THE EVOLUTION OF THE MODERN CORPORATION: CORPORATE GOVERNANCE REFORM IN CONTEXT

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This Article traces the evolution of the modern corporation from the American Civil War to the present. I begin with a focus on the period from 1865 to the Great Depression. This was the era of the Great Tycoon, the time of the second industrial revolution and the transformation of America's economy from small proprietorships and partnerships to the forerunner of the modern corporation. I then detail the transformational crisis of the Great Depression and Adolf Berle's central role in shaping America's changed understanding of the proper relationship between government and the modern corporation. It was Berle, both as a scholar and key advisor to Franklin Roosevelt, who recast America's history so that the New Deal seemed a natural extension of individualism. The following Part details the period encompassing the New Deal and the Second World War. It is this period in which the United States develops into a modern, Keynesian social democracy. It is this period when the United States, in partnership with the modern corporation, assumes the mantle of world hegemon. I then examine the modern corporation during the heyday of American hegemony and the so-called "golden age of American capitalism;" the period runs roughly from 1950 to 1973 and is characterized by the Galbraithian Corporation, with power devolved to the technocracy of the firm. I conclude with tentative intuitions as to the nature of the modern corporation and the CEO in recent times. The tentativeness of this final section is purposive. We are too close in time to the "present" to agree on what has transpired, much less what is about to transpire. Thus, my effort is to provide a common backdrop for understanding the slightly more distant past, in hopes that conversation about the near present and near future will be more fruitful.

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I. INTRODUCTION

The nature of the modern corporation has preoccupied scholars for more than a century. The seminal scholars—Thorstein Veblen, Adolf Berle, and John Kenneth Galbraith in particular—understood that the nature of the modern corporation is evolutionary, rooted in the past but changing along with the fortunes of men and nations. Following in that tradition, and placing special emphasis on the work, thoughts, and insights of Adolf Berle, this Article sketches an evolutionary account of the modern corporation from the American Civil War to the present. Central to my account is technological progress in the means of production—the first, second, and third industrial revolutions—and the effect of that progress on business organization and society. Necessarily, the story I tell places the entrepreneur and the CEO at the center of the evolving modern corporation, and the modern corporation at the center of the rising American empire. My story "ends" with some uncertainty as to where we are, or where we are going, as any account of the present must. Still, perhaps counter to the intuitions of many, I conclude that the current-day CEO's power has likely not diminished in recent years despite the corporate governance reforms of the past decade.

Writing in 1932, Adolf Berle identified the ascendancy of the modern corporation, and its rulers—the Princes of Industry.[1] Berle[2] painted a stark picture. Collectively, a few hundred of these corporations had taken ownership of a substantial portion of America's industrial assets.[3] The trend seemed clear and unstoppable. Within a few decades, the productive assets in every important sector of the economy would be owned by these increasingly large and powerful corporations.[4] An equally important trend was the ever-increasing dispersal of voting control from the hands of entrepreneurs/managers into the hands of the investing public. The result was a new normal—separation of ownership and control. In most large corporations, majority voting power was now in the hands of passive, geographically dispersed shareholders with no ability or incentive to challenge insiders' control.[5] As a result, the Princes of Industry—CEOs, investment bankers, and other representatives of great fortunes—could and did use the levers of corporate power as they chose, maintaining each other in corporate offices and in control of corporate boards of directors.[6]

1. ADOLF A. BERLE, JR. & GARDINER C. MEANS, THE MODERN CORPORATION AND PRIVATE PROPERTY 2 (1932) (describing how concentration of power "has brought forth princes of industry").

2. Berle is generally recognized as the primary author of *The Modern Corporation*. *See* Charles R.T. O'Kelley, *Berle and the Entrepreneur*, 33 SEATTLE U. L. REV. 1141, 1141 n.2 (2010).

3. BERLE & MEANS, *supra* note 1, at 33.

4. *Id.* at 18–46.

5. *Id.* at 47–125.

6. *Id.* at 3, 124.

Beginning after Enron,[7] the corporate governance landscape appeared to change fairly dramatically. Marcel Kahan and Ed Rock provide a useful summary of these changes in their 2010 article, *Embattled CEOs*.[8] The changing nature of corporate share ownership calls into question the traditional depiction of shareholders as passive, dispersed, and powerless. A majority, and steadily increasing, portion of corporate voting stock is owned by a decreasing number of institutional investors. Assisted by ever more muscular proxy advisory firms and aggressive hedge funds, institutional investors threaten to make shareholder activism the new normal.[9] Changes in governance rules have removed insider-controlled defenses to proxy contests; chief among these changes are the decline of staggered boards, the ascendancy of majority voting for the election of directors, and the successful-shareholder-proposal phenomenon.[10] Regulatory changes have impacted shareholders' access to the company proxy and the balance of power in the proxy solicitation process.[11] Legislation and related listing rule changes have resulted in the insider-dominated board becoming a dinosaur: the new norm is boards composed primarily of independent directors.[12] Finally, Kahan and Rock point to efforts to rein in executive compensation, including "say on pay" initiatives and enhanced compensation disclosure requirements.[13]

Kahan and Rock conclude:

> The story we tell above is a story of declining CEO power *over the last several years*, a decline that has occurred across almost all of the relevant dimensions and that we believe will last and continue. . . .
>
> [W]e argue that the balance of power between CEOs, boards, and shareholders has shifted notably in the last decade away from CEOs towards outside directors and shareholders. If, as we expect, that shift will continue in the same direction, CEOs are left ever more embattled, *at least in comparison to their predecessors a generation ago*.[14]

If Kahan and Rock are correct in their intuition (and they admit that it is an intuition),[15] then an evolutionary story of the modern corpo-

7. The phrase "after Enron" refers to the 2001, accounting-fraud-induced collapse and bankruptcy of the Enron Corporation and the numerous other corporate account scandals uncovered at around the same time. For a summary of these events, see David A. Westbrook, *Corporation Law After Enron: The Possibility of a Capitalist Reimagination*, 92 GEO. L.J. 61, 64–68 (2003).

8. Marcel Kahan & Edward Rock, *Embattled CEOs*, 88 TEX. L. REV. 987 (2010).

9. *Id.* at 995–1007.

10. *Id.* at 1007–13.

11. *Id.* at 1013–22.

12. *Id.* at 1022–32.

13. *Id.* at 1033–37.

14. *Id.* at 1051 (emphases added).

15. Kahan and Rock are unusually candid in acknowledging the tentativeness of their conclusions:

> The intuition that drives this Article is nicely captured in Milo Winter's famous 1912 illustration of Gulliver tied down by the Lilliputians. . . . [Numerous] complications make our analysis somewhat conjectural. Maybe we are completely wrong that CEO power has declined. Maybe CEOs are every bit as powerful as they once were. Maybe they were never very powerful. Or

ration from Berle's time to the present would seem to emerge. While the battle has been long and slow, the modern corporation and the Princes of Industry are finally being brought under shareholder and independent director control. CEOs are losing power. Boards are no longer dominated by insiders.

When I read an early draft of Kahan and Rocks's article, one claim struck me as odd. They claim that CEOs are losing power "*at least in comparison to their predecessors a generation ago*."[16] As evidence of how powerful CEOs were a generation ago, Kahan and Rock point to the picture of director impotence and CEO power painted by Myles Mace in his 1971 book, *Directors: Myth and Reality*.[17] Mace's work drew on interviews with directors and officers conducted from 1969 to 1971.[18] Relying solely on Mace's work for the proposition that CEOs were much more powerful "a generation ago" struck me as problematic given John Kenneth Galbraith's concurrent, negative, assessment of CEO power, set out in *The New Industrial State*.[19]

Kahan and Rock quoted the following interview excerpts from Mace's account:

> To put it bluntly, whether a board has any function or not, it must truly reflect the nature of the chief executive officer of the company more than anything else. If he wants to use the board, he will use them. And if he doesn't want to use the board, he will run over them pretty roughshod. Basically, the board can be made just about as useful as the president wishes it to be.
>
> The president of a company, or the chairman of the board, or whoever runs this operation, really determines the contribution the board makes. If all he wants to do is to get up in front of them and sort of go through some motions, see that fees get distributed, give them a bit of lunch—then that's the kind of performance you will get, because the chief executive officer controls the affair. If, on the other hand, the chief executive officer seeks out where in the management areas various board members might be able to make more of a contribution than in others, and then structures his board so that emphasis is placed on such questions rather than on the rote alternative, then the chief executive is making a direct impact on the contribution the board makes. This, I suppose, is a matter of style.
>
> . . . The old man [the president] has exactly the kind of a board he wants. They all live here in the city, and they just don't do a damn thing as directors. The old man thinks it is a great board, and

> maybe it is impossible to come up with a metric for measuring CEO power or, even if one can design a metric, to collect the data to determine whether CEO power has declined. On the other hand, we think that there are lots of reasons to think that one can intelligibly discuss CEO power, that it has declined, and that this decline has important implications.

Id. at 990, 994–95.

16. *Id.* at 1051 (emphasis added).
17. MYLES L. MACE, DIRECTORS: MYTH AND REALITY 178–206 (1971).
18. *Id.* at v–vii.
19. JOHN KENNETH GALBRAITH, THE NEW INDUSTRIAL STATE 46–59 (1967).

> from his point of view he is probably right. From my point of view they are a big glob of nothing. Not that there aren't some extremely able outsiders on the board—there are. But as board members, they know who is in control and they will never cross the old man. . . .
>
> What any new board member finds out very quickly in our company is that it is very difficult to do anything except go along with the recommendations of the president. Because directors who don't go along with them tend to find themselves asked to leave.[20]

Kahan and Rock then quote the conclusion Mace drew from his extensive interviews:

> Presidents of these [widely held] companies have assumed and do exercise the de facto powers of control of the companies for which they are responsible. To them the stockholders constitute what is in effect an anonymous mass of paper faces. Thus, presidents in these situations determine what directors do or do not do.[21]

From their reading of Mace, Kahan and Rock conclude that the late 1960s CEO (the CEO of a long generation ago)[22] was powerful because unshackled. Since the CEO of today appears increasingly shackled, then the 1960s CEO must be the more powerful of the two.

The problem is that Kahan and Rock's conclusion that the 1960s CEO was all-powerful, or at least powerful in comparison to the present-day CEO, does not square with John Kenneth Galbraith's observations as set out in *The New Industrial State*.[23] As Galbraith notes, the mantle of the all-powerful, entrepreneurial CEO was still often claimed by the 1960s CEO, but the reality was far different. The mature 1960s corporations had become far too complex for entrepreneurial direction. Instead, control devolved to the technostructure within the firm. The modern (1960s) reality was not risk-taking and swashbuckling leadership by individualistic CEOs. Rather, planning and collective decision making by experts was the key to survival and success.[24] The picture Galbraith painted is not a pretty sight.

> In romance the past greatly improves on the present. In the history of almost every industry, there has been a famous and sometimes flamboyant entrepreneur. Like the tank commander, the

20. Kahan & Rock, *supra* note 8 at 991–92 (citing Mace, *supra* note 17, at 78–79) (omissions and punctuation in original).

21. *Id.* at 992 (citing Mace, *supra* note 17 at 84) (alteration in original).

22. Kahan and Rock are using as their comparative temporal unit a "long generation"—that is, a period of time that covers a somewhat longer period than what we normally mean by a generation. Similarly, Giovanni Arrighi developed and used the term "long century" to refer to periods of more than 100 years that normally bracket a particular cycle of capitalist hegemony. *See* GIOVANNI ARRIGHI, THE LONG TWENTIETH CENTURY: MONEY, POWER, AND THE ORIGINS OF OUR TIMES 6–7 (1994) ("[C]onsecutive systemic cycles of accumulation overlap, and although they become progressively shorter in duration, they all last longer than a century: hence the notion of the 'long century,' which will be taken as the basic temporal unit in the analysis of world-scale processes of capital accumulation.").

23. GALBRAITH, *supra* note 19, at 49–50.

24. *Id.* at 60–71.

> head of the modern enterprise, in which all important actions are studiously considered by committees, all contingencies carefully anticipated and all adverse ones either prevented or negated, seeks to see himself in an earlier and more heroic image. Doubtless this does no harm. Additionally his function is to lend dignity and an aspect of power to stockholders' and directors' meetings, and other business ceremonials; to salute customers and clients of equal or greater dignity; to give the equivalent of the royal assent to agreements, contracts and indentures; to represent the enterprise in its more honorific relations with government; to act as an emissary to liberal learning; and to affirm, on appropriate public occasions, faith in free enterprise, the social responsibility of business and the continuing relevance of ancestral virtues. For all these rites the mantle of Carnegie, Rockefeller or Henry Ford is more than a little helpful.[25]

Much of Galbraith's book explains why the 1960s CEO looks nothing like the Princes of Industry so central to Berle's depiction of the modern corporation. However, in keeping with his dry sense of humor,[26] he offers as ultimate evidence what happened to the CEO upon his retirement. Galbraith first notes that some men are critically important to an organization's success, while others owe their status to the organization.[27] The 1960s CEOs fall into the latter category. When a CEO retired, the markets did not blink.[28] The financier understood that "retirement, death and replacement, however important for the individual involved, have not the slightest effect on General Motors or Continental Can. Power, it is implicitly recognized, has passed to the technostructure."[29] But the impact on the retired CEO in that era was drastic:

> Following the final flight in the company jet, there will be only an honorific association with the board of directors and sometimes not that. His memoirs will not be in demand; the United Fund will want a man more affirmatively identified with affairs; his only continuing public responsibilities will be in his own church; his name will not again appear in the papers until the day following his death. The great entrepreneur lived out his last days disposing of his wealth or resisting those who sought to have him do so. The modern executive does not have enough money so to occupy himself. Such is his recessional.[30]

25. *Id.* at 93.

26. Michael Stewart, *Obituary: JK Galbraith*, GUARDIAN (Apr. 30, 2006), http://www.guardian.co.uk/news/2006/may/01/guardianobituaries.usa ("His irony and wit were persistently deployed against the absurdities of the monetarist doctrines of Milton Friedman, and Arthur Laffer's notion that cutting income tax on the rich would increase government revenue. . . . He was fond, too, of characterising the trickle-down economics of the Reagan-Bush era as advocating feeding the horse more oats because some would pass through to the road for the sparrows.").

27. GALBRAITH, *supra* note 19, at 96.

28. *Id.* at 94–95.

29. *Id.* at 95.

30. *Id.* at 97.

What are we to make of this very different account of the 1960s CEO? The starting point for me was the discovery that Mace cited both Adolf Berle and John Kenneth Galbraith with approval,[31] suggesting that Mace's account and understanding of the 1960s CEO was intended to supplement and not conflict with the seminal work of either of these great scholars. Ultimately, my effort to reconcile the work of these authors and to understand the relationship between times past and times present led me to a different intuition than that reached by Kahan and Rock.

