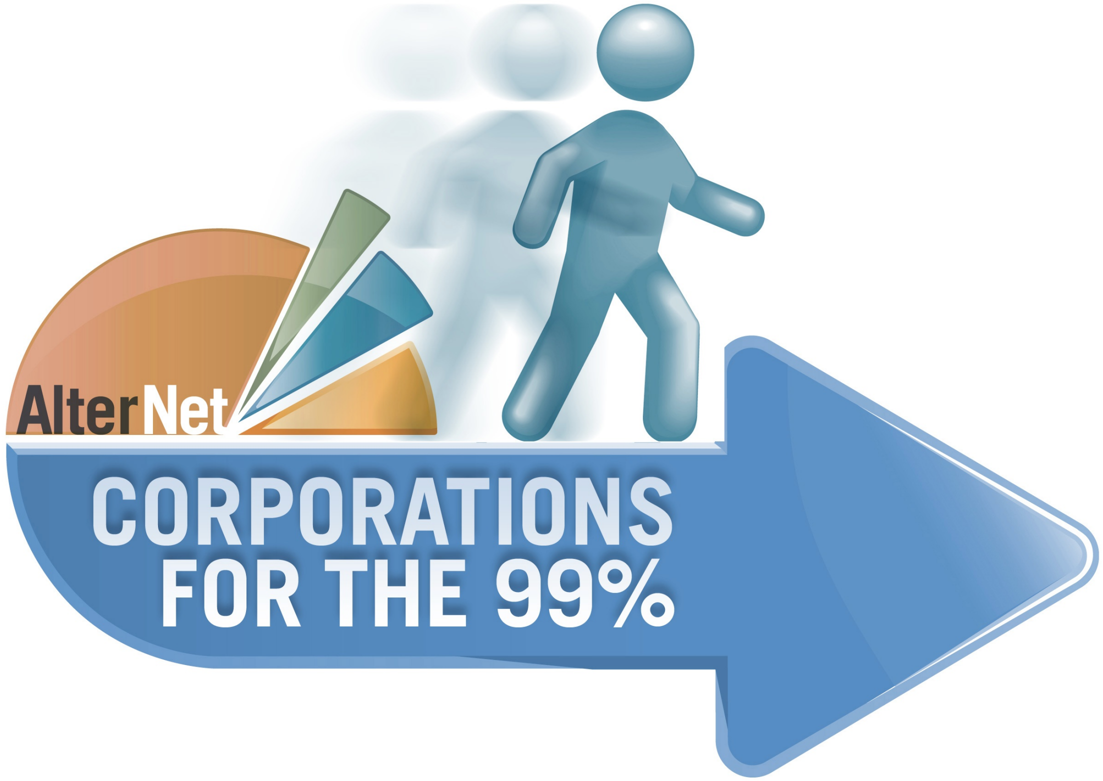

CORPORATIONS FOR THE 99%

HOW CAN THE PUBLIC TAKE CONTROL OF THE BUSINESS CORPORATION AND MAKE IT WORK FOR THE REAL ECONOMY?

EDITED BY LYNN PARRAMORE

Intro

As you've probably noticed, corporations are not working for the 99%. But this wasn't always the case. AlterNet takes an in-depth look at the American corporation in a special series that blasts through dangerous myths and provides indispensable tools for challenging the misguided ideology that grips our public dialogue. William Lazonick, professor at the University of Massachusetts, president of the Academic-Industry Research Network, and one of the leading expert on the American corporation, along with AlterNet's Lynn Parramore and journalist Ken Jacobson, examine the foundations, history, and purpose of the corporation to answer this vital question: How can the public take control of the business corporation and make it work for the real economy?

By William Lazonick

How American Corporations Transformed from Producers to Predators

Over the last 30 years, corporations have turned on the 99 percent. Here's how it happened and how to fight back.

In 2010, the top 500 U.S. corporations – the Fortune 500 – generated $10.7 trillion in sales, reaped a whopping $702 billion in profits, and employed 24.9 million people around the globe. Historically, when these corporations have invested in the productive capabilities of their American employees, we've had lots of well-paid and stable jobs.

That was the case a half century ago.

Unfortunately, it's not the case today. For the past three decades, top executives have been rewarding themselves with mega-million dollar compensation packages while American workers have suffered an unrelenting disappearance of middle-class jobs. Since the 1990s, this hollowing out of the middle-class has even affected people with lots of education and work experience. As the Occupy Wall Street movement has recognized, concentration of income and wealth of the top "1 percent" leaves the rest of us high and dry.

What went wrong? A fundamental transformation in the investment strategies of major U.S. corporations is a big part of the story.

A Look Back

A generation or two ago, corporate leaders considered the interests of their companies to be aligned with those of the broader society. In 1953, at his congressional confirmation hearing to be Secretary of Defense, General Motors CEO Charles E. Wilson was asked whether he would be able to make a decision that conflicted with the interests of his company. His famous reply: "For years I thought what was good for the country was good for General Motors and vice versa."

Wilson had good reason to think so. In 1956, under the Federal-Aid Highway Act, the U.S. government committed to pay for 90 percent of the cost of building 41,000 miles of interstate highways. The Eisenhower administration argued that we needed them in case of a military attack (the same justification that would be used in the

1960s for government funding of what would become the Internet). Of course, the interstate highway system also gave businesses and households a fundamental physical infrastructure for civilian purposes– from zipping products around the country to family road trips in the station wagon.

And it was also good for GM. Sales shot up and employment soared. GM's managers, engineers and other male white-collar employees could look forward to careers with one company, along with defined-benefit pensions and health benefits in retirement. GM's blue-collar employees, represented by the United Auto Workers (UAW), did well, too. In business downturns, such as those of 1958, 1961 and 1970, GM laid off its most junior blue-collar workers, but the UAW paid them supplemental unemployment benefits on top of their unemployment insurance. When business picked up, GM rehired these workers on a seniority basis.

Such opportunities and employment security were typical of most Fortune 500 firms in the 1950s, '60s and '70s. A career with one company was the norm, while mass layoffs simply for the sake of boosting profits were viewed as bad not only for the country, but for the company, too.

