Yale Journal on Regulation

Volume 37 | Issue 1 Article 7

2020

Accountable Compensation: The Progressive Case for Stakeholder-Focused, Board-Empowering Executive Compensation Laws

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Note

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Shareholder primacy has long dominated American legal thought and politics across the ideological spectrum. Over the past several years, however, U.S. political progressives have begun to criticize shareholder primacy, arguing that corporations should also serve other stakeholders. This Note conducts the first academic analysis of this emerging movement's executive compensation policy proposals. This Note finds that stakeholder-primacy progressives have failed to propose policies that would effectively regulate executive compensation. Given the connection between rising executive compensation and economic inequality, this finding is surprising and concerning. The final Part develops an original executive compensation policy proposal for the progressive stakeholder primacy movement.

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Introduction

In August 2018, U.S. Senator Elizabeth Warren announced her Accountable Capitalism Act[1]—a bold new proposal to "restore[] the idea that giant American corporations should look out for American interests."[2] The Accountable Capitalism Act is an ambitious bill geared toward promoting a populist ethos in American corporate law: as Senator Warren wrote in the *Wall Street Journal*, "[c]orporate profits are booming, but average wages haven't budged over the past year. The U.S. economy has run this way for decades. . . . I'm introducing legislation to fix it."[3]

Given the prominence of populism in American politics since the 2016 presidential election cycle, the bill's loudly populist bent was unsurprising. What was remarkable, however, was the legislation's chief philosophical target: shareholder primacy—the corporate-governance theory that boards of directors should primarily serve shareholders, rather than customers, workers, and other stakeholders, in making important corporate policy decisions. "What are the obligations of corporate citizenship in the U.S.?" asked Senator Warren in her op-ed. "For much of U.S. history, the answers were clear. Corporations sought to succeed in the marketplace, but they also recognized their obligations to employees, customers and the community. . . . This approach worked. American companies and workers thrived."[4] During the 1980s, however, according to Warren, "[t]he dynamic changed . . . . a new theory emerged that corporate directors had only one obligation: to maximize shareholder returns."[5]

This shareholder-centered theory of the firm was first introduced in the United States by law professor Adolf Berle in 1931.[6] Professor Berle asserted that the powers of corporate managers may be exercised only for the benefit of shareholders.[7] E. Merrick Dodd, one of Berle's contemporaries, sharply disagreed, responding that corporations have "a social service as well as a profit-making function" and igniting the famed Berle-Dodd debate of stakeholder versus shareholder primacy.[8] Berle's shareholder-primacy theory

1. The Accountable Capitalism Act, S. 3348, 115th Cong. (2018).
2. Elizabeth Warren, Opinion, *Companies Shouldn't Be Accountable Only to Shareholders*, WALL ST. J. (Aug. 14, 2018), https://www.wsj.com/articles/companies-shouldnt-be-accountable-only-to-shareholders-1534287687 [https://perma.cc/YH2V-D7V9].
3. *Id*.
4. *Id*.
5. *Id*.
6. Adolf A. Berle, Jr., *Corporate Powers as Powers in Trust*, 44 HARV. L. REV. 1049 (1931).
7. *Id*. at 1049.
8. E. Merrick Dodd, *For Whom Are Corporate Managers Trustees?*, 45 HARV. L. REV. 1365, 1367 (1932); *see* A.A. Sommer, Jr., *Whom Should the Corporation Serve? The Berle-Dodd Debate Revisited Sixty Years Later*, 16 DEL. J. CORP. L. 33 (1991). There is a related, longstanding corporate law debate in the United States and abroad between "contractarians" and "communitarians," or "institutionalists." *See, e.g.*, David K. Millon, *New Directions in Corporate Law: Communitarians, Contractarians, and the Crisis in Corporate Law*, 50 WASH. & LEE L. REV. 1373 (1993).

did not take hold as the dominant theory of corporate governance in the United States until the 1970s and early 1980s, when the theory was popularized by conservative economist Milton Friedman. Friedman claimed that the "primary responsibility" of corporate executives is to the firm's shareholders, who "own" the corporation.[9] In Friedman's view, corporate managers must not engage with "social responsibility" unless doing so would maximize returns to shareholders. "There is one and only one social responsibility of business," argued Friedman, "—to use its resources and engage in activities designed to increase its profits."[10]

Despite shareholder primacy's conservative nascence, by the late 2000s U.S. political progressives had adopted the theory as a mechanism to rein in misbehaving corporations. According to this new Democrat rationale, not only should the corporation primarily serve shareholders, but it should also be governed by them, with shareholders retaining influence over key managerial decisions. During the late 2000s, Democrats championed several shareholder power-enhancing policies in Congress.[11] In 2009, Senator Charles Schumer (D-NY) introduced the Shareholder Bill of Rights Act.[12] Cosponsored by Senator Maria Cantwell (D-WA), the bill's primary aim was to "provide shareholders with enhanced authority" over the nomination, election, and compensation of corporate executives and directors.[13] Senator Schumer, in unveiling the Act, argued that "shareholders had too little say" over corporate-governance matters during the Great Recession, allowing executives to take on excessive risk and earn "too much in salary."[14] Among the bill's stated findings was the assertion

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9. Milton Friedman, *The Social Responsibility of Business Is to Increase Its Profits*, N.Y. TIMES MAG. 1 (Sept. 13, 1970), http://umich.edu/~thecore/doc/Friedman.pdf [https://perma.cc/Y4EN-LXGV]. Shareholder primacy was further discussed and popularized by other prominent economists and legal scholars. *See, e.g.*, Michael C. Jensen & William H. Meckling, *Theory of the Firm: Managerial Behavior, Agency Costs and Ownership Structure*, 3 J. FIN. ECON. 305 (1976) (introducing the related, highly influential theory of "agency costs"). For some of Daniel Fischel's seminal work drawing on Jensen and Meckling's theories, see Frank H. Easterbrook & Daniel R. Fischel, *The Corporate Contract*, 89 COLUM. L. REV. 1416 (1989); and Daniel R. Fischel, *Efficient Capital Market Theory, the Market for Corporate Control, and the Regulation of Cash Tender Offers*, 57 TEX. L. REV. 1 (1978).

10. Friedman, *supra* note 9, at 6.

11. *See, e.g.*, Shareholder Bill of Rights Act of 2009, S. 1074, 111th Cong. (2009) (sponsored by Senator Charles Schumer (D-NY), requiring a shareholder vote on executive compensation, proxy statement disclosure of "golden parachute" arrangements, and establishing shareholder-friendly proxy access rules); Shareholder Protection Act, H.R. 4790, 111th Cong. (2010) (sponsored by Representative Michael Capuano (D-MA), providing for a shareholder vote on corporate political campaign expenditures). Notably, after the Great Recession, longtime consumer advocate Ralph Nader also jumped on the shareholder rights bandwagon, reasoning that "[o]nce you awaken shareholders . . . more civic values will be incorporated into society." Steven Davidoff Solomon, *Nader, an Adversary of Capitalism, Now Fights as an Investor*, DEALBOOK, N.Y. TIMES (Jan. 14, 2014), https://dealbook.nytimes.com/2014/01/14/nader-an-adversary-of-capitalism-now-fights-as-an-investor [https://perma.cc/69DF-FAYV].

12. S. 1074, 111th Cong. (2009).

13. *Id.* § 2(3), (4).

14. Karey Wutkowski, *U.S. Sen. Schumer Unveils Shareholder Bill of Rights*, REUTERS (May 19, 2009, 12:35 PM), https://www.reuters.com/article/us-financial-shareholders-schumer-idUSTRE54I4PF20090519 [https://perma.cc/S24L-5MHV] (quoting Senator Schumer).

that lack of accountability to shareholders—the corporation's "ultimate owners"—had contributed to the economic crisis, resulting in the loss of "trillions of dollars in shareholder value."[15]

The Shareholder Protection Act of 2010, sponsored by Representative Michael Capuano (D-MA) and cosponsored by forty-nine other House Democrats, aimed to mandate a binding shareholder vote on political campaign spending by corporations.[16] The legislation invoked the central rationale of shareholder primacy, finding that "[c]orporations, acting through their boards and executives, are obligated to conduct business for the best interests of their owners, the shareholders."[17]

Perhaps the most significant of these Democrat-backed policies was "say on pay" legislation that would require U.S. public companies to hold a regular advisory shareholder vote to approve their executive-compensation policies. The Shareholder Vote on Executive Compensation Act, an early say-on-pay bill, was introduced by Representative Barney Frank (D – MA) and then-Senator Barack Obama (D – IL) in the spring of 2007.[18] Though the Act failed, congressional Democrats eventually succeeded in enacting mandatory say-on-pay legislation for U.S. public companies as part of the 2010 Dodd-Frank Wall Street Reform and Consumer Protection Act.[19] Dodd-Frank also included other Democrat-supported policies intended to enhance shareholder choice such as the pay-ratio disclosure requirement,[20] which was later championed by Senator Warren herself.[21]

Given shareholder primacy's established Democrat backing, Senator Warren's unabashed rebuff of it may seem striking. But Senator Warren is not the only left-leaning American politician who has recently promoted the idea that corporations should serve societal interests beyond those of shareholders. In the past year, Democrat senators Bernie Sanders,[22] Tammy Baldwin,[23] Cory

15. S. 1074, 111th Cong. (2009).

16. H.R. 4790, 111th Cong. (2010).

17. *Id*. § 2(2).

18. H.R. 1257, 110th Cong. (2007); S. 1181, 110th Cong. (2007). These say on pay proposals were vigorously opposed by congressional Republicans. *See* Blog, *House Passes Executive Compensation Act*, SPEAKER OF THE HOUSE NANCY PELOSI (Apr. 20, 2007), https://www.speaker.gov/newsroom/house-passes-shareholder-vote-on-executive-compensation-act [https://perma.cc/6NJM-FQUZ] (describing a Republican motion to recommit the bill, which would "in effect kill[] it").

19. Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, § 951, 124 Stat. 1376, 1899 (2010) (requiring listed public companies to hold periodic say-on-pay shareholder votes on the compensation of executive officers).

20. *Id*. § 953(b).

21. Letter from Senator Elizabeth Warren, U.S. Senate to Mary Jo White, Chair, U.S. Sec. & Exch. Comm'n (June 2, 2015) https://www.warren.senate.gov/files/documents/2015-6-2_Warren_letter_to_SEC.pdf [https://perma.cc/N2VF-85PY].

22. *See* Stop WALMART (Welfare for Any Large Monopoly Amassing Revenue from Taxpayers) Act of 2018, S. 3410, 115th Cong. (2018); Chuck Schumer & Bernie Sanders, Opinion, *Schumer and Sanders: Limit Corporate Stock Buybacks*, N.Y. TIMES (Feb. 3, 2019), https://www.nytimes.com/2019/02/03/opinion/chuck-schumer-bernie-sanders.html [https://perma.cc/YQX5-LRKH].

Booker,[24] and Chuck Schumer,[25] representing multiple factions of the contemporary Democratic Party, have all proposed legislation that would require corporations to promote nonshareholder interests, such as by adopting worker representation on corporate boards and limiting corporate stock buybacks.[26] Viewed in perspective, Senator Warren and her colleagues are on the front line of a new wave of progressive corporate political thought, one that some have called "stakeholder primacy."[27]

Central to the progressive stakeholder primacy movement is a concern about the United States's ever-growing income and wealth inequality. According to shareholder primacy's critics, this philosophy has driven a surge in economic inequality in recent decades by funneling more and more corporate wealth to shareholders, a group that is already disproportionately rich. As Senator Warren wrote in the *Wall Street Journal*, "[b]ecause the wealthiest 10% of U.S. households own 84% of American-held shares, the obsession with maximizing shareholder returns effectively means America's biggest companies have dedicated themselves to making the rich even richer."[28]

The Accountable Capitalism Act is designed, first and foremost, to combat this ballooning economic inequality. The bill would require all U.S. companies with greater than $1 billion in annual revenue to obtain a federal corporate "charter" stating that the corporation "shall have the purpose of creating a general public benefit,"[29] which is defined as a "material positive impact on society."[30] Directors and officers of U.S. corporations covered by the Act would commit to balancing "the pecuniary interests of the shareholders . . . with the best interests of persons that are materially affected by the [corporation's] conduct," including employees, customers, the communities in which the company's offices and facilities are located, and "the local and global environment."[31] The Act would further require that the corporation's workers elect at least two-fifths of the board of directors.[32] Corporations seeking to make political campaign contributions would need to obtain

23. *See* Reward Work Act, S. 2605, 115th Cong. (2018).

24. *See* Worker Dividend Act, S. 2505, 115th Cong. (2018).

25. *See* Schumer & Sanders, *supra* note 22.

26. Eillie Anzilotti, *Elizabeth Warren's Bold New Plan to Give Corporate Wealth Back to Workers*, FAST CO. (Aug. 22, 2018), https://www.fastcompany.com/90223130/how-elizabeth-warrens-accountable-capitalism-act-works [https://perma.cc/8TRB-U8CZ].

27. *See, e.g.*, Martin Lipton, *Corporate Governance; Stakeholder Primacy; Federal Incorporation*, HARV. L. SCH. FORUM ON CORP. GOVERNANCE & FIN. REG. (Aug. 17, 2018), https://corpgov.law.harvard.edu/2018/08/17/corporate-governance-stakeholder-primacy-federal-incorporation [https://perma.cc/8CDU-2N92] (describing the Accountable Capitalism Act as "reject[ing] shareholder primacy and embrac[ing] stakeholder governance"). Proponents of stakeholder primacy generally include customers, employees, suppliers, and communities in their definition of a stakeholder. *See infra* note 147.

28. Warren, *supra* note 2.

29. S. 3348 §§ 4, 5(b)(2), 115th Cong. (2018).

30. *Id.* § 5(a)(1).

31. *Id.* § 5(c)(1).

