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# Notes Toward a Theory of the Executive Class

DAVID A. WESTBROOK†

The astounding levels of wealth regularly transferred to the top executives of American corporations, ostensibly as compensation for their services as managers, have raised controversy, or at the very least, eyebrows at the *New York Times* and other bastions of national propriety. The Securities and Exchange Commission has promulgated rules requiring more disclosure of executive compensation, following on various efforts taken under the aegis of the Sarbanes-Oxley Act of 2002, the Congressional response to shenanigans at Enron and elsewhere. So far, however, neither upper middlebrow disapproval nor mandatory disclosure has done anything discernible to diminish the pay packages of top U.S. executives.

The controversies surrounding executive compensation are rather funny in a mordant way that recalls the great social economist Thorstein Veblen, who lanced the pretensions of the gilded age in *The Theory of the Leisure Class*.<sup>1</sup> Veblen should be important to us today, however, not just as a mirror for contemporary vulgarities, but because he provides a very American corrective to that national intellectual weakness, excessive individualism. Specifically, executive compensation tends to be understood, criticized, and defended as *compensation*, the quid pro quo of an employment contract between a company and its executive. No doubt this relentless individualism has many sources—the microeconomic focus of business culture, the methodological individualism of academic economics,

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1. THORSTEIN VEBLLEN, *THE THEORY OF THE LEISURE CLASS* (1899).

Horatio Alger stories, the national tendency to view politics moralistically, and balance sheets all spring to mind—but understanding executive compensation in such individualistic terms has produced a rather inchoate “debate,” and has obscured other, perhaps more important, truths.

I maintain that the recent rise in CEO compensation should be understood in more social, as opposed to individualistic, terms. Much which is obscure or undecidable within contemporary debate on the issue makes perfect sense if we shift our focus from contract to property, from the quantity of payment to the social position that affords payment, and from rational self-interest (in this context called “incentives”) to status. We are witnessing an important development within our society, the effort to construct what, in a bow to Veblen, we should call an executive class, rather than a few cases of mere individual greed.

That American executives are being paid huge amounts is not in serious question. My favorite anecdote to this effect is about Richard Parsons, CEO of Time Warner, biannually taking the company jet to visit his twenty acre vineyard, which I would guess is almost twice the size of his dining room, but romantically located in Tuscany. You know, sometimes a man has to tend his vines, as the Bible says. The layered decadence in this story, especially the palpable desire for authenticity—land farmed for centuries, perhaps millennia, but of course, not by me—is kind of delicious. And the wine is also said to be very good.

Turning from anecdote to more general comparisons, CEO compensation has grown by virtually all metrics in recent years. This sort of statistic is hackneyed but still impressive: the average pay for a CEO of a large company was up 27% in 2005,<sup>2</sup> nicely outpacing the inflation rate of 3.3%. By comparison, Labor Department statistics suggest worker’s pay was up 2.9% in 2005, a fall in inflation-adjusted terms.<sup>3</sup> In probably the most cited metric, today’s CEOs make more, relative to their employees, than their

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2. Eric Dash, *Executive Pay: A Special Report: Off to the Races Again, Leaving Many Behind*, N.Y. TIMES, Apr. 9, 2006, at A5 (citing study by Pearl Meyer & Partners, the compensation practice of Clark Consulting).

3. *Id.*

counterparts of a generation or two ago. Average top executive salaries are, according to another study, 170 times the pay of the median (not least-well-paid) employee.<sup>4</sup> In 1940, the multiple was 68.<sup>5</sup> And if one compares the compensation of CEOs in America to that of their counterparts in comparable companies in other industrial countries, the Americans are paid much more, though there is some indication that, in an age of multinational markets for executives, the Europeans want to be paid like Americans.<sup>6</sup>

Some of my fellow aficionados of capitalism may need to be reminded that more than simple envy is at issue in this controversy. Compared with other nations, Americans traditionally have a high tolerance, even enthusiasm, for the wealth of others. But even corporation law scholars, institutional investors, and others who are quite comfortable around money and its inequalities are somewhat taken aback by today's executive compensation practices. Whether or not executive compensation is high vis-à-vis some moral standard, it is objectively high vis-à-vis traditional business practice in the same companies. Never before, not even in the golden age of organization man, have managers—as opposed to entrepreneurs, financiers, or conquistadors—been paid so much for their role in the ordinary business of an operating company.