Though my intuition—that CEO power has not diminished—is the opposite of what Kahan and Rock conclude, that difference is not the principal focus of the story I will tell. They may well be right, and others are better equipped than me to parse the details of recent changes that they so carefully describe. Instead, I will focus on providing an evolutionary account of the modern corporation from the real onset of the industrial revolution in the United States to the long generation ago which Mace and Galbraith describe. My goal is to provide a different backdrop or perspective against which to judge, as best we can, what the nature of the present really is. In other words, I want to help set the stage for a better writing of a legal history of the present.[32]

There are many ways this story could be told. I, however, will spin it with central reference to the work, thoughts, and insights of Adolf Berle, who foreshadowed much of Galbraith's work.[33] Fortunately for our generation of corporate law scholars, Berle fused his commanding understanding of corporate law and practice[34] with his keen understanding of history.[35] It was Berle, writing on the eve of the New Deal, who provided policy makers then and now with the central metaphor of the modern corporation—the separation of ownership and control.[36] It was Berle writing in the early 1930s who, drawing on the work of other great scholars including particularly Thorstein Veblen, described how the modern corporation had evolved from our country's founding to the New

31. MACE, *supra* note 17, at 74–75.

32. I have in mind a version of what George Kennan called "history of the present." *See* TIMOTHY GARTON ASH, HISTORY OF THE PRESENT: ESSAYS, SKETCHES, AND DISPATCHES FROM EUROPE IN THE 1990S, at xiv–xviii (1999).

33. Reading in the same sitting Adolph A. Berle, *Property, Production and Revolution*, 65 COLUM. L. REV. 1 (1965) and THE NEW INDUSTRIAL STATE, GALBRAITH, *supra* note 19, one sees that Galbraith's thinking is deeply intertwined with and influenced by Berle's critique of the modern corporation and *laissez-faire* individualism, and that Berle and Galbraith similarly understand the mature modern corporation of the 1960s.

34. Berle's unique expertise in the intricacies of corporate law are reflected in the fact that in 1930 he created the first Corporate Finance casebook. Boris I. Bittker, *Review: Cases and Materials on the Law of Business Organizations (Corporations) by Adolf A. Berle and William C. Warren*, 57 YALE L. J. 1443, 1443 (1948).

35. Had Berle followed his intellectual passion, rather than the demands of his father and the broader dictates of his talent, he would have been a historian rather than corporate lawyer, scholar, and influential public intellectual. *See* JORDAN A. SCHWARZ, LIBERAL: ADOLF A. BERLE AND THE VISION OF AN AMERICAN ERA 13–14 (1987).

36. *Id.* at 52; William W. Bratton & Michael L. Wachter, *Shareholder Primacy's Corporatist Origins: Adolf Berle and* The Modern Corporation, 34 J. CORP. L. 99, 105 (2008).

Deal.[37] It was Berle who understood the further evolution of the modern corporation from the New Deal until the late 1960s. And it was Berle who foresaw how the modern corporation might evolve from then to now.[38]

I will trace the evolution of the modern corporation from the Civil War to the present as follows: Part II focuses on the period from 1865 to the Great Depression. This was the era of the Great Tycoon, the time of the second industrial revolution, and the transformation of America's economy from small proprietorships and partnerships to the forerunner of the modern corporation. Part III details the transformational crisis of the Great Depression and Adolf Berle's central role in shaping America's changed understanding of the proper relationship between government and the modern corporation. It was Berle, both as a scholar and key advisor to Franklin Roosevelt, who recast America's history so that the New Deal seemed a natural extension of individualism.[39] Part IV details the period encompassing the New Deal and the Second World War. It is this period in which the United States developed into a modern, Keynesian social democracy.[40] It is this period when the United States, in partnership with the modern corporation, assumed the mantle of world hegemon.[41] Part V examines the modern corporation during the heyday of American hegemony and the so-called "golden age of capitalism;" the period runs roughly from 1950 to 1973 and is characterized by the Galbraithian corporation, with power devolved to the technocracy of the firm.[42] Finally, in Part VI, I share some tentative intuitions as to the nature of the modern corporation and the CEO in recent times. I suggest that CEOs' motivations are now much more pecuniary and entrepreneurial in nature than the CEOs of the Galbraithian era, and that CEO power is not in decline.

II. THE RISE OF THE MODERN CORPORATION—AMERICA FROM 1865 TO THE GREAT DEPRESSION

A. The Civil War to World War I

In 1865, America emerged from the Civil War as a nation intact, but still dwarfed economically and otherwise by the British Empire. The first industrial revolution, fueled by steam power and cotton, had reached its peak, and Great Britain ruled the world that revolution had made possi-

37. SCHWARZ, *supra* note 35, at 56; Bratton & Wachter, *supra* note 36, at 111–12.

38. *See* Bratton & Wachter, *supra* note 36, at 148; Marc T. Moore & Antoine Rebérioux, *Corporate Power in the Public Eye: Reassessing the Implications of Berle's Public Consensus Theory*, 33 SEATTLE U. L. REV. 1109, 1134–35 (2010); Charles R.T. O'Kelley, *Berle and Veblen*: *An Intellectual Connection*, 34 SEATTLE U. L. REV. 1317, 1317–18 (2011).

39. *See infra* Part III.B.2.

40. *See infra* notes 200–02 and accompanying text.

41. *See infra* notes 200–02 and accompanying text.

42. *See infra* Part IV.D.

ble. British manufacturers were the world's most efficient, British citizens were the world's most affluent, and British merchant fleets were the world's transport system.[43] Viewed from Britain, America appeared as merely a cog in the Empire's global wheel. William Stanley Jevons, the eminent English economist, described the scene:

> The plains of North America and Russia are our cornfields; Chicago and Odessa our granaries; Canada and the Baltic are our timber forests; Australasia contains our sheep farms, and in Argentina and on the western prairies of North America are our herds of oxen; Peru sends her silver, and the gold of South Africa and Australia flows to London; the Hindus and the Chinese grow tea for us, and our coffee, sugar and spice plantations are all in the Indies. Spain and France are our vineyards and the Mediterranean our fruit garden, and our cotton grounds, which for long have occupied the Southern United States, are now being extended everywhere in the warm regions of the earth.[44]

This view of America masked the emerging reality. A mere four decades later, America would eclipse Great Britain in economic power.[45] This changing of the guard occurred as soon as it did because of the devastating effects on Great Britain of World War I.[46] But by then, the change was inevitable and, indeed, almost complete. America had developed a uniquely efficient new business form—the modern corporation. Sitting astride these powerful economic entities were America's great entrepreneurs and financiers. Nothing could stem the modern corporation's swift rise to dominance, and, for a time, no reward seemed too great for the modern corporation's rulers—the Princes of Industry. The birth and ascendancy of the modern corporation resulted from the confluence of the second industrial revolution, the American Civil War, the bounteous American internal consumer market, and the unique American entrepreneurial response to the shortcomings of competitive markets.[47]

Around 1850, the Western world began to encounter a new stage of the industrial revolution. The exact onset of this new era—the second industrial revolution—is impossible to date with precision; it arrived in different places at different times.[48] In the period between 1850 and 1875, however, the material conditions of industrial life changed dramatically. Prior to 1850, the nature of industry was little changed from what had been present at the outset of the industrial revolution:

43. PAUL KENNEDY, PREPARING FOR THE TWENTY-FIRST CENTURY 8–9 (1993).

44. *Id.* at 9 (quoting William Stanley Jevons).

45. E.J. HOBSBAWM, INDUSTRY AND EMPIRE: FROM 1750 TO THE PRESENT DAY 156–59 (New Press 1999) (1968).

46. *Id.* at 128–29.

47. ARRIGHI, *supra* note 22, at 299–304.

48. Thorstein Veblen equated the beginning point of the industrial revolution with the end of the era of free competition. *See* O'Kelley, *supra* note 38, at 1337–38.

> Electricity, petroleum and rubber had no share in industry then, and even that extensive use of structural iron and steel that has characterized the later age was still in its beginnings. Industrial chemistry was but a slight and inconspicuous matter, and the industrial uses of the rarer metals were still unknown.[49]

By 1875, structural iron and steel, rubber, rare metals, and products from industrial chemistry, joined with new energy sources—petroleum and electricity—to totally transform the industrial system, paving the way for the assembly line and mass production of consumer and capital goods.[50] The old ways of manufacturing were swept away, unable to compete with the new processes and materials.[51]

The Civil War paved the way for the American economic ascendancy. After Waterloo, the world enjoyed one hundred years of relative peace with the tragic exception of the American bloodbath.[52] The Civil War's cost in treasure and human lives and suffering was something the world did not see again until World War I.[53] Just as the Napoleonic Wars had helped propel Britain to world leadership during the first industrial revolution,[54] however, the Civil War had a profoundly positive impact on the development of the American economy during the second industrial revolution.[55]

The Civil War exposed the governments of both North and South to unprecedented financial demands. While the South largely was forced to meet this challenge by printing fiat money, the North was able to raise a significant portion of its war budget via private borrowing in the form of bond sales to the public.[56] The proceeds of these private securities issuances in large measure were then passed on to business firms aiding the war effort in one way or another. Government money poured into railroads, gun foundries, iron mills, and manufacturers of shoes and clothing.[57] As the profits of those firms soared, so too did investors' interest in acquiring corporate securities. Due to the huge increase in bond and securities trading, Wall Street profited enormously from the war.[58] By the

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49. THORSTEIN VEBLEN, ABSENTEE OWNERSHIP AND BUSINESS ENTERPRISE IN RECENT TIMES: THE CASE OF AMERICA 74 (Viking Press 1964) (1923).

50. HOBSBAWM, *supra* note 45, at 150–56.

51. Or as Veblen put it: "The industrial system, the state of the industrial arts, as it stood before that date was complete without these things; since that time, since their invention has made them necessary, industry can not do without these things . . . ." VEBLEN, *supra* note 49, at 74.

52. ERIC HOBSBAWM, THE AGE OF EXTREMES: A HISTORY OF THE WORLD, 1914–1991, at 22–23 (Vintage Books 1996) (1994) ("In 1914 there had been no major war for a century, that is to say, a war in which all, or even a majority of, major powers had been involved . . . . Much the longest of [the few major wars] was not an international conflict but a civil war within the U.S.A. (1861–65).").

53. JOHN STEELE GORDON, AN EMPIRE OF WEALTH: THE EPIC HISTORY OF AMERICAN ECONOMIC POWER 191–94 (2004) ("The total military deaths in the war on both sides—officially 498,333—exceeded 3 percent of the American male population in 1860, four and a half times our percentage losses in World War II.").

54. ARRIGHI, *supra* note 22, at 258–61.

55. *Id.* at 281; CHARLES R. MORRIS, THE TYCOONS 11 (2005).

56. GORDON, *supra* note 53, at 194.

57. *Id.* at 199.

58. *Id.*

war's end, Wall Street had developed an expertise and credibility second only to London as a financial center, and that status was cemented in the ensuing decade with the creation and rise of the New York Stock Exchange and the related evolution of a workable system for private policing of the securities issuance process.[59] American business could now tap not only foreign lenders and investors, but also an increasingly large sum of home-grown capital[60] made available through the auspices of a sophisticated coterie of American investment bankers.

Post-Civil War America was thirsty for growth. America's influx of immigrants provided both a steady stream of new labor and new consumers.[61] The immense untamed expanses of the American West cried out for new rail and telegraph lines.[62] The new and expanding cities cried out for new homes, and more food, and more clothing.[63] This virtuous circle fueled a feverish expansion of existing businesses, and the search for new and more efficient industrial processes and products.[64]

Into the rapidly expanding post-Civil War economy stepped ambitious, forceful, intelligent, fearless men—Andrew Carnegie, John D. Rockefeller, Jay Gould, and J.P. Morgan—slated to be known as the Great Tycoons, along with a host of fellow capitalists, all competing for wealth, power, and respect.[65] Unlike the situation facing the British business elite as the second industrial revolution unfolded,[66] American businessmen had a nearly clean canvas on which to paint, and a nearly unlimited set of colors from which to choose.

> Carnegie, Rockefeller, Gould, and Morgan would have been dominant figures anywhere, but few places have ever been as open to people of talent as post-Civil War America; and in America, no field offered opportunities as unlimited as business. America's rad-

59. *Id.*

60. The war also changed the mindset of the American public toward investing. Before the war, private savings were almost entirely held outside the banking system. After the war, not only bank deposits but investment in securities became increasingly common for middle class Americans. *Id.* at 193.

61. *Id.* at 244.

62. *Id.* at 217.

63. MORRIS, *supra* note 55, at 166, 169–70; Arthur M. Schlesinger, *The City in American History,* 27 MISS. VALLEY HIST. REV. 43, 56–59 (1940).

64. GORDON, *supra* note 53, at 200–205.

65. Charles R. Morris summarizes:

> Andrew Carnegie, John D. Rockefeller, Jay Gould, and John Pierpont Morgan were all in their late twenties or early thirties, all on the first rungs of their careers, in the waning days of the Civil War. In an age of outsized business leaders, no others played so great a role in shaping and channeling the American boom. They forced the pace, drove the transition to ever larger scales, and, for good or ill, imposed personal stamps on the national economy that persisted well into the twentieth century.

MORRIS, *supra* note 55, at xii.

66. ARRIGHI, *supra* note 22, at 283–92, 291 ("[The] highly extroverted, decentralized, and differentiated structure of British business constituted a major obstacle for its corporate reorganization along German or US lines. Not only did it make horizontal combinations in restraint of competition difficult . . . but, in addition, it prevented British business from seizing opportunities to cut unit costs through a closer planning and integration of the sequential activities into which processes of production and exchange were divided . . . .").

> ically different manufacturing culture, its cult of the innovative entrepreneur, its obsession with "getting ahead" even on the part of ordinary people, its enthusiasm for the new—the new tool, the new consumer product—were all unique.[67]

America's business tycoons played a key role in the nation's rapid ascendance. They sought business advantage in a rapidly changing political and economic environment, dealing with corruption, uncertain legal institutions, and intense competition, along with the vagaries of rapidly evolving technologies.[68] These were Knightian entrepreneurs, drawn by the spirit of the greatest game known to man.[69] Uncertainty was the Tycoons' friend and enemy, but above all, the reason for their power and wealth. These Tycoons took the greatest business risks man had ever encountered, sometimes losing, but more often winning. Always, however, and each in his own way, they battled uncertainty.