What a difference three decades makes! Now mass layoffs to boost profits are the norm, while the expectation of a career with one company is long gone. This transformation happened because the U.S. business corporation has become in a (rather ugly) word "financialized." It means that executives began to base all their decisions on increasing corporate earnings for the sake of jacking up corporate stock prices. Other concerns -- economic, social and political -- took a backseat. From the 1980s, the talk in boardrooms and business schools changed. Instead of running corporations to create wealth for all, leaders should think only of "maximizing shareholder value."

When the shareholder-value mantra becomes the main focus, executives concentrate on avoiding taxes for the sake of higher profits, and they don't think twice about permanently axing workers. They increase distributions of corporate cash to shareholders in the forms of dividends and, even more prominently, stock buybacks. When a corporation becomes financialized, the top executives no longer concern themselves with investing in the productive capabilities of employees, the foundation for rising living standards for all. They become focused instead on generating financial profits that can justify higher stock prices – in large part because, through their stock-based compensation, high stock prices translate into megabucks for these corporate executives themselves. The ideology becomes: Corporations for the 0.1 percent -- and the 99 percent be damned.

The 99 percent needs to understand these fundamental changes in the ways in which top executives have decided to make use of resources if we want U.S. corporations to work for us rather than just for them.

The Financialization Monster

The beginnings of financialization date back to the 1960s when conglomerate titans built empires by gobbling up scores and even hundreds of companies. Business schools justified this concentration of corporate power by teaching that a good manager could manage any type of business -- the bigger the better. But conglomeration often became simply a method of using accounting tricks to boost earnings in the short-run to encourage speculation in the company's stock price. This focus on short-term financial manipulation often undermined the financial conditions for sustaining higher levels of earnings over the long term. But the interest of stock-market speculators was (as it always is) to capitalize on short-term changes in the market's evaluation of corporate shares.

When these giant empires imploded in the 1970s and 1980s, people began to see the weakness of the model. By the early 1970s the downgraded debt of conglomerates, known as "fallen angels," created the opportunity for a young bond trader, Michael Milken, to create a liquid market in high-yield "junk bonds." By the mid-'80s, Milken (who eventually went to jail for securities fraud) was using his network of financial institutions to back corporate raiders in junk-bond financed leveraged buyouts with the purpose of extracting as much money as possible from a company once it was taken over through layoffs of workers and by breaking up the company to sell it off in pieces.

Wall Street changed the way it made its money. Investment banks turned their focus from supporting long-term corporate investment in productive assets to trading corporate securities in search of higher yields. The great casino was taking form. In 1971, NASDAQ was launched as a national electronic market for generating price quotes on highly speculative stocks. The Employee Retirement Income Security Act of 1974 encouraged corporate pension funds to get into the game since inflation had eroded household savings. In 1975, competition from NASDAQ led the much more conservative New York Stock Exchange, which dated back to 1792, to end fixed commissions on stock transactions. This move only further encouraged stock market speculation by making it less costly for speculators to buy and sell.

In 1980, Robert Hayes and William Abernathy, professors of technology management at Harvard Business School, wrote a widely read article that criticized executives for focusing on short-term profits rather than investments in innovation. But in 1983, two financial economists, Eugene Fama of the University of Chicago and Michael Jensen of the University of Rochester, co-authored two articles in the *Journal of Law and Economics* which extolled corporate honchos who focused on "maximizing shareholder value" -- by which they meant using corporate resources to boost stock prices, however short the time-frame. In 1985 Jensen landed a higher profile pulpit at Harvard Business School. Soon, shareholder-value ideology became the mantra of thousands of MBA students who were unleashed in the corporate world.

Proponents of the Fama/Jensen view argue that for superior economic performance, corporate resources should be allocated to maximize returns to shareholders because they are the only economic actors who make investments without a guaranteed return. They say that shareholders are the only ones who bear risk in the corporate economy, and so they should also get the rewards. But this argument could not be more false. In fact, lots of people bear risks of investing in the corporation without knowing if they will pay off for them. Governments in the U.S., funded by the body of taxpayers, are constantly making investments in physical infrastructures and human capabilities that provide benefits to businesses, but without a guaranteed return to taxpayers. An employer expects workers to give time and effort beyond that required by their current pay to make a better product and boost profits for the company in the future. Where's the worker's guaranteed return? In contrast, most public shareholders simply buy and sell shares of a corporation on the stock market, making no contribution whatsoever to investment in the company's productive capabilities.

In the name of this misguided philosophy, major U.S. corporations now channel virtually all of their profits to shareholders, not only in the form of dividends, which reward them for holding shares, but even more importantly in the form of stock buybacks, which reward them for selling shares. The sole purpose of stock buybacks is to give a manipulative boost to a company's stock price. The top executives then benefit when they exercise their typically bountiful stock options and cash in by selling the stock. For 2001-2010, 459 companies in the S&P 500 Index in January 2011 distributed $1.9 trillion in dividends, equivalent to 40 percent of their combined net income, and $2.6 trillion in buybacks, equal to another 54 percent of their net income. After all that, what was left over for investments in innovation, including upgrading the capabilities of their workforces? Not much.

Falling to the Challenge

Big changes in markets and technologies since the 1980s have given U.S. corporations serious competitive challenges. Confronted by Japanese and then Korean competition, companies closed plants, permanently displacing blue-collar workers from what had been middle-class jobs. Meanwhile, the open systems technologies that characterized the microelectronics revolution favored younger workers with the latest computer skills. In the name of shareholder value, by the 1990s U.S. corporations seized on these changes in competition and technology to put an end to the norm of a career with one company, ridding themselves of more expensive older employees in the process. In the 2000s, American corporations found that low-wage nations like China and India possessed millions of qualified college graduates who were able and willing to do high-end work in place of U.S. workers. Offshoring put the nail in the coffin of employment security in corporate America.