32. *Id.* § 6.

approval from three-fourths of their shareholders and three-fourths of the board.[33] Finally, directors and officers receiving equity compensation would be prohibited from selling these shares within five years of receipt and within three years of a company stock repurchase.[34]

For those concerned by economic inequality in America, the bill contains commendable policy ideas. But a troubling deficiency remains: the bill lacks a robust policy to control the executive compensation distributed by U.S. corporations. Certainly, the bill contains provisions that would likely have some indirect effect on executive pay, in particular by limiting executives' ability to sell shares received as equity compensation in the short term, placing worker-appointees on boards, and giving directors an emphatic duty to consider non-shareholder interests. As this Note establishes in Part IV, however, these provisions fall short of effectively limiting the amounts of compensation paid to U.S. executives.

Senator Warren is not alone in her failure to promote a strong vision for executive-compensation regulation. After engaging in the first academic analysis of the progressive stakeholder-primacy movement's executive-compensation-policy proposals, this Note finds that none of these proposals would effectively regulate executive compensation.[35] Given the demonstrated link between skyrocketing executive compensation and the rising wealth and income inequality in the United States,[36] this oversight is both surprising and deeply concerning.

The answer to this political puzzle could lie in the widespread progressive support for and presumed success of say on pay. As mentioned above, section 951 of the Dodd-Frank Act requires U.S. public companies to give shareholders the opportunity to cast a nonbinding, advisory vote on executive compensation packages at least once every three years.[37] At the time of Dodd-Frank's enactment, many progressives cheered the inclusion of the say-on-pay provision as a success in the fight against corporate America's exponential C-suite pay growth.[38] The paucity of stakeholder-oriented CEO pay policy proposals would be reasonable if the U.S. say-on-pay law and other shareholder-empowering executive compensation laws could be trusted to work. Growing evidence, though, suggests they cannot. As I explain in Part II, executive-compensation and economic=inequality data show that say on pay

33. *Id*. § 8.

34. *Id*. § 7.

35. *See* discussion *infra* Part IV.

36. *See* discussion *infra* Part I.

37. Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, § 951, 124 Stat. 1376, 1899 (2010).

38. *See* Andrea Fuller, *House Approves Limits on Executive Pay*, N.Y. TIMES (July 31, 2009), https://www.nytimes.com/2009/08/01/business/01pay.html [https://perma.cc/UB7Y-S868] (quoting Speaker Pelosi arguing that "[e]mpowering financial regulators to prohibit risky bonus practices by financial firms is not only long overdue, but the responsible thing to do for the taxpayers, who have ended up footing the bill for too many corporate excesses").

has not been successful in slowing the growth of executive compensation and economic inequality in the United States.

Part III argues that the failure of shareholder-focused executive compensation laws should come as no surprise. Drawing on several studies analyzing shareholder voting behavior and demographics, I argue that U.S. dispersed shareholders possess neither the capacity nor the incentives to effectively limit executive pay. I conclude that in addition to being an ineffective regulator, say-on-pay voting has the potential to worsen economic inequality by ratifying high compensation and incentivizing short-termism and excessive risk-taking by corporate managers.

In Part IV, I engage in the first academic analysis of the emerging stakeholder-primacy movement's executive compensation policy proposals. In analyzing these policy proposals, I explain why they would fail to place effective limits on executive compensation. In Part V, I put forward my own stakeholder-oriented executive compensation proposal, one that returns the responsibility for controlling executive compensation to corporate directors and guides their decision-making by 1) imposing industry-based caps on CEO-worker pay ratios for large public companies, 2) mandating an advisory worker vote on executive compensation, and 3) repealing say on pay.

The literature on executive compensation is voluminous and dates back to some of the oldest debates in corporate law.[39] Like so many corporate-governance topics, the issue of how to regulate executive compensation boils down to the two most fundamental questions of corporate law: 1) whose interests should the corporation serve?;[40] and 2) who should decide?[41] As the first paper to connect the emerging wave of progressive stakeholder primacy in U.S. politics to our nation's current executive compensation laws, this Note contributes to the existing literature by identifying and analyzing the significant gap between these two regimes and proposing a novel, progressive way forward.

I. Economic Inequality and Rising Executive Compensation in the United States

In this Part, I address the key policy issue of the progressive stakeholder primacy movement—economic inequality in the United States—and show how rising executive compensation contributes to economic inequality. In Section I.A, I describe the current state of income and wealth inequality in the United

39. *See, e.g.*, Robert B. Mautz & Gerald W. Rock, *The Wages of Management*, 11 U. FLA. L. REV. 474, 474 (1958) (asking, "[w]ho manages this vast concentration of public wealth; how much compensation is paid to them; who controls the determination of the amount of compensation; and what standards are used to measure the price paid to management?").

40. *See* discussion *infra* Section IV.A.

41. *See, e.g.*, Stephen M. Bainbridge, *Is 'Say on Pay' Justified?*, 32 REG. 42, 46 (2009) ("There is no more basic question in corporate governance than 'Who decides?' Is a particular decision or oversight task to be assigned to the board of directors, management, or shareholders?").

States. In Section I.B, I examine executive compensation at American companies. I conclude with the connection between rising executive compensation and growing income inequality in Section I.C.

A. America's Ever-Growing Economic Inequality

Since the early 2000s, economists, the media, the public, and politicians have become increasingly concerned by America's widening income and wealth gaps. Economists Thomas Piketty, Emmanuel Saez, and Gabriel Zucman document the meteoric rise in income and wealth inequality in the United States from the 1980s through 2015.[42] Their findings paint a striking economic portrait of the United States, showing that the average pre-tax income of the bottom 50% of earners has stagnated since 1980, while the average income of the top 1% has more than tripled.[43]

According to Piketty and Saez, and supported by the findings of other economists,[44] the growth in income inequality since 1980 is largely due to the skyrocketing incomes of the top 1% of American earners:

> [T]he vast majority of the population—from the bottom up to the 87th percentile— experienced less growth than the (modest) macro rate of 1.4% a year . . . The only group that grew fast is the top 1%, whose average income increased 3.3% pre-tax and 3.2% post-tax. . . . The top 1% has pulled apart from the rest of the economy—not the top 20%.[45]

Growth in wealth inequality has been even more concentrated, with the majority of gains accruing to the top 0.1% of families (those with greater than $20 million in wealth in 2012).[46]

Saez provides important insight into how American economic-inequality trends compare to those of other countries. Using data from the World Wealth and Income Database, Saez shows that the United States, the United Kingdom and Canada have all experienced similar patterns of steadily rising income inequality since 1980, though the United Kingdom and Canada have seen slightly less growth.[47] Meanwhile, France, Sweden and Japan had levels of income inequality similar to that of the United States before 1970 but have not experienced nearly the same increase in income concentration in the decades since.[48] According to Saez, this finding indicates that the United States'

42. Thomas Piketty, Emmanuel Saez & Gabriel Zucman, *Distributional National Accounts: Methods and Estimates for the United States*, 133 Q.J. ECON. 553 (2018); Emmanuel Saez, *Income and Wealth Inequality: Evidence and Policy Implications*, 35 CONTEMP. ECON. POL'Y 7 (2017).

43. Piketty, Saez & Zucman, *supra* note 42, at 557.

44. *See infra* sources cited notes 50-53 and accompanying text.

45. Piketty, Saez & Zucman, *supra* note 42, at 580.

46. Saez, *supra* note 42, at 13.

47. *Id*. at 17.

48. *Id*. at 17-18.

growing income inequality must be due partially to domestic factors, because all six countries have been subject to the same general trends of globalization and technological progress.[49]

B. American Companies' Ever-Increasing Executive Compensation

Just as income inequality has increased steadily since the 1980s, so too has the gap between executive compensation and average wages. A series of reports by the Economic Policy Institute (EPI) charts the meteoric rise in CEO pay and the concurrent stagnation in worker wages since the 1960s.[50] Examining the CEO pay packages and average worker compensation granted by the top 350 U.S. firms (ranked by gross sales) since 1965, a 2018 EPI report shows that the CEO-worker pay ratio grew from 20-to-1 in 1965, to 58-to-1 in 1989, to a staggering 311.7-to-1 in 2017.[51] From a percentage growth perspective, this evolution looks even more devastating: as the EPI reported in 2012, "From 1978 to 2011, CEO compensation increased more than *725 percent*, a rise substantially greater than stock market growth and the painfully slow *5.7 percent* growth in worker compensation over the same period."[52] Between 2016 and 2017 alone, average CEO compensation for the top 350 U.S. firms jumped 17.6%, up to $18.9 million.[53] Unsurprisingly, the United States leads most other countries in its CEO-average worker pay ratio. According to Bloomberg, the United States' 2017 CEO-average worker pay ratio of 264.8 was nearly double that of Germany (136.1) and more than double those of Australia (109.5) and France (69.7). The United States' nearest pay-ratio peers were India (229.1) and the United Kingdom (201).[54]

C. Rising Executive Compensation as a Key Driver of Economic Inequality

The data on economic inequality and executive compensation in the United States reveal a strong link between rising executive compensation levels and the massive economic inequality growth since the 1980s. Piketty, Saez, and Zucman and the EPI studies show that growth in income inequality has been

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49. *Id*. ("[T]his very simple finding is important because it tells you that growing income inequality since the 1970s is not just due to globalization or technological progress (e.g., computers) because all six countries [studied]…have gone through the same process of technological progress, and they are subject to the same forces of globalization, yet the evolution of inequality or income concentration varies.").

50. Lawrence Mishel & Jessica Schieder, *CEO Compensation Surged in 2017*, ECON. POL'Y INST. (Aug. 16, 2018), https://www.epi.org/publication/ceo-compensation-surged-in-2017 [https://perma.cc/A5G7-ALW8]; Natalie Sabadish & Lawrence Mishel, *CEO Pay and the Top 1%: How Executive Compensation and Financial-Sector Pay Have Fueled Income Inequality*, ECON. POL'Y INST. (May 2, 2012), https://www.epi.org/publication/ib331-ceo-pay-top-1-percent [https://perma.cc/NYM3-ZXW9].

51. Mishel & Schieder, *supra* note 50, at 1, 6.

52. Sabadish & Mishel, *supra* note 50 at 2 (emphases added).

53. Mishel & Schieder, *supra* note 50, at 1, 6.

54. *See* Wei Lu, *Bloomberg Global CEO Pay Index*, BLOOMBERG NEWS (Dec. 28, 2017).

primarily caused by growth in the income of the top one percent of American earners.[55] The 2012 EPI study further establishes that this top-one-percent income growth is substantially due to rising executive compensation. According to the report, within the top 1% and top 0.1%, the majority of income gains accrued to households headed by executives or finance professionals.

> Executives, and workers in finance, accounted for 58 percent of the expansion of income for the top 1 percent and 67 percent of the increase in income for the top 0.1 percent from 1979 to 2005 . . . Households headed by a non-finance executive were associated with 44 percent of the growth of the top 0.1 percent's income share and 36 percent in the growth among the top 1.0 percent.[56]

Economist Joseph Stiglitz builds on these findings, attributing the growth in top incomes over the past three decades to "rent-seeking" by corporate executives.[57] Stiglitz defines rent-seeking as "getting an income not as a reward for creating wealth but by grabbing a larger share of the wealth that would have been produced anyway."[58] According to Stiglitz, rent-seekers typically destroy rather than create wealth in the process of funneling it away from others.[59] Thus, rather than promoting economic gains for society as a whole, expanding executive compensation has merely redistributed economic gains to the very top, and has destroyed some economic productivity in the process.

The established connection between rising executive compensation and America's ever-widening income gap highlights why stakeholder-primacy progressivism, due to its fundamental concern with economic inequality, should care deeply about constraining executive-compensation growth.

II. Executive Compensation Laws in the United States: Have They Worked?

In this Part, I describe and evaluate the United States's current executive-compensation legal regime, and explain how these laws have failed to limit executive-compensation growth. In Section II.A, I discuss the primary laws governing executive compensation in the United States today. I then delve more deeply into one of these laws—say on pay—in Section II.B and discuss

55. Piketty, Saez & Zucman, *supra* note 42, at 580; Saez, *supra* note 42, at 12-13; Sabadish & Mishel, *supra* note 50, at 1 ("Driving this ever-widening gap is the unequal growth in earnings enjoyed by those at the top. The average annual earnings of the top 1 percent of wage earners grew 156 percent from 1979 to 2007; for the top 0.1 percent they grew 362 percent….In contrast, earners in the 90th to 95th percentiles had wage growth of 34 percent, less than a tenth as much as those in the top 0.1 percent tier. Workers in the bottom 90 percent had the weakest wage growth, at 17 percent from 1979 to 2007.").

56. Sabadish & Mishel, *supra* note 50, at 2.

57. Joseph Stiglitz, *Inequality and Economic Growth*, 86 POL. Q. 134, 134 (2016).

58. *Id*. at 141.

59. *Id*.

its results since its enactment in 2011. I close Part II with a brief note on the early results of the CEO-worker pay ratio disclosure rule.

A. America's Executive Compensation Laws

United States law imposes five primary executive-pay-related regulations on U.S. public companies: 1) executive and director compensation disclosure requirements,[60] 2) corporate tax deductibility limitations on executive compensation over $1 million,[61] 3) state fiduciary duty laws,[62] 4) say on pay,[63] and 5) the CEO-median employee pay ratio disclosure requirement.[64] In this Section, I survey the first three of these laws, none of which impose meaningful limitations on executive compensation. I then turn to say on pay and the CEO-median employee pay ratio disclosure rule in the subsequent sections.