> Carnegie, Rockefeller, and Gould tapped into the national predilection for speed, the obsession with "moving ahead," the tolerance for experimentalism, to create one of history's purest laboratories of creative destruction. Most businessmen of the time believed in orderly markets and gentlemanly fair profits, but these three came with flaming swords. Morgan [the great financier] was the regulator, always on the side of reining in "ruinous competition," most especially of the kind regularly unleashed by the other three.[70]

As the last quarter of the nineteenth century unfolded, U.S. businessmen were battered by competition with each other, and, equally importantly, competition from Great Britain. This intense, cutthroat struggle greatly increased uncertainty. Prices ebbed and flowed. Consumer demand waxed and waned. Businessmen struggled to match supply to demand. Profit margins were thin or nonexistent, making firms depend-

67. MORRIS, *supra* note 55, at xiii.

68. GORDON, *supra* note 53, at 205–28.

69. FRANK H. KNIGHT, RISK, UNCERTAINTY AND PROFIT (Midway Reprint ed. 1985) (1921) is the seminal account of the entrepreneur. The entrepreneur is the captain of the business ship who determines what course to take and assumes the risk of failure. For Knight, the truest form of entrepreneurship is the sole proprietorship, where ownership and control are united; in that form the power and responsibility to make business decisions is joined with residual claimant status—the right to all profits and the responsibility for all losses. *See* Charles R.T. O'Kelley, *The Entrepreneur and the Theory of the Modern Corporation*, 31 J. CORP. L. 753, 766–67 (2006). Knight believed, however, that the entrepreneur would be motivated by his competitive spirit, even if the rewards of the venture were not solely his:

> For it is clear that the "personal" interests which our rich and powerful business men work so hard to promote are not personal interests at all . . . . The real motive is the desire to excel, to win at a game, the biggest and most fascinating game yet invented, not excepting even statecraft and war.

KNIGHT, *supra*, at 360.

70. MORRIS, *supra* note 55, at xii–xiii ("They were quite different people. Carnegie, Rockefeller and Gould tapped into the national predilection for speed, the obsession with 'moving ahead,' the tolerance for experimentalism, to create one of history's purest laboratories of creative destruction. . . . Morgan, the most traditional figure of the four, was the one American whom overseas financiers trusted.").

ent on lenders and investors for working capital needs.[71] Indeed, the period from 1873 to 1896 was experienced, at least by businessmen in America, as a period of sustained price deflation for which natural forces seemed to provide no answer.[72]

America and Britain both entered this period with an economy dominated by "family capitalism," small- to medium-sized firms with a relatively small number of "partners."[73] Britain's economy remained so structured. Britain's competitive advantage was as the dominant middle man in an integrated, trade-based, international economy.[74] Britain needed to buy raw materials at the lowest possible price in world markets and then sell its finished products at the best price possible. Even if profit margins were squeezed at times, British firms on average did far better than their international competitors.[75] As a result, British capitalists resisted innovation. Rather than plow profits into restructuring British industries, they invested surplus profits internationally, thereby staking enormous British claims to the future profits of foreign nations.[76] As Halford Mackinder noted in 1899, Britain's resulting control of world capital reinforced and was central to Britain's control of international markets.[77]

> [T]he world's clearing house tends, from its very nature, to remain in the single position, and that clearing house will always be where there is the greatest ownership of capital. This gives the real key to the struggle between our free trade policy and the protection of other countries—we are essentially the people with capital, and those who have capital always share in the activity of brains and muscles of other countries.[78]

Captive to the needs of this international system, British firms remained small, nimble, and "family" in structure.[79]

In America, this status quo quickly grew intolerable. While all Americans benefited as consumers from the low prices that unfettered

71. ARRIGHI, *supra* note 22, at 296–97.

72. *Id.* at 167.

73. *Id.* at 266–67. Even if these firms were incorporated for liability limitation purposes, the shareholders were close associates and thought of themselves as partners. *See* MORRIS, *supra* note 55, at 135–36.

74. Giovanni Arrighi describes Britain's dominant middle man role as follows:

> "[I]f by market we understand the place where demand and supply meet, then Britain *was* the world market since its governmental and business institutions were the chief intermediaries between the producers and the consumers of the world. The more intensely the producers (consumers) of the world competed for markets (supplies), the greater were the options open to British business to substitute sources of supply (markets) for one another, and hence the greater its power to control the world market."

ARRIGHI, *supra* note 22, at 289.

75. *Id.* at 293–94.

76. *Id.* at 270.

77. *Id.* at 294–95.

78. *Id.* at 285 (quoting PETER J. HUGILL, WORLD TRADE SINCE 1431: GEOGRAPHY, TECHNOLOGY, AND CAPITALISM 305 (1993)).

79. *Id.* at 282.

competition produced, the producers of these products saw only disadvantage.

> By the mid-1890s, in the midst of the third long depression in three successive decades, a revulsion against the unregulated market spread among the bourgeoisie in all major sectors of the economy. Whatever their programmatic differences, farmers, manufacturers, bankers, and merchants, in addition to already disenchanted railway capitalists, found a common ground in the idea that unregulated competitive market activity resulted in production of goods and services in excess of effective demand at prices that returned reasonable earnings to producers of normal efficiency. The watchword was "overproduction."[80]

The American counter-movement against the evils of overproduction coalesced in two extremes—the Populists and the Corporatists. The Populists saw the answer in even greater adherence to the ideal of competitive markets. In other words, the Populists sought to restore "a just market, defined as one that sustained the natural right of the small producer to remain an independent agent in the market."[81] The Corporatists thought the answer lay in bringing markets under the control of big business. Where the Populists fought against business combinations and saw big as bad, the Corporatists saw overproduction as a natural consequence of industrial development under conditions of intense market competition.[82] America's Great Tycoons, of course, saw big as good.

While the debate between Populists and Corporatists would continue in the arenas of politics and academics well into the twentieth century, U.S. capitalists knew from direct experience that overproduction was an evil to be overcome, and, further, knew that cutthroat competition was the root cause. "By the 1890s, their complaints that overproduction was destroying profit and causing depressions had become legion."[83] By then, however, American business had begun to experiment with a variety of solutions to the problem.

As John Kenneth Galbraith later described, with the increasing complexity of industry brought on by the second industrial revolution, competitive markets could no longer be relied upon to organize business activity.

> In the market economy the price that is offered is counted upon to produce the result that is sought. Nothing more need be done. The consumer, by his offer to pay, obtains the necessary responding action by the firm that supplies his needs. By offering to pay yet more he gets more. And the firm, in its turn, by similar offers gets the labor, materials and equipment that it requires for production.

80. MARTIN J. SKLAR, THE CORPORATE RECONSTRUCTION OF AMERICAN CAPITALISM, 1890–1916: THE MARKET, THE LAW, AND POLITICS 53–54 (1988).

81. *Id.* at 54.

82. *Id.* at 55.

83. *Id.*

> Planning exists because this process has ceased to be reliable. Technology, with its companion commitment of time and capital, means that the needs of the consumer must be anticipated—by months or years. When the distant day arrives the consumer's willingness to buy may well be lacking. By the same token, while common labor and carbon steel will be forthcoming in response to a promise to pay, the specialized skills and arcane materials required by advanced technology cannot similarly be counted upon. The needed action in both instances is evident: in addition to deciding what the consumer will want and will pay, the firm must take every feasible step to see that what it decides to produce is wanted by the consumer at a remunerative price. And it must see that the labor, materials and equipment that it needs will be available at a cost consistent with the price it will receive. It must exercise control over what is sold. It must exercise control over what is supplied. It must replace the market with planning.[84]

The Great Tycoons were at the forefront in both causing the "overproduction problem" and in finding a solution to it.[85] In the early years after the Civil War it was these and similar men whose innovations had led to tremendous productivity gains, huge increases in total output, and steadily falling prices.[86] Likewise it was these innovative entrepreneurs who later embraced horizontal and vertical integration and the creation of large business firms with increasingly sophisticated internal management bureaucracies in order to avoid market transactions as much as possible and ensure desired levels of profits.[87]

The great American entrepreneur instinctively understood that size in and of itself provides protection from uncertainty. And, under the persistent tutelage of powerful financier J.P. Morgan, they came to understand how to translate size into protection from the dictates of unfettered market competition.[88]

John Kenneth Galbraith later provided a theoretical explanation of how "bigness" and "cooperation" worked together to tame the market. Larger firms that retained earnings as a cushion could withstand market shocks that would destroy smaller firms.[89] Moreover, larger firms had greater ability to substitute planning for the uncertainties flowing from market determination of price and supply. This could be done by suspending, controlling, or superseding the market.[90] Large size equated to both power and reliability. A promise from Carnegie Steel Company

84. GALBRAITH, *supra* note 19, at 23–24.

85. MORRIS, *supra* note 55, at 106–18.

86. *Id.* at 102–03. Output increased dramatically across the economy. *Id.* at 102–06. Perhaps the most striking and important increase was in steel. "America had no steel production to speak of in 1870, but was neck and neck with Great Britain by the early 1880s." *Id.* at 102. By 1899 "the Carnegie Steel Company alone would outproduce Britain." GORDON, *supra* note 53, at 248.

87. *See* MORRIS, *supra* note 55, at 239.

88. *See id.* at xiii.

89. GALBRAITH, *supra* note 19, at 31–33.

90. *Id.* at 27.

could be relied upon to a great extent, whereas a promise from a small proprietorship was subject to substantial worry as to whether the proprietor could be trusted or would be able to perform as promised.[91] Thus, large firms could enter into long-term contracts with each other stipulating prices, amounts, and procedures for adjustment when unexpected contingencies warranted. Thus, Galbraith notes, "In a world of large firms, it follows, there can be a matrix of contracts by which each firm eliminates market uncertainty for other firms and, in turn, gives to them some of its own."[92] The large firm can also control the market vis-à-vis smaller firms by virtue of its market share. Smaller firms must take the price that the market offers. "Not so with [the larger firm]. Its decision to buy or not to buy will usually be very important to its suppliers; it may be a matter of survival. This induces a highly cooperative posture."[93] Finally, U.S. firms learned how to suppress the market via vertical integration—taking within themselves sub-processes that previously had been undertaken by independent suppliers. "As viewed by the firm, elimination of a market converts an external negotiation and hence a partially or wholly uncontrollable decision to a matter for purely internal decision."[94]

America presented its entrepreneurs with a unique geographic advantage in growing larger firms. To a greater extent than other countries, the United States had within its borders everything that a business needed.

> The larger and more populous the economic territory, [other things being equal] the larger the individual plant can be, the lower the costs of production, and the greater the degree of specialization within the plant, which also reduces costs of production. The larger the economic territory, the more easily can industry be located where the natural conditions are most favourable and the productivity of labour is highest. The more extensive the territory, the more diversified is production and the more probable it is that the various branches of production will complement one another and that transport costs on imports from abroad will be saved.[95]

During the 1870s and 1880s, businessmen sought to suppress the market primarily through cartels and trade associations.[96] This strategy did not survive the Supreme Court's interpretation of the Sherman Antitrust Act, enacted in 1890.[97] One path remained open. "After 1899 lawyers were advising their corporate clients to abandon all agreements or

91. *Id.* at 30–31.
92. *Id.*
93. *Id.* at 29.
94. *Id.* at 28.
95. RUDOLF HILFERDING, FINANCE CAPITAL: A STUDY OF THE LATEST PHASE OF CAPITALIST DEVELOPMENT 311 (Tom Bottomore ed., Morris Watnick & Sam Gordon trans., 1981).
96. *See* ALFRED D. CHANDLER, JR., THE VISIBLE HAND: THE MANAGERIAL REVOLUTION IN AMERICAN BUSINESS 316–17 (1977).
97. *Id.* at 331–33.

alliances carried out through cartels or trade associations and to consolidate into single, legally defined enterprises."[98]

As instructed, American entrepreneurs embraced vertical integration with fervor. From 1899 to 1901, a flurry of merger activity occurred, the likes of which would not be seen again until the 1960s.[99] With the creation of the United States Steel Company in 1901, the contours of the modern corporation were firmly in place. The next thirty years would simply witness the unfolding of this design.

The merger flurry that ushered in the twentieth century allowed a very small number of firms in each industrial sector to substitute internal decision making for the uncertainties of the market. These modern corporations were made up of numerous processes and sub-processes that could be, and often had been, conducted by separate and autonomous small firms.[100] The integrated firm then substituted internal, administrative decision making for the market transactions that occur between separate firms. As Alfred Chandler observed, internalization produces savings only if an effective internal decision-making organization exists.[101] Central to the success of the modern corporation was the creation of such systems.

> [The advantages of vertical integration] could be achieved only when a group of managers had been assembled to carry out the functions formerly handled by price and market mechanisms. Whereas the activities of single-unit traditional enterprises were monitored and coordinated by market mechanisms, the producing and distributing units within a modern business enterprise are monitored and coordinated by middle managers. Top managers, in addition to evaluating and coordinating the work of middle managers, took the place of the market in allocating resources for future production and distribution. In order to carry out these functions, the managers had to invent new practices and procedures which in time became standard operating methods in managing American production and distribution.[102]

The advantages of vertical integration produced a self-reinforcing feedback loop. Successful management innovations produced surplus cash flows that were plowed back into further improving internal processes. The result was the rapid hegemonic rise of the modern, multi-unit business firm.[103] "Almost nonexistent at the end of the 1870s, these integrated enterprises came to dominate many of the nation's most vital industries within less than three decades."[104] At the same time, these

98. *Id.* at 333. In addition to Supreme Court interpretation of the Sherman Act, vertical integration was further encouraged when New Jersey "modernized" its corporation laws to allow direct corporate ownership of out-of-state property. *See* Gordon, *supra* note 53, at 258–59.

99. MORRIS, *supra* note 55, at 252.

100. CHANDLER, *supra* note 96, at 50–121.

101. *See id.* at 7.

102. *Id.*

103. ARRIGHI, *supra* note 22, at 239.

104. CHANDLER, *supra* note 96, at 285.

modern firms used the advantages gleaned in conquering U.S. markets to compete abroad. "U.S. corporations began to move to foreign countries almost as soon as they had completed their continent-wide integration. . . . In becoming national firms, U.S. corporations learned how to become international."[105] By the coming of the first World War, American entrepreneurs were poised to benefit from the horror to be visited disproportionately on citizens of other lands.