In response to these challenges, U.S. corporations could have used their profits to upgrade the capabilities of the U.S. labor force, laying the foundation for a new prosperity. Instead, the same misguided financialized responses have meant big losses for taxpayers and workers while the top 1 percent has gained. Instead of rising to the challenge, they've fallen into greed and short-sightedness that chips away at our chances for a prosperous economy.

Yet properly governed, corporations can be run for the 99 percent. In fact, that's still the case in many successful economies. The truth is that it's possible to take back the corporations for the 99 percent in the U.S. if we can really wrap our heads around the problem and the solutions. Here are three places to start:

1) **Ban It**. Ban large established companies from buying back their own stock, and reward them instead for investing in the retention and training of their employees.

2) **Link It.** Link executive pay to the productive performance of the company, with increases in executive pay being tied to increases for the corporate labor force as a whole.

3) **Occupy It.** Recognize that taxpayers and workers bear a significant proportion of the risk of corporate investment, and put their representatives on corporate boards where they can have input into the relation between risks and rewards.

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BY WILLIAM LAZONICK

How High CEO Pay Hurts the 99 Percent

Why are top executives making outrageous amounts of money for not doing their jobs? It's time to fight back -- because they work for us..

While most Americans struggle to make ends meet, the CEOs of major U.S. business corporations are pulling eight-figure, and sometimes even nine-figure, compensation packages. When they win, the 99 percent lose. We rely on these executives to allocate corporate resources to investments in new products and processes that, in a world of global competition, can provide us with good jobs. Yet the ways in which we permit top corporate executives to be paid actually gives them a strong disincentive to invest in innovation and training. The proper function of the executive is to figure out how to develop and use the corporation's productive capabilities (business schools call it "competitive strategy"). But that's not happening.

In effect, U.S. top executives rake in obscene sums by not doing their jobs.

The Runaway Compensation Train

The data from corporate proxy statements will show that 2011 was another banner year for top executive pay. Over the previous three years the average annual compensation of the top 500 executives named on corporate proxy statements was "only" $17.8 million, compared with an annual average of $27.3 million for 2005 through 2007. Yet even in these recent "down" years, the compensation of these named top executives was more than double in real terms their counterparts' pay in the years 1992 through 1994.

It might surprise you to learn that in the early 1990s, executive pay was already widely viewed as out of line with what average workers got paid. In 1991 Graef Crystal, a prominent executive pay consultant, published a best-selling book, *In Search of Excess: The Overcompensation of American Executives*, in which he calculated that over the course of the 1970s and '80s, the real after-tax earnings of the average manufacturing worker had declined by about 13 percent. During the same period, that of the average CEO of a major US corporation had quadrupled! Bill Clinton took up the issue in his 1992 presidential campaign, and immediately upon taking office had Congress pass a law that forbade companies from recording as tax-deductible expenses executive salaries plus bonuses in excess of $1 million.

Unfortunately Clinton chose the wrong pay target. In 1992 salaries and bonuses represented only 23 percent of the total compensation of the top 500 executives named on proxy statements. The largest single component of executive compensation was gains from exercising stock options, representing 59 percent of the total. The Clinton administration left this so-called "performance pay" unregulated.

Perversely, one reaction of corporate boards to the Clinton legislation was to take $1 million in salary plus bonus as the "government-approved minimum wage" for top executives, and therefore to raise these components of executive pay if they fell short of that minimum. The number of named executives with salaries plus bonuses that totaled $1 million or more increased from 529 in 1992 to 703 in 1993 and 922 in 1994.

The other reaction of corporate boards was to lavish more stock options on their top executives. When the stock market boomed in the late 1990s, these executives cashed in. The average annual compensation of the top 500 named executives reached $21 million in 1999 with gains from exercising stock options representing 71 percent of the total, and $32 million in 2000 with option gains now 80 percent of the total.

From 1982 to 2000 the U.S. experienced the longest stock market boom in its history. Average annual stock-price yields of S&P 500 companies were 13 percent in the 1980s and 16 percent in the 1990s. So it didn't require any great genius to make money from stock options. In fact, it became a no-brainer. In 1991, the Securities and Exchange Commission waived the longstanding rule that, as corporate insiders, top executives had to hold stock acquired through exercising their options for six months to prevent "short-swing" profit-taking. As before, executives did not have to put any of their own money at risk in being granted stock options. But now they could also pick the opportune moment to exercise their options without any risk that the value of the company's stock would subsequently decline before they could sell the stock and lock in the gains.

The New Normal of Corporate Greed

The speculation-fueled "irrational exuberance" of the late 1990s brought unprecedented pay bonanzas to top executives, thus establishing a "new normal" for corporate greed. When boom turned to bust in the early 2000s, money-hungry executives had to look for another way to get stock prices up and make their millions. Their favorite "weapon of value extraction" over the past decade has been the stock buyback (aka stock repurchase). Top executives allocate massive sums of corporate cash to repurchasing their company's own stock with the purpose of boosting their company's stock price. Stock buybacks and stock options have become the yin and yang of executive compensation.

Let's take a look at how it works: The board of directors of Acme Corporation authorizes the CEO to repurchase the company's own outstanding shares up to a specified value (say $5 billion) over a specified period of time (say three years). On any dates within this three-year period, the CEO then has the authority to instruct the company's broker to use the company's cash to buy back shares on the open market up to the $5 billion limit and subject to the SEC rule that the buybacks on any one day can be no more than 25 percent of the company's average daily trading volume over the previous four weeks. That might permit Acme to do buybacks worth, say, $100 million per day. It may be the end of the quarter, and the CEO and CFO want to meet Wall Street's expectations for earnings per share. Or they may want to offset a fall in the company's stock price because of bad news. Or they may want to ensure that the increase in the company's stock price keeps up with those of competitors, who may also be doing buybacks. Whatever the reason, by the laws of supply and demand, when the corporation spends cash on buybacks, it "manufactures" an increase in its stock price.

Then, with the stock price up, the CEO, CFO and other insiders may choose to cash in their stock options. Presto! They make tons of money for themselves.

