companies paid to executives were, absent evidence of procedural irregularities or self-dealing, almost always thrown out of court.[203]

A fresh avenue for shareholder suits opened up with the growing popularity of stock options.[204] Following changes in 1950 to tax law that were favorable to stock options,[205] a wave of lawsuits challenged the stock option schemes companies had begun adopting, with many resting on claims that executives gave inadequate consideration in exchange for the options.[206] Litigants had some success in the early 1950s in Delaware's normally pro-management courts.[207] However, subsequent shareholder lawsuits targeting stock option grants almost always failed.[208] The consideration question was easily solved by advance legal planning,[209] and courts turned out to be no more willing to police stock option grants on the basis of unreasonableness than they were willing to second-guess other compensation decisions.[210] Delaware also amended its corporate legislation in 1953 to make a board's determination as to consideration offered for stock options conclusive "absent fraud."[211] Litigation over other forms of compensation was fairly rare during the

roundly defeated"); *Bosses' Pay: Executive Salary Lags in Economic Race, but 'Fringes' Ease Pain*, WALL ST. J., Feb. 24 1955, at 1 ("[T]he failure of most Gilbert pay-curbing efforts suggest their views are not widely shared by stockholders."). An exception was in 1969 when 19% of shareholder votes were cast in favor of a Gilbert proposal to put a $350,000 ceiling on the pay of any GM executive. *About 19%*, *supra* note 123.

200. *See* Randall S. Thomas & Harwell Wells, *Executive Compensation in the Courts: Board Capture, Optimal Contracting, and Officers' Fiduciary Duties*, 95 MINN. L. REV. 846, 865–80 (2011) (outlining the history of these lawsuits).

201. Rogers v. Hill, 289 U.S. 582 (1933).

202. Wells, *supra* note 19, at 711–16, 732–37.

203. Thomas & Wells, *supra* note 200, at 868–73. Some challenges were successful when it was argued a bonus had been swelled by improper accounting that overstated earnings, but adoption of standardized accounting measures ended this line of attack. WASHINGTON 1962, *supra* note 185, at 920.

204. Vagts, *supra* note 44, at 262–64.

205. *See supra* text accompanying note 143.

206. *See* WASHINGTON 1962, *supra* note 185, at 573–74, n.21 (setting out the major companies involved in litigation over their options plans).

207. Gottlieb v. Heyden Chem. Corp., 90 A.2d 660, 666 (Del. 1952); Kerbs v. Cal. E. Airways Inc., 90 A.2d 652, 659 (Del. 1952).

208. *See* Vagts, *supra* note 44, at 263 ("These cases thus had no particular impact on the generosity with which boards of directors rewarded their employees.").

209. *See* Note, *supra* note 189, at 87–88.

210. WASHINGTON 1962, *supra* note 185, at 572–74, 906–09.

211. *Id.* at 578–79.

rest of the 1950s.[212] There was an uptick in shareholder litigation involving executive pay in public companies as the 1960s began, but most such lawsuits again failed.[213]

As we will see,[214] norms relevant to public companies likely had a meaningful role in compressing executive pay during the middle decades of the 20th century. It is possible that, despite a lack of tangible evidence that shareholders had a marked impact on executive pay, concern about shareholder agitation helped to reinforce these norms and thereby dissuaded firms from adopting outsize compensation schemes. For instance, Washington and Rothschild, in the 1951 edition of a manual on executive pay, acknowledged shareholder lawsuits and the attendant publicity could have some effect: "[l]itigation or the possibility of litigation . . . have probably brought down compensation levels, or at least kept compensation levels lower than they might otherwise have been."[215] Overall, though, it would appear that shareholder intervention did relatively little to slow the growth of executive compensation during the middle decades of the 20th century.

B. External Variables

We have just seen that, during the middle decades of the 20th century, the manner in which boards were structured prompted concerns that the setting of executive pay was "a congenial give-and-take affair"[216] and that shareholders were at best bit players with managerial compensation. Nevertheless, the data set out in Part II shows there was no wanton executive pay free-for-all. This was known at the time. As economist John Kenneth Galbraith acknowledged in 1971, "[m]anagement does not go out ruthlessly to reward itself – a sound management is expected to exercise restraint."[217] Correspondingly, he said, "[t]here are few corporations in which it would be suggested that executive salaries are at a maximum."[218]

Why did management not reward itself ruthlessly during the mid-20th century? Our analysis in Part IV indicated that tax played at best a subsidiary role. We will now consider various additional "external" variables that may have operated as constraints and correspondingly explain executive pay during this era. We will begin with direct regulation of pay and then consider disclosure regulation, union power, the market for managerial talent, and corporate "culture" in the form of "norms." We will see that, while each played a role, the final three do the most to account for executive pay being modest by present day standards during the mid-20th century.

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212. *Id.* at 915. There was at least one high profile compensation suit in the late 1950s, Nadler v. Bethlehem Steel Corp., 154 A.2d 146 (Del. Ch. 1959) (dealing with a special bonus plan linked to corporate dividends); discussed in *Bethlehem Steel Stock Option, Change in Pay for Executives Voted*, WALL ST. J., Sept. 18, 1957, at 32.

213. Harlan Byrne, *Companies in Court: Stockholders File More Suits, Sparking Debate Among Lawyers*, WALL ST. J., Apr. 27, 1961, at 1. *Cf.* Daniel J. Dykstra, *The Revival of the Derivative Suit*, 116 U. PA. L. REV. 74, 77–78 (1967) (indicating that with a random sample of recent derivative suits there were "many instances" where excessive salaries were challenged but it is likely most of these lawsuits involved closely held companies).

214. *Infra* Section V.B.5.

215. WASHINGTON 1962, *supra* note 185, at 921. They also cautioned that "so many forces are at work—such as varying corporate profits or varying stock market prices—that it is unsafe to generalize." *Id.*

216. *Supra* note 167 and accompanying text.

217. JOHN KENNETH GALBRAITH, THE NEW INDUSTRIAL STATE 115 (2d ed., 1971).

218. *Id.* at 115–16.

1. Direct Regulation

Statutory measures that give government officials scope to stipulate how much companies can pay executives—"direct regulation"—theoretically can address the configuration of managerial compensation in a more forthright manner than any other variable.[219] On the other hand, this sort of intervention has been characterized as "the last available cure for excessive paychecks" because "the government [c]ould be quickly drawn into an intricate process generating intense political pressure and threatening to produce arbitrary, rigid results."[220] In 1942, President Franklin Roosevelt relied on a broadly phrased wartime mandate for price stabilization to impose an upper limit of $25,000 annually on executives' after-tax salaries, but Congress quickly overrode the measure.[221] Otherwise, to the extent that direct regulation has shaped executive pay in American public companies, this has occurred through regulatory schemes affecting the economy generally.[222] Laws of this sort would have had an impact on managerial compensation at particular points in time. Direct regulation, however, does relatively little to explain why executive pay was suppressed in general terms from the 1940s to the 1970s.

Economy-wide regulation impacting executive pay was initially implemented during World War II as part of sweeping controls aimed at holding down wartime inflation. There was a salary freeze applicable to all companies from 1942 until late 1946 overseen by a complex bureaucracy which evaluated requests for salary adjustments.[223] The regulations froze not only salaries but also bonuses and, in some cases, stock option plans, but they did not cover deferred compensation, pension plans, and health and life insurance, each apparently exempted as unlikely catalysts for inflation.[224] Frydman and Malloy, in a careful econometric study, reported that the controls may have held down executive compensation during the years they were in place while affording average workers' wages some scope to grow.[225] Frydman and Malloy also found, however, that the effects of the salary controls were short-lived, meaning they did not explain a decline in executive pay that occurred during the remainder of the 1940s.[226]

During the Korean War, limits were again placed on executive salaries as part of a regulatory regime targeting wartime inflation. This time a separate Salary Stabilization Board was established in recognition of the "peculiar nature of many forms of compensation paid to the executive, administrative and professional employees."[227] This episode of direct regulation had little impact on levels of executive pay because the Board did not get to work until late 1951 and was within a year largely moribund because the

219. Cheffins & Thomas, *supra* note 88, at 262.

220. BOK, *supra* note 8, at 116–17.

221. WASHINGTON 1951, *supra* note 142, at 299–300; Mark Leff, *The Politics of Sacrifice on the American Home Front in World War II*, 77 J. AM. HIST. 1296, 1299 (1991).