Reporting on such developments, journalists for the *New York Times* and other disapproving parties tend to adopt a classic populist stance of being shocked, simply shocked, at the impropriety of it all. This stance, which is sometimes genuine, rests on a fundamental misapprehension of what “executive compensation” is and how it works. More interestingly, however, even those who criticize “executive compensation” on corporate governance grounds tend to see the practice with a sophisticated myopia. As suggested, the essence of these misapprehensions is to understand executive compensation on its own terms, i.e., as an individual company's purchase of management services

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4. *Id.* (citing study by Carola Frydman and Raven Saks).

5. *Id.*

6. See Geraldine Fabrikant, *U.S.-Style Pay Packages Are All the Rage in Europe*, N.Y. TIMES, June 16, 2006, at A1.

from an individual executive, who must be compensated for the time and effort needed to provide such service. Presumably those most obviously responsible for current levels of executive compensation, the managers who benefit and the corporate boards who approve, are content with such misapprehensions—for who doesn't expect to get paid, and as well as the market will bear, for a job well done?

To begin simply, there are many ways for a company to pay its management. Top executives are typically paid a lavish but otherwise ordinary salary, and enjoy a host of perquisites—interest free loans and those company jets to Tuscany and the like—as well as substantial benefits in the event of a number of contingencies, e.g., they are sued, or retire, or the company is acquired, or things simply do not work out. The huge numbers bandied about in discussions of executive compensation, however, are driven by so-called “performance based compensation.” The idea of “performance based compensation” is probably familiar in roughly the following form: if a company pays its executives with stock, or stock options, then managers will have direct incentives to make the company a success, because the company's success will be reflected in its stock price, which means that the managers will be paid more. Although successful managers stand to receive a massive paycheck, shareholders will not care, because their shares, too, have increased in value.

The argument for performance based compensation has been incredibly persuasive. As IBM has taken to saying, in growth, “all pots are watered.” And Silicon Valley, for all its excesses, still a source of national pride, was largely built on options. Even after Enron and other scandals, almost nobody in corporate governance circles argues that an executive's compensation should not somehow be linked to the company's performance. This enthusiasm for performance based compensation has been written into law: the corporate tax code was amended in 1993 to ensure that all executive compensation above \$1 million be linked to performance.<sup>7</sup> At least in part as a result of this change in tax law, compensation schemes that are essentially massive grants of property have been generally adopted.

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7. I.R.C. § 162(m) (2000).

From time to time, property transferred under such schemes must, according to the tax laws, be priced and the increases in individual wealth reported as income (e.g., upon the exercise of options). Herein lies the misapprehension: that number is reported, and then criticized or defended, as if it were an hourly wage, a payment for services rendered. It is, of course. But then again, medieval kings granted titles of nobility and appurtenant lands in return for doughtiness in battle or other service to the crown—the political significance of such transfers was hardly the *quid pro quo*, and the wealth subsequently derived from holding such property hardly reflected the ongoing performance, as an aristocrat, of the talented nobleman who received the fiefdom.

Operating under the misapprehension that executives are being paid for their labor, journalists and other populist critics often use the pay of the least or median well-paid employee as a sort of yardstick to argue that today's executives are being paid "too much." If a secretary makes  $x$ , then it might be okay for the CEO to make  $10x$ , or even  $50x$ , but not 100 or 170 times what the secretary makes. 170 times is too high. Certainly it cannot be right that anybody is paid \$144,573 *a day*, year in and year out, as Exxon CEO Lee Raymond was paid.<sup>8</sup> Superman couldn't work that hard.