Meanwhile, these executives will tend to ignore investments in innovation and training. Some companies actually fund their buybacks by laying off workers, offshoring jobs to low-wage countries, and taking on debt. The top executives' weapon of value extraction becomes a weapon of value destruction. They are rewarded handsomely by not doing their jobs.

In 1981, 292 major corporations spent less than 3 percent of their combined net income on buybacks. In 1982, however, the SEC passed a rule (10b-18) that gave corporations that did very large-scale stock repurchases a "safe harbor" from charges of stock-price manipulation. Buyback activity then became larger and more widespread, increasing substantially over the course of the 1990s. From 2003 to 2007, buybacks really took off, and by 2007 the very same 292 corporations now spent *over 82 percent of their net income repurchasing their own stock*.

The financial crisis and the Great Recession forced a slowdown in buybacks. S&P 500 companies repurchased a record $609 billion in 2007 but pared it down to $360 billion in 2008 and $146 billion in 2009. They stepped it back up to about $289 billion in 2010 and an estimated $440 billion in 2011. It is quite possible that buybacks in 2012 will be even higher than in the previous record year of 2007. And look for executive pay to increase as well.

Concentration of Income at the Top

Make no mistake about it. Executive pay is a prime reason why in 2005-2008 the top 0.1 percent captured a record 11.4 percent of all household income (including capital gains) in the U.S., compared with 2.6 percent three decades earlier. In 2010 (the latest Internal Revenue Service data available), this number was 9.5 percent. The income threshold among taxpayers for being included in the 0.1 percent in 2010 was $1,492,175. Of the executives named in proxy statements in 2010, 4,743 had total compensation greater than this threshold amount, with a mean income of $5,034,000 and gains from exercising stock options representing 26 percent of their combined compensation.

Total corporate compensation of the named executives does not include other non-compensation income (from securities, property, fees for sitting on corporate boards, etc.) that would be included in their IRS tax returns. If we assume that named executives whose corporate compensation was below the $1.5 million threshold were able to augment that income by 25 percent from other sources, then the number of named executives in the top 0.1 percent in 2010 would have been 5,555.

Included in the top 0.1 percent of the US income distribution were a large, but unknown, number of US corporate executives whose pay was above the $1.5 million threshold but who were not named in proxy statements because they were neither the CEO nor the four other highest paid in their particular companies. To take just one example, of the five named IBM executives in 2010, the lowest paid had total compensation of $6,637,910. There were presumably large numbers of other IBM executives whose total compensation was between this amount and the $1.5 million top 0.1 percent threshold.

Let's Put CEOs to Work for Us

Under the Obama administration, virtually nothing has been done to constrain top executive pay. President Obama signaled his unwillingness to take on the issue when, in an interview in February 2010, he was asked about the many millions paid in 2009 to Jamie Dimon, CEO of JPMorgan and Lloyd Blankfein, CEO of Goldman Sachs, in the wake of the financial meltdown and bank bailouts. "I know both those guys; they are very savvy businessmen," the president said. "I, like most of the American people, don't begrudge people success or wealth. That is part of the free-market system."

The "Say-on-Pay" provision in the 2010 Dodd-Frank Wall Street Reform and Consumer Protection Act sounds good, but it just reinforces a system of incentives that does not work. This provision gives public shareholders the right to express their non-binding opinion to corporate management on issues related to executive compensation. If Congress had understood what drives executive pay in the U.S., however, it would have recognized that the granting of Say-on-Pay rights to public shareholders is part of the problem, not the solution. Through a combination of stock options and stock buybacks, Say-on-Pay provisions reinforce an alignment between the incentives of top executives and the interests of public shareholders that has been undermining investment in America's future.

It is about time that we took control of exploding executive pay. It is not just that the sums involved are unfair, and as history has shown, will only become more obscene. These executives control the allocation of resources that represent the well-being of the 99 percent, and the ways in which they bank their booty is doing severe damage to the U.S. economy. The investment strategies of business corporations are too important to be left under the control of those who gain when the 99 percent lose.

William Lazonick is professor of economics and director of the UMass Center for Industrial Competitiveness. He is president of the Academic-Industry Research Network. His book, Sustainable Prosperity in the New Economy? Business Organization and High-Tech Employment in the United States *(Upjohn Institute, 2009) won the 2010 Schumpeter Prize.*

By Ken Jacobson

Whose Corporations? Our Corporations!

The idea that corporations are obligated only to shareholders is a dangerous fad. Law and precedent say they owe a strong duty to the 99%.

Historically, corporations were understood to be responsible to a complex web of constituencies, including employees, communities, society at large, suppliers, and shareholders. But in the era of deregulation, the interests of shareholders began to trump all the others. How can we get corporations to recognize their responsibilities beyond this narrow focus? It begins in remembering that the philosophy of putting shareholder profits over all else is a matter of ideology which is not grounded in American law or tradition. In fact, it is no more than a dangerous fad.

The Myth of Profit Maximizing

"It is literally – literally – malfeasance for a corporation not to do everything it legally can to maximize its profits. That's a corporation's duty to its shareholders."

Since this sentiment is so familiar, it may come as a surprise that it is factually incorrect: In reality, there is nothing in any U.S. statute, federal or state, that requires corporations to maximize their profits. More surprising still is that, in this instance, the untruth was not uttered as propaganda by a corporate lobbyist but presented as a fact of life by one of the leading lights of the Democratic Party's progressive wing, Sen. Al Franken. Considering its source, Franken's statement says less about the nature of a U.S. business corporation's legal obligations – about which it simply misses the boat – than it does about the point to which laissez-faire ideology has wormed its way into the American mind.

The notion that the law imposes a duty to "maximize shareholder value" – a phrase capturing the notion that profits are mandatory and it is the shareholders who are entitled to them – is so readily accepted these days because it jibes perfectly with assumptions about economic life that constantly come down to us from business and political leaders, from academia, and from the preponderance of the media. It is unlikely to occur to anyone under the age of 40 to question this idea – or the idea that the highest, or even sole, purpose of a corporation is to make a profit – because they have rarely if ever been exposed to an alternative view. Those in middle age or beyond may have trouble remembering a time when the corporation's focus on shareholders' interests to the exclusion of all other constituencies –customers, employees, suppliers, creditors, the communities in which it operates, and the nation – did not seem second nature.