222. There have also been instances where executive pay has been regulated directly in a particular industry. For instance, during the middle decades of the 20th century state utility regulators sought to impose limits on executive pay by refusing to grant rate increases when companies had made managerial compensation payments thought to be "excessive" or by "excluding excessive salaries from the rate base." WASHINGTON 1962, *supra* note 185, at 791.

223. WASHINGTON 1951, *supra* note 142, at 300–5.

224. *Id.* at 305–7.

225. Frydman & Malloy, *supra* note 11, at 232.

226. *Id.* at 225–30.

227. Rudolf Sobernheim, *Salary Stabilization Under Defense Mobilization*, 13 FED. BAR J. 117, 134 (1952).

inflationary conditions that had been expected did not materialize.[228]

The final period in which the Federal government significantly regulated executive pay on an economy-wide level was during the early 1970s. From 1971 to 1974, wage and price controls were imposed to attempt to contain growing inflationary pressures.[229] Under this regime, following an initial 90-day freeze on compensation increases, the Federal government's Wage Board limited increases in executive pay to 5.5% annually. It is doubtful whether the controls had a marked impact on top management pay, given that 1972 and 1973 surveys of executive compensation by *Business Week* indicated CEO pay, on average, increased by more than the 5.5% limit.[230] One reason may be that the restrictions were initially imposed on a corporation's executives as a group, thereby leaving scope for companies to increase CEO pay while curtailing that of lower-ranking executives.[231] Also, the wage and price control scheme may have done more to alter the composition of pay than reduce pay overall. The adoption of new incentive plans was permitted so long as they were "directly related to increased productivity" and, not surprisingly, "scores of companies introduced performance-based bonus plans linked to accounting data or revenues."[232]

2. Disclosure Regulation

Mandatory disclosure of executive pay constitutes a less intrusive form of government intervention than direct regulation because whatever impact the law might have does not arise from the fact of disclosure itself. Instead, it is the reactions disclosure elicits—the shareholders it potentially angers, the politicians it may push to impose new laws, and the journalists it prompts to disseminate the data to a receptive public. Disclosure thus might facilitate the curbing of managerial compensation, but it is alone not sufficient to achieve this objective.

Mandatory disclosure of executive pay at public companies has been in place in the United States since federal securities law was introduced in the mid-1930s. Though investor protection is typically cited as the rationale underlying the enactment of federal securities law, the primary motive underlying the introduction of executive pay disclosure requirements in the Securities Act of 1933 and the Securities Exchange Act of 1934 was to respond to inflammatory revelations concerning managerial compensation and more broadly to "shame" executives discredited by the Depression into limiting their compensation.[233] The 1934 Act was the more consequential, requiring corporations traded on national stock exchanges to reveal annually, in registration documents to be filed with the SEC and made available to the public, remuneration paid to directors and officers, including "bonus and profit-sharing arrangements."[234] Form 10-K, issued to implement this requirement, required corporations to report the compensation received by the three

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228. Murphy, *supra* note 25, at 259.

229. *Id.* at 259–60; ALLEN J. MATUSOW, NIXON'S ECONOMY: BOOMS, BUSTS, DOLLARS, AND VOTES 62–67, 109–16, 228–34 (1998).

230. Murphy, *supra* note 25, at 260.

231. *Id.* This loophole was circumscribed in 1973.

232. *Id.*

233. *Supra* text accompanying note 25.

234. 15 U.S.C. § 78l(b)(1)(F), Securities Exchange Act of 1934 § 12(b).

highest-paid "officers, directors, [or] employees" of the firm.[235]

Disclosure regulation would become more demanding over time. We have already seen that major reforms were carried out in 1992,[236] but this was preceded by various other changes that made the disclosure requirements more rigorous. For instance, mindful that it was advisable (though not mandatory) for companies to seek shareholder approval for executive bonus schemes and stock option plans,[237] the SEC required in 1938 that proxy statements corporations sent to shareholders disclose full details of any compensation plan for which shareholder approval was sought.[238] Four years later, the SEC further amended the proxy rules to require that compensation arrangements that were reported in proxy solicitation documentation sent to shareholders be set out in a tabular form for each director and each officer paid more than $20,000 a year.[239]

In 1952 the SEC amended the proxy reporting rules to oblige companies to divulge, again in tabular form, compensation for each director as well as for the "top 3" executives receiving more than $25,000 annually and to respond to a widening of the range of the types of compensation companies were awarding by stipulating that executive pay taking the form of deferred remuneration, including pension and retirement plans, had to be divulged separately.[240] Also, shareholders who were asked to approve a bonus, profit sharing, or stock option plan had to be furnished with data about both the plan and the benefits to be awarded to each director or "top 3" officer.[241] In 1978, companies were required to factor in payoffs from long-term incentive schemes in a way that had not occurred previously. In particular, disclosures formerly made in nearly incomprehensible tables at the back of corporate proxy statements had henceforth to be dealt with in a clearer fashion near the front of the disclosure documentation.[242]

There are no empirical studies that have isolated the impact of disclosure on the level of executive pay.[243] Even documenting its effects anecdotally is difficult.[244] One potential stumbling block is that, as Lucian Bebchuk and Jesse Fried have observed, companies can seek to avoid public criticism of executive pay through a process of "camouflage" where much of the compensation awarded to executives is channelled into forms where disclosure can be obscured or avoided altogether.[245]

The camouflage pattern was evident almost as soon as disclosure of executive pay

235. *See* BAKER, *supra* note 23, at 258 (reprinting original Form 10-K).

236. *Supra* text accompanying note 79.

237. *Supra* text accompanying note 185.

238. Securities Exchange Act of 1934, Release No. 34-1823 (Aug. 11, 1938).

239. Securities & Exchange Commission Release Notice, Release No. 3347, 1942 WL 34864 (Dec. 18, 1942).

240. *Id.*

241. Securities Exchange Act of 1934, Release No. 4775 (Dec. 11, 1952).

242. Kevin J. Murphy, *Top Executives are Worth Every Nickel They Get*, 64 HARV. BUS. REV. (Mar. 1986), https://hbr.org/1986/03/top-executives-are-worth-every-nickel-they-get. Information on options was included in the proxy statements, but consisted primarily of details from which the reader had to carry out a computational process to determine what an executive had earned. BURGESS, *supra* note 132, at 198. In 1983 the SEC moved to a more narrative (and less informative) approach to executive compensation disclosure, but returned in 1992 to the requirements for formatted tables as well as requiring that additional information be divulged. *Supra* text accompanying note 79.

243. Suárez, *supra* note 25, at 90.

244. Jensen & Murphy, *supra* note 49, at 145; George T. Washington, *The Corporation Executive's Living Wage*, 54 HARV. L. REV. 733, 766 (1941).

245. BEBCHUK & FRIED, *supra* note 92, at 67–70.

was required. In the late 1930s, firms that awarded executive compensation in the form of deferred compensation plans, pensions, stock bonuses, and stock options would often disclose background information by way of a footnote rather than take such compensation into account in tabular data and justify doing so on the basis that such compensation could not be reliably valued.[246] Boards also began to "look for supplemental methods of compensating their corporate executives" that would not be subject to compulsory disclosure.[247]

A 1986 article by executive pay expert Kevin Murphy indicates how gaps in disclosure requirements can make it difficult to ascertain accurately the impact of disclosure on executive pay.[248] Murphy relied on executive pay data compiled by *Forbes* to illustrate key compensation trends and reported substantial increases in CEO pay in the late 1970s and early 1980s. The "compressed" executive pay regime in place in public companies from 1940 through to the 1970s likely was ending during this period.[249] Murphy, however, said the large increases he found could be explained in great measure on the basis that the 1978 changes to SEC rules meant that stock options and other forms of long-term incentive-oriented compensation were being factored in a way that had not been the case previously.[250]

Another problem that complicates assessment of the impact of mandatory disclosure on executive pay levels that is particularly relevant for present purposes is that disclosure's effects may vary over time. As we have already seen, it is widely thought that the bolstering of disclosure requirements by the SEC in 1992 amid concerns over rising levels of executive pay had the unintended consequence of fostering higher executive pay.[251] Executive pay expert Graef Crystal, who was a consultant to the SEC chairman at the time this reform occurred, observed ruefully in the mid-2000s, "I absolutely thought it would cause comp to go down because the disclosures would be so embarrassing. But it turned out that when somebody is hauling in $200 million, he's not embarrassable."[252]

Crystal's assumption about the likely impact of increased disclosure on executive pay, though ultimately erroneous, was understandable. This is because disclosure's impact on executive pay levels may well have been different in the early 1990s than it would have in earlier decades. In particular, while disclosure reform may have caused executive pay to increase in the early 1990s, during the middle decades of the 20th century, disclosure may have put downward pressure on executive pay because corporate boards, mindful of possible negative publicity, refrained from awarding executives compensation likely to attract attention and criticism.