Built into this argument is a labor theory of value: people get paid (or should get paid) for how hard they work. I think this is wrong in general, but it is certainly wrong in this context. A CEO is paid almost entirely with property, stock, and stock options, along with the perquisites of office. The Queen of the Netherlands is not paid well because she works hard. She is paid well because she is the Queen, and she owns things, notably a sizeable portion of Royal Dutch Shell. Roughly the same could be said of Mr. Raymond. This does not mean CEOs do not work. Presumably, they must work very hard—to become CEOs. But their effective pay is a function of their political fortunes in the company, and of the company's fortunes in the stock market, not of effort

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8. See Jad Mouawad, *For Leading Exxon to Its Riches, \$144,573 a Day*, N.Y. TIMES, Apr. 15, 2006, at A1. Mouawad discusses the compensation of outgoing Exxon CEO Lee R. Raymond. Mr. Raymond's "pension" was a 98.4 million dollar single payment—there is nothing "pensionesque" about it. *Id.*

expended or even job done.

One need not go back to the Middle Ages to conceptualize pay in terms of position, that is, as a consequence of status, rather than as compensation. In the words of the Supreme Court in the famous *Howey* case, we ordinarily expect securities investors to profit “solely from the efforts of others.”<sup>9</sup> An investor’s wealth has to do with what is owned, not what is done. I certainly am not doing much to generate whatever wealth is in my retirement portfolio (“Bearing risk” is not unlike “breathing”). And if I died tomorrow, leaving everything to my three year old, he certainly would not have earned his wealth, he would have inherited his position. In paying CEOs with stock and stock options, however, we make them investors first, and salarymen second. As investors, the wealth that CEOs receive is a function of the success of the company (which necessarily represents the efforts of many, many other people, as measured in the financial markets, which represents the assessments of very many people indeed). Thus, even when operating as intended, the phrase “executive compensation” is deeply misleading. CEOs are only tangentially paid in exchange for the sweat of their brow. Executives compete for powerful positions from which wealth flows.

In those circles of the academic and business worlds that concern themselves with corporate governance issues, executive compensation also tends to be understood as much like paying the secretary, only with more zeros. To ask the question practically, from the perspective of the board of directors, the question is how does a company pay an executive to do a good job? To the uninitiated, this might seem to require figuring out what would constitute a good performance on the job. Obviously, however, in a context as amorphous as being a top manager of a complicated business in an even more complicated environment, assessing performance would be very difficult, much as assessing the individual performance of a political leader is a difficult task, even for historians with the benefit of hindsight.

Corporate governance theory, however, provides a

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9. SEC v. *Howey*, 328 U.S. 293, 301 (1946).

ready-made understanding of the problem of how to understand executive performance, and unsurprisingly, leads to ready-made answers. Since Berle and Means wrote their classic *The Modern Corporation and Private Property*,<sup>10</sup> the problem of corporate governance has been understood to be the separation of ownership of the company from control over the company. Shareholders own the company; management controls the company. Since they have control, management is likely to use their power to benefit themselves, in one way or another, to pay themselves too much, which makes the company less valuable, and therefore hurts shareholders. In this understanding, a CEO does a good job if he serves the (financial) interests of the company's shareholders, rather than benefiting himself. Thus, in corporate governance circles, both the problem of executive compensation and its solution are understood structurally, in terms of the relationship between the company's executive and its owners, rather than in terms of an objective idea of "performance" for which the executive is paid.