This narrow conception of corporate purpose has become predominant only in recent decades, however, and it flies in the face of a longer tradition in modern America that regards the responsibilities of a corporation as extending far beyond its shareholders. Owen D. Young, twice chairman of General Electric (1922-'40, 1942-'45) and 1930 *Time* magazine Man of the Year, told an audience at Harvard Business School in 1927 that the purpose of a corporation was to provide a good life in both material and cultural terms not only to its owners but also to its employees, and thereby to serve the larger goals of the nation:

"Here in America, we have raised the standard of political equality. Shall we be able to add to that, full equality in economic opportunity? No man is wholly free until he is both politically and economically free. No man with an uneconomic and failing business is free. He is unable to meet his obligations to his family, to society, and to himself. No man with an inadequate wage is free. He is unable to meet his obligations to his family, to society, and to himself. No man is free who can provide only for physical needs. He must also be in a position to take advantage of cultural opportunities. Business, as the process of coordinating men's capital and effort in all fields of activity, will not have accomplished its full service until it shall have provided the opportunity for all men to be economically free."

This holistic declaration was echoed, albeit in more specific and practical terms, by the chairman of another massive US corporation, Johnson & Johnson, during World War II. In his 1943 "Credo," a somewhat modified version of which can be found on the company's Web site today, Robert Wood Johnson II identified five distinct constituencies and established an order of priority in which they would be served by his firm. Johnson & Johnson's "first responsibility," he wrote, was to its customers: "the doctors, nurses, hospitals, mothers, and all others who use our products." In second place came employees; in third, management; and in fourth, "the communities in which we live." The interests of the stockholders, the corporation's "fifth and last responsibility," appear subordinate in his mind both to the firm's sound operation, which depends on attention to the interests of the other constituencies, and to its long-term welfare:

"Business must make a sound profit. Reserves must be created, research must be carried on, adventurous programs developed, and mistakes paid for. Adverse times must be provided for, adequate taxes paid, new machines purchased, new plants built, new products launched, and new sales plans developed. We must experiment with new ideas. When these things have been done the stockholder should receive a fair return."

A Shift in Accountability

By 1978 the era of deregulation had begun and signs had appeared that corporate attitudes were shifting. In that year another GE chief executive, Reginald H. Jones, wrote that the "central principle of the present system is that a director's accountability is to the owners of the enterprise." Having set aside the broader visions of corporate duty held by his GE predecessor Young and by Johnson, Jones in effect moved the firm's responsibility to its shareholders from last on the list to first: "If this principle is abandoned, if other corporate constituencies are placed on a plane with shareowners, if directors are required to represent directly the interests of nonshareowner groups…there will be no clear measure of directors' responsibility because there will be no clear consensus on primary corporate goals."

His personal preferences aside, however, Jones realized that Americans were not yet ready to accept firms' turning their backs on the general good, and that he and his fellow executives had something to gain from being accommodating:

"If the concern is social responsiveness, or 'public accountability,' the short answer is that in this country at this time, no large corporate enterprise can afford to be perceived as oblivious or contemptuous of matters of genuine social or public concern. These enterprises have to earn from the general public and their political representatives – and earn from year to year – the right to continue to function without radical new governmental constraints."

The dawn of Ronald Reagan's presidency found the corporate community on the fence. The "Statement on Corporate Responsibility" issued in October 1981 by the Business Roundtable, which groups the CEOs of the largest US firms, recognizes six constituencies – customers, employees, communities, society at large, suppliers, and shareholders – as forming the "web of complex, often competing relationships" within which corporations operate. It accepts the idea that "shareholders have a special relationship to the corporation" but doesn't allow their interests to trump all others:

"Balancing the shareholder's expectations of maximum return against other priorities is one of the fundamental problems confronting corporate management. The shareholders must receive a good return but the legitimate concerns of other constituencies also must have appropriate attention. Striking the appropriate balance, some leading managers have come to believe that the primary role of corporations is to help meet society's legitimate needs for goods and services and to earn a reasonable return for the shareholders in the process. They are aware that this must be done in a socially acceptable manner. They believe that by giving enlightened consideration to balancing the legitimate claims of all its constituents, a corporation will best serve the interest of the shareholders."

Even after eight years of Reagan and amid the burgeoning of free-market ideology, the Business Roundtable remained reluctant to place shareholders first, affirming in 1990 that "corporations are chartered to serve both their shareholders and society as a whole" and adding creditors to the 1981 list of constituencies, which it otherwise retained intact. It was only in 1997, in a new statement whose title substituted "Corporate Governance" for "Corporate Responsibility," that it renounced attempts to balance the interests of corporate constituents and, having reversed its view, argued that taking care of shareholders was the best way to take care of the remaining stakeholders, rather than the other way around:

"In the Business Roundtable's view, the paramount duty of management and of boards of directors is to the corporation's stockholders; the interests of other stakeholders are relevant as a derivative of the duty to stockholders. The notion that the board must somehow balance the interests of stockholders against the interests of other stakeholders fundamentally misconstrues the role of directors."

This doctrine, known as "shareholder primacy," now reigns in the corporate world today, and it has so increased the power of those whom it has benefited that it will not be easy to dislodge. Those who propagate it believe, or would have us believe, that it is based in law; in fact, it is supported by no more than ideology. They believe, or would have us believe, that it reflects incontrovertible and eternal truths; in fact, it is an expression of transient self-interest. They believe, or would have us believe, that it honors long precedent – but, as we have seen, its ascendency is recent, and, rather than honor it undermines precedent. Yet despite these contradictions, corporations and their allies have been exceedingly successful at selling their viewpoint to the American people.