There is anecdotal evidence indicating that disclosure did serve as a moderating influence on executive pay during the middle decades of the 20th century. George Thomas Washington, a law professor who co-authored a leading executive pay manual, said in 1941 of the mandatory disclosure regime introduced by federal securities law in the mid-1930s, "the publicity given to compensation in recent years had largely removed the unhealthy

246. GEORGE T. WASHINGTON, CORPORATE EXECUTIVES' COMPENSATION, 233–34, n.35 (1942).
247. WASHINGTON 1962, *supra* note 185, at 9.
248. Murphy, *supra* note 242.
249. *Supra* notes 43–45 and accompanying text.
250. Murphy, *supra* note 242.
251. *Supra* note 86 and related discussion.
252. Nocera, *supra* note 86 (quoting Crystal).

atmosphere of the boom days."[253] After World War II, he indicated in his executive pay manual that the disclosure requirements administered by the SEC "expose[] management's proposals to public view and criticism and, like other disclosure requirements . . . serve[] as a restraint."[254] Jensen and Murphy, in their 1990 *Harvard Business Review* article advocating supercharging executive pay with performance-oriented compensation, explained why companies had been paying executives like "bureaucrats" partly on the basis that compensation committees mindful of executive pay disclosure had been seeking to forestall criticism of "what the boss makes" by capping what their CEOs earned.[255]

Particularly telling is the complete absence of pay packages exceeding $1 million a year—the kind of pay packages that triggered outcries in the 1930s—from the 1940s to the late 1970s.[256] For many years, "the one million dollar line . . . seemed . . . to serve as a psychological barrier to advances."[257] For instance, *Business Week* observed in its 1974 survey of executive salaries, "[m]ore executives edged closer to the magic $1 million mark in 1973," including Paul Hofmann of Johnson & Johnson, who earned $978,000.[258] Still, while inflation averaged over 8% annually between 1974 and 1976,[259] no executive joined the $1 million club until 1977,[260] likely because of concerns about negative publicity fostered by disclosures made to the SEC.

If disclosure regulation may have put downward pressure on executive pay during the middle decades of the 20th century, why would the impact of disclosure vary over time?[261] The most likely answer is that mentioned above: disclosure does not work by itself. Its impact instead depends on who is using the information divulged and how. Jensen and Murphy said in 1990 of the effect that disclosure had on managerial labor contracts "[t]hird parties play an important role in the contracting process, and strong political forces operate inside and outside companies to shape executive pay."[262] As we will see in the following sub-sections, during the middle decades of the 20th century, unions were influential and social norms militated against extremely high pay. In this environment, disclosure likely put downward pressure on managerial compensation because union officials could find out readily what top executives were paid, and because those setting managerial compensation knew that the results of their decisions would be in the public domain and could prompt criticism. When union power faded and social norms evolved, disclosure's effects changed and changed in a way that meant regulation could prompt *increases* in executive pay. We

253. WASHINGTON 1962, *supra* note 185, at 766.

254. *Id.* at 27.

255. Jensen & Murphy, *supra* note 49.

256. *Supra* note 34 and accompanying text.

257. Vagts, *supra* note 44, at 232.

258. *Executive Compensation*, *supra* note 127.

259. *Historical Inflation Rates: 1914–2016*, http://www.usinflationcalculator.com/inflation/historical-inflation-rates/ (last visited Oct. 22, 2016) (averaging 11.0% in 1974, 9.1% in 1975, and 5.8% in 1976).

260. *Supra* note 34 and accompanying text.

261. *But see* Suárez, *supra* note 25, at 90 (arguing that disclosure regulation has always driven pay upwards, saying that executive pay rose steadily from the early 1950s to the 1970s, when the increases began to accelerate rapidly). While it is true that executive pay did increase in nominal terms from the 1950s through the 1970s, the fact that it remained essentially unchanged after inflation and was outpaced by wage increases awarded to rank-and-file employees meant there was restraint of a sort that disappeared completely by the 1980s. S*upra* notes 32–33 and accompanying text. The evidence presented here indicates that disclosure regulation contributed to that outcome.

262. Jensen & Murphy, *supra* note 49.

consider next in more detail the impact of unions on managerial compensation.

3. Unions

There has been speculation in the academic literature that downward pressure unions put on executive pay helps to explain the flatness of executive pay during the mid-20th century.[263] Given the weakness of unions in the private sector presently—union membership in the United States in the private sector is under seven percent[264]—this conjecture seems scarcely plausible. During the middle decades of the 20th century, however, matters were much different.

Between the mid-1930s and the mid-1940s, union power grew substantially, bolstered by the enactment of federal legislation that facilitated efforts by workers to organize.[265] Union membership among non-agricultural workers had risen to 35% in 1954 and strikes were considerably more frequent than they would be as the 20th century drew to a close.[266] Correspondingly, mid-20th century executives had to be mindful of maintaining the goodwill of organized labor in a way their counterparts in later decades did not. This was potentially relevant for executive pay. Companies entering labor negotiations probably would have preferred to avoid giving unions a significant bargaining chip by increasing executive compensation substantially.[267] Union officials also likely would have been opposed as a matter of ideological principle to senior executives getting rich due to the hard work of modestly paid union members.[268]

There is anecdotal evidence indicating that, during the middle decades of the 20th century, union power influenced the setting of executive pay. Washington and Rothschild drew attention in the 1951 edition of their executive pay manual to the fact that it could be seen as "provocative of labor problems" for a chief executive to be paid $500,000 a year when the workers at the same company received $2000 per annum and said, "[t]he board of directors of today, before approving [executive pay], may well consider the effect upon the company's next collective bargaining negotiation."[269] A study of the impact of taxation on business behavior published the same year suggested "[t]he probable effect on labor relations and union demands is undoubtedly a factor in any consideration of executive compensation" and quoted a senior executive as saying "[i]t is important not to let the

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263. Suárez, *supra* note 25, at 97 (calling this idea "a promising area of research"); Xavier Gabaix & Augustin Landier, *Why Has CEO Pay Increased So Much?*, 123 Q.J. ECON. 49, 75–76 (2008); Thomas Piketty & Emmanuel Saez, *The Evolution of Top Incomes: A Historical and International Perspective*, 96 AMER. ECON. REV. 200, 203 (2006) (citing unions in seeking to explain "the nonrecovery of top capital incomes during the post-1945 period").

264. *See Union Membership and Coverage Database from the CPS*, CURRENT POPULATION SURVEY, http://unionstats.gsu.edu (last visited Oct. 22, 2016) (providing data under "U.S. Historical Tables," tables for "Private Sector" and "Private Nonagricultural," each reporting 6.7% union membership in 2015).

265. WYATT WELLS, AMERICAN CAPITALISM, 1945–2000: CONTINUITY AND CHANGE FROM MASS PRODUCTION TO THE INFORMATION SOCIETY 18 (2003).

266. Steven Greenhouse, *Strikes at 50-Year Low*, N.Y. TIMES (Jan. 29, 1996), http://www.nytimes.com/1996/01/29/us/strikes-at-50-year-low.html?pagewanted=all.

267. BOK, *supra* note 8, at 105 ("Lavish executive earnings have already complicated union negotiations in more than one corporation.").

268. This was not always the case. *See, e.g.*, Thomas C. Hayes, *The "Front-End" Bonus Lure*, N.Y. TIMES, July 7, 1980, at D1 (quoting an AFL-CIO spokesman as saying, "[w]e don't give a hoot about executive pay levels as long as workers get their fair share").