B. World War I

Similar to the Civil War, World War I provided U.S. business with an enormous stimulus. Both Great Britain and Germany lost access to export markets, which turned instead to U.S. products.[106] Great Britain could no longer obtain supplies from many of its key suppliers and, in any event, needed to focus its production on war supplies.[107] Those needs could not be met with internal production. American industry was the primary beneficiary of this disruption.[108]

> Markets in Latin America and Asia, which had been served by European companies, were now open to be taken over by American firms. Far more important was the avalanche of orders that began to roll in to American firms from Great Britain and its allies, for steel, vehicles, railroad rolling stock, and rails. . . .
>
> Munitions, of course, were in the greatest demand by the British, French, and Italian militaries. Du Pont had been only a midsized manufacturer of gunpowder before the war, but would come to supply the Allies with fully 40 percent of their munitions. In the four years of the war, Du Pont's military business increased by a factor of 276. And it became one of the world's largest chemical companies as well. Germany had dominated the world's chemical industry in the decades before the war, but it lost its export market with the Royal Navy's blockade. Du Pont and other American chemical companies quickly seized that vast market. By the end of the war, Du Pont had annual revenues twenty-six times as large as they had been in 1913. . . .
>
> Overall, the gross national product of the United States increased by 21 percent in the four years of the war, while manufacturing increased by 25 percent.[109]

World War I accelerated the end of British world dominance. Before the war the United States was heavily indebted to Great Britain.[110] After the war, Great Britain was substantially in debt to the United

105. Stephen Hymer, *The Multinational Corporation and the Law of Uneven Development*, *in* ECONOMICS AND WORLD ORDER FROM THE 1970'S TO THE 1990'S, at 113, 121 (Jagdish N. Bagwhati ed., 1972).
106. *See* GORDON, *supra* note 53, at 288.
107. *See id.* at 286–89.
108. *Id.* at 286.
109. *Id.* at 288–89.
110. *Id.* at 293.

States.[111] Worse for Great Britain, its substantial loans to Russia could not be collected due to the Communist takeover.[112] The U.S. dollar joined the British pound as a world reserve currency.[113] While Britain was still powerful, its economy had been far surpassed by the U.S. economy, and the transfer of world hegemony was now unstoppable.[114]

For the United States' rapidly growing large firms, World War I was a godsend. Not only did it provide a Civil-War-like laboratory in which to further refine industrial, marketing, and sales processes and further develop internal bureaucracies for efficient, authoritarian resource management, war also paved the way for widespread public investment in the modern corporation's stocks and securities.[115] In 1915, the Dow Jones Industrial Average experienced its largest percentage gain in history.[116] The huge inflow in capital was coming from Americans investing their surplus income. At the same time, Britain and France were liquidating their U.S. investments to help finance the war.[117] The U.S. government and investors emerged from the war in control of the largest store of world capital.[118]

C. The Roaring Twenties

The decade following World War I—the Roaring Twenties—was a period of unprecedented wealth creation.[119] At the decade's center were the modern corporation and its managers. In basic concept, the modern corporation was fully mature by 1920. But there was much still to unfold before that maturity was fully realized in practice. During the decade, the great American corporations established ever greater control over their own enterprises and over the possibilities available to U.S. labor and capital.[120] The changes they wrought in themselves and the U.S. economy were hidden in plain sight, at least until the coming of the Great Depression.

America's possible replacement of Great Britain as global hegemon seemed possible in large part because of the modern corporation. During the 1920s, American firms prospered at the expense of foreign firms,

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111. *Id.*
112. *See* ARRIGHI, *supra* note 22, at 271.
113. *Id.*
114. *Id.*
115. GORDON, *supra* note 53, at 288–89.
116. *Id.*
117. *Id.* at 290.
118. ARRIGHI, *supra* note 22, at 279.
119. There was a brief but deep recession in 1920–1921. *See* CHRISTOPHER DOW, MAJOR RECESSIONS: BRITAIN AND THE WORLD, 1920–1995, at 146–57 (1998). And, of course, the Great Depression traces its onset to the stock market crash that began in late October, 1929. *See* ARTHUR M. SCHLESINGER, JR., THE AGE OF ROOSEVELT: THE CRISIS OF THE OLD ORDER: 1919–1933, at 157 (1957).
120. A.A. Berle, Jr. & Gardiner C. Means, *Corporations and the Public Investor,* 20 AMER. ECON. REV. 54, 56–57 (1930).

and Americans and American firms replaced the British as leading accumulators of foreign capital.[121]

> Throughout the 1920s productivity continued to grow faster in the United States than in any of the debtor countries, further increasing the competitive edge of US business and the difficulties of debtor countries to service, let alone repay, their debts. And as the dependence of the world's payments system on the US dollar increased, the United States acquired foreign assets "with a rapidity . . . which . . . is unparalleled in the experience of any major creditor nation in modern times."[122]

In a sense, the great industrial firms were merely working out the blueprint inherent in what we call the second industrial revolution. As U.S. industries continued to innovate, the publicly visible result was a rich array of new consumer products at what appeared to be constantly falling prices.

> Natural resources were readily available and cheap. Standardization and the techniques of mass production pioneered by Henry Ford allowed large companies to lower manufacturing costs and to sell their goods to an expanding market. The success of Ford and the automotive industry in general had a domino effect on other industries; many other companies took up Ford's policy of high wages and low prices, with work compartmentalized for increased efficiency.[123]

Along with this readily apparent enhancement in consumer goods at increasingly favorable prices came a revolutionary change in the nature of personal savings. The ordinary American experienced this as the decade's great romance with the stock market. Initial public offerings increased threefold from 1923 to 1927.[124] Sales in the secondary trading markets increased fourfold from 1923 to 1928.[125] Shares traded on the New York Stock Exchange rose in market value by almost 250% between 1925 and 1929.[126] For those who had savings, the stock market seemed the only place to put it.

This stock market boom accelerated the final stage in the construction of the modern corporation. As Adolf Berle first documented, the twenties saw a rapid shift in the control of both U.S. productive assets and U.S. dominant business enterprises.[127] By decade's end, U.S. industry was dominated by a handful of truly giant corporations, and a few hundred very large ones.[128]

121. ARRIGHI, *supra* note 22, at 281.
122. *Id.* at 273 (quoting MAURICE DOBB, STUDIES IN THE DEVELOPMENT OF CAPITALISM 332 (1963) (omissions in original)).
123. TOM STREISSGUTH, THE ROARING TWENTIES 276 (rev. ed. 2007).
124. SCHLESINGER, *supra* note 119, at 68.
125. *Id.*
126. *Id.*
127. BERLE & MEANS, *supra* note 1, at 18–19, 32–34.
128. *Id.* at 32.

> The size of the modern giant corporation is difficult to grasp. . . . On the basis of assets, the American Telephone and Telegraph Company would be equivalent to over 8,000 average sized corporations, and both the United States Steel Company and the Pennsylvania Railroad Company to over 4,000. . . . [T]he two hundred largest non-banking corporations . . . [had] combined assets [that] amounted to . . . nearly half of all corporate wealth in the United States . . . [and] roughly 22 per cent of the total wealth of the country.[129]

This concentration of wealth in the giant corporations had been occurring rapidly during the 1920s, with approximately one-sixth of productive property shifting from individual to corporate ownership during the last seven years of the decade. Berle correctly predicted that the trend would continue indefinitely.[130]

Equally important to the final maturation of the modern corporation was the dispersion of stock ownership and the resulting separation of ownership and control. As Berle documented, most of the giant corporations were controlled by managers who owned far less than a majority of the company's stock.[131] Theoretical voting control was dispersed among tens of thousands of passive investors who had no interest in or practical ability to participate in corporate management or the election of directors. Shareholders, if they bothered to vote at all, merely rubber-stamped the slate of directors nominated by the board itself.[132]

As Berle powerfully described, the modern corporation had now conquered the product and labor markets in every respect, and its managers—Berle's Princes of Industry—had conquered the market for corporate control supposedly residing in the annual election contest to be decided by a majority of the corporation's shareholders.[133] So long as the United States held to *laissez-faire* policies, the Princes of Industry would unilaterally determine how the gains from industry were distributed between and among themselves, shareholders, workers, and society as a whole.

The results of the roaring twenties demonstrated that without government intervention, the Princes of Industry and the shareholders (predominantly rentiers) would take a disproportionate share of the gains from industry. Though the economy prospered, and Americans in general benefited, the modern corporations and their managers fared even better. "Through the decade, profits rose over 80 per cent as a whole, or

129. *Id.* at 18–19, 31.

130. Berle, *supra* note 33, at 3–4 ("My co-author, V.E. Pederson and I estimated that in a single decade (1922–1932) more than one-sixth of the entire national wealth had shifted from individual hands into managerial—that is, corporate—hands, and we suggested that at that rate forty years would see the wealth of the entire country split, most of it being operated by corporate management . . . .").

131. *Id.* at 2.

132. BERLE & MEANS, *supra* note 1, at 81 ("The normal apathy of the small stockholder is such that he will either fail to return his proxy, or will sign on the dotted line, returning his proxy to the office of the corporation.").

133. *Id.* at 2, 124.

twice as much as productivity; the profits of financial institutions rose a fantastic 150 per cent."[134]

The incomes of managers and rentier shareholders[135] reflected this success. From 1920 to 1929, the share of national income going to the top one percent of Americans rose from 14.5% to almost 20%.[136] The CEOs of top American corporations were clearly in that group. While we do not have comprehensive data on CEO income relative to the average worker, we do know that incomes were substantial and at levels not to be seen again even in nominal terms until the 1960s.[137] In 1929, Eugene Grace, President of Bethlehem Steel, received total compensation of $1,623,753, the equivalent of $21,920,665 in 2012 dollars.[138] In the same year, John Ryan, Chairman of the Board of Anaconda Copper, was paid $300,000, the equivalent of $4,050,000 in 2012 dollars.[139]

As the 1920s roared to a close, the modern U.S. corporation and its managers sat at the pinnacle of the most powerful economy in the world. In two generations since the Civil War, the Great Tycoons and their successors had created the modern corporation, an economic engine of unparalleled efficiency. The modern corporation had conquered the market. Its managers determined what was bought and sold and at what prices. The U.S. President, Herbert Hoover, himself a self-made man and a wealthy former engineer and entrepreneur, was running the country on sound business principles.[140] The future looked bright indeed for the modern corporation and its managers as the twenties roared to a close.

134. SCHLESINGER, *supra* note 119, at 66.

135. Thomas Piketty & Emmanuel Saez, *Income Inequality in the United States: 1913–1998*, 118 Q. J. ECON. 1, 17 (2003).

136. *Id.* at 12 fig.2.

137. *See* Harwell Wells, "*No Man Can Be Worth $1,000,000 a Year": The Fight over Executive Compensation in 1930s America*, 44 U. RICH. L. REV. 689, 690 (2010) ("[A] series of disclosures revealed that executives at some of the nation's largest corporations had made huge sums in the years immediately before the Great Crash. A few executives even earned the then-unthinkable sum of $1 million a year . . . .").

138. ROBERT HESSEN, STEEL TITAN: THE LIFE OF CHARLES M. SCHWAB 270 (1975). Calculations are based on the Minneapolis Federal Reserve Bank yearly CPI calculator, comparing 1929 to 2012. *See Consumer Price Index*, FED. RES. BANK MINNEAPOLIS, http://www.minneapolisfed.org/community_education/teacher/calc/hist1913.cfm (last visited Mar. 27, 2013).

139. BERNARD J. REIS, FALSE SECURITY: THE BETRAYAL OF THE AMERICAN INVESTOR 22 (1937).

140. SCHLESINGER, *supra* note 119, at 77–89.

III. THE GREAT DEPRESSION—THE IMPETUS FOR CHANGE

A. Overview

After World War I, the United States surpassed Great Britain economically, but not in terms of what we now call "soft power."[141] Britain still had the monetary and banking leadership of the world via its central bank and related institutions. Its political institutions and bureaucracies dwarfed those of the still quite lean U.S. government. And its business organizations were still much more tightly connected with political actors in consciously pursuing British interests.[142] The Great Depression exposed the shortcomings of U.S. monetary and governmental institutions, and starkly illuminated the need for a new relationship between government and the modern corporation. These needs, however, had a larger international context. British world hegemony was now clearly over, but a new hegemon was not yet in place. If the United States was to assume that role, it would need to escape the limiting, and now thoroughly discredited, tendrils of *laissez-faire* individualism. The Great Depression provided the necessary "shock," and the 1932 election campaign provided the political crucible for beginning that transition.

B. Reframing the Relationship Between Government and the Modern Corporation

1. Darkness

In the aftermath of the stock market crash of October 1929, the United States rapidly descended into the Great Depression. At first, government and business leaders assumed that a turnaround would naturally occur with only mild government nostrums required.[143] But this depression was different than the doldrums the country had experienced periodically in the last three decades of the nineteenth century. This time ordinary people suffered terribly as compared to business.[144] The great modern corporations were no longer subject to market control. Rather than suffer lower profits, the modern corporations cut wages, reduced production, and laid off workers.[145] The modern corporations got

141. The term "soft power" refers to the non-coercive or non-military mechanisms that enable a nation to accomplish its political and economic ends. Joseph Nye coined the term in 1990 and has been responsible for its development into an internationally recognized concept. For his account of the evolution of the concept, and the misunderstanding which its use sometimes generates, see JOSEPH S. NYE, JR., SOFT POWER: THE MEANS TO SUCCESS IN WORLD POLITICS, at ix–xiii (2004).

142. ARRIGHI, *supra* note 22, at 298–99, 302–04.

143. SCHLESINGER, *supra* note 119, at 177–80.

144. *See* MURRAY N. ROTHBARD, A HISTORY OF MONEY AND BANKING IN THE UNITED STATES: THE COLONIAL ERA TO WORLD WAR II, at 161–65 (2002); CHANDLER, *supra* note 96, at 316–317.

145. SCHLESINGER, *supra* note 119, at 249–51 ("The Year 1932 brought new anguish. By spring, when United States Steel made its second large wage slash, the attempt to maintain pay scales had pretty well foundered.").

leaner but retained full functionality and the ability to make a profit.[146] Many Americans, adults and children, got leaner, much leaner, in body and in spirit. There was no work and no way to put food on the table.[147] "Faith in life itself seemed to be ebbing away: the national birthrate for 1931 was 17 per cent below 1921 and 10 per cent below 1926."[148]

The Great Depression was a tremendous shock to the American psyche. It caused even conservative businessmen to understand at a visceral level that fundamental change was necessary—or else. As the depression deepened, Daniel Willard, long-time president of the Baltimore and Ohio Railroad, was representative of this emerging consensus:

> Throughout his seventy years he had never questioned the capitalist order. Yet a system that denied millions of men work and relief, he had come to feel, could not "be said to be perfect or even satisfactory." The problems of unemployment and the distribution of wealth were forcing him to doubt "the very foundations of our political and economic system." For himself, he continued, "I would steal before I would starve."[149]

The presidential campaign of 1932 was fought over which vision would govern the United States going forward—the long dominant *laissez-faire* individualism or a different model of corporate capitalism. Some progressives leaned towards socialism or communism.[150] Others hewed to the old populist dream—a world in which there were no "big" businesses and the market magically produced a just society.[151] Herbert Hoover staked his political future on maintaining the status quo.[152] But the bulk of progressives and mainstream policy makers circled around a new relationship between government and the modern corporation that better served the public and the nation.[153] And Franklin Roosevelt, cautiously, placed his chips on the side of a more assertive role for government, particularly in its relationship with the modern corporation.[154] Roosevelt's bet was the winner.