An important step toward countering their influence can come in refusing to accept the legitimacy of shareholder primacy. Up to now, this fad has had the power to neutralize opposition in part because it has obscured the tool needed to challenge it: a clear understanding of the economic realities. For this reason, we must learn what contributions all stakeholders – not just the shareholders, but all the others as well – make to the corporation, and the extent of the risks and rewards those contributions truly entail. We must learn about the interrelation of business and government in all its complexity, going far beyond the headlines about taxes and regulation to discover who needs whom for what, and who does what for whom. And we must learn what rights corporations legitimately hold, what privileges they enjoy, and what duties they are obliged to carry out.

Without this effort, without this knowledge, we are in danger of continuing to be held captive by a fad.

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By Lynn Parramore

Capitalism's Dirty Secret: Corporations Don't Create Jobs, They Destroy Them

If we want good jobs and long-term career opportunities, we have to tame the wild horses of big business.

For the last four decades, U.S. corporations have been sinking our economy through the off-shoring of jobs, the squeezing of wages, and a magician's hat full of bluffs and tricks designed to extort subsidies and sweetheart deals from local and state governments that often result in mass layoffs and empty treasuries.

We keep hearing that corporations would put Americans back to work if they could just get rid of all those pesky encumbrances – things like taxes, safety regulations, and unions. But what happens when we buy that line? The more we let the corporations run wild, the worse things get for the 99 percent, and the scarcer the solid jobs seem to be.

Yet the U.S. Chamber of Commerce wants us to think that corporations – preferably unregulated! – are the patriotic job creators in our economy. They want us to think it so much that in 2009, after the financial crash, they launched a $100 million campaign, which, among other things, draped their Washington, DC building with an enormous banner proclaiming "Jobs: Brought to you by the free market system."

But the truth is that unfettered corporations are just about the worst thing for creating decent jobs. Here's a look at why, and where the good jobs really come from.

Taming the Wild Horses

Corporations are kind of like wild horses. They can run you down. Or sweep you around in circles till you're exhausted. And in today's world, they'll surely run off and take your jobs to China or someplace else if you don't learn how to tame them.

Bad things happen when corporations are unconstrained by strong national policies that force players to think long term, behave decently, and refrain from dumping their short-term costs on the rest of us. They tend to focus single-mindedly on maximizing profits for shareholders at the expense of all else – including jobs. Executives set their sights on a path to short-term boosts in share prices paved with layoffs, wage cuts, and jobs moved overseas, while slashing research and development and investing in the skills of their employees.

The U.S. Department of Commerce found that from 2000 to 2009, U.S. transnational corporations, which employ about 20 percent of all American workers, cut their domestic employment by 2.9 million even as they boosted their overseas workforce by 2.4 million. The result was an enormous loss of jobs nationally, as well as a net loss globally.

In the 1990s, these companies added more jobs at home than abroad. What changed? 1) The rise of India and China, with 37 percent of the world's population, as hotspots for off-shoring; and 2) the availability of tens of millions of workers in these places, many with college degrees, to do the jobs previously done by American workers.

In India, indigenous companies like TCS, Infosys and Wipro along with transnationals like IBM, HP and Accenture, employ hundreds of thousands of college-educated workers to perform IT services, in large part for American firms. In China, the electronics contract manufacturer Foxconn (headquartered in Taiwan) barely existed a decade ago, but now employs about 1.2 million workers, with Apple its single biggest customer.

And yet Big Business still trumpets itself as the American Job Creator Fairy. Apple has released a report claiming to have created half a million domestic jobs – a highly dubious number which takes credit for everything from the app industry to FedEx delivery jobs (never mind that drivers would be hauling someone else's gadgets if Apple went out of business). It's true that in the U.S. managers, engineers and other professionals have found good jobs at Apple. But the non-professional employees are just barely scraping by. A study of the iPod value chain in 2006 calculated that among Apple's domestic employees, professionals earned around $85,000, not counting stock options, but the retail workers in Apple's stores earned only $26,000. This is troubling because as Apple has grown in size, most of the employees it has hired in the U.S. work in retail. Are these jobs paths to long-term, stable careers? Quite likely they are not.

While a company like Apple whistles "God Bless America", executives are not going to talk about the job losses induced by off-shoring, nor the horrifically abused foreign workforce that moving jobs to China has produced. And they're not going to tell us about Apple's preference for hiring part-time employees who can't afford to buy health insurance. When such uninsured people have health emergencies, someone has to pay, and the burden falls on the taxpayers.

Here is what Apple executives tell us instead: "We don't have an obligation to solve America's problems."

The Real Deal

Corporate executives have lost the sense that they owe anything to the public. They have forgotten that the 99 percent, as taxpayers, have made huge investments in them. They fight to lower taxes as if all the money “belongs” to the companies. They fight regulations as if the public doesn’t have the right to interfere in their business.

All nonsense.

Despite the anti-government rhetoric from conservative leaders, the truth is that the government, elected by the people, plays a critical role in creating the conditions in which companies can succeed and good jobs can flourish. The government is able to invest in human capital through key services like education. What’s the point of a job if you don’t have an educated worker to fill it? The government also creates job-friendly conditions by investing in infrastructure. How can you get to work if your roads and bridges are falling apart? And it boosts job creation through investing in technology. How could Google create its amazing search engine without state investment in the creation of the Internet? When the government invests in the knowledge infrastructure, businesses can then employ and train people who can, in turn, engage in the kind of organizational learning that leads to that wondrous thing called "innovation."

We learned this once before. After Wall Street financiers ran amok to cause the Great Depression in the 1930s, the government responded by putting in place regulations on banks and corporations, a highly progressive tax system, and a robust social safety net. President Franklin D. Roosevelt created the conditions in which good jobs were possible with programs like the Civilian Conservation Corps and other New Deal initiatives. He focused on the development of highways, railways, airports and parks, investing in the future rather than focusing solely on short-term profits. The GI Bill, rather than leaving graduates with big debts, left them well educated and therefore with a chance to provide a middle-class life for their families and to retire with dignity.

After victory in World War II, America was able to emerge as the world’s most powerful nation because it had a large middle-class and a strong industrial and technological base. The horses of Big Business were tamed, and they could be harnessed to do useful things for society. Then came the Reagan Revolution and Big Business freed itself from the regulations, unions and taxes that had curbed its worst instincts and it began to shred the nation’s economic and social safety net. The gap in income inequality grew, and jobs were eliminated and outsourced. Long-term investment in innovation and human capital slowed down, while fraud and financial speculation took off.