269. WASHINGTON 1951, *supra* note 142, at 9, 16.

executives get so much that they steam up the labor boys."[270] Similarly, a specialist in executive compensation suggested in 1970 that "cutting executive pay" could "be a good tactic if a company is preparing for union negotiations."[271]

A 2012 study by Frydman and Malloy of executive pay in the 1940s substantiates the theory that union power influenced executive pay patterns during the middle decades of the 20th century.[272] They found a statistically significant negative correlation between executive compensation and unionization that meant that, while managerial pay was slightly higher in unionized firms at the beginning of the 1940s, it was markedly lower in such firms by the end of the decade and remained so at least up to 1955. A study focusing on data from the 1970s involving larger employers similarly found a negative association between unionization and CEO pay.[273]

Just as the rise of union power likely was a constraint on executive pay during the middle decades of the 20th century, the subsequent marginalization of unions may well have contributed to the subsequent trend in favor of higher managerial compensation. Executive pay, as Part II described, began to increase in earnest in the second half of the 1970s before gaining additional momentum in the 1980s. Similarly, union influence began to decline markedly in the 1970s due to companies deploying robust union avoidance strategies, and the process accelerated in the Reagan era as federally prompted deregulation of labor law weakened unions.[274] By 1985, the percentage of employees who were union members was merely half of the 1954 figure (Fig. 2). Hence, while union officials denounced the substantial increases in executive pay occurring in the 1980s,[275] their views seemingly were doing little to impose checks on those setting managerial compensation.

270. THOMAS H. SANDERS, EFFECTS OF TAXATION ON EXECUTIVES 100 (1951).

271. Michael C. Jensen, *Growing Trend: Paychecks Shrink*, N.Y. TIMES, Nov. 1, 1970, at 139.

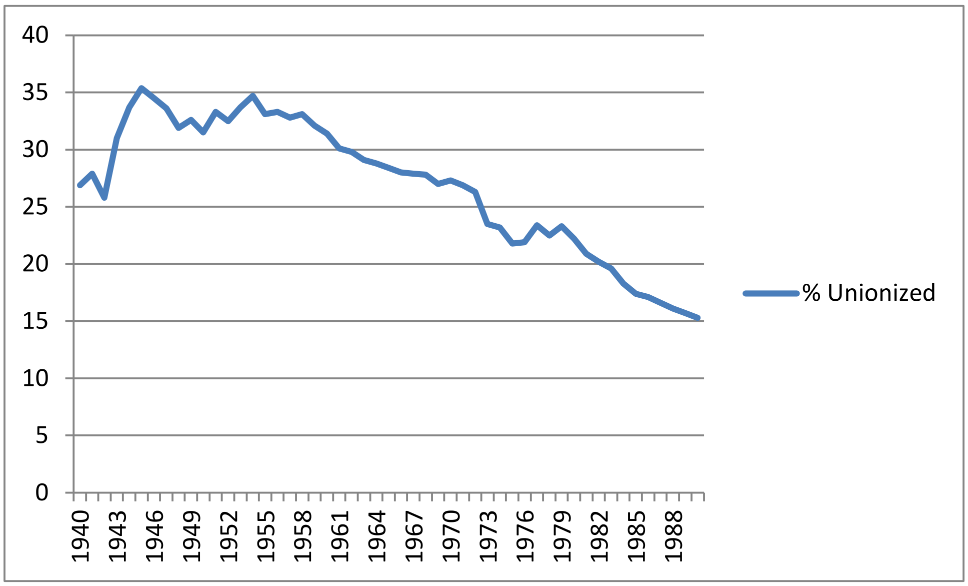
272. Frydman & Molloy, *supra* note 11, at 241–42, 244–45, 247.

273. *See* John DiNardo et al., *Unions and Managerial Pay* 22–23 (Nat'l Bureau of Econ. Research, Working Paper No. 6318, 1997).

274. MICHAEL GOLDFIELD, THE DECLINE OF ORGANIZED LABOR IN THE UNITED STATES 3, 5–7, 19–21, 53 (1987) (indicating, though, that longer term trends were also highly relevant); BENNETT HARRISON & BARRY BLUESTONE, THE GREAT U-TURN: CORPORATE RESTRUCTURING AND THE POLARIZING OF AMERICA 49–50, 100–03 (1988).

275. *See, e.g.*, John Holusha, *Executive Bonuses Draw Union's Fire*, N.Y. TIMES (May 4, 1984), http://www.nytimes.com/1984/05/04/us/executive-bonuses-draw-union-s-fire.html (discussing union opposition to bonuses paid to automobile executives); John Holusha, *Union Angered by Pay of Top Chrysler Executives*, N.Y. TIMES (Apr. 20, 1988), http://www.nytimes.com/1988/04/20/us/union-angered-by-pay-of-top-chrysler-executives.html.

Figure 2: Union Membership—Non-agricultural Workers[276]



Although union pressure may have helped to flatten executive pay during the middle decades of the 20th century, it is doubtful organized labor played the decisive role. Only once, in 1945, did union membership among private sector workers exceed the 35% level achieved in 1954.[277] The fact that, even at the peak of labor power, only a minority of the workforce was unionized inevitably would have diluted whatever impact unions had on executive pay. The preferences of organized labor can have a spill-over effect to non-unionized workplaces because the threat of unionization can prompt non-unionized employers to grant pre-emptive concessions to staff and because unions publicly espouse social solidarity and advocate redistributive governmental policies.[278] It is impossible to gauge the magnitude of this spill-over effect. Still, with union membership peaking at barely more than one-third of the workforce, even if unions discouraged increases in executive pay during the mid-20th century, they would only have been one of a variety of factors doing so.

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276. GERALD MAYER, UNION MEMBERSHIP TRENDS IN THE UNITED STATES 22–23 (2004).

277. GOLDFIELD, *supra* note 274, at 10 (providing annual statistics, 1930–1978).

278. Bruce Western & Jake Rosenfeld, *Unions, Norms, and the Rise in U.S. Wage Inequality*, 76 AMER. SOC. REV. 513, 517–19 (2011).

4. The Market for Managerial Talent

If companies are competing intensely in the market for managerial talent to retain or recruit senior executives, this should bolster the bargaining power of these executives and drive up managerial compensation. Correspondingly, developments affecting this market potentially explain why executive pay was flat during the middle decades of the 20th century. While the term "market for managerial talent" has been in use at least since the 1950s,[279] this market apparently operated at a significantly lower level of intensity during the 1940s, 1950s, and 1960s than it did at the end of the 20th century. This in turn likely helps to explain historical trends concerning managerial compensation.

Systematic empirical research on the market for managerial talent was lacking up to the end of the 1970s.[280] Nevertheless, the available evidence indicates that the market was listless, at least compared to more recent times. During the middle decades of the 20th century, companies would search quite intensely for managerial talent at entry level.[281] At the very top of the managerial hierarchy, in contrast, "the average company [had] but scant recourse to the outside market for top officials."[282] Most top executives in large corporations were "company men" who joined their corporate employers during their 20s and then continued to work with the firm for at least a couple of decades before taking up their senior managerial posts.[283]

Recruiting executives from other companies was by no means unknown in the mid-20th century. However, "mobile manager" bosses were usually only hired from a company operating in the same industry and were brought in because a company was in serious trouble or because a vacuum at the top had arisen due to a failure to grapple successfully with executive succession issues.[284] Hence, a 1996 study of the American corporation as an employer during the 1950s and 1960s maintained, "[m]anagers . . . were generally treated by corporations as fixed assets who would enjoy long-term security and careers as long as they conformed to the expectations of the prevailing corporate culture that respected hierarchy and conformity."[285] Likewise, a 2006 analysis of governance of the modern corporation said of large firms during the mid-20th century, "[t]op jobs, including that of CEO, were usually awarded to those from within the company, often as a result of orderly succession planning."[286]

The 1970s was something of a transitional decade for the market for managerial talent

279. *See, e.g.*, HERRYMON MAURER, GREAT ENTERPRISE: GROWTH AND BEHAVIOR OF THE BIG CORPORATION 100 (1955) (suggesting that such a market existed in steel, textile, and auto industries).

280. Dan Schneiderman, *The Supply of and Demand for Executives*, *in* CHIEF EXECUTIVE OFFICER COMPENSATION 42, 72 (Harold L. Wattel ed., 1978).