Performance based compensation directly addresses such a persuasive idea because it directly addressed this structural understanding of the problem of executive compensation. If the problem identified by Berle and Means was that executives would pay themselves too much, thereby impoverishing the company and its shareholders, then the answer was to pay executives with equity and options to buy equity. Executives would only make money if they improved the fortunes of the company, and in that case all shareholders would be happy. Performance based compensation dissolved the conflict of interest that Berle and Means identified between the shareholders and executives by making executives into major shareholders. In 1990, Michael Jensen and Kevin Murphy provided explicit academic statements of this position.<sup>11</sup> It was a brilliant solution, particularly for people with traditional

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10. ADOLF A. BERLE & GARDINER MEANS, *THE MODERN CORPORATION AND PRIVATE PROPERTY* (1932).

11. See Michael C. Jensen & Kevin J. Murphy, *CEO Incentives—It's Not How Much You Pay, But How*, HARV. BUS. REV., May-June 1990, at 138; Michael C. Jensen & Kevin J. Murphy, *Performance Pay and Top-Management Incentives*, 98 J. POL. ECON. 225 (1990).



understandings of corporate governance, i.e., everybody that mattered.

Since the 1990s, at least two things have happened to make performance based compensation seem like a less than perfect solution to the problem of executive compensation, which we can summarize in two words: Enron and Disney. First, Enron: if executives are paid with stock, they might work really hard to make the share price look good, if necessary messing with the company's accounting.<sup>12</sup> Second, Disney: boards of directors have been voting stratospheric pay packages for people who do not perform, like short-term Disney President Michael Ovitz. Evidently, the problem raised by Berle and Means is not laid to rest by granting some options, and critics within corporate governance circles are again arguing that shareholders are being taken advantage of by managers, that executive compensation is "too high."<sup>13</sup>

Contemporary critics of executive compensation tend to persist, however, in viewing the matter in the conceptual frame established by Berle and Means, and indeed, largely through the lens provided by Jensen and Murphy, as basically a matter of getting an employment contract right. This perspective limits the discourse in a number of ways.

If we view the matter in quantitative terms, it is not at all clear that excessive executive compensation imposes substantial costs on shareholders, or on society as a whole. The amounts of money involved are sometimes difficult to comprehend. In the recent *Disney* decision, the Supreme Court of Delaware noted that while short-term Disney president Michael Ovitz was paid approximately \$130 million in severance, which sounds like a lot of money to do a bad job, Disney had \$19 billion in revenues, and over \$3 billion in operating revenues, for the year.<sup>14</sup> Nor is it clear what the social impact of such a payout might be: presumably some of Ovitz's gains were available to the

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12. See David A. Westbrook, *Corporation Law After Enron: The Possibility of a Capitalist Reimagination*, 92 GEO. L.J. 61 (2003).

13. See generally LUCIAN BEBCHUCK & JESSE FRIED, *PAY WITHOUT PERFORMANCE: THE UNFULFILLED PROMISE OF EXECUTIVE COMPENSATION* (2004) (stating this currently influential position).

14. *In re Walt Disney Co. Derivative Litig.*, 906 A.2d 27, 54 n.72 (Del. 2006).

capital markets through reinvestment, and some to the market for lawn care, but there is no reason to think that much of the money disappeared down a rabbit hole.

A second, more subtle, reason not to worry too much about shareholders whose companies are overpaying for managerial services, at least in the short to medium term, is that most executive compensation is not cash (that would impose tax burdens on both the company and the individual). By using stock and options, so long as stock prices remain high, the company can essentially print money for compensating executives. Unsettling, perhaps, but, at least in a long bull market in which lots of liquidity is looking for a place to invest, quite manageable. So long as executives are willing to take, in effect, company script in lieu of cash, why should we care? More generally, if corporations are paying too much for executive compensation, such overpayment should be reflected in the company's stock price, and should, like almost all else that ails corporations, be self-correcting in a reasonably efficient capital market.

There is more to say, of course, but long story short, corporate governance critics who insist both (i) that executive compensation is too high; and (ii) on understanding executive compensation in terms of a bargained-for pay agreement between a company and its manager, leave themselves open to endless debate culminating in a Scottish verdict of "not proven"—within corporate governance discourse, the faith in contract and markets generally is very strong, and any argument that something might be amiss has an uphill battle.