1. Executive Compensation Disclosure Requirements

The U.S. Securities and Exchange Commission (SEC) has required public companies to disclose their executive and director compensation in some form since 1938. In 1992, the SEC amended Item 402 of Regulation S-K (which lists information that must be disclosed in issuers' regular filings and proxy statements) to require "tabulated" disclosure of compensation, including a formatted summary compensation table that highlights the dollar value of director and executive compensation awards.[65] In 2006, the SEC further amended these requirements to add a narrative "Compensation Discussion and Analysis" summary of the "material factors underlying compensation policies and decisions," particularly how the issuers' executive-compensation policy is designed to respond to performance.[66] The amendments may have succeeded in providing enhanced executive-compensation information to shareholders, allowing the market to more accurately price corporate stock by factoring in executive-compensation expenditures. However, some think that the 1992 enhanced-disclosure rule also caused a ratcheting-up effect in executive pay, as

60. Executive Compensation and Related Person Disclosure, 71 Fed. Reg. 53,158 (Sept. 8, 2006) (to be codified at 17 C.F.R. pts. 228, 229, 232, 239, 240, 245, 249, 274).

61. I.R.C. § 162(m) (2018).

62. *See infra* Subsection II.A.3.

63. Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, § 953(b), 124 Stat. 1376 (2010); S.E.C. Rule 14a-21 (2018).

64. Regulation S-K, Item 402, 17 C.F.R. § 229.402 (2018); Dodd-Frank Wall Street Reform and Consumer Protection Act § 953(b).

65. *See* 57 Fed. Reg. 48,126, Executive Compensation Disclosure, S.E.C. Release No. 33-6962 (Oct. 16, 1992).

66. *See* Executive Compensation and Related Person Disclosure, 71 Fed. Reg. 53,158, 53,160 (Sept. 8, 2006) (to be codified at 17 C.F.R. pts. 228, 229, 232, 239, 240, 245, 249, 274).

management took note of how much competitors were paying and companies tried to outbid each other for top talent.[67]

2. Tax Deductibility Limitations

Another executive compensation policy of the 1990s was Section 162(m) of the Internal Revenue Code.[68] Concerned with excessive executive pay, Congress in 1993 adopted Section 162(m), which limited publicly traded corporations' ability to deduct executive compensation over $1 million. However, "[q]ualified performance-based" compensation, defined as compensation "payable solely on the account of the attainment of one or more performance goals," was exempted from the deductibility cap.[69] In the years following its enactment, this exception was much criticized for being a significant loophole and promoting high-value equity payouts, contributing to ballooning executive pay.[70] In response to this widespread criticism, the Tax Cuts and Jobs Act of 2017 eliminated the performance-based compensation exception to 162(m).[71] Analysis of company pay practices after the adoption of 162(m), though, shows that the elimination of the performance-based pay exception will likely have little effect on corporate pay packages. According to a ProPublica study of compensation at the 40 largest firms in the S&P 500, since 1992, the year before 162(m) became effective, executive compensation subject to the deductibility cap has risen almost twice as fast as fully deductible performance-based pay, far exceeding the $1 million cap.[72] This statistic indicates that 162(m)'s deductibility cap does not meaningfully constrain executive compensation awards, and so it is unlikely that the new 162(m) will have a significant effect on executive pay.

67. *See* DAN ARIELY, PREDICTABLY IRRATIONAL 17 (2009) ("Once salaries became public information, the media regularly ran special stories ranking CEOs by pay. Rather than suppressing the executive perks, the publicity had CEOs in America comparing their pay with that of everyone else. In response, executives' salaries sky-rocketed.").

68. Pub. L. No. 103-66, § 13211, 107 Stat. 312, 469-71 (1993) (codified at I.R.C. § 162(m) (2012)).

69. I.R.C. § 162(m)(4)(C) (2012).

70. Senator Warren, among others, criticized the old § 162(m) for this reason. *See* Max Ehrenfreund, *Why Elizabeth Warren Thinks Bill Clinton Made CEO Pay Even Worse*, WASH. POST (Apr. 27, 2015, 8:00 AM EST), https://www.washingtonpost.com/news/wonk/wp/2015/04/27/bill-clinton-tried-to-limit-ceo-pay-but-elizabeth-warren-thinks-he-made-it-worse [https://perma.cc/U45R-SZGU].

71. I.R.C. § 162(m) (2018); *see* Jean M. McLoughlin & Ron M. Aizen, *IRS Guidance on Section 162(m) Tax Reform*, HARV. L. SCH. FORUM ON CORP. GOV. & FIN. REG. (Sept. 26, 2018), https://corpgov.law.harvard.edu/2018/09/26/irs-guidance-on-section-162m-tax-reform [https://perma.cc/9SGD-T6RT].

72. *The Executive Pay Cap That Backfired*, PROPUBLICA (Feb. 12, 2016, 8:00 AM EST), https://www.propublica.org/article/the-executive-pay-cap-that-backfired [https://perma.cc/GJ7A-EGMK].

3. State Fiduciary Duty Law

Engaging in a full discussion of state fiduciary-duty law as it relates to executive compensation is beyond the scope of this Note. However, it is worth stating that current state fiduciary duty law, most pertinently Delaware law,[73] gives directors significant discretion in setting executive pay packages.[74] Under Delaware law, executive compensation decisions are primarily constrained by the corporate-waste doctrine, under which plaintiffs have the burden to prove that the compensation-setting process was "so one sided that no business person of ordinary, sound judgment could conclude that the corporation has received adequate consideration."[75] According to the Delaware Supreme Court, "[a] claim of waste will arise only in the rare, 'unconscionable case where directors irrationally squander or give away corporate assets.'"[76] In other words, plaintiffs must show that the board's decision cannot be "attributed to any rational business purpose."[77] As the bar for holding directors accountable for agreeing to excessive-compensation policies is quite high, very few executive-compensation shareholder suits prevail under Delaware law.[78] Most scholars believe that, as a result, Delaware law does not effectively limit corporate executive-compensation payouts.[79]

B. Say on Pay in the United States: Has it Worked?

As discussed above, the U.S. say-on-pay provision was enacted as section 951 of the Dodd-Frank Act in 2010.[80] Section 951, and its implementing rule by the SEC,[81] require that U.S. public companies give shareholders the opportunity to cast an advisory vote on the compensation of the corporation's executives as disclosed pursuant to Item 402 of Regulation S-K at least once every three years.[82] Related provisions of the Dodd-Frank Act also require

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73. Here, Delaware corporate fiduciary law is the most pertinent state fiduciary-duty law because the vast majority of large U.S. public companies are incorporated in Delaware. In 2018, 67.2% of Fortune 500 companies were incorporated in Delaware, and 82% of companies undergoin g a U.S.-based initial public offering chose to incorporate in Delaware. *Annual Report Statistics*, DEL. DIV. OF CORPS. (2018), https://corpfiles.delaware.gov/Annual-Reports/Division-of-Corporations-2018-Annual-Report.pdf [https://perma.cc/G734-QKAR].

74. Delaware law, however, does apply the stricter "entire fairness" test to directors' setting of their own compensation in the absence of shareholder ratification. *See, e.g.*, Calma v. Templeton, 114 A.3d 563 (Del. 2015).

75. *In re* The Walt Disney Co. Derivative Litigation, 906 A.2d 27, 74 (Del. 2006) (quoting Brehm v. Eisner, 746 A.2d 263 (Del. 2000)).

76. *Id*.

77. *Id*. (quoting *Sinclair Oil Corp*. *v*. *Levien*, 280 A.2d 717, 720 (Del. 1971)).

78. *See* Lisa M. Fairfax, *Sue on Pay: Say on Pay's Impact on Directors' Fiduciary Duties*, 55 ARIZ. L. REV. 1, 25-26 (2013).

79. *Id*. at 5.

80. Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, § 951, 124 Stat. 1376, 1899 (2010).

81. 17 C.F.R. § 240.14a-21(a) (2011).

82. *Id*.

corporations to give shareholders an advisory vote on the frequency of the say-on-pay vote and on so-called "golden parachute" severance packages following mergers or acquisitions.[83]

The say-on-pay provision was hotly debated in Congress, with critics voicing concerns about governmental intrusion into the boardroom and about hampering companies' ability to attract top talent.[84] Proponents of the provision voiced a general concern that executive compensation had become too high across all firms and emphasized their view that the shareholder vote would help stop the upward trend in CEO pay.[85] The policy debate on say on pay in the United States evidenced that its supporters expected that it would constrain general executive compensation levels and help slow the overall rate of compensation growth.[86]

So, has U.S. say-on-pay legislation achieved these goals? In the next two Subsections, I answer this question in the negative by citing findings showing that say on pay has not had a significant observable effect on overall compensation levels (Subsection II.B.1) and that say-on-pay voting patterns are most strongly linked to shareholder returns (Subsection II.B.2).

1. Say on Pay Has Not Had a Significant Effect on Executive Compensation Growth

Studies analyzing executive-compensation packages since mandatory say-on-pay voting became effective overwhelmingly indicate that say on pay has failed to slow the growth in executive-compensation levels in the United States. A 2018 EPI report finds that average executive pay levels have climbed steadily since the initiation of say-on-pay voting in 2011.[87] While CEO pay levels have not yet returned to the record highs of the early 2000s, average executive-compensation payouts have grown consistently since 2009, with a 17.6% gain in average compensation based on options realized just between 2016 and 2017.[88] The academic commentary on the first years of say on pay

83. Dodd-Frank Act § 951.

84. *See* Randall S. Thomas, Alan R. Palmiter & James F. Cotter, *Dodd-Frank's Say on Pay: Will it Lead to a Greater Role for Shareholders in Corporate Governance?*, 97 CORNELL L. REV. 1213, 1236 (2012).

85. *Id*. (citing H.R. REP. NO. 110-88, at 3 (2007) which notes that median CEO pay had grown to $13.5 million during the 2005 fiscal year at the 1,400 largest U.S. public companies).

86. Randall S. Thomas & Christoph Van der Elst, *Say on Pay Around the World*, 92 WASH. U. L. REV. 653, 729 (2015).

87. Mishel & Schieder, *supra* note 50, at 1, 6.

88. *Id*.

echoes this finding.[89] As recent executive compensation figures demonstrate, this trend continued into 2017 and 2018.[90]

Much of the scholarly commentary blames highly deferential shareholder voting as partially responsible for the lackluster effects of say-on-pay voting in the United States. Voting data gathered by the private research firm Proxy Insight supports this view, showing that the average percentage of shareholders voting for executive compensation packages at S&P 500 companies (rather than voting against or abstaining) is 91.7%.[91]

2. Say on Pay is a Vote on Firm Financial Performance

Several notable studies have concluded that shareholder "against" votes on executive compensation are highly correlated with poor firm financial performance, with shareholders only voting against pay packages at seriously underperforming firms.[92] A recent study reveals that share returns impact shareholder say-on-pay votes, independent of actual executive pay levels. Professors Jill Fisch, Darius Palia, and Steven Davidoff Solomon studied the effect of executive pay level, sensitivity of pay relative to economic performance, and economic performance on say-on-pay vote outcomes and found that, after controlling for executive pay level and pay sensitivity, firm performance (and thus shareholder return) still has a "substantial effect" on vote outcomes.[93] Consistent with earlier academic analysis, Fisch, Palia, and Solomon further find that "shareholders do not appear to care about executive compensation unless an issuer is performing badly."[94] This is a troubling result,

89. Peter Iliev & Svetla Vitanova, *The Effect of the Say-on-Pay Vote in the U.S.*, *in* MANAGEMENT SCIENCE 4451 (2019); Vincente Cuñat, Mireia Giné & Maria Guadalupe, *Say Pays! Shareholder Voice and Firm Performance*, 20 REV. OF FIN. 1799 (2015).

90. *See supra* Section I.B; Jacob Rund, *Pay Raises for U.S. CEOs Trend Toward 7-Year High, ISS Says*, BLOOMBERG LAW (Mar. 28, 2018, 5:06 PM), https://www.bloomberglaw.com/document/XB1HTLNG000000?bna_news_filter=employee-benefits&jcsearch=BNA%25200000016268e4dcf2a3eaefefe4810003#jcite [https://perma.cc/F2H9-LPEM].

91. *S&P500 SoP Voting 2018*, PAY TRACKER, PROXY INSIGHT (June 22, 2018) (on file with author).

92. TED ALLEN ET AL., INSTITUTIONAL S'HOLDER SERVS., PRELIMINARY 2011 U.S POSTSEASON REPORT 2 (2011) (cited in Thomas, Palmiter & Cotter, *supra* note 86, at 1248-49); Joseph E. Bachelder III, *Say-on-Pay Under Dodd-Frank*, HARV. L. SCH. FORUM ON CORP. GOV. & FIN. REG. (Sept. 17, 2011), https://corpgov.law.harvard.edu/2011/09/17/say-on-pay-under-dodd-frank [https://perma.cc/F8UK-NF8H]; Thomas, Palmiter & Cotter, *supra* note 84, at 1216; *see also* VOTING ANALYTICS: AN ANALYSIS OF VOTING RESULTS AND PERFORMANCE AT RUSSELL 3000 COMPANIES, EQUILAR 1 (July 2011), http://www.shareholderforum.com/sop/Library/20110728%20Equilar%20-%20Voting%20Analytics%20-%20An%20Analysis%20of%20Voting%20Results%20and%20Performance%20at%20Russell%203000%20Companies.pdf [https://perma.cc/4KCZ-25C5] (finding that, of the 38 Russell 3000 companies with negative say-on-pay votes in 2011, 73% were below the median total shareholder return for 2011).

93. Jill Fisch, Darius Palia & Steven Davidoff Solomon, *Is Say on Pay All About Pay? The Impact of Firm Performance*, 8 HARV. BUS. L. REV. 101, 101 (2018).

94. *Id.*

given that legislators and other proponents of say on pay had hoped it would dampen growth in executive compensation levels across all companies.