146. *Id.* at 249–51.

147. The following is a small excerpt from Arthur Schlesinger's wrenching account:

> The Philadelphia Community Council described its situation in July 1932 as one of "slow starvation and progressive disintegration of family life." In the Pennsylvania coal fields, miners kept up a subdued battle against starvation, freezing in rickety one-room houses, subsisting on wild weed-roots and dandelions, struggling for life in black and blasted valleys. In Kentucky . . .wan children attended school without coats, shoes or underclothes.

Id. at 250.

148. *Id.* at 251.

149. *Id.* at 180–81.

150. *Id.* at 204–23, 435–36.

151. *See id.* at 418–19; ARTHUR M. SCHLESINGER, JR., THE AGE OF ROOSEVELT: THE POLITICS OF UPHEAVAL 234 (1960) (stating that in Justice Brandeis's view, "bigness was always badness").

152. SCHLESINGER, *supra* note 119, at 295–96.

153. *See id.* at 423.

154. *Id.* at 422–34.

2. *Reimagining Individualism—Berle and the American Narrative*

The reshaping of the U.S. relationship with the modern corporation followed the ideological blueprint and reimagining of America articulated by Adolf Berle.[155] Berle was the perfect person for the task. With the passing of Thorstein Veblen, Berle had become the public intellectual with the widest and deepest understanding of history, corporation law, economics, and politics. And, unlike Veblen, Berle was not a cynic. He saw his task not as demolishing the existing institutions, but in building on them.[156] Moreover, unlike Veblen, Berle was at the right place at the right time. In 1930, he published a law review article detailing research into the nature of the modern corporation.[157] This report, along with earlier law review articles written by Berle, transmuted into Berle's seminal work, *The Modern Corporation and Private Property*, published first in 1931, and then republished in 1932.[158] In it, Berle detailed the fundamental nature of the modern corporation, and the unfettered power that separation of ownership and control bestowed on corporate managers—the Princes of Industry.[159] The book was received by progressive policy makers, hungry for ammunition in the coming fight to reshape America, as a rich source book of near biblical significance.[160]

In 1932, Berle was drawn into Franklin Roosevelt's campaign in large measure because of this visionary work on the modern corporation. Behind the scenes, Berle and a handful of other public intellectuals and leaders fought to shape the vision that Roosevelt would take to the American people and that would form the framework for his first administration.[161] Berle found in Roosevelt a receptive ear. Though not an intellectual himself,[162] Roosevelt understood the need for a positive framing of the coming changes, and Berle offered an intellectual but pragmatic vision.[163]

On August 15, 1932, Berle proposed that Roosevelt deliver a major address tackling head-on Hoover's insistent harping on the theme of "individualism."[164] Berle had in mind an address that would help define a core difference between Hoover and Roosevelt. Hoover conflated "individualism" with the continuance of a *laissez-faire* relationship between

155. Particularly in his seminal work, THE MODERN CORPORATION AND PRIVATE PROPERTY and in the important campaign speech, "The New Individualism," one of Roosevelt's greatest speeches.

156. O'Kelley, *supra* note 2, at 1156–57.

157. Berle & Means, *supra* note 120.

158. Bratton & Wachter, *supra* note 36, at 105–22.

159. *Id.* at 120.

160. *Id.*

161. *Id.* at 109–10.

162. SCHLESINGER, *supra* note 119, at 407–09 ("His intellectual processes had always been intuitive rather than logical. He often thought lazily and superficially.").

163. *Id.* at 426–27 ("[T]he Commonwealth Club address provided impressive reasons for enlarging the role of government. For Roosevelt, who was more interested in results than in systems, this was probably more important than the basic framework of interpretation.").

164. Davis W. Houck, *FDR's Commonwealth Club Address: Redefining Individualism, Adjudicating Greatness*, 7 RHETORIC & PUB. AFF. 259, 265–66 (2004).

government and the modern corporation.[165] Berle wanted Roosevelt to expose Hoover and develop a new understanding: the individual cannot prosper unless the modern corporation is brought to heel. Roosevelt concurred.[166]

On the night of September 22, 1932, Roosevelt received Berle's final draft; it was Roosevelt's first look at the speech. "He read it over, made a few slight corrections, and that was that."[167] The following day, at noon, Roosevelt delivered "his" famous speech to the Commonwealth Club in San Francisco.[168] Later it would be heralded as one of the twentieth century's greatest addresses,[169] a result that could be seen as undeserved.[170] True, the speech attracted less immediate attention when delivered than other of Roosevelt's major campaign addresses.[171] True, the academic points represented Berle's intellect more than Roosevelt's.[172] Detractors, however miss the larger point. The speech[173] represents the view of the modern corporation and its relation to government and society that would prevail for the next forty years.

Berle correctly saw the modern corporation as an amazingly productive engine, but he saw the remnants of the Great Tycoons' control as a now totally useless, indeed destructive, appendage. With his historian's eye, he pulled together a grand narrative that honored the past and reaffirmed America's commitment to individualism, but a new individualism grounded in an active partnership between the modern corporation and government. It was a story of the ebb and flow of recurrent themes. It was a story running from the United States of America's European roots, through its founding, and into its future.[174]

The first recurrent theme was society's periodic need for "[men] of ruthless force."[175] Berle described Europe's transition from feudalism and the establishment of the Americas' colonies as a fight for individual freedom and security in which men of ruthless force played the lead role.[176]

> When we look about us, we are likely to forget how hard people have worked to win the privilege of government. The growth of the national governments of Europe was a struggle for the devel-

165. *Id.* at 266.
166. *Id.* at 266–67.
167. *Id.* at 262 (quoting Raymond Moley).
168. *Id.*
169. *Id.* at 262–63.
170. *Id.* at 275–77.
171. *Id.* at 262.
172. *Id.* at 262, 275–76.
173. President Franklin Delano Roosevelt, Commonwealth Club Address (Sept. 23, 1932), *available at* http://www.americanrhetoric.com/speeches/fdrcommonwealth.htm [hereinafter Commonwealth Club Address].
174. Some of the "details" of this story were implicit in the San Francisco speech, but detailed by Berle elsewhere. I include that other detailing as part of the overall "story" told by the San Francisco speech.
175. *See* Commonwealth Club Address, supra note 173; *see also* Houck, *supra* note 164, at 268–69.
176. *See* Houck, *supra* note 164, at 268–69.

> opment of a centralized force in the nation, strong enough to impose peace upon ruling barons. In many instances the victory of the central government, the creation of a strong central government, was a haven of refuge to the individual. The people preferred the master far away to the exploitation and cruelty of the smaller master near at hand.
>
> But the creators of national government were perforce ruthless men. They were often cruel in their methods, but they did strive steadily toward something that society needed and very much wanted, a strong central state, able to keep the peace, to stamp out civil war, to put the unruly nobleman in his place, and to permit the bulk of individuals to live safely. The man of ruthless force had his place in developing a pioneer country, just as he did in fixing the power of the central government in the development of nations.[177]

Berle then introduced his second theme: the need for ruthless men to bring order out of chaos eventually runs its course; then, countervailing power must be introduced to reestablish the rights of the individual.[178] This was the case in the three revolutions most important to our own development: the English Revolution of 1688, and the late eighteenth-century American and French Revolutions.

> There came a growing feeling that government was conducted for the benefit of a few who thrived unduly at the expense of all. The people sought a balancing—a limiting force. There came gradually, through town councils, trade guilds, national parliaments, by constitution and by popular participation and control, limitations on arbitrary power.[179]

Berle then introduced his third theme: reestablishing the rights of the individual after a period of rule by ruthless men always involves a contest between those who would preserve as much of the old power as possible against those who believe that power should be distributed and determined democratically.[180]

The United States, after its struggle for independence from Great Britain, had faced two different visions. Hamilton "believed that the safety of the republic lay in the autocratic strength of its government, that the destiny of individuals was to serve that government, and that fundamentally a great and strong group of central institutions, guided by a small group of able and public spirited citizens could best direct all government."[181] In Jefferson's opposing view, which prevailed in the election of 1800, government should not be an end in itself; rather government existed to serve the people.[182]

177. Commonwealth Club Address, *supra* note 173.
178. Houck, *supra* note 164, at 269.
179. Commonwealth Club Address, *supra* note 173.
180. Houck, *supra* note 164, at 269.
181. Commonwealth Club Address, *supra* note 173.
182. *Id.*

With Jefferson's election, the golden age of individualism unfolded in America.

> So began, in American political life, the new day, the day of the individual against the system, the day in which individualism was made the great watchword of American life. The happiest of economic conditions made that day long and splendid. On the Western frontier, land was substantially free. No one, who did not shirk the task of earning a living, was entirely without opportunity to do so. Depressions could, and did, come and go; but they could not alter the fundamental fact that most of the people lived partly by selling their labor and partly by extracting their livelihood from the soil, so that starvation and dislocation were practically impossible. At the very worst there was always the possibility of climbing into a covered wagon and moving west where the untilled prairies afforded a haven for men to whom the East did not provide a place.[183]

In the United States, then, the individual replaced the autocrat. In so doing, the United States was relocating power, not eliminating it, and adopting the system of economic liberty that we attribute to Adam Smith.[184]

> Whereas the organization of feudal economic life rested upon an elaborate system of binding customs, the organization under the system of private enterprise has rested upon the self-interest of the property owner—a self-interest held in check only by competition and the conditions of supply and demand. Such self-interest has long been regarded as the best guarantee of economic efficiency. It has been assumed that, if the individual is protected in the right both to use his own property as he sees fit and to receive the full fruits of its use, his desire for personal gain, for profits, can be relied upon as an effective incentive to his efficient use of any industrial property he may possess.[185]

Government had a limited role at the outset of America. "[E]ven Jefferson realized that the exercise of the property rights might so interfere with the rights of the individual that the government, without whose assistance the property rights could not exist, must intervene, not to destroy individualism but to protect it."[186] Conditions during America's golden age of individualism did not make the need for government intervention likely, however. Ownership and control were still united, and that naturally limited the possibility of individual abuse of power.

> At that time, ownership and possession, or at least ownership and management, were substantially united. What was known as the absentee owner was the exception rather than the rule, and a man could control his property *in absentia* only in the most precari-

183. *Id.*
184. BERLE & MEANS, *supra* note 1, at 345.
185. *Id.* at 8.
186. Commonwealth Club Address, *supra* note 173.

> ous ways. The richest man in the United States at the time the Constitution was adopted was George Washington; and to him, riches—unlimited right of possession—meant his broad acres of Mount Vernon, a couple of stud farms which he kept not so far away . . . and a few other bits of property, all under his direct and immediate supervision. What is known as the corporation hardly existed. . . .
>
> In a word, there was no way by which the property idea which was guaranteed to individuals in the Constitution . . . could extend very much beyond two great limitations. The first was the power of the individual to manage and assume responsibility, and the second, his willingness to assume direct legal liability for the results in terms of debts or damages.[187]

But the golden age of individualism would be short lived. As the eighteenth century reached midpoint, what we now call the second industrial revolution presented opportunities that the United States could not ignore. The old concept of individualism still reigned in men's hearts and minds, but it was again time for ruthless men of force to take the lead and reap the rewards.

> It was the middle of the 19th century that a new force was released and a new dream created. The force was what is called the industrial revolution, the advance of steam and machinery and the rise of the forerunners of the modern industrial plant. The dream was the dream of an economic machine, able to raise the standard of living for everyone; to bring luxury within the reach of the humblest; to annihilate distance by steam power and later by electricity, and to release everyone from the drudgery of the heaviest manual toil. It was to be expected that this would necessarily affect government.
>
> Heretofore, government had merely been called upon to produce conditions within which people could live happily, labor peacefully, and rest secure. Now it was called upon to aid in the consummation of this new dream. There was, however, a shadow over the dream. To be made real, it required use of the talents of men of tremendous will, and tremendous ambition, since by no other force could the problems of financing and engineering and new developments be brought to a consummation.
>
> So manifest were the advantages of the machine age, however, that the United States fearlessly, cheerfully, and, I think, rightly, accepted the bitter with the sweet. It was thought that no price was too high to pay for the advantages which we could draw from a finished industrial system. The history of the last half century is accordingly in large measure a history of a group of financial Titans, whose methods were not scrutinized with too much care, and who were honored in proportion as they produced the results, irrespec-

187. A.A. Berle, Jr., *The New Deal and Economic Liberty*, 178 ANNALS AM. ACAD. POL. & SOC. SCI. 37, 38 (1935).

> tive of the means they used. The financiers who pushed the railroads to the Pacific were always ruthless, we have them today. It has been estimated that the American investor paid for the American railway system more than three times over in the process; but despite that fact the net advantage was to the United States. As long as we had free land; as long as population was growing by leaps and bounds; as long as our industrial plants were insufficient to supply our needs, society chose to give the ambitious man free play and unlimited reward provided only that he produced the economic plant so much desired.[188]

Berle's story then moves to his present—the presidential election year of 1932. The Roaring Twenties and its celebration of big business have come to a crashing end. The Great Depression is intensifying. Unemployment is at record levels. Despair is everywhere. Plants sit idle, while men hunger for work. And in this time of desperate suffering, the part of the United States that is suffering the least are the modern corporations and their managers. While ordinary men and women cannot put food on the table or find a job, the Princes of Industry are still wealthy and in control of their powerful firms. They, individually and collectively, are getting more and more powerful.

> Recently a careful study was made of the concentration of business in the United States. It showed that our economic life was dominated by some six hundred odd corporations who controlled two-thirds of American industry. Ten million small business men divided the other third. More striking still, it appeared that if the process of concentration goes on at the same rate, at the end of another century we shall have all American industry controlled by a dozen corporations, and run by perhaps a hundred men. Put plainly, we are steering a steady course toward economic oligarchy, if we are not there already.[189]

The story's next move is crucial. A strong sentiment simmered among progressives for a return to the golden age of individualism.[190] It was a view championed by Justice Brandeis and others[191] to whom Roosevelt might listen: if the modern corporation and the evolving corporation system threatened to become an economic oligarchy more powerful than government, then was not the answer to put real teeth in the antitrust laws and break these industrial giants into small pieces? The answer Roosevelt delivered in San Francisco was "yes" to government intervention, but a resounding "no" to an attack on "bigness."

> Just as in older times the central government was first a haven of refuge, and then a threat, so now in a closer economic system the central and ambitious financial unit is no longer a servant of na-

188. Commonwealth Club Address, *supra* note 173.
189. *Id.*
190. *See* SCHLESINGER, *supra* note 119, at 27–33.
191. ARTHUR M. SCHLESINGER, JR., THE AGE OF ROOSEVELT: THE COMING OF THE NEW DEAL (1959).