Today, corporate executives ask for more special treatment and freer rein in calling the shots in our economy, and they threaten to pack their bags if we don’t agree. Some politicians and policy makers respond to this blackmail by saying that we have to create a “friendly business climate” to convince them to stay. But what makes a "friendly business climate"–low wages, minimal taxes and so on --

creates a very hostile climate for the 99 percent, which is ultimately bad for everyone – business included. The state of Mississippi and Rick Perry's Texas, where city and state officials bent over backwards to lure Big Business with subsidies and other perks, are hardly bursting with good jobs.

Many researchers have concluded that tax rates are actually not terribly important to where a company locates. Further, a common rule of thumb for business headquarters location is that quality of life for key personnel is decisive. True, vastly different levels of regulation in the U.S. and China is a problem for which there are no easy answers. But there are real costs to ignoring the environment and keeping workers in a state of misery. If you want job growth, you have to have demand growth: profits and consumption go hand in hand.

That's why the best way to unleash America's job-creating potential is to support rights and protections for ordinary people. A climate friendly to the 99 percent is not just fair, it makes the best sense for the economy. We need to remember the complementary roles that government and business have to play in creating well-paid, stable employment opportunities and then ensuring that people can access these opportunities over the course of their careers. To get corporations working for the 99 percent on the job front, we have three major challenges:

1) Education: Young people from low-income groups (especially blacks and Hispanics) need schooling and training to move to good career jobs.

2) Incentives: Corporations must have incentives to retain educated and experienced workers instead of laying them off or off-shoring their jobs. (To do so forces valuable workers into low-skill jobs and wastes their human capital, which was expensive to acquire.)

3) Investment: Executives of financialized corporations who want the government to invest in the knowledge base have to make complementary investments in people that can keep the U.S. economy innovative and generate good jobs. That would mean changing the single-minded focus on boosting company stock prices through buybacks and other financial manipulations that serve the 1 percent but no one else.

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By William Lazonick and Ken Jacobson and Lynn Parramore

3 Corporate Myths that Threaten the Wealth of the Nation

It's time to restore corporate power to the people by blasting through the myths about how corporations should be run, and for whom.

The wealth of the American nation depends on the productive power of our major business corporations. In 2008 there were 981 companies in the United States with 10,000 or more employees. Although they were less than two percent of all U.S. firms, they employed 27 percent of the labor force and accounted for 31 percent of all payrolls. Literally millions of smaller businesses depend, directly or indirectly, on the productivity of these big businesses and the disposable incomes of their employees.

When the executives who control big-business investment decisions place a high priority on innovation and job creation, then we all have a chance for a prosperous tomorrow. Unfortunately, over the past few decades, the top executives of our major corporations have turned the productive power of the people into massive and concentrated financial wealth for themselves. Indeed the very emergence of "the 1%" is largely the result of this usurpation of corporate power. And executives' use of this power to benefit themselves often undermines investment in innovation and job creation.

These corporations do not belong to them. They belong to us. We need to confront some powerful myths of corporate governance as part of a movement to make corporations work for the 99%. To start, we have to recognize these corporations for what they are not.

• They are not "private enterprise."
• They should not be run to "maximize shareholder value."
• The mega-millions in remuneration paid to top corporate executives are not determined by the "market forces" of supply and demand.

Let's take a closer look at each of these myths.

1. Public corporations are not private enterprise.

Here's something you'll rarely hear stated by today's politicians and pundits: Publicly listed and traded corporations are not private enterprise. As documented by the pre-eminent business historian Alfred D. Chandler, Jr., in a book aptly called *The Visible Hand*, about 100 years ago the managerial revolution in American business placed salaried managers in charge of running the nation's largest and most productive business corporations.

This was a peaceful revolution in which a generation of owner-entrepreneurs who had founded these companies some decades earlier used initial public offerings on the New York Stock Exchange to sell their ownership stakes to the public, leaving decision-making power in the hands of salaried managers. In effect, these corporate employees, and the boards of directors whom they selected, became trustees of the immense productive power that these corporations had accumulated.

Even when founders of companies that evolve into major public corporations become their CEOs, they generally occupy the top positions as corporate employees, not owners. For example, when the late Steve Jobs returned to Apple Computer in 1997, 11 years after being denied the CEO position of the company he had founded, his ascent to the top position was as a manager, not an owner. When a company founder like Larry Page of Google gives up private ownership by publicly selling shares, he may become CEO of the new corporation, but he is occupying this position as a hired hand, not as a private entrepreneur.

In other words, private owners make choices to transform a private enterprise into a public company that then needs to be regulated as such. There are other choices that could have been made. When the retiring owner of a private company wants to pass on control over a prosperous company to his or her employees, an alternative to the public corporation is to establish an Employee Stock Ownership Plan, or ESOP. There are many successful companies in the U.S. that are not public corporations precisely because they are under the collective ownership of their employees.

It is also possible for some investors to agglomerate sufficient shares to take a public company private (Mitt Romney made his millions doing just that), but that only emphasizes the point: public corporations are not private enterprise. We regulate public corporations far more stringently than private businesses precisely because they are publicly held. And as U.S. citizens, how we regulate public corporations (or even private businesses, for that matter) is up to us.

2. Corporations should be run to benefit everyone who contributes to their success - not just shareholders.

It's a myth that corporations have a legal duty to maximize profits to shareholders at the expense of everyone else. Historically, the executives and directors of U.S. public corporations understood that they had a responsibility to other constituencies – customers, employees, suppliers, creditors, the communities in which they operate, and the nation.

Today, however, the dominant ideology is that a corporation should "maximize shareholder value." At the most basic level, the rationale for this ideology is that shareholders own the company's assets, and therefore have exclusive claim on its profits. A more sophisticated argument is that that among all stakeholders in the business corporation only shareholders bear the risk of getting a positive return from the firm, while all other participants receive guaranteed returns for their productive contributions. If society wants risk-bearing, so the argument goes, firms need to return value to shareholders.