In the years since the Dodd-Frank say-on-pay provision came into effect, an ample body of scholarship has explored whether the policy has succeeded.[95] Most of this scholarship concludes that say on pay has not yet had a significant observable effect on executive-compensation levels for most U.S. public companies, with highly deferential say-on-pay votes for the vast majority of companies.[96] Some scholars, however, posit that say-on-pay votes may incentivize boards of directors to preemptively limit executive compensation awards in order to avoid a negative say-on-pay vote.[97] If this disciplining effect exists, it is likely small, because executive compensation levels have risen steadily since say on pay's enactment.[98] Other scholars find that, while say on pay has only a minor effect on executive salary levels, it positively impacts shareholder value, incentivizing executives to improve their firm's performance in anticipation of the shareholder say-on-pay vote.[99] But this potential benefit is unlikely to ameliorate income inequality because it delivers enhanced value only to shareholders, a group that is already overwhelmingly wealthy.[100]

C. CEO-Median Worker Pay Ratio Disclosure: Will It Work?

In August 2015, the SEC adopted a rule pursuant to Section 953(b) of the Dodd-Frank Act amending Item 402 of Regulation S-K to "require disclosure of the median of the annual total compensation of all employees of a registrant (excluding the chief executive officer), the annual total compensation of that registrant's chief executive officer," and the ratio of the two figures under newly added Item 402(u).[101] The final rule was adopted by a 3-2 Commission

95. *See, e.g.*, James F. Cotter et al., *The First Year of Say-on-Pay Under Dodd-Frank: An Empirical Analysis and Look Forward*, 81 GEO. WASH. L. REV. 967 (2013); Fisch, Palia & Solomon, *supra* note 93; Thomas, Palmiter & Cotter, *supra* note 84; Thomas & Van der Elst, *supra* note 86.

96. *See* Fisch, Palia & Solomon, *supra* note 93, at 102 ("Issuers have now experienced five years of say on pay votes, and the effect of the provision remains heavily debated. Although shareholders at a few issuers have rejected compensation plans, shareholders at the overwhelming majority of issuers vote to approve executive compensation, and the average percentage of votes in favor exceeds 90%. The link between say on pay and Chief Executive Officer (CEO) compensation is unclear-CEO pay continued to rise for the first several years after Dodd-Frank, declined in 2015, and rose to record levels in 2016."); *see also* Cotter et al., *supra* note 95, at 970; Thomas, Palmiter & Cotter, *supra* note 84, at 1216; Thomas & Van der Elst, *supra* note 86, at 661-662.

97. *See, e.g.*, Cotter et al., *supra* note 95, at 970 ("[M]andatory say on pay seems to have encouraged management to be more responsive to shareholder concerns about executive pay and corporate governance.").

98. *See supra* notes 87-92 and accompanying text.

99. *See* Cuñat, Giné & Guadalupe, *supra* note 89 at 4-5.

100. *See infra* notes 117-119 and accompanying text.

101. *See* Pay Ratio Disclosure, 80 Fed. Reg. 50,103 (Aug. 18, 2015) (amending 17 C.F.R. pts. 229 & 249).

vote after a series of delays that drew ire from Senator Warren[102] and others.[103] Despite much press attention when the rule became effective for all companies on January 1, 2017, it is unclear that shareholders have taken much notice of the new disclosure.[104] Furthermore, as I explain in Part III, there is evidence indicating that additional executive compensation disclosures are not meaningful to investors.[105]

III. Do Shareholders Understand and Care About Executive Compensation?

This Part argues that the failure of shareholder-focused executive-compensation laws to constrain executive pay levels should not be surprising, because shareholders, dispersed geographically, possess neither the capacity nor the incentives to effectively limit executive pay. I extend the implications of several recent studies that have provided greater insight into shareholder behavior and demographics. This Part applies, for the first time, these studies' findings to say-on-pay voting by dispersed U.S. shareholders and asserts that 1) shareholders do not understand executive compensation disclosures (Section III.A); 2) shareholders do not care strongly about levels of executive compensation at the firms in which they invest and instead care only about investment returns (Section III.B); and 3) shareholders are disincentivized to vote against pay packages at firms that are succeeding in the market, for fear of how a negative vote could affect the firm's stock price (Section III.C). Lastly, Section IV.D argues that, in addition to being ineffective, say-on-pay voting potentially worsens economic inequality by "ratifying" high pay and promoting short-termism and excessive risk-taking by corporate managers.

A. Shareholders Do Not Adequately Understand Executive Compensation

In this Section, I draw on the findings of a recent study of say-on-pay voting in the United Kingdom to assert that U.S. shareholders likely do not

102. *See* Letter from Senator Elizabeth Warren, U.S. Senate, to Mary Jo White, Chair, U.S. Sec. & Exch. Comm'n, *supra* note 21 (calling on Commissioner White to finalize and adopt the pay ratio disclosure rule).

103. *See, e.g.*, *Senators Weigh in on CEO-to-Worker Pay Ratio Rule During SEC Public Comment Period*, SEN. BOB MENENDEZ FOR NEW JERSEY (Nov. 26, 2013), https://www.menendez.senate.gov/news-and-events/press/senators-weigh-in-on-ceo-to-worker-pay-ratio-rule-during-sec-public-comment-period [https://perma.cc/MP7A-TERC] (describing the efforts of 13 Democrat senators to persuade the SEC to finalize the pay-ratio disclosure rule in a timely manner).

104. *See, e.g.*, *American Firms Reveal the Gulf Between Bosses' and Workers' Pay*, THE ECONOMIST (May 29, 2018), https://www.economist.com/graphic-detail/2018/05/29/american-firms-reveal-the-gulf-between-bosses-and-workers-pay [https://perma.cc/FMC4-DBHQ]; Anders Melin, *American CEO Pay is Soaring, But the Gender Pay Gap is Drawing the Rage*, BLOOMBERG BUSINESSWEEK (Aug. 21, 2018, 5:00 AM EST), https://www.bloomberg.com/news/articles/2018-08-21/american-ceo-pay-is-soaring-but-the-gender-pay-gap-is-drawing-the-rage [https://perma.cc/MMS9-H2B3] (reporting that CEO-worker pay ratio disclosures have not received significant attention from investors, particularly in comparison to corporate #MeToo scandals).

105. *See infra* Section III.A.

adequately understand executive-compensation disclosures. Extending the study's findings to the U.S. context, this Section argues that these findings undermine the legitimacy and effectiveness of say-on-pay voting and enhanced executive compensation disclosures such as CEO-median worker pay ratio disclosure.

Scholarship in the field of comparative corporate governance often uses policy outcomes in the United Kingdom to predict how similar policies might function in the United States, and vice versa.[106] Such cross-country comparison is sometimes ill-advised due to significant cultural and institutional differences between countries. Corporate-governance scholars generally consider the United States and the United Kingdom to have quite similar corporate governance landscapes due to the prevalence of dispersed share ownership in both countries, however, making U.K.-U.S. policy comparison more likely to offer meaningful insights.[107]

A 2018 study of say-on-pay voting behavior in the United Kingdom by Professors Gerner-Beuerle and Kirchmaier indicates that dispersed shareholders often base their votes on a faulty understanding of executive-compensation disclosures, and institutional shareholders generally rely on proxy advisory firms.[108] Gerner-Beuerle and Kirchmaier "do not find any evidence that [shareholders] assess the structure of a company's remuneration policy comprehensively."[109] The study further finds that shareholders primarily base their votes on the amount of remuneration received by the CEO in the previous year and the CEO's total remuneration opportunity in the next year, both highly incomplete measures of companies' executive compensation policies.[110] The total remuneration received figure excludes the often-substantial deferred remuneration awarded to the CEO, and the CEO's total remuneration opportunity is an imprecise indicator of what the executive can actually expect to receive, as it is the merely the highest end of a wide range of possible payouts.[111] These results should not lead to the conclusion that shareholders care about limiting top-level pay generally. Rather, these findings show that in deciding whether to vote "for" or "against" executive pay packages, shareholders primarily rely on imprecise and incomplete indicators of executives' total compensation awards.[112]

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106. *See, e.g.*, Jeffrey N. Gordon, *Say on Pay: Cautionary Notes on the U.K. Experience and the Case for Shareholder Opt-In*, 46 HARV. J. ON LEGIS. 323 (2009) (using the UK experience with Say on Pay to predict how Say on Pay will fare in the United States); Thomas & Van der Elst, *supra* note 86 (same).

107. Luca Enriques et al., *Shareholder Interests*, *in* THE ANATOMY OF CORPORATE LAW (John Armour ed., 3d ed. 2017).

108. Carsten Gerner-Beuerle & Tom Kirchmaier, *Say on Pay: Do Shareholders Care?* (ECGI Working Paper No. 579, 2018).

109. *Id*. at 1.

110. *Id*. at 4.

111. *Id*. at 4-5.

112. *See id*. at 27-28.

Applied to the United States, these findings suggest that shareholder say-on-pay voting may often be underinformed. If shareholders are poorly informed about executive-compensation policies, it seems less likely that they will be able to use say-on-pay voting to exert meaningful influence on these policies. These findings further cast doubt on whether enhanced executive compensation disclosures—most pertinently CEO-median worker pay ratio disclosure—better enable shareholders to discipline corporations for excessive executive pay. If shareholders do not process additional compensation disclosures and incorporate this information into their voting and stock ownership decisions, it seems unlikely that further enhancements of disclosure regulations will lead to additional constraints on executive compensation.

B. Shareholders Lack the Incentives to Care About High Executive Pay

In this Section, I draw on research analyzing the socioeconomic characteristics of American shareholders to assert that U.S. shareholders lack adequate incentives to constrain high executive compensation. Since the rise of equity ownership by middle- and working-class families through defined-contribution plans in the 1970s, a greater portion of American households have owned some publicly traded shares,[113] creating a perception that the shareholder class is representative of the American public.[114] Given the established connection between rising executive compensation and growing economic inequality, if shareholders were in fact representative of the American public, then at least some shareholders would be motivated to control executive compensation levels, because high executive pay contributes to the dynamic that has depressed income growth for all income brackets below the top 10%.[115] If shareholders are typically members of the top 10% of wealth holders, however, they will not be personally harmed by economic inequality, and thus will only be motivated to limit executive compensation to the extent it hurts their investment returns. According to the Efficient Capital Markets Hypothesis, the amount of executive compensation paid out by a public company is already incorporated into the stock price paid by the shareholder, so unless there is an unexpected increase in the company's total executive compensation while the shareholder owns the shares,[116] the shareholder's return will not be negatively impacted. Shareholders in the top 10% will thus not be

113. *See* Martin Gelter, *The Pension System and the Rise of Shareholder Primacy*, 43 SETON HALL L. REV. 911, 911 (2013).

114. *Id*.

115. *See* discussion *supra* Part I. This reasoning rests on the assumption that for some hypothetical group of shareholders below a certain income level, the potential benefits of constraining income inequality would outweigh the potential costs of harming the company's stock returns.

116. Robert J. Rhee, *Intrafirm Monitoring of Executive Compensation*, 69 VAND. L. REV. 695, 734 (2016). Unexpected increases in compensation would likely only cause shareholders to discipline boards in the rare case that total compensation payouts unexpectedly increase, *and* the firm performs worse than or just as expected, leading to a net decrease in the stock price.

personally incentivized to constrain high executive compensation absent an unexpected compensation increase.

A recent 2013 study confirms that the vast majority of U.S. public company shares are held by the wealthiest 10% of American households,[117] finding that in 2007 the top 10% of U.S. wealth holders owned 81% of U.S.-public-company shares, with the top 1% owning 38%. The bottom 80% of wealth holders owned only 9% of U.S.-public-company shares.[118] Even as public stock ownership has "diffused downward," this trend has done "nothing to erode the percentage share of the top ten percent of households."[119]

Given that 81% of U.S. public company shares are held by the wealthiest 10% of households, and this top 10% lacks incentives to constrain executive compensation merely because it is excessive, it seems unlikely that significant numbers of shareholders will vote against high pay packages absent poor shareholder returns. This theory is supported by say-on-pay voting data, which shows that 91.7% of voting shareholders on average vote for executive pay packages, and that shareholders only vote against executive compensation when the company has performed poorly in the market.[120]

C. Shareholders Are Reluctant to Vote "Against" Due to Expected Market Response

In addition to the fact that shareholders lack sufficient incentive to vote against excessive compensation packages, shareholders may be disincentivized from voting against say-on-pay proposals for fear that the announcement of a low say-on-pay vote could negatively affect the market price of their shares. A recent paper studying the behavior of institutional investors provides evidence of this dynamic: Schwartz-Ziv and Wermers conducted an events study to observe the market reaction to the announcement of a low say-on-pay vote result (i.e., where a significant percentage of shareholders voted against the company's executive compensation packages).[121] The authors found that the market responds negatively to the announcement of a low say-on-pay vote.[122] This finding further explains why shareholders may be reluctant to vote against

117. William W. Bratton & Michael L. Wachter, *Shareholders and Social Welfare*, 36 SEATTLE U. L. REV. 489, 490 (2013).

118. *Id*. at 518.

119. *Id*. at 510, 518.

120. *See supra* note 91 and accompanying text.

121. Miriam Schwartz-Ziv & Russ Wermers, *Do Institutional Investors Monitor Their Large vs. Small Investments Differently? Evidence from the Say-On-Pay Vote* (Eur. Corp. Gov. Inst. Working Paper No. 541, 2018).

122. *Id*. at 3 ("We find that the announcements of low support rates are indeed followed by negative cumulative abnormal returns (CARs). For example, during a nine-day event window around the vote (-4,+4), the average abnormal return across companies that receive SOP support rates below 70% is approximately 0.79% lower than that of companies receiving support rates equal to or exceeding 70%.").

corporate compensation packages: a low vote could hurt the market value of their shares.