> tional desire, but a danger. I would draw the parallel one step farther. We did not think because national government had become a threat in the 18th century that therefore we should abandon the principle of national government. Nor today should we abandon the principle of strong economic units called corporations, merely because their power is susceptible of easy abuse. In other times we dealt with the problem of an unduly ambitious central government by modifying it gradually into a constitutional democratic government. So today we are modifying and controlling our economic units.[192]

It was important, however, to emphasize that the modern corporations were not the root cause of the Great Depression or of the larger malaise. Much of the problem could be traced to the breakdown of the international order—to the inability of Great Britain to maintain economic hegemony after the catastrophe of World War I. The era of free trade was over, and the U.S. insistence on steadily raising tariffs had finally passed the limits of other countries' tolerance.[193] Corporations, following the "logic of profit" had no choice but to reduce employment in America.

> Our system of constantly rising tariffs has at last reacted against us to the point of closing our Canadian frontier on the north, our European markets on the east, many of our Latin American markets to the south, and a goodly proportion of our Pacific markets on the west, through the retaliatory tariffs of those countries. It has forced many of our great industrial institutions who exported their surplus production to such countries, to establish plants in such countries within the tariff walls. This has resulted in the reduction of the operation of their American plants, and opportunity for employment.[194]

Likewise, advances in production processes and of "science" generally, combined with the profit imperative, left individual corporations with no choice but to eliminate jobs. Examples abounded.

> In the railroad field, for example, in which a few years ago 1,800,000 men were employed, and now approximately 1,000,000, the best traffic experts in the field estimate that if business were to return to 1929 levels tomorrow, they would employ approximately 1,250,000 men, leaving about 550,000 men permanently out of employment, because they have learned in the years of the depression to do their job more efficiently.[195]

There were areas where the modern corporations were at fault and where their power needed to be curbed. But this could not be an across-the-board restraint on management power. What was needed was re-

192. Commonwealth Club Address, *supra* note 173.
193. *See id.*
194. *Id.*
195. Berle, *supra* note 187, at 46.

straint on management's ability to self-deal, not its ability to manage the business.

> A management may well insist on as free a managerial hand as possible as to how it shall run its business. Nor has anyone grudged managements this group of powers, not only in law but in ideology. No better principle in carrying on business has yet been worked out than to find able men and give them the completest latitude possible in handling the enterprise.
>
> Latitude of power in the field of distribution of interests or as affecting the property rights of the participants raises different issues. It is one thing to say that a management shall be sole judge of how a factory shall be run. It is quite another to give that same group sole power to determine which of the various groups in a corporation shall receive the income; or to give it power to take away at will rights formerly belonging to stockholders and hand them over to outsiders or appropriate them to the management.[196]

The disproportionate rewards claimed by the Great Tycoons could no longer be afforded or justified. The American frontier had closed. The second industrial revolution was essentially complete. Now was the time for a reorientation of the modern corporation and the empowerment of the U.S. government. It was time for a new deal.

> Clearly, all this calls for a re-appraisal of values. A mere builder of more industrial plants, a creator of more railroad systems, and organizer of more corporations, is as likely to be a danger as a help. The day of the great promoter or the financial Titan, to whom we granted anything if only he would build, or develop, is over. Our task now is not discovery or exploitation of natural resources, or necessarily producing more goods. It is the soberer, less dramatic business of administering resources and plants already in hand, of seeking to reestablish foreign markets for our surplus production, of meeting the problem of under consumption, of adjusting production to consumption, of distributing wealth and products more equitably, of adapting existing economic organizations to the service of the people. The day of enlightened administration has come.[197]

The framework had now been laid for both the New Deal, the taming of the modern corporation, and, ultimately, the United States of America's ascension to the role of world hegemon. All that remained were the details.

196. Berle & Means, *supra* note 157, at 60.
197. Commonwealth Club Address, *supra* note 173.

IV. THE RISE OF THE AMERICAN EMPIRE—FROM THE NEW DEAL TO 1950

A. Overview

As Franklin Roosevelt assumed the presidency on Saturday, March 4, 1933, the United States and the world were in crisis.[198] The Great Depression roared on. The international order was disintegrating. War lurked around the corner. Roosevelt would preside over the U.S. response to this chaos—a response that upon the close of World War II would see a transformed American state assume the mantle of world hegemon.[199] From Roosevelt's presidency to the early 1970s, the United States of America would develop and rule a new world economic order. The modern corporations and its managers would be transformed in this period; the corporations would become fully partnered with the U.S. government in the orderly administration of the U.S. economy and society; the managers would recede into the twilight, no longer Titans, content in their role as enlightened administrators of the technocracy, content along with shareholders in receiving a lesser share of U.S. wealth.[200] The modern corporations, however, would remain in control of their changed environment, locked in a mutually advantageous, symbiotic relationship with government. Berle's vision of a dynamic partnership between the modern corporation and government—a vision of capitalism embedded within a socially democratic society[201]—would be realized.

B. The New Deal—The Partnerships Between Government and the Modern Corporation

The New Deal unfolded over Roosevelt's first two terms. In the famous first hundred days, a landslide of legislation began the United States of America's transition from *laissez-faire* to a Keynesian activist state.[202] Over the remainder of the 1930s and the course of World War II, the new relationships between government and the modern corporation

198. SCHLESINGER, *supra* note 119, at 480–85.

199. For discussion of the attributes of hegemony, see ARRIGHI, *supra* note 22, at 30–33. The U.S. ascension to full hegemony coincided with the end of World War II. *Id.* at 338–39.

200. For comprehensive treatment of this point, see GALBRAITH, *supra* note 19.

201. I use the term "social democracy" with the meaning ascribed by Tony Judt:

> A liberal is someone who opposes interference in the affairs of others: who is tolerant of dissenting attitudes and unconventional behavior. . . . Most genuine liberals remain disposed to leave other people alone.
>
> Social democrats, on the other hand, are something of a hybrid. They share with liberals a commitment to cultural and religious tolerance. But in public policy social democrats believe in the possibility and virtue of collective action for the collective good. Like most liberals, social democrats favor progressive taxation in order pay for public services and other social goods that individuals cannot provide themselves; but whereas many liberals might see such taxation or public provision as a necessary evil, a social democratic vision of the good society entails from the outset a greater role for the state and the public sector.

TONY JUDT, ILL FARES THE LAND 4–5 (2010).

202. *Id.* at 41–80.

emerged. Decentralized governance of the economy had failed. The modern corporations were alone incapable of providing opportunity, incomes, and security to the American worker. Nor were the modern corporations able to control the overall stability of the economy. It was time for government to enter the fray.

With respect to the modern corporation, the New Deal began with a radical departure from *laissez-faire* individualism—the adoption of the National Industrial Recovery Act of 1933 (the NRA).[203] The leaders of America's great corporations were ready for the change. Presaging the NRA was the idea put forth most prominently by Gerald Swope, then president of General Electric.

> Swope's idea was the organization into trade associations of all firms with more than 50 employees engaged in interstate business. These trade associations would be self-governing units with responsibility for "coordinating" production and consumption and "stabilizing" prices; to accomplish this coordination, there would have to be uniform accounting practices and access to company books. The companies would further adopt pension and unemployment insurance systems, to be paid for and managed by both employers and employees. On top of the cluster of trade associations would be a national economic council. In short, in exchange for the cartelization of a substantial part of American industry, Swope proposed to guarantee to labor a high degree of employment or, that failing, unemployment insurance.[204]

Title I of the NRA authorized cartelization along the lines proposed by Swope.[205] Title II of the same act authorized a broad public works program.[206] The goal was to quickly stimulate demand, while putting in place the apparatus of central economic planning.[207] At the signing ceremony on June 16, 1933, President Roosevelt elaborated.

> The purpose of the bill, the President said . . . was to put people back to work. It was to raise the purchasing power of labor by limiting hours and increasing wages. It was to elevate labor standards by making sure that no employer would suffer competitive disadvantages as a result of paying decent wages or establishing decent working conditions. Above all, it represented an historic experiment in government partnership with business.[208]

Prophetically, Roosevelt concluded, "History probably will record the National Industrial Recovery Act as the most important and far-reaching legislation ever enacted by the American Congress."[209] Despite

203. National Industrial Recovery Act of 1933, ch. 90, 48 Stat. 195 (partially overturned by A.L.A. Schechter Poultry Corp. v. United States, 295 U.S. 495 (1935)).
204. SCHLESINGER, *supra* note 119, at 182.
205. SCHLESINGER, *supra* note 191, at 98–99.
206. *Id.* at 99.
207. *Id.* at 102.
208. *Id.*
209. *Id.*

the Supreme Court's repeal of much of the NRA in 1935,[210] Roosevelt's pronouncement proved correct. The NRA signified national agreement on the future partnership of government and the modern corporation. Some details would ultimately be worked out in context-specific legislation—for example, the National Labor Relations Act, and the Social Security Act. More important, however, was the shared understanding between government and business elites: America could recognize its promise only through the partnership between two equal forces—the modern corporation and a strengthened, activist, U.S. government.[211]

As the 1930s drew to a close, the United States had transformed from *laissez-faire* governance to a modern social democracy. Government and business had accepted Keynesianism as the answer to business cycles and periodic fluctuations in demand.[212] Put simply, "[t]he essence of the New Deal was the notion that big government must spend liberally in order to achieve security and progress."[213] The 1930s provided only a limited opportunity to test the possibilities of the Keynesian state. World War II would fill that gap.

C. 1940 to 1950—World War II and Post-War Reconstruction

World War II provided the final impetus for U.S. world hegemony. Entering the 1940s, the United States was the world's greatest economic power[214] but clung to isolationism. The United Sates still viewed World War I as a mistake not to be repeated. Congress had spun a web of neutrality-enforcing legislation intended to prevent a repeat engagement.[215]

210. *See* A.L.A. Schechter Poultry Corp. v. United States, 295 U.S. 495 (1935).

211. SCHLESINGER, *supra* note 191, at 103–76. Schlesinger summarizes the NRA's lasting impact as follows:

> The more enduring achievements of NRA lay not in the economic but in the social field. Here NRA accomplished a fantastic series of reforms, any one of which would have staggered the nation a few years earlier. It established the principle of maximum hours and minimum wages on a national basis. It abolished child labor. It dealt a fatal blow to sweatshops. It made collective bargaining a national policy and thereby transformed the position of organized labor. It gave new status to the consumer. It stamped out a noxious collection of unfair trade practices. It set new standards of economic decency in American life—standards which could not be rolled back, whatever happened to NRA. . . .
>
> More than this, NRA helped break the chains of economic fatalism which had so long bound the nation. . . . The psychological stimulus gave people new confidence in their capacity to work out their economic salvation. . . . Of equal importance, NRA taught the people the meaning and implications of the national economy. . . . It accustomed the country to the feasibility of government regulation and taught people to think in terms of national policy for business and for labor.

Id. at 174–75.

212. *Id.* at 219–30 (describing the genesis of John Maynard Keynes's personal and intellectual influence on American monetary and fiscal policy).

213. FRANZ SCHURMANN, THE LOGIC OF WORLD POWER: AN INQUIRY INTO THE ORIGINS, CURRENTS, AND CONTRADICTIONS OF WORLD POLITICS 67 (1974).

214. *See* ARRIGHI, *supra* note 22, at 284–85 ("In 1938 US national income was already about the same as the combined national incomes of Britain, France, Germany, Italy and the Benelux countries, and almost three times that of the USSR.").

215. CHARLES A. STEVENSON, WARRIORS AND POLITICIANS: US CIVIL-MILITARY RELATIONS UNDER STRESS 95–96 (2006).

Content with the protection provided by its geographic insularity,[216] the United States had invested little in its military.[217]

> The US military was a pitiful force, labeled by General George C. Marshall "a third-rate power." The US army in 1939 ranked nineteenth in size, between Portugal and Bulgaria, and was forty-fifth in terms of the percentage of the population under arms. Its units were mostly under strength, and it did not even have enough ammunition for target practice.[218]

As the war in Europe spread, however, American sentiment gradually changed. Slowly the United States began to rearm. With Japan's attack on Pearl Harbor, isolationism vanished, and the United States mobilized on an unparalleled scale.[219] For the first time since the Great Depression, all who wanted work could find it.[220] The United States now could experiment on a grand scale with Keynesianism and the new relationship between government and business.

And experiment on a grand scale it did. Just as it had done in World War I, "the United States acted as the workshop of the Allied war effort."[221] The U.S. government served as central coordinator of economic production, determining what should be produced, providing financing to accelerate construction of new facilities, and tightly controlling prices and wages.[222]

> It [was] one of the most astonishing feats in all economic history. In the first six months of 1942, the government gave out more than $100 billion in military contracts, more than the entire gross national product of 1940. In the war years, American industry turned out 6,500 naval vessels; 296,400 airplanes; 86,300 tanks; 64,546 landing craft; 3.5 million jeeps, trucks, and personnel carriers; 53 million deadweight tons of cargo vessels; 12 million rifles, carbines, and machine guns; and 47 million tons of artillery shells, together with millions of tons of uniforms, boots, medical supplies, tents, and a thousand other items needed to fight a modern war. . . . [From 1940 to 1945] GNP increased by 56.3 percent.[223]

At war's end, the United States began its reign as world hegemon. "[T]he world was in a shambles but the national wealth and power of the United States had reached unprecedented and unparalleled heights."[224] The United States had seventy percent of the world's gold reserves and total control over world liquidity.[225] The United States had the world's largest pool of consumption capacity and investment capital. It had the

216. *Id.* at 93.
217. *Id.* at 93–94.
218. *Id.* at 93.
219. GORDON, *supra* note 53, at 353.
220. *Id.* at 358.
221. ARRIGHI, *supra* note 22, at 275.
222. GORDON, *supra* note 53, at 353–59.
223. *Id.* at 353–54, 357.
224. ARRIGHI, *supra* note 22, at 275–76.
225. *Id.* at 275.

strongest military. And its modern corporations provided the world's most efficient production capacity.

The American state now turned to reestablishing international order. It did not repeat the errors of World War I. Rather than humiliating the defeated nations, the United States focused its efforts on rebuilding Germany and Japan in its own image as model social democracies.[226] Similar efforts were focused broadly on the reconstruction of Europe via the Marshall plan.[227]

> Thus, postwar security would require liberal outlays by the United States in order to overcome the chaos created by the war. . . . Aid to . . . poor nations would have the same effect as social welfare programs within the United States—it would give them the security to overcome chaos and prevent them from turning into violent revolutionaries. Meanwhile, they would be drawn inextricably into the revived world market system. . . . Helping Britain and the remainder of Western Europe would rekindle economic growth, which would stimulate transatlantic trade and, thus, help the American economy in the long run.[228]

The refinement and execution of this plan would frame the age of U.S. world hegemony—the period running from the end of World War II to 1973.