281. Peter Cappelli, *The Rise and Decline of Managerial Development*, 19 INDUS. CORP. CHANGE 509, 520, 533–39 (2010).

282. ROBERTS, *supra* note 121, at 148.

283. MAURER, *supra* note 279, at 96–97; BURGESS, *supra* note 132, at 180–81; *From the Bottom Up*, FORBES, Nov. 15, 1957, at 35.

284. NEWCOMER, *supra* note 161, at 133; BURGESS, *supra* note 132, at 181; *When the Boss is a "Foreigner"*, BUS. WK., Nov. 8, 1958, at 107; *The Mobile Managers*, FORBES, Nov. 15, 1957, at 49.

285. Thomas A. Kochan, *The American Corporation as an Employer: Past, Present, and Future Possibilities*, *in* THE AMERICAN CORPORATION TODAY 242, 244 (Carl Kaysen ed., 1996).

286. SMITH & WALTER, *supra* note 176, at 101; *see also* RAKESH KHURANA, SEARCHING FOR A CORPORATE SAVIOR: THE IRRATIONAL QUEST FOR CHARISMATIC CEOS, 61–64, 162 (2002); Peter Cappelli & Monika Hamori, *The New Road to the Top*, HARV. BUS. REV. (Jan. 2005), https://hbr.org/2005/01/the-new-road-to-the-top.

in the same way it was for executive pay. It has been said, "[f]rom the 1950s through the 1970s, American executives looked a lot alike,"[287] and in the 1970s, "CEOs were usually 'company men,' promoted from within"[288] with "the vast majority of CEO openings [being] filled by incumbents rather than outside hires."[289] Nevertheless, at the CEO level, the market for managerial talent was evolving in various ways that were potentially significant for executive pay.[290] For instance, companies began looking for new chief executives more often, with turnover doubling between 1960 and 1980.[291] Moreover, forced exits became more prevalent. The annual firing rate for CEOs doubled from five to ten percent per annum between 1976 and 1981, prompting the *New York Times* to publish a story entitled *Why Big Business is Firing the Boss*.[292]

Companies also became increasingly willing in the 1970s to shop externally for top managerial talent, particularly as the decade was drawing to a close. According to a 1986 book on "headhunters" (executive search firms), "[t]he greatest growth of the business occurred in the 1970s" due partly to the fact that the "[c]orporate appetite for outside management talent rose as the traditional promotion-from-within notion of advancement grew fusty and executives viewed ship-jumping mobility as a career strategy."[293] The 1981 *New York Times* article that discussed accelerating CEO turnover said top management had "come to accept this rising transience in executive life."[294] A *Chicago Tribune* article from the same year indicated that companies were explaining and defending the rapid growth of the club of executives being paid more than $1 million per year on the basis they had to pay the going rate to attract and keep competent executives.[295]

The most prominent illustration of changing attitudes was Chrysler's 1978 recruitment of Lee Iaccoca. Reportedly, "[t]he Chrysler board was desperate to get someone as experienced as Iacocca, and agreed to whatever he demanded."[296] Iacocca was paid a then-largely unprecedented "front-end bonus" of $1.5 million before turning up for work, a practice that Revlon began in 1974 when it paid the same amount to recruit as CEO

287. Cappelli & Hamori, *supra* note 286, at 25.

288. Robert J. Samuelson, *The New Economic Warriors*, WASH. POST (Apr. 13, 2005), http://www.washingtonpost.com/wp-dyn/content/article/2005/04/12/AR2005041201446.html.

289. Murphy, *supra* note 25, at 267; *see also* PATRICIA BONFIELD, U.S. BUSINESS LEADERS: A STUDY OF OPINIONS AND CHARACTERISTICS 28–29, 31 (1980) (discussing data from a 1978 questionnaire sent to the CEOs of large companies indicating that, in terms of age, length of time working for the company and number of companies worked for the profile of chief executives was little different in the 1970s than it had been in the 1950s or 1960s).

290. Cappelli & Hamori, *supra* note 286 ("There were hints throughout the 1970s that things were changing.").

291. *See* William Ocasio, *Political Dynamics and the Circulation of Power: CEO Succession in U.S. Industrial Corporations, 1960–1990*, 39 ADMIN. SCI. Q. 285 (1994); *see also* Michael Useem, *Corporate Restructuring and the Restructured World of Senior Management*, *in* BROKEN LADDERS: MANAGERIAL CAREERS IN THE NEW ECONOMY 23, 31 (Paul Osterman ed., 1996).

292. Douglas Bauer, *Why Big Business is Firing the Boss*, N.Y. TIMES (Mar. 8, 1981), http://www.nytimes.com/1981/03/08/magazine/why-big-business-is-firing-the-boss.html?pagewanted=all.

293. JOHN BYRNE, THE HEADHUNTERS 21 (1986); *see also* Todd Fandell, *Recruiting Executives is Big Business*, CHI. TRIB., Oct. 14, 1979, at Q3 (indicating that the number of executives hired each year with the assistance of executive search firms had increased from 4,000 in the late 1960s to 16,000).

294. Bauer, *supra* note 292.

295. Thompson, *supra* note 34.

296. SMITH & WALTER, *supra* note 176, at 105.

an International Telephone & Telegraph executive.[297]

The trend in favor of a more robust interaction between supply and demand in the market for managerial talent that began in the 1970s continued in the 1980s. The *Wall Street Journal*, in a 1988 article that sought to explain why CEOs were "the richest hired hands in history" despite a stock market crash in 1987, cited the views of a "market forces camp" that contended "[p]eople at the chief-executive level are in short supply" and indicated "[m]any companies say they must pay their chief executives handsomely lest others lure them away."[298] Chief executive turnover also continued to accelerate. As of the mid-1990s, a CEO appointed after 1985 was three times more likely to be fired for a similar level of performance than one appointed before that date.[299] Moreover, U.S. public companies were casting the net wider to find an executive who was the right fit. A CEO appointed in 1990 was half again more likely to have been hired from outside the company than in 1970.[300]

The 1980s market for managerial talent was not a model of theoretical perfection. In 1985, Michael Jensen was arguing that senior executives of public companies were underpaid, resulting in a brain drain at some major companies as talented individuals opted for fields such as investment banking, real estate, and high-tech startups.[301] He and Kevin Murphy, in the 1990 *Harvard Business Review* article where they urged public companies to stop paying chief executives like bureaucrats, asserted "[t]he CEO position is not a very risky job."[302] Law professor Carl Bogus also contended in 1993, "[t]he CEO labor market is highly restricted . . . . Most CEOs are promoted from below, and it surely is not necessary to offer a vice president a gargantuan sum to persuade him to accept the top job."[303] Nevertheless, it does seem that the market for managerial talent was operating with greater intensity during the 1980s than in previous decades, which might help to explain why executive pay increased substantially during that decade.

While changes to the market for managerial talent in the 1970s and 1980s seemingly help to explain the executive pay "regime change" occurring then, this leaves open an important question: why did the market for managerial talent intensify? The most likely explanation is that perceptions of the contribution top executives could make to corporate success evolved. In particular, those responsible for appointing senior management and setting executive compensation increasingly believed that managerial talent was a scarce commodity for which paying premium prices in the form of higher executive pay was necessary and worthwhile.

In the 1950s and 1960s, there was a general consensus that, while executive talent was important, corporate success was not contingent upon a corporation having a dynamic

297. Hayes, *supra* note 268. Iacocca received $1 million in 1979 and $500,000 in 1980. *Stocks Sweeten Pay at the Top*, BUS. WK., May 12, 1980, at 56.

298. Amanda Bennett, *Top Dollar*, WALL ST. J., Mar. 28, 1988, at 1.

299. *Thank You and Goodbye*, ECONOMIST, Oct. 30, 1999, at 91 (citing a study by Rakesh Khurana examining 1300 instances where CEOs of *Fortune* 500 companies left their jobs).

300. *Are CEOs Worth Their Salaries?*, WASH. POST, Oct. 2, 2002, at E1 (citing data compiled by economists Robert Frank and Philip Cook).