D. Say on Pay Potentially Contributes to Economic Inequality

As established in Parts II and III, there is significant reason to believe that say-on-pay legislation is an ineffective regulator of rising executive compensation in the United States. Is it a harmful policy, though? In this Section, I argue that, yes, say on pay does have the potential to contribute to economic inequality. For one, a favorable say-on-pay vote may act as an informal "ratifying" mechanism for massive executive pay packages.[123] A highly deferential say-on-pay vote may diminish the power of the so-called "outrage constraint."[124] Professors Lucian Bebchuk and Jesse Fried (themselves supporters of say on pay and other shareholder-power-enhancing policies) famously posited that in the absence of strong mechanisms for shareholders to regulate executive compensation, executive pay may still be constrained by the "outrage" of the general public when they perceive an executive pay award to be "unjustified" or "egregious."[125] Favorable say-on-pay voting may defuse potential outrage over high corporate pay awards, limiting the public's ability to act as an external constraint on executive-compensation growth.

Say-on-pay voting could also promote short-termism and excessive risk-taking by corporate managers. As Fisch, Palia, and Solomon assert, because shareholder say-on-pay voting outcomes are highly correlated with the company's short-term stock performance, executives may feel pressure to maximize short-term stock price instead of investing in long-term value creation.[126] The authors further argue that say-on-pay voting could promote excessive risk-taking by corporate managers trying to maximize their respective companies' short-term stock price.[127] Most shareholders will be

123. This is not a claim that say-on-pay voting can act as shareholder ratification for the purposes of state fiduciary-duty law (and, indeed, section 951 of the Dodd-Frank Act expressly provides that the shareholder vote does not "create or imply any change to the fiduciary duties" of the issuer or its board). Dodd-Frank Act § 951(c).

124. Professor Minor Myers was the first to make this argument. *See* Minor Myers, *The Perils of Shareholder Voting on Executive Compensation*, 36 DEL. J. CORP. L. 417, 421 (2011) (arguing that shareholder voting on executive compensation may "cloud[] the functioning of the outrage constraint").

125. LUCIAN BEBCHUK & JESSE FRIED, PAY WITHOUT PERFORMANCE: THE UNFULFILLED PROMISE OF EXECUTIVE COMPENSATION 65 (2004); *see* Paul Krugman, Opinion, *The Outrage Constraint*, N.Y. TIMES (August 23, 2002), https://www.nytimes.com/2002/08/23/opinion/the-outrage-constraint.html [https://perma.cc/9NCZ-3E62] (describing Bebchuck & Fried's outrage constraint theory); *see also* Kym Maree Sheehan, *Is the Outrage Constraint an Effective Constraint on Executive Remuneration? Evidence from the UK and Preliminary Results from Australia* (Working Paper, 2007) (on file with author) (discussing Bebchuk & Fried's theory at length).

126. Fisch, Palia & Solomon, *supra* note 93, at 126.

127. *Id*. at 127.

sufficiently diversified to bear this risk,[128] but other stakeholders—such as workers, local community members, and society—could be harmed.[129]

IV. The Progressive Stakeholder Primacy Movement: Can It Solve American Economic Inequality?

In this Part, I engage in the first academic analysis of the emerging progressive stakeholder-primacy movement's executive compensation policy proposals. A strong stakeholder-primacy approach to executive compensation would avoid the pitfalls of the United States' current executive compensation laws by eschewing reliance on shareholders to discipline corporate boards in their compensation decisions. As the discussion in Parts II and III has shown, policies that rely on enhanced disclosures and shareholder participation to constrain executive compensation have failed in the past and will likely continue to fail, because shareholders lack both the ability to adequately understand compensation disclosures and the incentives to discipline corporate compensation policies.[130] Laws that target compensation levels only indirectly, such as by limiting tax deductibility, or laws that target only one form of compensation are also unlikely to succeed, as the history of Section 162(m) has demonstrated.[131] Thus an effective stakeholder-primacy approach to executive-compensation regulation would directly restrain the board of directors in their pay-setting practices for all forms of executive compensation.

Progressive stakeholder primacy has enormous potential to address rising economic inequality, but, as established in Parts I, II, and III of this Note, it will not do so sufficiently without strong policies specifically targeting executive compensation. My analysis finds that several of the movement's policy proposals have potential to address executive pay, but that progressive politicians have not yet articulated a strong vision for effectively controlling executive compensation growth. This finding is unexpected and inconsistent with these politicians' stated concern with corporate excess and its contribution to economic inequality.

I begin in Section IV.A with the contemporary scholarly debate over whether corporate managers should primarily serve shareholders or also serve the interests of other stakeholders: workers, consumers, local communities, and society as a whole. In Section IV.B, I document stakeholder primacy's recent emergence in U.S. politics, led by congressional Democrats such as Elizabeth

128. *See id*.

129. Notably, the risk-taking incentive described could result in broader systemic harms which hurt the value of even diversified shareholders' portfolios by negatively impacting all firms. *See* John Armour & Jeffrey N. Gordon, *Systemic Harms and Shareholder Value*, 6 J. LEGAL ANALYSIS 35, 35 (2014). However, as Fisch, Palia, and Solomon's analysis suggests, it does not seem that this risk is sufficiently salient to shareholders to alter their voting behavior. *See* Fisch, Palia & Solomon, *supra* note 93, at 127.

130. *See supra* Parts II and III.

131. *See supra* Subsection II.A.2.

Warren, Bernie Sanders, Chuck Schumer, Tammy Baldwin, and Cory Booker. I analyze several of these politicians' proposed executive-pay-related policies and find that they would not effectively limit executive-compensation payouts. In Section IV.C, I turn to Senator Warren's Accountable Capitalism Act and analyze several of its provisions, explaining why they would not effectively constrain executive compensation growth either.

A. The Contemporary Scholarly Debate: Stout v. Bebchuk

As discussed in the Introduction, shareholder primacy began as a somewhat revolutionary, conservative rethinking of the corporate purpose in the 1970s and became the dominant theory through the 1980s and 90s. In the early 2000s, shareholder-focused policies were adopted en masse by Democrats as an asserted tool to discipline the corruption and excess of corporate managers, particularly by constraining executive compensation.[132] Professor Lucian Bebchuk (along with frequent co-author Jesse Fried) authored a body of scholarship that aimed to rein in executive pay policies by enhancing shareholders' power to influence and control management.[133] This work asserted that the corporation should not only primarily serve shareholders (the traditional shareholder primacy view), but also that shareholders should have more control over corporate management.[134]

According to Bebchuk, the problem with executive pay is "board capture"—a dynamic whereby executives wield significant influence over boards of directors and compromise arm's-length bargaining, allowing them to secure highly lucrative pay packages untethered from any measure of performance.[135] The solution, according to Bebchuk and his co-authors is corporate governance reform that makes boards "more accountable to shareholders."[136] Bebchuk's ideas were often cited by U.S. political proponents of say on pay, including President Barack Obama.[137]

132. *See supra* Introduction.

133. *See* BEBCHUK & FRIED, *supra* note 125; Lucian A. Bebchuk, Jesse M. Fried & David I. Walker, *Managerial Power and Rent Extraction in the Design of Executive Compensation*, 69. U. CHI. L. REV. 751 (2002); Lucian A. Bebchuk & Jesse M. Fried, *Executive Compensation as an Agency Problem*, 17 J. ECON. PERSPECTIVES 71 (2003); Lucian A Bebchuk, Alma Cohen & Holger Spamann, *The Wages of Failure: Executive Compensation at Bear Sterns & Lehman 2000-2008*, 27 YALE J. ON REG. 257 (2010); Lucian A. Bebchuk & Holger Spamann, *Regulating Banker's Pay*, 98 GEO. L.J. 247 (2010).

134. *See* Lucian A. Bebchuk, *The Case for Increasing Shareholder Power*, 118 HARV. L. REV. 833 (2005); Lucian A. Bebchuk, *The Myth of the Shareholder Franchise*, 98 VA. L. REV. 675 (2007); Lucian A. Bebchuk, *The Long-Term Effects of Hedge Fund Activism*, 115 COLUM. L. REV. 1085 (2015).

135. BEBCHUK & FRIED, *supra* note 125, at ix.

136. *Id*. at 2.

137. *See, e.g.*, *Obama Imposes Limits on Executive Pay*, NBC NEWS (Feb. 4, 2009, 8:13 PM EST), http://www.nbcnews.com/id/29003620/ns/business-us_business/t/obama-imposes-limits-executive-pay [https://perma.cc/N2TP-NZDL] ("'This is America. We don't disparage wealth. We don't begrudge anybody for achieving success,' Obama said. 'But what gets people upset—and rightfully so—are executives being rewarded for failure. Especially when those rewards are subsidized by U.S. taxpayers.'").

While Bebchuk represents the majority view in American legal academia,[138] he has long had two sets of critics. One set, led by Professor Stephen Bainbridge, argues that U.S. corporate law empowers the board of directors to make most decisions for the company unilaterally because this system is more efficient.[139] Bainbridge calls this view "director primacy."[140] The other, spearheaded by Professor Lynn Stout, asserts that rather than solely existing to maximize shareholder value, corporations must serve the interests of a broad range of stakeholders—consumers, workers, local communities, and society—in addition to promoting the interests of shareholders.[141] From a policy perspective, argues Stout, shareholder primacy simply does not work: it harms society and also, ironically, hinders shareholder value by focusing on short-term returns at the expense of long-term development.[142]

From a legal perspective, shareholder primacy is not actually law. For one, shareholders do not actually "own" the corporation—the corporation is a legal entity that owns itself.[143] Further, outside of bankruptcy, shareholders are not actually the residual claimants on the corporation's profits.[144] Finally, the relationship between shareholders and directors is not, in fact, a principal-agent relationship, because shareholders do not have the legal authority to control directors.[145] The best corporate-governance approach, Stout maintains, is one that empowers the board to sufficiently promote the interests of all stakeholders, rather than making directors beholden solely to shareholders.[146]

B. The Emerging Progressive Stakeholder Primacy Movement

Though shareholder primacy maintains a stronghold in the academy, Stout's theory of stakeholder primacy is swiftly gaining ground in U.S. politics.[147] In just the past year, in addition to Senator Warren's Accountable

138. *See, e.g*., Henry Hansmann & Reinier Kraakman, *The End of History for Corporate Law*, 89 GEO. L.J. 439 (2001) (asserting that corporate law around the world is converging toward shareholder primacy, and arguing that shareholder primacy's widespread success is warranted); Jonathan Macey, *Sublime Myths: An Essay in Honor of the Shareholder Value Myth and the Tooth Fairy*, 91 TEX. L. REV. 911 (2013) (reviewing Lynn Stout's "The Shareholder Value Myth" and arguing for shareholder primacy theory).

139. *See* STEPHEN M. BAINBRIDGE, THE NEW CORPORATE GOVERNANCE IN THEORY AND PRACTICE, Preface (2008).

140. *Id*.

141. *See* LYNN A. STOUT, THE SHAREHOLDER VALUE MYTH: HOW PUTTING SHAREHOLDERS FIRST HARMS INVESTORS, CORPORATIONS, AND THE PUBLIC (2012).

142. *Id*. at 8-9.

143. *Id*. at 8.

144. *Id*.

145. *Id*.

146. *Id*. at 10-11.

147. Based on significant recent developments, it also seems that stakeholder primacy is making headway in U.S. business culture. In August 2019, the Business Roundtable issued a new Statement on the Purpose of a Corporation, signed by 181 CEOs committing "to lead their companies for the benefit of all stakeholders—customers, employees, suppliers, communities and shareholders." *Business Roundtable Redefines the Purpose of a Corporation to Promote "An Economy That Serves All*

Capitalism Act, congressional Democrats have introduced four major legislative proposals that would require corporate boards to better balance the interests of stakeholders with those of shareholders. Across the aisle, Republican Senator Marco Rubio (FL) recently introduced his own stakeholder-oriented policy proposal.

This Section makes several findings about the emerging stakeholder primacy movement's policy proposals. First, the policies themselves and the rhetoric used to promote them indicate that prominent Democrat politicians are swiftly abandoning shareholder primacy in favor of stakeholder primacy.

Marco Rubio's adoption of similar policies and rhetoric could indicate that more conservatives will move toward stakeholder-oriented politics. Second, while these policy proposals contain provisions designed to address executive compensation indirectly, only one proposal contains a provision that places direct limits on executive compensation. Perplexingly, this provision was dropped in a more recent version of the legislation. Third, as asserted throughout this Section, the proposed indirect limits on executive compensation are unlikely to be effective. Stakeholder primacy progressivism's inability to control executive compensation would be a critical failure for economic inequality, because, as economists such as Piketty, Saez, and Stiglitz have established, executive compensation is a key driver of economic inequality in the United States.[148] This Section discusses and analyzes each of these policy proposals individually before turning to a more extensive analysis of Warren's Accountable Capitalism Act in the next Section.

1. The Stop WALMART Act

In November 2018, Senator Bernie Sanders (I-VT) and Representative Ro Khanna (D-CA) introduced the Stop WALMART Act.[149] The legislation would prohibit companies with over 500 employees from initiating stock buybacks unless they adopt a set of worker-protective policies.[150] In order for companies covered by the bill to engage in share buybacks, they would need to 1) pay all employees at least $15 per hour, 2) allow employees to earn up to seven days of paid sick leave, and 3) maintain a CEO-median employee pay ratio no higher than 150.[151] The Stop WALMART Act contains several promising provisions

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Americans", BUSINESS ROUNDTABLE (Aug. 19, 2019), https://www.businessroundtable.org/business-roundtable-redefines-the-purpose-of-a-corporation-to-promote-an-economy-that-serves-all-americans [https://perma.cc/M94M-LVAS].

148. *See supra* Section I.C.

149. *See* Stop WALMART (Welfare for Any Large Monopoly Amassing Revenue from Taxpayers) Act of 2018, S. 3410, 115th Cong. (2018).

150. *Id*. § 2.