V. 1950 TO 1973—THE HEYDAY OF AMERICAN CAPITALISM

The golden era of the modern corporation corresponds with the period of American world hegemony. The period begins around 1950, when U.S. post-World War II reconstruction efforts had stabilized Europe and Japan, and when hostilities in the Korean Peninsula had reached the boiling point; the endpoint coincides with America's acceptance of defeat in the Vietnam War in early 1973.[229] During this period the world economy experienced unprecedented growth fueled by U.S. militarization.[230] U.S. corporations were critical partners in this effort, and, like the American state, experienced a period of unprecedented growth and security.[231] During this period, as Berle had forecast, the modern corporation increased its control over U.S. industry. Further, as Berle had predicted, the Great Tycoons, the ruthless men of force, receded into the crannies of U.S. business. Within the modern corporation, managers were but part of the technocracy. As such, the compensation they received paled in comparison to pre-Great Depression business

226. *Id.* at 296.
227. *Id.*
228. SCHURMANN, *supra* note 213, at 67.
229. *See* ARRIGHI, *supra* note 22, at 306–07; THOMAS J. MCCORMICK, AMERICA'S HALF-CENTURY: UNITED STATES FOREIGN POLICY IN THE COLD WAR 99 (1989).
230. MCCORMICK, *supra* note 229, at 92–99 (noting that the United States consciously adopted militarism as the best way to spur the economy).
231. ARRIGHI, *supra* note 22, at 307.

elites.[232] Rentier shareholders similarly accepted a much smaller share of U.S. income and wealth than pre-Great Depression counterparts.[233]

As predicted by Berle in 1930, modern corporations would continue to grow larger, controlling an ever-increasing share of the nation's industrial wealth. As Berle noted, "It is the *large* corporation which makes the difference."[234] This remained true in the 1950s and 1960s. Another feature of the economy also remained unchanged. As Berle observed in 1967, "American economics at present is dominantly, perhaps overwhelmingly, industrial."[235] Thus, in 1932, and still in the 1950s and 1960s, it was the *large industrial* corporation that controlled the economy.

A broader point also remained true. Berle had argued in 1932 that

> [O]ur industrial plant is built . . . . Our last frontier has long since been reached, and there is practically no more free land. . . . The day of the great promoter or the financial Titan, to whom we granted anything if only he would build, or develop, is over. . . . The day of enlightened administration has come.[236]

By conflating the building of our industrial plant and the closing of our western frontier, Berle was highlighting a key reality: the second industrial revolution essentially had been completed. Vaclav Smil has recently amplified that point:

> [M]any techniques whose everyday use keeps defining and shaping the modern civilization had not undergone any fundamental change during the course of the 20th century. Their qualitative gains (higher efficiency, increased reliability, greater convenience of their use, lower specific pollution rates) took place without any change of basic, long-established concepts.
>
> . . . [T]he fundamental means to realize nearly all of the 20th-century accomplishments were put in place even before the century began, mostly during the three closing decades of the 19th century and in the years preceding WWI. That period ranks as history's most remarkable discontinuity not only because of the extensive sweep of its innovations but also because of the rapidity of fundamental advances that were achieved during that time.[237]

The second industrial revolution had been brought to fruition by the Great Tycoons and by an assortment of entrepreneurial inventors.

> [A] notable characteristic of the great pre-WWI technical discontinuity is *the imagination and boldness of new proposals*. There is no better testimony to the remarkable pioneering spirit of the era than the fact that so many of its inventors were eager to bring to life

232. *See infra* notes 264–69 and accompanying text.
233. *See infra* notes 264–69 and accompanying text.
234. Berle & Means, *supra* note 157, at 58 (emphasis in original).
235. ADOLF A. BERLE & GARDINER C. MEANS, THE MODERN CORPORATION AND PRIVATE PROPERTY, at ix (rev. ed. 1967).
236. Commonwealth Club Address, *supra* note 173.
237. VACLAV SMIL, CREATING THE TWENTIETH CENTURY: TECHNICAL INNOVATIONS OF 1867–1914 AND THEIR LASTING IMPACT 5–6 (2005).

> practical applications of devices and processes that seemed utterly impractical, even impossible, to so many of their contemporaries.[238]

It was these ruthless, forceful men, individualists, lone wolves, whose work was done at the time of the New Deal. But, of course, the work of the second industrial revolution itself was not done, and it was the job of the modern corporation to continue that work[239]—to innovate and improve industrial processes, further develop products, and continue to make practical the teachings of science.

Berle foresaw correctly that the modern corporation, in carrying out the unfolding blueprint of the second industrial revolution, would need enlightened administration. By the 1950s that enlightened administration was fully in place. As Berle predicted it lay not in autocratic, top-down, entrepreneurs. Rather, direction of the modern corporation had devolved to the internal bureaucracy of the firm, what John Kenneth Galbraith termed "the technocracy."[240]

Studying the modern corporation during the 1950s and 1960s, Galbraith discovered an internal decision-making society at work. Contrary to the simple world modeled by Adam Smith,[241] the modern corporation of that era (what I sometimes call "the Galbraithian modern corporation") was involved in economic planning that often spanned many years between the initiation of a product's development and the actual bringing of that product to market.[242] The modern corporation could not depend on the market to accomplish these complex, long-term projects. For example, capital could not be invested years in advance in the "hope" that profitable sales would ultimately occur. The modern corporation must "know" that a profitable market will exist. Accordingly, product development and other decisions require foresight, which depends on the information, knowledge, and specialized skills of the modern corporation's technocracy. Importantly, the input of each member of the technocracy must be coordinated, and almost all decisions will be made by groups. The formal hierarchy of the firm—the descending chain of command envisioned by organization charts—plays almost no role in the actual functioning of the firm.

> Thus decision in the modern business enterprise is the product not of individuals but of groups. The groups are numerous, as often informal as formal, and subject to constant change in composition. Each contains the men possessed of the information, or with access to the information, that bears on the particular decision together with those whose skill consists in extracting and testing this information and obtaining a conclusion. This is how men act successful-

238. *Id.* at 11.

239. James P. Hull, *The Second Industrial Revolution and the Staples Frontier in Canada: Rethinking Knowledge and History*, 18 CANADIAN J. HIST. SCI., TECH. & MED. 22, 23 (1994).

240. GALBRAITH, *supra* note 19, at 62–74.

241. *Id.* at 48–59.

242. *Id.* at 18–21.

ly on matters where no single one, however exalted or intelligent, has more than a fraction of the necessary knowledge.[243]

As for the Galbraithian modern corporation's president,[244] he "exercise[s] only modest powers of substantive decision."[245] This is necessary. The president cannot meaningfully review the substantive work done by the technocracy, whose group decisions collectively involve knowledge and expertise that the president does not possess. Moreover, interfering with decisions of the technocracy in this way would undercut the motivational incentives of members of the technocracy.

One of Galbraith's most important contributions to our understanding of the mature modern corporation is his deconstruction of motivation.[246] Traditional economic theory assumes that persons make economic decisions primarily by pecuniary calculus; this assumption undergirds the *laissez-faire* ideology that we associate with Adam Smith and the Chicago School of Economics.[247] Galbraith found a very different dynamic at work in the modern corporation. The principal problem for any organization is how to coordinate the activities of members—this is the job of motivation. Four motivation strategies are theoretically available, alone or in combination—compulsion, pecuniary motivation, identification, and adaptation.[248] Contrary to the assumptions of traditional economic theory, pecuniary motivation is not the sole motivator explaining decisions made by corporate actors.

Compulsion—forcing someone to perform—produces no loyalty and the highest cost to the firm in terms of oversight and monitoring. Pecuniary motivation—paying someone to perform—provides loyalty only until another firm makes a better offer. Persons who work simply for the monetary reward also have little loyalty, and cannot be expected to work cooperatively and for the best interests of the corporation, unless their compensation will be affected. Moreover, if the opportunity to shirk presents itself, the employee will probably take advantage. Thus, monitoring and supervisory costs are high and cascade throughout the firm when pecuniary compensation is the primary motivation strategy.

Within the Galbraithian modern corporation, pecuniary compensation is rarely the sole motivating factor. Rather, members of the technocracy are motivated to differing degrees either because they identify with the goals of the firm and derive tremendous satisfaction therefrom, or because they partially identify with the goals of the firm and hope to be able to change the firm—to adapt it to their own goals.[249] Even lower-level workers are not solely motivated by compensation.[250] Interestingly,

243. GALBRAITH, *supra* note 19, at 65.
244. The 1960s president is the formal organization chart equivalent of today's CEO.
245. GALBRAITH, *supra* note 19, at 70.
246. *Id.* at 140–58.
247. *See id.* at 49–54, 121–25; O'Kelley, *supra* note 38, at 1332–34.
248. GALBRAITH, *supra* note 19, at 130–32.
249. *Id.* at 166–78.
250. *Id.* at 134–39.

viewed from this perspective, we see shareholder claims in a different light.

> In the outermost circle in the mature corporation are the ordinary stockholders. This for all practical purposes is a purely pecuniary association. . . .
>
> The next inward circle is occupied by the production workers. Here, already, motivation becomes mixed. . . . [A]n individual comes to think of himself as an IBM man, a Corning Glass man or a Sears man. . . .
>
> Next, as one moves inward, are foremen and supervisory personnel and the clerical, sales and other routine white collar personnel. These merge at their inner perimeter with technicians, engineers, sales executives, scientists, designers and other specialists who comprise the technostructure. Beyond these at the center are the executives or management. As one moves through these inner circles, identification and adaptation become increasingly important.[251]

Traditional economic theory models the firm as a profit-maximizing unit.[252] Adolf Berle feared that managers of the modern corporation, freed from the control of shareholders, would selfishly allocate corporate profits. But by the 1950s, the mature modern corporation responds not to the dictates of the shareholders or senior managers but to the needs and wishes of the technocracy.[253] The goals of the technocracy do not include maximizing firm wealth or shareholder wealth. Rather, goal one is ensuring the survival of the corporation, and, thus, the survival of the technocracy.[254] For that, seeking to maximize profit or wealth is risky. Instead, the modern corporation seeks to maximize a dependable and safe level of earnings, while minimizing the risk of catastrophic loss. Closely related is a second goal—maintaining the autonomy of the technocracy.[255] This, too, is not consistent with maximizing shareholder returns. Rather, the technocracy will seek to protect itself from the need to obtain outside loans or new infusions of capital by retaining earnings at the highest possible level. A third, related goal is growth.[256] The technocracy seeks to maximize growth. Because the technocracy works in groups, firing a member of the technocracy is demoralizing and cuts against members' ability to identify with the firm. Growth provides a cushion against temporary downturns in business fortune. Finally, the technocracy seeks "technological virtuosity."[257] Successful innovation means promotions and more hiring for the technocrats in the firm. It al-

251. *Id.* at 150–53.
252. *Id.* at 121–25.
253. *See id.* at 86.
254. *Id.* at 167.
255. *Id.* at 169–71.
256. *Id.* at 171–72.
257. *Id.* at 174–75.

so increases technocrats' sense of satisfaction and identification with the firm.[258]

The Galbraithian-era CEO sits at the top of the technocracy, and his personal satisfaction is intertwined with the goals of the technocracy. The corporation is his life. While the CEO has limited substantive decision-making power, he does have an important role: "Leadership does cast the membership of the groups that make the decisions and it constitutes and reconstitutes these groups in accordance with changing need. This is its most important function. In an economy where organized intelligence is the decisive factor of production, this is not unimportant."[259]

In wielding this power to determine group membership, however, the Galbraithian CEO is not acting as the classic, Knightian entrepreneur to maximize profits: "Apart from access to capital, [the classical entrepreneur's] principal qualifications were imagination, capacity for decision and courage in risking money . . . . None of these qualifications are especially important for organizing intelligence . . . ."[260]

As Berle noted, ownership has been separated from control. Rather than pursue selfish ends, however, the CEO is left with a far greater attachment to the technocracy which he "leads" and serves, and with whom he identifies. The CEO uses his authority to organize the firm's working groups and structure, not to maximize profits of the firm or shareholders, but to further the goals of the technocracy which are largely his own. Thus, decisions are made in order to enhance the ability of technocrats to identify with the firm, to reward team members who are able to further the goals of the technocracy, and, if possible, to subtly and incrementally adapt the corporation to the CEO's own values. None of this has much to do with shareholder or firm wealth maximization.

As for his own wealth and happiness, the Galbraithian-era CEO looks largely to his place in the corporation for the satisfaction of his needs.

> In very recent times, it has become fashionable, although not yet obligatory, for the corporation executive to have some non-business interests apart from therapeutic recreation and community service. . . . But it is still normally a matter of pride that the corporation absorbs nearly all his waking energy. All else including family, politics, sometimes even alcohol and sex, are secondary. "To the executive there is between work and other aspects of one's life a unity he can never fully explain. . . . How can you overwork, executives ask, if your work is your life?" This is to say that the organization satisfies his needs with marked repleteness—that this inducement to identification is also fully satisfied.[261]

258. *Id.*
259. *Id.* at 70.
260. *Id.* at 58.
261. *Id.* at 154–55.

Necessarily, then, the Galbraithian-era CEO could not lobby for substantially higher compensation than others near his rank in the technocracy, nor could management as a group ask for such treatment, or, indeed, allow themselves to think in pecuniary terms about their relationship to the firm.

> Identification and adaptation . . . are the operative motivations. They are also the only personally reputable ones: the executive cannot afford to have it thought that his commitment to the goals of the corporation is less than complete or that he is at all indifferent to his opportunity to shape these goals. To suggest that he subordinates these latter motives to his response to pay would be to confess that he is an inferior executive.[262]

As a result, in terms of pecuniary wealth and income, the CEO of the Galbraithian era was a pauper compared to the CEOs of 1930 and of the current millennium. His lifestyle so reflected.