301. William J. Powell, *Could it be That Corporate Leaders are Underpaid?*, BUS. WK., May 6, 1985, at 87.

302. Jensen & Murphy, *supra* note 49.

303. Carl T. Bogus, *Excessive Executive Compensation and the Failure of Corporate Democracy*, 41 BUFF. L. REV. 1, 29 (1993).

leader at the helm. In the mid-1950s, supposedly chief executives "of many companies . . . like[d] to remark jocularly that they are the most expendable men in their organizations."[304] A 1966 essay in the *New York Times* on corporate America said of "the typical corporation head," "[t]he power he exercises is less discretionary than we would like to believe and the range of decisions that can be called uniquely his own is severely limited."[305] A 1969 study of corporate executives said that top management usually "gets the job done . . . by mastering the 'science of muddling through'" and attributed "[t]he relative indifference of the stock market" to the death or replacement of chief executives to shrewd investors deducing "changes at the top have little if any effect on the prospective earnings and growth of the company."[306] These conjectures were substantiated by a "groundbreaking"[307] 1972 empirical study of 167 major public companies which indicated that, once the strength of the economy, the industry in which a corporation was operating, and various company-specific features were taken into account, executive "leadership" did very little to explain corporate performance.[308]

Things seemed to be different in the 1980s. Rakesh Khurana, in a 2002 study of "charismatic CEOs" who had come to replace "the professional Organization Man who toiled in anonymity," said "the advent of this new breed of corporate leader" could be traced back to Iacocca's 1979 appointment.[309] The *New York Times* picked up on the trend in a 1985 article entitled *A New Breed of CEO*, saying that, while "until fairly recently the most obvious trait of the CEO was his relentless dullness," Iacocca and various other leading chief executives eschewed "the old ways of managing and have brought new excitement to rusty companies."[310] Boards, in turn, apparently re-evaluated assumptions about the impact top executives could have on corporate performance and became prepared to adjust pay upward to get and keep the right person in charge.[311] The stock market also was becoming sensitive to circumstances surrounding departures from office by CEOs, with share prices typically rising when a CEO left due to poor performance.[312]

So long as perceptions of the contribution executives were making to corporate success were changing, even if managers did not "matter" more in reality, the shift in attitudes should have sufficed to jump start the market for managerial talent in a way that would have driven executive pay upward.[313] Nevertheless, there is empirical support for

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304. MAURER, *supra* note 279, at 81.

305. Andrew Hacker, *A Country Called Corporate America*, N.Y. TIMES: SUNDAY MAGAZINE, July 3, 1966, at 9, 24.

306. DAVID FINN, THE CORPORATE OLIGARCH 14–15, 18 (1969).

307. Harris Collingwood, *Do CEOs Matter?*, ATLANTIC, (June 2009), http://www.theatlantic.com/magazine/archive/2009/06/do-ceos-matter/307437.

308. Stanley Lieberson & James F. O'Connor, *Leadership and Organizational Performance: A Study of Large Corporations*, 37 AM. SOC. REV. 117, 117 (1972).

309. KHURANA, *supra* note 286, at 71.

310. N.R. Kleinfield, *What it Takes: The Life of a C.E.O.*, N.Y. TIMES, Dec. 1, 1985, Sunday Magazine, 76.

311. David Leonhardt, *For the Boss, Happy Days Are Still Here*, N.Y. TIMES (Apr. 1, 2001), http://www.nytimes.com/2001/04/01/business/executive-pay-a-special-report-for-the-boss-happy-days-are-still-here.html?pagewanted=all.

312. Stewart D. Friedman & Harbir Singh, *CEO Succession and Stockholder Reaction: The Influence of Organizational Context and Event Content*, 32 ACAD. MGMT. J. 718, 740 (1989).

313. DORFF, *supra* note 5, at 80–81 (drawing attention to the possibility that the beliefs of directors setting executive pay could have prompted an increase in executive pay even if the market for managerial talent did not change dramatically in fact).

the proposition that chief executives were having a greater impact on corporate performance in the 1980s and 1990s than they were in the 1950s and 1960s. Timothy Quigley and Donald Hambrick, following in the footsteps of the "seminal" 1972 study of the "CEO effect," provide a unique historical perspective in a 2015 study where they filter out the strength of the economy, the nature of the industry corporations operated in, and specific features of the firms in question to isolate the impact of CEOs between 1950 and 2009.[314] They report that the CEO effect, which accounted for just under 10% of corporate performance in the 1950s and 1960s, hovered in the 10% to 12% range from 1970 until the mid-1980s before increasing to the 15% to 17% range as the 1990s drew to a close.[315]

Taken together, then, there is quite strong evidence in favor of the proposition that the operation of the market for managerial talent accounted at least partly for the flatness of executive pay between 1940 and the mid-1970s and fostered the subsequent dramatic increases in managerial compensation. One point we have left open is *why* top management might have mattered more over time. For present purposes, it suffices to say that there were various reasons why those who set executive pay might have plausibly believed that the executive function had become more important, and more important in a way that justified higher compensation. John Kotter, a Harvard Business School academic, offered in 1990 a helpful summary of factors that likely played a role:

> [A]fter twenty-five to thirty years of relatively easy growth . . . the business world became more competitive, more volatile, and tougher. A combination of faster technological change, greater international competition, market deregulation, overcapacity in capital-intensive industries, an unstable oil cartel, raiders with junk bonds, and a demographically changing workforce all contributed to this shift.[316]

In sum, changing perceptions of the importance of corporate executives likely helped to foster from the late 1970s onwards a more robust market for managerial talent that in turn contributed to the dramatic rise in executive pay that began then. One additional explanatory variable, however, needs to be taken into account to round out our survey of explanations for what "worked" during the middle decades of the 20th century, namely evolving norms within public companies relevant to the setting of executive pay. We consider norms next.

5. Norms

Norms—social rules not dependent upon on the government for promulgation or enforcement[317]—constitute a popular explanation for why executive pay held steady

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314. Timothy J. Quigley & Donald C. Hambrick, *Has the "CEO Effect" Increased in Recent Decades? A New Explanation for the Great Rise in America's Attention to Corporate Leaders*, 36 STRAT. MGMT. J. 821, 822 (2015).

315. *Id.* at 826–27.

316. JOHN P. KOTTER, A FORCE FOR CHANGE: HOW LEADERSHIP DIFFERS FROM MANAGEMENT 12 (1990). Quigley and Hambrick speculate on various causes of the increased CEO effect they document. Quigley & Hambrick, *supra* note 314, at 828. For a similar analysis, see Kevin J. Murphy & Ján Zábojník, *Managerial Capital and the Market for CEOs*, 25, 28–32 (Apr. 2007), http://ssrn.com/abstract=984376.

317. This definition is derived from Richard A. Posner & Eric B. Rasmusen, *Creating and Enforcing Norms, With Special Reference to Sanctions*, 19 INT'L. REV. L. & ECON. 369, 369 (1999).

during the mid-20th century.[318] For instance, noted economist Paul Krugman wrote in his 2002 *New York Times* essay on equality that some economists believed the New Deal "imposed norms of relative equality in pay that persisted for more than 30 years . . . [that] began to unravel in the 1970's and have done so at an accelerating pace" and cited executive compensation as "Exhibit A for this view."[319] Frydman and Malloy have acknowledged in their empirical research on the historical development of executive pay that evolving norms impacting managerial compensation may explain why they found that changes to income tax only explained in a limited way managerial compensation trends from the 1940s onwards.[320] Economists Xavier Gabaix and Augustin Landier, who in a widely cited 2008 article attributed a six-fold inflation adjusted increase in executive pay between 1980 and 2003 to a similarly sized increase in the market capitalization of the companies executives were running, said that social norms might well explain why the same pattern did not hold when executive pay was "flat" from the mid-1930s to the 1970s while firms were growing substantially.[321] Piketty, having suggested in a co-authored 2006 article that norms may well have helped to keep "executive pay below market" during the mid-20th century,[322] said in *Capital in the Twenty-First Century* that his tax analysis provided "the best explanation of the observed facts" but acknowledged that "social norms concerning executive pay directly influence the levels of compensation."[323]

While various observers have invoked norms to explain historical executive pay trends, the norms that were relevant during the middle of the 20th century have gone largely unspecified. Krugman's 2002 essay provides, however, a helpful departure point: "[I]t's a matter of corporate culture. For a generation after World War II, fear of outrage kept executive salaries in check. Now the outrage is gone . . . a relaxation of old strictures . . . . By the end of the 1990's, the executive motto might as well have been 'If it feels good, do it.'"[324] "Outrage" is a term Lucian Bebchuk and Jesse Fried, well-known critics of current executive pay arrangements in U.S. public companies, have used to make the point that the ability of executives to use their power to extract "rents" by way of overly generous managerial compensation is "not unlimited."[325] Instead, "the need for board approval, and social sanctions . . . do place some constraints on compensation arrangements."[326]

Bebchuk and Fried, writing in 2004, acknowledged that norms could help to predict the evolution of compensation but stressed that managerial power explained more effectively "executive-friendly compensation practices that [had] developed and quickly spread during the last decade or two."[327] Their reasoning implies that managerial power was greater in the 1980s and 1990s than it was beforehand—if it was not, the "executive-friendly compensation practices" presumably would not have grown in importance. Given

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318. Suárez, *supra* note 25, at 74.