151. *Sanders, Khanna Introduce the Stop WALMART Act to Put Workers Over Shareholders*, SEN. BERNIE SANDERS (Nov. 15, 2018), https://www.sanders.senate.gov/newsroom/press-releases/sanders-khanna-introduce-the-stop-walmart-act-to-put-workers-over-shareholders [https://perma.cc/38WT-94A8].

that could help address economic inequality, but, save for the pay-ratio cap, would not effectively limit executive compensation. Notably, in a more recently announced, broader-focused version of the Stop WALMART Act, discussed in Subsection IV.B.2, Senator Sanders appears to have dropped the pay-ratio-cap provision.

Limiting stock buybacks could, in theory, help reduce corporate payouts to shareholders and executives. Corporate stock buybacks contribute to economic inequality by enriching shareholders and corporate executives (who generally own a significant equity stake in their company due to stock-based compensation) while depriving workers, consumers, and communities of economic value.[152] Many think that corporate managers are motivated to promote stock buybacks due to the incentive structures built into their compensation packages, which often award higher payouts for meeting certain share-related benchmarks, such as earnings per share, return on equity, and share price.[153] These performance measures typically improve following a stock buyback, because the company's earnings are distributed among fewer outstanding shares.[154] Corporate share buybacks surged in 2018, likely because the Tax Cuts and Jobs Act lowered corporate tax rates, freeing up corporate funds to buy back additional stock.[155]

Limitations on stock buybacks, however, are unlikely to significantly constrain corporate payouts to executives. For one, corporations have other ways to distribute funds to executives that would not be hindered by the proposed stock-buyback limitation. Corporations could respond by paying higher dividends to shareholders—using the same funds to enrich shareholders over time rather than buying them out.[156] While higher dividends might be superior to share buybacks because they reward long-term shareholders, they would still funnel corporate funds to shareholders and executives rather than

152. Under this theory, the funds that corporations use to purchase their stock from shareholders could instead be used to pay employees higher wages, lower the prices or improve the quality of goods, or engage in long-term investment. *See* Lenore Palladino, *The $1 Trillion Question: New Approaches to Regulating Stock Buybacks*, 36 YALE J. ON REG. BULLETIN (2018), http://yalejreg.com/the-1-trillion-question-new-approaches-to-regulating-stock-buybacks [https://perma.cc/9T2U-BE3L].

153. *See* James Reda, *How Stock Buybacks Can Affect Executive Compensation*, COLUM. L. SCH. BLUE SKY BLOG (Aug. 3, 2018), http://clsbluesky.law.columbia.edu/2018/08/03/how-stock-buybacks-can-affect-executive-compensation [https://perma.cc/5YRJ-XH4B].

154. *Id*.

155. Anne Marie Knott, *Why the Tax Cuts And Jobs Act (TCJA) Led To Buybacks Rather Than Investment*, FORBES (Feb. 21, 2019, 4:47 PM), https://www.forbes.com/sites/annemarieknott/2019/02/21/why-the-tax-cuts-and-jobs-act-tcja-led-to-buybacks-rather-than-investment/#9737eef37fbc [https://perma.cc/F56J-Q9QN].

156. Shareholders tend to prefer buybacks over dividends if they can earn a higher return by investing their money elsewhere. Additionally, some dividends are taxed at ordinary-income tax rates (though many are taxed at capital-gains rates), while proceeds from buybacks are always taxed at the lower capital gains rates. *See, e.g.*, Dylan Scott & Emily Stewart, *Marco Rubio's Plan to Fix the GOP Tax Cuts Starts with Stock Buybacks*, VOX (Feb. 20, 2019, 8:30 AM EST), https://www.vox.com/policy-and-politics/2019/2/20/18225086/marco-rubio-stock-buybacks-tax-plan?fbclid=IwAR0sqlK3LhbhArB-B1VimqLRQVDhoFW1P1kphWhw20GZjzFuReJC-eNVk [https://perma.cc/9MWZ-YNHW]

investing these funds in workers and long-term growth. Corporate management might also respond to share-buyback limitations by paying a greater portion of executive compensation in cash rather than equity.

More fundamentally, excessive and poorly designed executive compensation packages incentivize stock buybacks, but it is not clear that the causal connection runs the other way.[157] As discussed above, stock buybacks are just one way for corporate executives to ensure that they can easily reap the benefits of excessive pay. While reducing equity compensation and amending performance-based incentive compensation triggers could reduce incentives for corporate executives to promote share buybacks, it does not follow that limiting stock buybacks would result in lower executive compensation levels.

The proposed $15 minimum wage and mandatory employee benefits could also help address economic inequality. Undoubtedly, higher worker wages and greater benefits are a key component of any comprehensive plan to resolve economic inequality in the United States. It is not clear, however, that these measures would result in lower executive compensation payouts. Walmart's January 2018 wage increase provides an example of how large corporations could respond to pressure to raise worker wages. In early 2018, Walmart announced that it would raise entry-level wages to $11 per hour, but on the same day announced that it would close 63 of its Sam's Club stores and lay off thousands of workers.[158] Walmart did not reduce its executive compensation payouts in fiscal year 2018 and in fact paid its executives larger bonuses than they were set to receive under the terms of their publicly disclosed incentive compensation policies.[159] This example, though merely anecdotal, shows that higher worker wages will not necessarily lead to lower executive compensation.

The pay-ratio cap provision is the only policy that has been proposed as part of the progressive stakeholder primacy movement that would impose a direct limitation on corporate boards in setting executive compensation. As Part V asserts, the pay-ratio cap has strong potential to directly limit executive compensation levels.[160] Troublingly, Senator Sanders seems to have dropped the pay-ratio cap from a planned bill that would extend the proposals of the

157. One industry commentator has made a similar argument, describing the proposed limitations on stock buybacks as addressing the "symptoms" but not the "disease." Roger L. Martin, *Stock Buybacks Are a Problem But the Sanders-Schumer Solution Is Not the Answer*, BARRON'S (Feb. 7, 2019, 8:00 AM EST), https://www.barrons.com/articles/stock-buybacks-ban-wont-fix-the-problem-51549495689 [https://perma.cc/5GR3-6DAW].

158. Nandita Bose, *Walmart Hikes Minimum Wage, Announces Layoffs on Same Day*, REUTERS (Jan. 11, 2018, 8:10 AM), https://www.reuters.com/article/us-walmart-wages/walmart-hikes-minimum-wage-announces-layoffs-on-same-day-idUSKBN1F01N8 [https://perma.cc/YF2D-D85T].

159. Alicia Ritcey et al., *Walmart Said It Would Cut the CEO's Bonus Last Year. It Didn't.*, BLOOMBERG (Apr. 25, 2018, 4:07 PM EST), https://www.bloomberg.com/news/articles/2018-04-25/walmart-said-it-would-cut-ceo-s-bonus-last-year-and-then-didn-t [https://perma.cc/4R3V-W44Z].

160. *See infra* Section V.A.

Stop WALMART Act to a broader set of companies, discussed in the next Section.

2. Senator Bernie Sanders's and Senator Chuck Schumer's Corporate Stock Buyback Bill

In early February 2019, senators Bernie Sanders and Chuck Schumer (D – NY) announced planned legislation[161] to prohibit corporations from buying back their own stock unless they "invest[] in workers and communities first, including things like paying all workers at least $15 an hour, providing seven days of paid sick leave, and offering decent pensions and more reliable health benefits."[162] Perplexingly, the proposal includes all of the major provisions of the Stop WALMART Act *except* for the CEO-median worker pay ratio cap. As discussed above in Subsection IV.B.1, the pay-ratio cap is the only proposed provision that would impose effective, direct limits on executive compensation levels.

Another striking aspect of this proposal is the rhetoric Sanders and Schumer have used to contextualize it. In announcing the proposal, Sanders and Schumer framed it as a sharp rejection of shareholder primacy, parroting much of the language Senator Warren used six months before in announcing the Accountable Capitalism Act:

> From the mid-20th century until the 1970s, American corporations shared a belief that they had a duty not only to their shareholders but to their workers, their communities and the country that created the economic conditions and legal protections for them to thrive. . . . But over the past several decades, corporate boardrooms have become obsessed with maximizing only shareholder earnings to the detriment of workers and the long-term strength of their companies, helping to create the worst level of income inequality in decades.[163]

This rhetoric is especially remarkable because neither politician has ever articulated this view of shareholder primacy before. Senator Sanders, though he has focused much of his political career on addressing income inequality, corporate greed, and the need for corporate social responsibility,[164] has never before taken a stated position on shareholder primacy. Senator Schumer, notably, was an outspoken advocate for shareholder power not even a decade

161. As of August 19, 2019, Senators Sanders and Schumer had not yet introduced this legislation nor released a draft of the bill.

162. *See* Schumer & Sanders, *supra* note 22.

163. *Id*.

164. *See, e.g.*, Ritsa Gountoumas, *The Hybrid Approach: Balancing a Corporation's Economic Desires Against Its Social Responsibility*, 17 U.C. DAVIS BUS. L.J. 197, 197-98 (2016) (discussing Sanders's views on these issues); N.Y. Daily News Editorial Bd., *Transcript: Bernie Sanders Meets with the Daily News Editorial Board, April 1, 2016*, N.Y. DAILY NEWS (Apr. 4, 2016) https://www.nydailynews.com/opinion/transcript-bernie-sanders-meets-news-editorial-board-article-1.2588306 [https://perma.cc/D9UK-GY69] (same).

ago. As discussed in the Introduction, in 2009, Schumer introduced the Shareholder Bill of Rights Act,[165] which included a suite of shareholder-power-enhancing policies, including say on pay, mandatory proxy-statement disclosure of golden-parachute arrangements, and shareholder-friendly proxy access rules.[166] The anti-shareholder-primacy rhetoric used by Senators Sanders and Schumer, as well as Schumer's sudden change in position on shareholder primacy, indicates that progressive stakeholder primacy is swiftly gaining political traction.

3. The Reward Work Act

In March 2018, Senator Tammy Baldwin (D-WI) introduced the Reward Work Act,[167] which would "improve[] disclosure of [stock] repurchases and require[] public companies to give workers the right to directly elect one-third of their company's board of directors."[168] Senator Baldwin also explicitly targeted shareholder primacy in discussing the bill, asserting that corporate profits overwhelmingly go to "wealthy shareholders" and should instead "be shared with the workers who actually create value."[169] In October 2018, Senator Baldwin turned her focus to regulatory reform, calling on the SEC to consider the merits of directly electing workers to public company boards, and "address the obligations of corporations to all of their public stakeholders, including employees, consumers, local communities, and taxpayers—in addition to public shareholders."[170]

While mandating worker board representation and creating an express duty to stakeholders are both reasonable, stakeholder-oriented policy proposals, neither would impose strong limits on executive compensation. As discussed further in Subsection IV.C.2, evidence from Germany, where worker board representation has been mandatory for decades, indicates that this policy would likely not result in lower executive compensation levels.[171] Additionally, it is

165. Shareholder Bill of Rights Act of 2009, S. 1074, 111th Cong. (2009).

166. *See supra* Introduction. Senator Schumer's seeming duplicity on shareholder rights is perhaps not surprising, as he has long been accused of hypocrisy in trying to appeal to populism while remaining beholden to wealthy donors and the financial industry. *See, e.g.*, Brian Montopoli, *Charles Schumer's Wall Street Dance*, CBS NEWS (June 29, 2011, 3:20 AM), https://www.cbsnews.com/news/charles-schumers-wall-street-dance [https://perma.cc/R3SN-UF7E].

167. Reward Work Act, S. 2605, 115th Cong. (2018).

168. *U.S. Senator Tammy Baldwin Introduces Legislation to Rein in Stock Buybacks and Give Workers a Seat at the Table*, U.S. SEN. TAMMY BALDWIN (Mar. 22, 2018), https://www.baldwin.senate.gov/press-releases/reward-work-act [https://perma.cc/ZH2C-BQJ8].

169. *Id*.

170. *See U.S. Senator Tammy Baldwin Leads Effort to Give Workers a Greater Voice at Public Companies*, U.S. SEN. TAMMY BALDWIN (Oct. 16, 2018), https://www.baldwin.senate.gov/press-releases/baldwin-leads-effort-to-give-workers-a-greater-voice-at-public-companies [https://perma.cc/VDB4-XUNV]. The letter to the SEC was also signed by Senators Sherrod Brown (D-OH), Cory Booker (D-NJ), Kirsten Gillibrand (D-NY), Elizabeth Warren (D-MA), Ben Cardin (D-MD), Chris Van Hollen (D-MD), Bernie Sanders (D-VT), Edward Markey (D-MA), Mazie Hirono (D-HI), Kamala Harris (D-CA), Jeff Merkley (D-OR) and Patty Murray (D-WA). *Id.*

171. *See infra* notes 204-206 and accompanying text.

far from certain that creating an express duty to stakeholders would promote direct constraints on executive pay.[172]

4. The Worker Dividend Act

Also in March 2018, Senators Cory Booker (D-NJ) and Bob Casey (D-PA) introduced a bill[173] requiring U.S. public companies that buy back shares to "also pay out a commensurate sum to all of its employees – the 'workers dividend.'"[174] Senator Booker targeted shareholder-value maximization and short-termism in announcing the Worker Dividend Act: "Today, a culture of 'short-termism' pervades industry and financial markets, as companies prioritize short-run returns to investors and executives over investments in workers, like higher wages and expanded training, which pay off over the long run."[175] But, as asserted in the earlier discussion of the Stop WALMART Act, it is uncertain that limiting stock buybacks and increasing payments to workers would lead to lower executive compensation payouts.[176]

5. Marco Rubio's Stock Buyback Proposal

Stakeholder-primacy progressives seem to have gained an unlikely ally in Senator Marco Rubio (R-FL). In a December 2018 *Atlantic* opinion piece,[177] and later in a series of tweets in February 2019,[178] announced a plan to correct the "tax advantage for buybacks over dividends" by taxing share buyback proceeds at ordinary income rates.[179] It is debatable whether Senator Rubio's plan would meaningfully alter the incentives for corporations to engage in share buybacks over dividend issuances, because many dividends are already taxed at the lower capital gains rate.[180]

Beyond the merits of Senator Rubio's plan, the rhetoric he has used to argue for it indicates that stakeholder primacy may have bipartisan appeal. In his *Atlantic* piece and subsequent tweets, Senator Rubio repeatedly criticized shareholder primacy, implying that shareholder-value maximization deprives the economy and workers of economic value: "When a corporation uses its

172. *See infra* Subsection IV.C.3.