> [A] top executive . . . lives on an economic scale not too different from that of the man on the next-lower income rung. He surrenders around 40 per cent of his salary to the Bureau of Internal Revenue (he may cough up as much as 75 per cent) but still manages to put a little of his income in stocks, bonds, life insurance. He owns two cars, and gets along with one or two servants. What time he has left from his work—on weekends and brief vacations—he spends exercising, preferably outdoors, and usually at golf. Next to golf, fishing is the most popular executive diversion. . . .
>
> Twenty-five years have altered the executive way of life noticeably; in 1930 the average businessman had been buffeted by the economic storms but he had not yet been battered by the income tax. The executive still led a life ornamented by expensive adjuncts that other men could not begin to afford, a life attended by a formality that other men did not have time for. In Boston, which set the highest tone if not the fastest pace, the archetype of the high-salaried executive of 1930 arrived at his office in his chauffeur-driven Pierce-Arrow, uncompromisingly attired in dark suit and detachable stiff collar. For weekend lounging white flannels were *de rigueur*.
>
> Today an executive, outside of Boston at least, may arrive at his office in tan shoes, sometimes in a tweed jacket with side vents. And he may well do his weekending in shorts—pink ones this year. . . .
>
> The executive's home today is likely to be unpretentious and relatively small—perhaps seven rooms and two and a half baths. (Servants are hard to come by and many a vice president's wife gets along with part-time help. So many have done so for so long, in fact, that they no longer complain much about it). . . .
>
> As executives' homes have dwindled in size, so have their parties. Frederick J. Thibold, catering manager at Sherry's in New

262. *Id.* at 138–39.

> York, can remember dances for 2,000 with a "sumptuous supper" twenty-five years ago. A big dance today is one for 400, and at some of these, Thibold confides in a whisper, Sherry's has served hot dogs and hamburgers. . . .
>
> The large yacht has also foundered in the sea of progressive taxation. In 1930, Fred Fisher (Bodies), Walter Briggs, and Alfred P. Sloan cruised around in vessels 235 feet long; J.P. Morgan had just built his fourth *Corsair* (343 feet). Today, seventy-five feet is considered a lot of yacht. One of the biggest yachts launched in the past five years is the ninety-six-foot *Rhonda III*, built and owned by Ingalls Shipbuilding Corp., of Birmingham, Alabama. The *Rhonda III* cost half a million dollars to build, and the annual bill for keeping a crew aboard her, stocking her, and fueling her runs to around $130,000. As Chairman Robert I. Ingalls Jr. says, only corporations today can own even so comparatively modest a craft. The specifications of the boat that interests the great majority of seagoing executives today are "forty feet, four people, $40,000." In this tidy vessel the businessman of 1955 is quite happily sea-borne.[263]

A look at the empirical data helps us interpret this anecdotal account. The income share of the top one percent of Americans reached 19.5% immediately before the Great Depression, and fell to 15% by 1933.[264] Though it fluctuated higher at times during the New Deal, it had fallen again to 15% at the commencement of World War II.[265] During the War, income shares again fell sharply for the top 1%, reaching 11% in 1943 and remaining at or near that level until the Korean War.[266] During that engagement, income shares of the top percentile fell again. From the late 1950s to the early 1970s, the income share of the top percentile of Americans remained eerily steady at around 8%.[267]

Not only did income shares fall for the top one percent, the source of income changed dramatically. In 1928, top percentile income came predominantly from capital gains and dividends.[268] By the 1960s, top percentile income came primarily from wages.[269] This suggests that the popular comparison of Galbraithian-era CEOs to Roaring Twenties CEOs is misleading. The owners of great yachts and throwers of great parties were the Great Tycoons and others who had made or inherited tremendous fortunes during the sixty years or so following the Civil War. These were the Great Tycoons that, as Berle said, society could no longer afford. And, in fact, from the New Deal onward, the Great Tycoons and rentier shareholders claimed an increasingly smaller share of the profits created by the modern corporation.

263. Duncan Norton-Taylor, *How Top Executives Live*, FORTUNE, July 1955, at 78, 79, 80.
264. Piketty & Saez, *supra* note 135, at 12 & fig.II.
265. *See id.*
266. *See id.*
267. *Id.*
268. *See id.* at 14–18, 15 tbl.III, 16 fig.IV.
269. *Id.*

During the Galbraithian era, from 1950 to 1973, the modern corporation reached the maturity prophesized in Roosevelt's Commonwealth Club address. Control of the modern corporation—separated from stockholders—now resided firmly in the technostructure, the enlightened administrators called for by Berle.[270] The share of corporate profits and national income going to Great Tycoons and rentier shareholders had declined, reflecting the modern corporation's diminished need for the services of both capital and the entrepreneur.

As Adolf Berle observed in 1967, it appeared that the U.S. economic revolution, begun with the New Deal, was well under way. The average American was healthier and more secure. Income inequality had diminished greatly. The opportunity to participate in American economic life had been broadened substantially by the Civil Rights movement of the 1960s. The future looked bright and the path clear.[271] Few would have predicted that almost overnight the motivational ethos and underpinnings of the Galbraithian modern corporation would go gentle into the night,[272] to be only dimly remembered a long generation later.

VI. CONCLUDING THOUGHTS—THE NATURE AND POWER OF THE MODERN-DAY CEO

Against the backdrop I have painted—the evolution of the modern corporation from the Civil War to 1973—I will close with some observations and intuitions about the power of the modern-day CEO. I share these thoughts most tentatively, as the very first stage of bringing sense to what we are experiencing with respect to the continuing evolution of the American business firm. What we need, of course, is another Berle to write what Timothy Garton Ash calls "a history of the present."[273] Like all attempts to order events that are near in time—trends, currents, and themes that seem obvious to me today—my thoughts and intuitions may prove as prophetically wrong as were the historians who did not see coming the collapse of the Soviet Union.

Reaching back to 1973, it is now accepted that a wholly unexpected change in the expected course of contemporary history happened very rapidly, much the same way the Great Depression and New Deal had blindsided America at the end of the Roaring Twenties. The change that occurred had a profound ideological dimension, although it is difficult to say which came first—the shift in ideology or the very stark changes in America's relationship to the world.

The ideological shift, in the making during the mid-1970s, substantially in place in the early 1980s and popularly identified as the Reagan

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270. *See supra* notes 197–201 and accompanying text.

271. Berle, *supra* note 33, at 18, 20.

272. The allusion is to Dylan Thomas. DYLAN THOMAS, *Do Not Go Gentle into That Good Night*, *in* THE POEMS OF DYLAN THOMAS 239 (New Directions rev. ed. 2003).

273. *See supra* note 32 and accompanying text.

Revolution, represented a return to a species of *laissez-faire* capitalism. Glorified were the power of free markets, privatization of previously government functions, curtailment of social welfare spending, sweeping reductions in trade barriers, and extensive deregulation of industry.[274] In the field of corporation law scholarship and in the board rooms of America's dominant corporations, an insistent new mantra was heard—the purpose of the corporation is to maximize shareholder value.

Corporate CEOs almost overnight became rock stars, and their compensation quickly reflected this new status. In 1980, the CEO of an S&P 500 corporation received compensation forty-two times the pay of an average U.S. worker.[275] By 2011, that same CEO made 380 times the pay of an average American worker.[276] Pay gains, however, have not been restricted to the top percentile. The top ten percent of Americans have also done exceedingly well compared to the bottom ninety percent. From World War II to the 1970s, the top decile's income share remained near constant at thirty-three percent.[277] Since then, the top ten percent have seen their share of income rise steadily, reaching 47.9% in 2011.[278] As Emmanuel Saez concludes, "the labor market has been creating much more inequality over the last thirty years, with the very top earners capturing a large fraction of macroeconomic productivity gains."[279] Most of these top earners are corporate CEOs, entrepreneurs, and other members of the modern corporation's technocracy. Those who are losing are blue-collar workers, government employees, and others not in the inner circle of the technocracy.

These changes in income shares correspond to a loss in job security for ordinary workers. The impact of the streamlining of American firms fueled by the bust-up takeover phenomena in the early 1980s and the substantial job losses resulting from computerization were most heavily felt by less skilled, already lower-paid, workers.[280] Additionally, the offshoring of significant segments of America's industrial production activities adversely affected blue-collar workers.

This startling return to free-market ideology[281] and the return to inequality not seen since the Roaring Twenties occurred at the same time

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274. Gil Troy, *Ronald Reagan's 100-Day Revolution*, *in* LIVING IN THE EIGHTIES 10, 10–23 (Gil Troy & Vincent J. Cannato eds., 2009).

275. *CEO-to-Worker Pay Gap*, AFL-CIO, http://www.aflcio.org/Corporate-Watch/CEO-Pay-and-the-99/CEO-to-Worker-Pay-Gap (last visited Mar. 27, 2013).

276. *Id.*

277. Emmanuel Saez, Striking It Richer: The Evolution of Top Incomes in the United States (Updated with 2009 and 2010 Estimates) 2 (Mar. 2, 2012), *available at* http://elsa.berkeley.edu/~saez/saez-UStopincomes-2010.pdf (updating Emmanuel Saez, *Striking It Richer: The Evolution of Top Incomes in the United States*, PATHWAYS MAG., Winter 2008, at 6).

278. *Id*.

279. *Id.* at 5.

280. HOBSBAWM, *supra* note 52, at 413.

281. *Id.* at 103 ("Those of us who lived through the years of the Great Slump still find it almost impossible to understand how the orthodoxies of the pure free market, then so obviously discredited, once again came to preside over a period of depression in the late 1980s and 1990s, which, once again, they were equally unable to understand or to deal with.").

as the crisis in American hegemony. In 1971, after its profligate spending on the Vietnam War, the United States was forced to abandon the gold standard, ushering in a new era of fiat money and floating exchange rates.[282] As a result, the U.S. government lost its ability to spend without limit in advancing its interests and the interest of U.S. corporations.[283] At the same time, the recovery of Europe and Japan, and the emergence of strong economies in Southeast Asia, challenged U.S. economic dominance.[284] Firms globally had now successfully copied the internal management and vertical integration strategies of the U.S. corporation.[285] With the creation of the unified European market and the reduction of world trade barriers, the geographical advantage of controlling a large home market substantially diminished.[286] In short, the United States and its corporations were losing dominance in world markets. These facts alone would suggest a need for a renewed focus on productivity, and why the measuring rod used would be the rather crude, but objective, focus on corporate profits and shareholder wealth maximization.

At the same time it is possible that the world is entering what some have termed the third industrial revolution. In 1965, Adolf Berle, always a visionary and a keen "historian of the present," quoted the following from a Research Institute of America study:

> A third industrial revolution is in the making, as dramatic as those which followed the harnessing of steam power and the proliferation of electricity. This one will be sired by the release of nuclear and thermonuclear energy, the electronic conversion of energy to work, and the use of cybernetics and computers to free human energy from routine decision-making. By 1980, the industrial world will be as different from today's as today is different from the 19th century.[287]

Could it be that the coming of the third industrial revolution has caused America once more to call forth its ruthless men of force—this generation's Knightian tycoons—to conquer the new frontiers? My intuition is that this is at least partially the case. The imperatives of the third industrial revolution cry out for Schumpeterian creative destruction. As always, established elites resist. It is only by the exercise of the entrepreneurial CEO's will that creative destruction can take place.[288]

Whatever the reason for our return to *laissez-faire* sentiments and policies, the new ideology has permeated the modern corporation to the core. Pecuniary compensation, so subdued as a motivational strategy in the Galbraithian era, is now central to the sense of accomplishment and

282. *Id.* at 241–42.
283. ARRIGHI, *supra* note 22, at 318–24.
284. *Id.* at 306–07.
285. *Id.* at 322–23.
286. *Id.* at 316–19.
287. Berle, *supra* note 33, at 7.
288. *See* JOSEPH A. SCHUMPETER, CAPITALISM, SOCIALISM, AND DEMOCRACY 80–86 (1942) ("This process of Creative Destruction is the essential fact about capitalism.").

worth for all members of the technocracy. The natural consequence is a lessened sense of identity with the goals of the firm and a lessened sense of solidarity among members of the technocracy. For the CEO, however, there may be a heightened sense of satisfaction from the ability to adapt the firm to the CEO's goals. Additionally, for the CEO and entrepreneurial members of the technocracy, there may be an enhanced sense of identification that comes from participating in the Darwinian struggle for corporate power and business success—the modern version of what Frank Knight called "the biggest and most fascinating game yet invented."[289]

Admittedly, the last decade has seen changes that could be interpreted as enhancing shareholder power at the expense of CEO power. My intuition, however, is to the contrary.[290] It is important to differentiate between the office of the CEO and the man or woman who holds that office. Job tenure may be less secure for the modern-era CEO, but the actual powers of the office do not seem diminished. Moreover, job security is anathema to the motivational scheme that seems to drive the true Knightian entrepreneur. The ultimate motivation may be to play the greatest game on earth, win or lose. The greatest game requires the possibility of losing. So making the playing field more difficult to maneuver is not necessarily a negative for the ruthless men of force who are drawn to the CEO role.

Time will tell how the modern corporation actually evolves and whether CEO power rises or falls. How history plays out in this regard will be part of the answer to much larger questions. Will Giovanni Arrighi prove correct in his intuition that we are now in a period of transition between American hegemony and a still only dimly understood replacement system?[291] Will American society fall prey to the pitfalls of hyper-efficiency warned of by Joseph Schumpeter?[292] Or, instead, righting itself and following the path described by Daron Acemoglu and James Robinson in *Why Nations Fail*, will the United States once again

289. KNIGHT, *supra* note 69, at 360; *see also supra* notes 68–69 and accompanying text.

290. Recent changes in corporate governance rules may on the whole enhance CEO power. Many of the shareholder protective provisions of recent federal legislation greatly increase the responsibility and stress felt by *outside* directors while imposing no additional stress on the CEO. Other provisions, like the certification requirements of the Sarbanes-Oxley legislation actually enhance the CEO's power. Finally, while directors are now required to "ratify" and "oversee" CEO actions with much more regularity and intensity, in Galbraithian terms, such ratification and oversight does not make the directors the actual decision makers. The directors cannot replicate the knowledge and skills possessed by the technocracy; thus, any effort by the board to interfere in the technocracy's decision making would be counterproductive.

291. ARRIGHI, *supra* note 22, at 322–24.

292. [S]ince we are dealing with a process whose every element takes considerable time in revealing its true features and ultimate effects, there is no point in appraising the performance of that process *ex visu* of a given point of time; we must judge its performance over time, as it unfolds through decades or centuries. A system—any system, economic or other—that at *every* given point of time fully utilizes its possibilities to the best advantage may yet in the long run be inferior to a system that does so at *no* given point of time, because the latter's failure to do so may be a condition for the level or speed of long-run performance.

SCHUMPETER, *supra* note 288, at 83.

assume the mantle of world hegemon?[293] Trying to understand the "present history" of corporate governance reform in this larger context strikes me as an essential part of our work as we follow in the footsteps of Berle and Galbraith, who so powerfully illuminated the past while living it.

293. DARON ACEMOGLU & JAMES A. ROBINSON, WHY NATIONS FAIL: THE ORIGINS OF POWER, PROSPERITY, AND POVERTY 368–403 (2012) (arguing that nations prosper when they have inclusive economic institutions, and encourage creative destruction; to the contrary, nations fail when they adopt extractive economic institutions that protect existing elites and discourage innovation).