This argument sounds logical – until you question its fundamental assumption. Innovation, defined as the process that generates goods or services that are higher quality and/or lower cost than those previously available, is an inherently uncertain process. Anyone who invests their labor or their capital in the innovation process is taking a risk that the investment may not generate a higher quality, lower cost product. Once you understand the collective and cumulative character of the innovation process, you can easily see that the assumption that shareholders are the only participants in the business enterprise who make investments in productive resources without a guaranteed return is just plain false. In an innovative economy, workers and taxpayers habitually make these risky investments.

How do workers make these risky investments? As is generally recognized by employers who declare that "our most important assets are our human assets", the key to successful innovation is the extra time and effort, above and beyond the strict requirements of the job, that employees expend interacting with others to confront and solve problems in transforming technologies and accessing markets. Anyone who has spent time in a workplace knows the difference between workers who just punch the clock to collect their pay from day to day and workers who use their paid employment as a platform for the expenditure of creative and collective effort as part of a process of building their careers.

As members of the firm, these forward-looking workers bear the risk that their extra expenditures of time and effort will not yield the gains to innovative enterprise from which they can be rewarded. If, however, the innovation process does generate profits, workers, as risk-bearers, have a claim to a share in the forms of promotions, higher earnings and benefits. Instead, shareholder-value ideology is often used as a rationale for laying off workers whose hard and creative work has contributed to the company's success. That's grossly unfair.

Taxpayers also invest in the innovation process without a guaranteed return. Through government agencies, taxpayers fund infrastructural investments that, given their cost and the uncertainty of returns, business enterprises would not have made on their own. It is impossible to explain U.S. leadership in information technology and biotechnology without recognizing the role of government in making investments to develop new knowledge and facilitate its diffusion. As one example, the current annual budget of the National Institutes of Health (http://www.nih.gov/about/budget.htm) is about $31 billion, twice in real terms its level in the early 1990s. Without this government expenditure on research, year in and year out, we would not have a medicinal drug industry. Yet shareholder-value ideology is often used to justify low taxes that deny taxpayers a return on these investments.

So shareholder-value ideology provides a flawed rationale for excluding workers and taxpayers from sharing in the gains of innovative enterprise. To turn this ideology on its head, what risk-bearing role do public shareholders play in the innovation process? Do they confront uncertainty by strategically allocating resources to innovative investments? No. As portfolio investors, they diversify their financial holdings across the outstanding shares of existing firms to minimize risk.

They do so, moreover, with limited liability, which means that they are under no legal obligation to make further investments of "good" money to support previous investments that have gone bad. Even for these previous investments, the existence of a highly liquid stock market enables public shareholders to cut their losses instantaneously by selling their shares – what has long been called the "Wall Street walk".

3. Executive compensation is a rigged game, not the result of the laws of supply and demand.

You often hear that stratospheric executive pay is the result of some inexorable law of supply and demand. If we don't give top executives their multimillion dollar compensation, they won't be willing to come to work and do their jobs. They are supposedly the bearers of "scarce talent" that demands a high price in the market place. Even Robert Reich, Secretary of Labor in the Clinton administration and a critic of U.S. income inequality, has justified the explosion in executive pay, arguing that intense competition makes it much more difficult than it used to be to find the talent who can manage a large corporation (*Supercapitalism,* 2008, pp 105-114).

That is not what determines executive pay. Here is how it works: Top executives select other top executives to sit on "their" boards of directors. These directors hire compensation consultants to recommend an executive pay package, which consists of salary, bonus, incentive pay, retirement benefits, and all manner of other perks. The consultants look at what top executives at other major corporations are getting, and say that, well, this executive should get more or less the same. Since the directors are mostly these very same "other executives", they have no interest in objecting – and if any of them were to do so, they would find that they are no longer being invited to sit on corporate boards.

Meanwhile, given the preponderance of stock-based compensation (especially stock options) in executive pay, whenever there is speculative boom in the stock market, top executives of the companies with most rapidly rising stock prices make out like bandits. The higher compensation levels then create a "new normal" for executive pay that, via the compensation consultants and compliant directors, ratchets up the pay of all the top dogs. And, when the stock market is less speculative, these corporate executives do massive stock buybacks to push stock prices up.

What we have here is not "market forces" at work but an exclusive club that promotes the interests of the 0.1%. All too often executives allocate corporate resources to benefit themselves rather than to invest in innovation and job creation. It is time that the 99% see through the ideology, break up the club, and get the U.S. economy back on track.

Corporate power for the people!

Business corporations exist as part of the collective and cumulative development of our economy. The investments in innovation and job creation that these corporations make or decline to make are key to our future prosperity. Public shareholders, the supposed owners of these corporations, are in general only willing to hold shares in a company because of the ease with which they can terminate this relation by selling their shares on the stock market. Yet, almost unanimously, corporate executives proclaim that they run their companies for the sake of shareholders. In fact, their personal coffers pumped up with stock-based compensation, our business "leaders" have increasingly run the corporations for themselves.

The real corporate investors are taxpayers and workers. Through government agencies at federal, state, and local levels, taxpayers supply business corporations with educated labor and physical infrastructure. Through their interaction in business organizations, workers expend the time and effort that can generate innovative products. In the name of shareholder value, however, taxpayers and workers have been losing out. It's time to confront the myths of "private enterprise", "shareholder value", and "market-determined executive compensation" with arguments about how the innovation process actually works with sustainable prosperity as the result.

What will it take to build a movement that can make the business corporation work for the 99%?

We have to elect politicians who will take on corporate power rather than shill for corporate power-brokers. We have to support labor leaders who recognize that gaining a voice in corporate governance is the only way to ensure that corporations will invest in workers and create good jobs. We need teachers at all levels of the education system who understand what business corporations are and what they are not. We need the responsible media to escape from the grip of corporate control. And we have to put in place business executives who represent the interests of civil society rather than those of an elite egotistical club.

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