173. Worker Dividend Act, S. 2505, 115th Cong. (2018).

174. *Booker, Casey Introduce Bill Aimed at Corporate Short-Termism, Stock Buybacks*, SENATE.GOV (Mar. 7, 2018), https://www.booker.senate.gov/?p=press_release&id=761 [https://perma.cc/79XN-QN7Z].

175. *Id*.

176. *See supra* Subsection IV.B.1.

177. Marco Rubio, Opinion, *America Needs to Restore Dignity of Work*, THE ATLANTIC (Dec. 13, 2018), https://www.theatlantic.com/ideas/archive/2018/12/help-working-class-voters-us-must-value-work/578032/?mod=article_inline [https://perma.cc/V3E7-ER2T].

178. Marco Rubio (@marcorubio), TWITTER (Feb. 13, 2019), https://twitter.com/marcorubio/status/1095720592672784386 [https://perma.cc/6F69-D2TF].

179. *Id*.

180. *See* Scott & Stewart, *supra* note 156.

profits to buy back stock, it is actively deciding that returning capital to shareholders is a better activity for business than investing in the company's product or workforce," wrote Senator Rubio in the *Atlantic*.[181] In his tweets, Senator Rubio lamented that over the past forty years, "money back to shareholders has tripled as a % of our GDP, but investment into business dropped by 20%" and cited attorney Martin Lipton, a well-known critic of shareholder primacy, for the assertion that companies would rather invest earnings in "improving their product [and] improving workers' skills than return it to shareholders."[182]

Senator Rubio has not mentioned executive compensation in his discussion of share buybacks, even though many policymakers and analysts view executive incentive compensation as a key driver of share buybacks.[183] Senator Rubio's rhetoric provides evidence that stakeholder-oriented policies to address economic inequality could garner bipartisan support in the 2020 election cycle.

6. A Note on the "Wealth Tax"

Progressives have recently proposed policies that would place a higher tax burden on America's wealthiest individuals. Senator Warren would impose an annual 2% tax on wealth above $50 million, and an additional 1% surcharge on wealth above $1 billion.[184] Senator Sanders would expand the estate tax, establishing a 45% tax on inherited estates between $3.5 million and $10 million, and a 50% tax on inherited estates between $10 million and $50 million.[185] Representative Alexandria Ocasio-Cortez (D-NY) has proposed a 70% marginal tax rate on income above $10 million.[186] These tax proposals all have promising potential, and any comprehensive plan to address economic inequality would be remiss to overlook progressive taxation. However, given the potential for tax avoidance and the massive scope of the United States' income and wealth gaps, there is reason to fear that tax-only policies would not do enough to correct economic inequality. Further, some progressive policy analysts have asserted that laws addressing pre-tax incomes—so-called "pre-

181. Rubio, *supra* note 177.

182. Rubio, *supra* note 178.

183. *See supra* Subsection IV.B.1.

184. Neil Irwin, *Elizabeth Warren Wants a Wealth Tax. How Would That Even Work?*, N.Y TIMES, THE UPSHOT (Feb. 18, 2019), https://www.nytimes.com/2019/02/18/upshot/warren-wealth-tax.html [https://perma.cc/UB3K-T8SV].

185. Megan Henney, *Bernie Sanders to Propose Significant Wealth Tax Expansion*, FOX BUS. (Jan. 31, 2019), https://www.foxbusiness.com/politics/bernie-sanders-to-propose-significant-wealth-tax-expansion [https://perma.cc/L9FC-76NX].

186. Jacob Pramuk & John W. Schoen, *Alexandria Ocasio-Cortez and Elizabeth Warren Want the Rich to Pay a Lot More in Taxes—Here's Why History May Be on Their Side*, CNBC (Feb. 5, 2019, 7:57 AM EST), https://www.cnbc.com/2019/02/05/warren-sanders-ocasio-cortez-propose-taxes-on-the-rich-ahead-of-2020-election.html [https://perma.cc/RGD6-EXZ3].

distribution" policies—are superior to redistributive taxation because they are less costly and more politically viable.[187]

C. An Analysis of the Accountable Capitalism Act

In this Section I analyze Senator Warren's Accountable Capitalism Act and find that while it contains stakeholder-focused policies with promising potential to address some of the ills of shareholder primacy, these policies would not amount to effective limits on executive compensation and thus will not alone reduce income inequality. As discussed in the Introduction, Senator Warren's Accountable Capitalism Act includes three provisions that could be viewed as having the potential to rein in executive pay. Most directly, the Act would prohibit directors and officers who acquire corporate shares, either by purchasing them directly or through equity compensation, from selling these shares within five years of acquiring ownership or beneficial ownership of the stock, and within three years of a company stock repurchase.[188] The Act would also impose a requirement that workers elect two-fifths of the board of directors.[189] Finally, directors and officers would be obligated to balance "the pecuniary interests of the shareholders . . . with the best interests of persons that are materially affected by the [corporation's] conduct," including employees, customers, the communities in which the company's offices and facilities are located, and "the local and global environment."[190]

1. Limitations on Executive Stock Sales

The proposed limitations on executive share sales are a laudable policy idea. If executives are required to hold onto shares of their company for a longer duration, they will retain personal incentives to promote the company's long-term value. Another likely hoped-for effect of the provision is to discourage companies from paying such significant portions of their executive compensation in high-value corporate equity by imposing strenuous holding period requirements on this equity, thus reducing the overall value of executive pay packages. Finally, the provision seems to seek to reduce the attractiveness of share buybacks to corporate managers, because beginning on the date of the

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187. *See* Steven K. Vogel, Opinion, *Elizabeth Warren Wants to Stop Inequality Before It Starts*, N.Y. TIMES (Jan. 3, 2019), https://www.nytimes.com/2019/01/03/opinion/elizabeth-warren-economic-policy-democrats.html?action=click&module=RelatedLinks&pgtype=Article [https://perma.cc/TR7S-G6NT] (asserting the merits of policies that political scientist Jacob Hacker has called "pre-distribution").

188. S. 3348 § 7, 115th Cong. (2018).

189. *Id*. § 6.

190. *Id*. § 5(c)(1).

share buyback, executives would be restricted from selling any company stock for three years.[191]

The provision's potential to achieve its goals of discouraging equity compensation and corporate stock buybacks, however, is undercut by the reality of corporate policies and regulations already constraining executive-stock sales. This Section's analysis of the current limitations imposed by large public companies and the U.S. securities laws on the sale of shares by executives and directors reveals that the proposed provision would not impose significantly more stringent limitations than those already in place, making it unlikely that this provision would spur changes in executive compensation policies or stock buyback decisions.[192] These limitations, discussed in turn, include 1) company-imposed stock-ownership guidelines, 2) requirements attached to restricted stock units, and 3) federal insider trading laws.

Most large U.S. public companies require their top executives to comply with a set of "stock ownership guidelines."[193] These ownership guidelines generally require that the executives 1) obtain a specified value of shares within a certain timeframe, 2) maintain ownership of at least this specified value of shares throughout their executive service, and 3) hold a specified percentage of shares and options received as compensation until they accumulate enough shares to fulfill the ownership guidelines.[194] The stated purpose of these guidelines is to incentivize managers to promote the long-term value of the company.[195]

According to a 2018 report by Meridian Compensation Partners analyzing the executive compensation policies of the "Meridian 200," "200 large publicly traded companies across a variety of industries . . . with median revenues and market capitalization of $15.5B and $30.5B, respectively," 99% of firms

191. From a close reading of the proposed statute, it seems that the provision would also prohibit executives from selling their own shares into a stock buyback. According to § 7(b)(1)(B) of the Act, the three-year period "begins *on the date* on which that United States corporation, or an affiliate of that United States corporation, effects a Rule 10b–18 purchase." Thus, the three-year prohibition appears to include the stock buyback itself. Senator Warren's public description of how the provision would work, however, is not clear on this point: "[T]he bill prohibits directors and officers of United States corporations from selling company shares within five years of receiving them or within three years of a company stock buyback." *Warren Introduces Accountable Capitalism Act*, U.S. SEN. ELIZABETH WARREN (Aug. 15, 2018), https://www.warren.senate.gov/newsroom/press-releases/warren-introduces-accountable-capitalism-act [https://perma.cc/UGK3-BRYD].

192. At least one commentator has echoed this view in general terms. *See* Denise Kuprionis, *Will Warren's Accountable Capitalism Act Help? The Answer is No*., HARV. L. SCH. FORUM ON CORP. GOVERNANCE & FIN. REG. (Sept. 10, 2018), https://corpgov.law.harvard.edu/2018/09/10/will-warrens-accountable-capitalism-act-help-the-answer-is-no [https://perma.cc/X3DN-CQ98] ("Because many, if not most, stock awards to directors and management are granted with vesting restrictions, this requirement does not improve current practices.").

193. EQUILAR, 2016 STOCK OWNERSHIP GUIDELINES 1, 6 (Mar. 9, 2016), https://www.equilar.com/reports/34-executive-stock-ownership-guidelines.html [https://perma.cc/RRY8-H3LK].

194. *Id.*

195. *Id.*

impose stock ownership guidelines on their top executives.[196] On average, these firms require that their CEO obtain and maintain company shares with a value of at least 6.3 times their annual salary.[197] Most companies (67%) specify that the ownership amount requirement must be achieved within five years.[198] Fifty-five percent of companies further require executives to hold a specified percentage of shares and options received as compensation until the ownership amount requirement has been achieved: 47% of these firms say 100% of shares received must be held, and 41% say 50% must be held.[199] According to Equilar, stock-ownership guidelines have rapidly increased in popularity and restrictiveness in recent years.[200]

In addition to ownership guidelines, 68% of firms include restricted stock units as part of their executive compensation packages (on average, 20% of an executive's long-term incentive plan is made up of restricted stock units).[201] Restricted stock units generally vest over a period of several years and thus are further subject to time-based sale limitations.[202]

The federal securities laws regulating insider trading impose additional limitations on the sale of company shares by executives and directors. In general, executives and directors must always be concerned about potential insider trading liability when selling and buying company shares, because these individuals are, by the nature of their work, often in possession of material non-public information. One way of avoiding insider trading liability is to only sell shares pursuant to a 10b5-1 plan, which provides a safe harbor if the executive sells shares under a plan adopted and filed with the SEC before obtaining material non-public information that specifies the amounts, prices, and dates of the to-be-conducted sales.[203]

The numerous restrictions imposed on executive share sales, while not adding up to a blanket five-year sale limitation, create a system whereby executives are unable to sell significant portions of their shares for at least several years and must also hold a substantial amount of equity throughout their entire period of service. It thus seems unlikely that the Accountable Capitalism Act provision would promote a significant change in executive compensation

196. MERIDIAN COMPENSATION PARTNERS, 2018 CORPORATE GOVERNANCE & INCENTIVE DESIGN SURVEY 1, 21 (Fall 2018), http://www.meridiancp.com/2018-meridian-corporate-governance-and-incentive-design-survey [https://perma.cc/3BL4-7P5J].

197. *Id.*

198. *Id.*

199. *Id.* at 23.

200. EQUILAR, *supra* note 193.

201. MERIDIAN, *supra* note 196, at 33.

202. Julia Kagan, *Restricted Stock Unit (RSU)*, INVESTOPEDIA (June 25, 2019), https://www.investopedia.com/terms/r/restricted-stock-unit.asp [https://perma.cc/Y7FX-ZUJS]. It is not clear from the language and description of the proposed statute whether the five-year clock would start ticking on the date the restricted stock units are awarded, or on the date they vest. A close reading of the statute and Section 3(a) of the Securities Exchange Act of 1934 (defining "equity security") suggests the former.

203. *See* Securities Exchange Act Rule 10b5-1(c)(i), 17 C.F.R. § 240.10b5-1 (2018).

policies or managerial behavior. If executives are already required to hold a significant amount of their company's stock throughout their tenure, retain most of their equity compensation for up to several years, and pre-file their share sale plans with the SEC, it is doubtful that executives would view Senator Warren's proposed five-year and three-year sale limitations as attaching significant additional burdens to equity compensation. Additionally, while restricting corporate share buybacks is a laudable goal, as discussed earlier in Subsection IV.B.1, it is unlikely that restricting stock buybacks alone would result in lower levels of executive compensation.

2. Worker Representation on Boards

Worker representation on boards is another promising, stakeholder-empowering policy proposal. Worker representatives would add economic diversity to corporate boards and could advocate for the interests of the company's workers and other stakeholders. One might also expect worker representatives to advocate for limits on executive compensation payouts because this would free up corporate funds to increase wages or benefits. However, based on evidence from Germany, where worker supervisory board representation has been mandatory since 1976,[204] there is reason to predict that worker board representation alone would be insufficient to effectively constrain executive pay growth. Worker board representation in Germany did not promote sufficient constraints on executive compensation and may have made it more difficult for corporate boards to control executives.

According to some German corporate-governance scholars, worker representation on supervisory boards significantly altered board dynamics in ways that made it more difficult to control management.[205] A number of factors have likely contributed to this effect, including fractionalization of the supervisory board into adverse factions, dilution of the supervisory board's powers as some authority shifted to shareholders or management, and collusion by one of the two "benches" (either the shareholder or worker representatives) and management.[206] Further, the history of Germany's say-on-pay law indicates that worker board representation did not sufficiently resolve executive compensation excess. Concern over rising executive pay was widespread into the late 2000s, prompting the German legislature to adopt Germany's own say-on-pay law in 2009.[207] This history shows that while mandatory worker board

204. Martin Vesper-Graske, *Say on Pay in Germany: The Regulatory Framework and Empirical Evidence*, 14 GERMAN L.J. 749, 774 (2013).