319. Krugman, *supra* note 9.

320. Frydman & Saks, *supra* note 11, at 2131–32; Frydman & Malloy, *supra* note 11, at 1435–36.

321. Gabaix & Landier, *supra* note 263, at 76. This concession did not preclude critiques of their research citing the chronology issue. *See, e.g.*, Bertrand, *supra* note 156, at 137; Frydman & Saks, *supra* note 11, at 2129–30.

322. Piketty & Saez, *supra* note 162, at 204.

323. PIKETTY, *supra* note 13, at 512.

324. Krugman, *supra* note 9.

325. BEBCHUK & FRIED, *supra* note 92, at 64.

326. *Id.*

327. *Id.* at 76.

that the proportion of independent directors on boards was higher during these decades than it was previously,[328] it is unclear why there would have been any such trend. Perhaps, instead, changes affecting norms in the boardroom, and corporate culture more broadly, opened the way for the more lucrative executive pay arrangements of which Bebchuk and Fried are critical. There is evidence suggesting that might well have been the case.

A perusal of contemporary sources indicates that norms in U.S. public companies, which in turn likely were shaped by society-wide values, probably did constrain executive pay during the middle of the 20th century. Washington and Rothschild, in the 1951 edition of their manual on executive compensation, said, "the executive will damage his own cause if he insists on being given the ultimate dollar to which he believes himself entitled."[329] A 1955 study of 50 leading U.S. corporations indicated "moneygrubbing of substantial proportions is no longer possible for corporate managers" and suggested that "maximizing the emoluments . . . of money-minded managers" would put a company "in danger of outraging the public, including its own employees and customers . . . ."[330] *Business Week* observed in 1960 that executives of public companies were eager not to be "pilloried as greedy, grasping, and domineering" and wanted to be "the man everyone likes."[331]

As the 1960s drew to a close, a new generation of managerial talent was moving to the forefront that was less patient with "the rituals of the system" than the executives who had inculcated a "team first" ethos during the crisis conditions of the Depression and World War II.[332] Specifically, with managerial compensation there were "some stirrings of unrest" among key businessmen who felt their pay should be increased at a faster pace.[333] The basic norm structure, however, did not change materially. As we have seen, economist John Kenneth Galbraith said in 1971 that executives were not paid as much as they might have been because of management's self-restraint.[334] Graef Crystal said similarly in 1970 that "compensation practices of too many companies in the United States bear an uncomfortable resemblance to those of Eastern Europe. At these companies everyone 'gets a little something.'"[335]

By the mid-1980s, matters had changed considerably. "Superstars" who could dominate the activities in which they engaged and cash in accordingly were growing in importance throughout the economy,[336] and attitudes in public companies were adjusting accordingly. Edward Herman, a business school professor, was quoted in a 1984 newspaper article on executive pay as saying that, while "huge salaries" were thought to be "slightly dubious," "they're obviously not dubious enough so they're not done," with at least part of the explanation being "the free market is back . . . . This is the age of laissez-faire."[337]

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328. *Supra* text accompanying notes 159–60.

329. WASHINGTON 1951, *supra* note 142, at 17.

330. MAURER, *supra* note 279, at 14, 91.

331. *Broadside at U.S. Management*, BUS. WK., Feb. 20, 1960, at 129 (citing views expressed by Cameron Hawley, an author of best-selling business novels, noting that there was considerable agreement with what he was saying).

332. Arch Patton, *Motivating Tomorrow's Executives*, MCKINSEY Q., Mar. 1968, at 20, 21.

333. Everett Groseclose, *Giving the Boss a Raise*, WALL ST. J., Nov. 14, 1969, at 40.

334. *Supra* note 217 and accompanying text.

335. CRYSTAL, *supra* note 126, at 33.

336. Sherwin Rosen, *The Economics of Superstars*, 71 AM. ECON. REV. 845, 845 (1981); *see also* PHILIP J. COOK & ROBERT H. FRANK, THE WINNER-TAKE-ALL SOCIETY 67–72 (1995) (discussing executive compensation and the expansion of "winner-take-all" markets).

337. Michael Blumstein, *Executives Being Challenged on Salaries and Self-Interest*, N.Y. TIMES (May 8,

James Tobin, a distinguished economist, likewise cited in a 1984 interview a political shift rightward to explain why "[t]he undiluted pursuit of personal gain is more accelerated in our society" in a way that affected how businessmen thought about what they were doing.[338] A *New York Times* article published the same year entitled *The Age of 'Me-First' Management* that focused on concerns that top executives were "losing sight of moral standards in the new frenzy to get rich" cited upheaval for executives caused by an unprecedented wave of hostile takeovers as a key reason "why some of the traditional constraints on corporate behavior appear to be unravelling."[339] The impact norms have on CEO pay depends on their substantive content rather than their mere existence.[340] Correspondingly, it seems likely that changing views concerning the propriety of getting rich help to explain the executive pay "regime change" occurring as the 20th century drew to a close.

Evolving norms may well have fostered the growth of executive pay in another way. Given that executives, for various reasons, will prefer not to have their pay linked closely to the performance of the companies they manage, if those setting managerial compensation begin to prioritize a pay/performance link, this will tend to drive upward aggregate executive pay.[341] In the middle of the 20th century, there certainly was awareness that, with executives rarely owning more than a tiny number of shares in the companies they managed, a failure to tie pay to performance could result in them being primarily "devoted to conserving present assets and 'living out their terms.'"[342] Nevertheless, tying pay to performance was not a top priority. According to a 1955 study of top management in 50 large U.S. corporations, pride in the corporation and a job well done, not incentive-based pay, were the strongest motivating forces for senior executives.[343] Crystal said in 1970 it would only be "the gutty company" that would de-emphasize executive salaries in favor of increased bonus opportunities even though top management would have the potential to receive higher total compensation.[344] Reputedly, as of 1975, for the "average CEO," "the best way to get ahead was to 'grow the company' through diversifying acquisitions. Most of the money CEOs made came in the form of salary, and the bigger your company, the bigger your salary."[345]

Matters were changing at least to some degree in the 1980s as a small but growing number of companies adopted compensation plans that incorporated performance measures assumed to be much more closely allied to the creation of shareholder value than the standard measure of earnings per share.[346] By the early 1990s, the idea that executive pay should be tied closely to shareholder outcomes was quickly becoming received wisdom

1984), http://www.nytimes.com/1984/05/08/business/executives-being-challenged-on-salaries-and-self-interest.html?pagewanted=all.

338. Ann Crittenden, *The Age of 'Me-First' Management*, N.Y. TIMES (Aug. 19, 1984), http://www.nytimes.com/1984/08/19/business/the-age-of-me-first-management.html?pagewanted=all (quoting Tobin).

339. *Id.*

340. DORFF, *supra* note 5, at 55.

341. *Supra* notes 61–64 and accompanying text.