205. Katharina Pistor, *Co-Determination in Germany: A Socio-Political Model with Governance Externalities*, *in* EMPLOYEES AND CORPORATE GOVERNANCE 163 (Margaret M. Blair & Mark J. Roe eds., 1999).

206. *Id*.

207. *See* Vesper-Graske, *supra* note 204, at 774.

representation in the United States may serve other progressive goals, it will probably not lead to direct limits on executive pay.

3. An Affirmative Duty to Stakeholders

The Accountable Capitalism Act would impose a duty on corporate officers and directors to balance the "pecuniary interests of shareholders" with those of other stakeholders.[208] A full discussion of this potentially promising proposal is beyond the scope of this Note. Without more information about how this obligation would work in practice, though, it is unclear that it would directly and effectively limit executive compensation growth.

The recent wave of progressive, stakeholder-oriented legislative proposals is evidence of an emerging consensus on the proper role of corporate law in addressing economic inequality. The new progressive stakeholder-primacy theory of corporate law holds that shareholder interests are currently overvalued at the expense of the rest of society. The proper cure is to require and enable corporate boards to serve the interests of stakeholders in addition to those of shareholders, reallocating corporate profits away from shareholders and toward workers, communities, and consumers. In order to fully effect this reallocation, boards must be directly incentivized and empowered to place limits on executive compensation in all forms. Further, as the extensive findings of economists such as Piketty, Saez, and Stiglitz have established, direct limits on executive compensation are critical to sufficiently addressing economic inequality in the United States.[209] Progressive politicians have yet to rally behind a strong vision for executive-compensation regulation. If they are going to sufficiently address economic inequality, though, they must do so.

This finding naturally raises the question of why progressive politicians have failed to propose policies that would impose effective, direct constraints on corporate boards' discretion in setting executive pay. Though a full discussion of the political dynamics at play here is beyond the purview of this Note, some exploration of the most salient potential factors is warranted. For one, electoral concerns are undoubtedly influential.[210] Three of the senators discussed in this Note have announced their intention to run in the 2020 Democratic presidential primary: Elizabeth Warren, Cory Booker, and Bernie Sanders.[211] These politicians may have shied away from proposing policies that

208. S. 3348 § 5(c)(1), 115th Cong. (2018).

209. *See supra* Section I.C.

210. Indeed, according to political scientist David Mayhew's famous maxim, as "single-minded seekers of reelection," congressional representatives consider the electoral consequences of each and every action they take while in office. DAVID MAYHEW, CONGRESS: THE ELECTORAL CONNECTION 5 (2d ed. 2004).

211. *See* Alexander Burns et al., *Who's Running for President in 2020?*, N.Y. TIMES (updated Sept. 20, 2019), https://www.nytimes.com/interactive/2019/us/politics/2020-presidential-candidates.html [https://perma.cc/4NYB-L6JM].

would impose direct, hard limitations on executive compensation levels for fear of losing potential wealthy donors, many of whom could be corporate political action committees (PACs) or corporate executives themselves.[212] Secondly, such a policy would be unprecedented. As discussed in Part II, none of the United States' current executive compensation laws impose direct, meaningful limitations on corporate boards in setting executive compensation policies.[213] A truly effective stakeholder-primacy approach to executive compensation would need to break free of the current policy framework. The next Part outlines how this might be achieved while avoiding potential political pitfalls.

V. Toward Stakeholder-Focused, Board-Empowering Executive Compensation Laws

In this Part, I present a three-pronged executive-compensation policy proposal for the new progressive stakeholder primacy movement. My proposed policy aims to place much-needed, meaningful restrictions on executive compensation levels and fit within the corporate-governance framework of stakeholder primacy. This policy would avoid the failings of our nation's current executive-compensation laws and those recently proposed by progressive politicians by 1) targeting and empowering the board of directors directly, rather than relying on shareholder participation, 2) applying equally to all forms of compensation, and 3) giving a voice to stakeholders in the pay-setting process. As discussed throughout this Part, timing and messaging would be critical to the political viability of this proposal.

The proposed policy would 1) require boards to balance the interests of all stakeholders by placing a cap on the permissible executive-median employee pay ratios of U.S. companies (Section V.A), 2) give workers a voice in approving executive-compensation policies (Section V.B), and 3) push back on shareholders' ability to steer corporations toward short-termism, excessive risk-taking, and shareholder value maximization by repealing say on pay (Section V.C). I discuss each of these policy proposals in turn.

212. Senator Sanders has proudly run a campaign based on small-dollar donations and boasts that he is the only 2020 Democratic presidential candidate who has not received a donation from a billionaire. *See* Eoin Higgins, *No Billionaires for Bernie: Alone Among Democratic Frontrunners, Sanders Gets No Cash from Wealthiest Americans*, COMMON DREAMS (Aug. 6, 2019), https://www.commondreams.org/news/2019/08/06/no-billionaires-bernie-alone-among-democratic-frontrunners-sanders-gets-no-cash [https://perma.cc/D2UK-F6M7]. Yet, even Sanders receives significant campaign dollars from corporate employees and/or corporate PACs. *See Sen. Bernie Sanders – Vermont, Contributors 2015 – 2020*, OPEN SECRETS (last visited Nov. 16, 2019), https://www.opensecrets.org/members-of-congress/contributors?cid=N00000528&cycle=2020&recs=100&type=C [https://perma.cc/8PX8-LJP6] .

213. *See supra* Part II.

A. Industry-Based Caps on Corporations' Top Executive-Median Employee Pay Ratios

This Section argues for a mandatory cap on the ratios of U.S. companies' top executive-compensation payouts and median-worker wages. The past several decades of failed executive-compensation laws in the United States have underscored an enduring reality: policies that seek to rein in executive pay levels solely through indirect, incentive-based means do not work. The lackluster legacies of the executive compensation deductibility cap, executive compensation disclosure requirements, and shareholder say on pay are all evidence of this actuality.[214] Direct limitations on executive pay levels are the only certain way to constrain America's runaway executive compensation growth. This is why I propose federally mandated, industry-based caps on corporations' highest-paid executive-median employee pay ratios.[215]

Though Americans generally detest hard caps regulating companies' policy decisions,[216] there is growing precedent for this proposal in the United States and abroad. Most notably, Senator Sanders's proposed Stop WALMART Act would impose a CEO-median worker pay ratio cap of 150 on companies with over 500 employees as a prerequisite to engaging in stock buybacks.[217] Several state governments, including California, Illinois, Massachusetts, and Portland, Oregon, and local governments, have considered imposing business tax surcharges of between ten and twenty-five percent on businesses with pay ratios above a specified cap.[218] Looking farther afield, policymakers in Germany and the Norwegian sovereign wealth fund have both proposed setting hard caps on allowable executive-compensation payouts.[219]

This proposal would undoubtedly carry political risks. As noted in Part IV, some progressive politicians may have declined to propose policies that would directly and effectively limit executive compensation levels in order to avoid upsetting potential donors. Strategic messaging would be key to avoiding

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214. *Id*.

215. A recent paper argues that the CEO-median worker pay ratio, as currently disclosed, is "lacking in accuracy, difficult to interpret, and incomplete," though it has "high public salience." Steven A. Bank & George S. Georgiev, *Securities Disclosure as Soundbite: The Case of CEO Pay Ratios*, 60 B.C. L. REV. 1123, 1123 (2019). I agree that the accuracy and uniformity of this disclosure may need improvement and would encourage a retooling of the disclosure requirements as part of this policy proposal.

216. *See, e.g*., Richard Coniff, *The Political History of Cap and Trade*, SMITHSONIAN MAG. (Aug. 2009), https://www.smithsonianmag.com/science-nature/the-political-history-of-cap-and-trade-34711212 [https://perma.cc/C932-88KZ] (describing the difficult political history of cap and trade in the United States).

217. *See* Stop WALMART (Welfare for Any Large Monopoly Amassing Revenue from Taxpayers) Act of 2018, S. 3410, 115th Cong. (2018).

218. *See* THE ECONOMIST, *supra* note 104.

219. *See* Thomas & Van der Elst, *supra* note 86, at 693; Anders Melin, Brandon Kochkodin & Mikael Holter, *World's Largest Wealth Fund Says Companies Pay CEOs All Wrong*, BLOOMBERG (Sept. 24, 2018), https://www.bloomberg.com/news/articles/2018-09-24/world-s-largest-wealth-fund-says-companies-pay-ceos-all-wrong [https://perma.cc/W7WE-X6DD].

such a risk. In announcing this proposed provision, progressive politicians could focus on the provision's use of the pay ratio as its relevant benchmark, emphasizing that the legislation's goal is to strike a reasonable balance between worker and executive pay and ensure that American workers earn a decent wage.

This provision could be added to the Accountable Capitalism Act model, requiring that companies keep their pay ratios below the industry caps in order to obtain and maintain a federal corporate charter through the Office of United States Corporations. Consistent with other provisions of the Act,[220] the pay-ratio cap could be implemented jointly by the National Labor Relations Board (NLRB) and the SEC. This policy could also be implemented outside of the Accountable Capitalism Act model. The pay-ratio cap could be added to the federal securities laws as a requirement for all companies that are registered issuers of securities under the Securities Act of 1933 or reporting issuers under the Securities Exchange Act of 1934. To prevent large private companies from skirting the pay-ratio cap, the proposed law could amend the Securities Exchange Act to provide a separate, lower cap which companies must remain below to avoid triggering public company status. In order to create a regime responsive to changing market dynamics and industry-specific considerations, the pay-ratio schedule would be industry-specific and updated every several years. The legislation's definition of "worker" would need to be carefully drafted to include independent contractors, overseas employees, and part-time employees.[221]

B. Worker Say on Pay

An important policy goal of the progressive stakeholder-primacy movement is involving stakeholders in corporate-governance processes. One way to achieve this goal while placing further constraints on executive compensation levels would be to create a mandatory, nonbinding worker "say-on-pay" vote for all U.S. companies with annual revenues above $1 billion or with more than a specified number of employees. This policy would be administered jointly by the SEC and the NLRB.

Requirements in the United Kingdom's Takeover Code provide a rough analogue for this proposed policy. A provision of the U.K. Takeover Code gives target company employee representatives the opportunity to publicly opine on a takeover bid's potential impact on employees.[222] Another provision,

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220. *See* The Accountable Capitalism Act, S. 3348 § 6(a), 115th Cong. (2018).

221. The salaries of part-time employees would be adjusted pro rata to approximate what these workers' earnings would be if they worked full time.

222. Sarah Gadd, Latham & Watkins LLP, *The Revised UK Takeover Code: Employment Considerations*, MONDAQ (Dec. 6, 2011), http://www.mondaq.com/uk/x/155898/Human+Resources/The+Revised+UK+Takeover+Code+Employment+Considerations [https://perma.cc/H5TS-VR5K].

adopted in May 2013, provides trustees of target-company employee pension plans the opportunity to publicly share their opinion on the likely effects of the acquirer's bid on the target's pension plans.[223]

There is also precedent for similar policy proposals in the emerging stakeholder primacy movement. In October 2018, Senator Tammy Baldwin and twelve other Senate Democrats wrote a letter to the SEC encouraging it to expand its concept of "corporate ownership" and consider policies "to give workers a greater voice at public companies," particularly through worker board representation.[224] Worker say on pay would not be vulnerable to the pitfalls of shareholder say on pay because workers would be much more incentivized to discipline growth in income inequality and promote long-term investment through non-deferential voting. Further, worker say on pay would avoid the managerial-control problems potentially introduced by worker board representation, because this policy would not affect the composition of boards of directors.

C. Repealing Shareholder Say on Pay

The discussion in Section IV.D established that in addition to being ineffective at controlling general executive compensation levels, shareholder say on pay likely exacerbates economic inequality by "ratifying" massive pay packages and encouraging short-termism and excessive risk-taking by managers.[225] The obvious fix is to repeal the Dodd-Frank Act's say-on-pay provision. Consistent with stakeholder primacy's governance ethos, the repeal of shareholder say on pay would make corporate boards less beholden to shareholder-value maximization and would empower directors to consider a balanced set of stakeholder interests in setting executive compensation policies. The political viability of this proposal would be highly dependent on careful messaging. Policy-makers proposing this legislation would need to emphasize shareholder say on pay's record of inefficacy, the economic inequality harms created by shareholder say on pay, and statistics showing that, contrary to popular perception, shareholders represent the wealthy few rather than the average working American.

Conclusion

It has been decades since Americans began complaining about sky-high executive pay packages, and nearly as long since the nation became concerned

223. *See UK Takeover Code: New Pensions Obligations*, SQUIRE SANDERS (May 2013), https://www.squirepattonboggs.com/~/media/files/insights/publications/2013/05/uk-takeover-code-new-pensions-obligations/files/uktakeovercodenewpensionsobligations/fileattachment/uktakeovercodenewpensionsobligations.pdf [https://perma.cc/2YEQ-LR39].

224. *See* U.S. SEN. TAMMY BALDWIN, *supra* note 170

225. *See supra* Section IV.D.

with its swiftly widening income and wealth gaps. Emboldened by a rising populist sentiment in U.S. politics, the emerging progressive stakeholder-primacy movement seems poised to finally address this inequality through bold, targeted policies. Extensive economic research has established that policies aimed at lessening American economic inequality will not succeed unless they address income and wealth at the very top—a large portion of which is due to meteoric executive compensation growth. Progressive politicians are in the process of developing promising, stakeholder-oriented policy proposals, some of which will likely be included in the Democratic Party's 2020 policy platform. The eighty-seven percent of Americans who have been negatively affected by economic inequality growth should hope that a robust policy proposal to constrain executive compensation is among them.