342. Wentz, *supra* note 141, at 442.

343. NEWCOMER, *supra* note 161, at 129.

344. CRYSTAL, *supra* note 126, at 79.

345. Dobbin & Zorn, *supra* note 57, at 183.

346. *Rewarding Executives for Taking the Long View*, BUS. WK., Apr. 2, 1984, at 99.

in public companies.[347] Jensen and Murphy's 1990 *Harvard Business Review* article and the research underpinning it[348] were influential in this process.[349] As pay-for-performance became a key governance objective in public companies in the early 1990s,[350] higher levels of executive compensation would have logically followed, given managerial antipathy toward a riskier stream of income.[351]

The public company norms relevant to the setting of executive pay were clearly different in the 1980s and the 1990s than they were in the 1950s and 1960s, but it cannot be taken for granted that those changes explain the end of the era of remuneration moderation prevailing during the mid-20th century. As we have seen, the trend in favor of higher executive pay likely can be traced back to the mid-1970s. To the extent that this is accurate, if norms relevant to executive pay only changed in public companies in the 1980s and the beginning of the 1990s, then other factors must account for the pivot away from executive pay moderation. It is even conceivable that causation worked in reverse, with the move toward higher executive pay helping to set the scene for prevailing norms to change.

While it is possible that changes affecting executive pay may have reconfigured social norms rather than vice versa, there is some evidence that norms had begun to change in the mid-to-late 1970s in a way that fostered the trend in favor of higher executive pay that prevailed thereafter. The 1970s were famously referred to as the "'Me' Decade,"[352] reflecting a growing predilection for self-discovery and self-indulgence.[353] Derek Bok, in his 1993 study of executive and professional pay, acknowledged that the "Reagan revolution" of the 1980s lifted to the status of an "official ideology" a belief in individualism and admiration of successful entrepreneurs, but indicated that surveys of college students showed that making money was moving up the priority list as early as the start of the 1970s.[354] These broader societal trends in their turn may well have influenced attitudes in a way that made higher compensation more acceptable. Arch Patton, the executive pay expert, suggested in 1976 that "executive self-interest has replaced company loyalty to a substantial degree" and said this had helped "to raise the pay expectations of executives above any level sustainable without rampant inflation."[355] Correspondingly, changing norms coincided with, and likely contributed to, the late 1970s shift away from the executive pay model that prevailed during the mid-20th century.

Caution should be used in drawing upon norms as an explanatory variable with respect to corporate governance. This is because the term can potentially be defined so broadly that the behavior in question can be accounted for adequately by reference to incentives

347. *Supra* note 57 and accompanying text; Lublin & Thurm, *supra* note 7; BEBCHUK & FRIED, *supra* note 92, at 72.

348. Jensen and Murphy discussed their findings in more detail in Michael C. Jensen & Kevin J. Murphy, *Performance Pay and Top-Management Incentives*, 98 J. POL. ECON. 225, 255–56 (Apr. 1990).

349. *Supra* notes 51 and 58 and accompanying text.

350. Frydman & Jenter, *supra* note 12, at 84–87.

351. *See* Frydman & Saks, *supra* note 11, at 2130 (reporting that the growth in the level of executive pay was explained partly, if not fully, by the strengthening of managerial incentives).

352. Tom Wolfe, *The "Me" Decade and the Third Great Awakening*, N.Y. MAG. (Aug. 23, 1976), http://nymag.com/news/features/45938/#print.

353. ANTHONY J. MAYO & NITIN NOHRIA, IN THEIR TIME: THE GREATEST BUSINESS LEADERS OF THE TWENTIETH CENTURY 258 (2005).

354. BOK, *supra* note 8, at 249, 253–54.

355. Arch Patton, *Executive Compensation: The Past, Present and Future*, FIN. EXEC., July 1976, at 24, 30 (quoted by Balkcom, *supra* note 197, at 22).

traditional economic analysis addresses.[356] Nevertheless, it appears that a corporate culture underpinned by norms that discouraged "money grubbing" by top executives helps to explain why, between the 1940s and the 1970s, they were not paid as generously as their counterparts in later decades.

VI. CONCLUSION

Executive pay has been a highly controversial issue for the past quarter-century. Various reforms have been introduced as a response, seemingly to little avail. Ironically, not long before the controversy began, during the middle decades of the 20th century, an executive compensation regime was in place in U.S. public companies that likely would have appealed to many of today's critics of executive pay. How was it that executive pay was modest by present-day standards prior to the introduction of reforms designed to address concerns that would subsequently arise? We have addressed that question in this Article. By identifying "what worked," we are able to offer insights for those advocating executive pay reform today, albeit of a rather pessimistic nature.

Tax provides at first glance the most obvious explanation for executive pay arrangements in place during the middle of the 20th century. The top marginal tax rates on income were eye-wateringly high compared with present levels, which might have been expected to keep executive pay down. Thomas Piketty has indeed argued that restoring the tax regime in place in the United States during the mid-20th century would do much to address concerns which currently exist about executive pay. As we have shown, however, tax likely only had a modest impact on executive pay levels during the middle of the 20th century. The tax "hit," though substantial by present-day standards, was not robust enough to result in top executives leaving substantial sums "on the table."

Unions likely exerted some downward pressure on executive pay during the mid-20th century, with unionized companies refraining from increasing managerial compensation substantially to reduce friction in labor negotiations with unions that had considerably more clout than they do presently. Unions, however, never represented a majority of the workforce at any point in time, which would have diluted the impact they had on executive pay economy-wide.

The market for managerial talent and norms within public companies do more to explain the mid-20th century executive pay compression. While, by the end of the 20th century, CEOs were widely thought of as being genuine "difference makers" who would be worth paying generously and even poaching if they were the right person for the job, from the 1940s through the 1970s, top executives were perceived of as mere bureaucrats with often fungible talents and were seemingly paid accordingly. Also, a "team first" ethos and a fear of being pilloried as greedy stemming from the crisis conditions of the Depression and World War II fostered the development of strong norms within companies against the awarding of highly lucrative executive pay.

Could such historical conditions return to create a new era of executive pay moderation? It is doubtful. Pleas made to today's CEOs to leave money on the table voluntarily have fallen on deaf ears,[357] so it seems improbable corporate leaders will do

356. Marcel Kahan, *The Limited Significance of Norms for Corporate Governance*, 149 U. PA. L. REV. 1869, 1870–71 (2001).

357. *See* Skapinker, *supra* note 1 (discussing why CEOs should request lower salaries); *see also* Michael

much to lead by example. Humility reputedly is "the flavor du jour" among senior executives right now.[358] Still, it seems unlikely that CEOs will be thought of anytime soon as mere "organization men" meriting merely bureaucratic pay. There is also little chance that a "team first" ethos will become sufficiently prevalent and potent in public companies to drive executive pay downward toward mid-20th century levels. While there is nostalgia for the industrial giants that dominated the U.S. (and world) economy during the middle decades of the 20th century, Americans came to view such firms as bastions of soul-destroying conformism and ultimately preferred a more individualistic arrangement.[359] There probably is little appetite for a return to the orderly but potentially demoralizing uniformity of mid-20th century corporate life, which likely precludes norm-driven reform of executive pay.

Perhaps Americans would be amenable to a return to the bureaucratic corporate ethos of the 1940s, 1950s, and 1960s if what can be referred to as "America's Midcentury Moment," characterized by substantial faith in government and widespread acceptance of a highly egalitarian income distribution, was to return.[360] The Midcentury Moment, however, may well have been unique in U.S. history, following on from the deprivations of the Depression and the collective effort associated with World War II. This likely is not a bad thing, given that these were traumatic events few, if any, would want to see repeated. To draw matters together, in this Article we have identified what "worked" with executive pay in the sense that we have explained why managerial compensation remained relatively flat during the middle decades of the 20th century in a way that regulation introduced since the early 1990s has not been able to replicate. Putting into practice, however, the insights we have offered in a way that will satisfy today's critics of executive pay may well be impossible.

Skapinker, *CEOs need to join the 20 times club now*, FIN. TIMES (Nov. 30, 2011), http://www.ft.com/cms/s/0/13ff9b0e-19e7-11e1-9888-00144feabdc0 (providing a 2015 plea following on from the previous article to the same effect).

358. Joann S. Lublin, *The Case for Humble Executives*, WALL ST. J. (Oct. 20, 2015, 7:51PM), http://www.wsj.com/articles/the-case-for-humble-executives-1445385076.

359. Christopher Caldwell, *In lament to America's lost bargain*, FIN. TIMES (Sept. 19, 2010), http://www.ft.com/cms/s/2/06cc2c58-c40d-11df-b827-00144feab49a.html.

360. Michael Barone, *The Surprising Roots of Liberal Nostalgia*, WALL ST. J. (June 22, 2011), http://www.wsj.com/articles/SB10001424052702303714704576385262844826944.