Normatively, critics of executive compensation tend to focus on making executive pay actually reflect performance. In this view, performance based compensation is a fine idea, but just has not been tried yet, as was long said of Marxism. The reform of performance based compensation rests on two dubious propositions. First, reformers maintain that the problem with current practice is that executives get paid regardless of performance. If the company's stock price goes up, executives are paid for doing a good job; if the company's stock price is stable, executives are paid for strategic positioning; if the company's stock price goes down, executives are paid for coping with difficult circumstances. As it now stands, executive "performance" is

so amorphous a concept that it does not mean anything. Thus the reform of executive compensation requires a better definition of executive performance.

While it is difficult to imagine making matters much worse, a degree of skepticism may be in order. Reformers look to define executive performance objectively and with some degree of precision; clearly "being executive while the stock market price rises" is not enough. Well and good, but taken seriously, the idea of defining "executive performance" objectively is tantamount to saying that the selection and compensation processes for executives can be depoliticized, and accepted as such (I suggest SAT scores).

The second dubious presumption of corporate governance reformers is the psychology entailed in performance based compensation, which is indeed the individualistic psychology of liberal economics more generally, viz., rational self-interest. Executive compensation is about setting incentives; people work harder if they are paid more. While again there is obviously some truth here, it is difficult to believe that this truth is very important. Do executives even know exactly what they do when they work? Does anyone believe (on what basis?) that executives can correlate their own performance to their pay? If we paid everybody in the United States twice as much for one day, would national productivity double? An executive's performance is not a bushel of wheat, which he can sell more or less of, bargaining against the board. And if the executive is not sure precisely what he is selling, we may be certain that the board of directors has only a foggy notion of what it is buying. Thus, the idea of incentives—a rigorous correlation between pay and performance—is structurally neat, but practically useless.

Less practically, but even more interestingly, understanding executive compensation in terms of employment contracts obscures perhaps the most obvious question raised in this controversy: pretty much everybody believes executive compensation is "too high," at least almost nobody defends it, but it continues to go up. Why? To pose the puzzle from the perspective of accounting and corporate governance: executive compensation, like salaries generally, is clearly a cost to companies, and therefore it is in the interest of corporations and their shareholders to keep the cost of executive compensation, like other costs,

down. Boards of directors, who set compensation for the CEO and other officers, are supposed to protect the interests of corporations and their shareholders. So if these rates of executive compensation are, by widespread consensus, excessive, and not in the interest of shareholders, why are boards still approving them?

The usual, rather lame, answer is collusion—management has too much influence over the board of directors. But after Enron, Congress passed the Sarbanes-Oxley Act, which, among other things, requires boards to establish compensation committees comprised of outside directors, and to do a better job disclosing CEO compensation to the shareholders.<sup>15</sup> And, as mentioned, the SEC recently has required more disclosure of executive compensation. More deeply, management greed is not new. Nor is the possibility that directors are too cozy with management. This is, as also mentioned above, the fundamental problem of corporation law, and has been for generations. So why do we see an explosion of CEO salaries *now*?

A hint is provided by a third objection to the current explosion in CEO salaries which is somewhat less common and which, notably, is not individualistic. Some critics maintain that even in a hierarchical setting like a company (or more broadly, a market society) only a certain degree of inequality can be politically tolerated. At least in the abstract, such criticism is inescapably vague. It is unclear why employees who tolerate a 10 to 1 ratio between CEO pay and their salaries would balk at a ratio of 50 to 1, or 100 to 1, or 170 to 1—at some point, one crosses a line, but where? It is even more unclear why directors would think it proper to transfer substantial ownership of companies to management in lieu of paying them with cash—and how substantial an ownership interest? Answers to such judgment calls turn on the significance of positions, and hence the assessment of inequality, in a given cultural setting. That setting—bluntly, the meaning of inequality—is currently changing in the United States.

Thinking more socially (and more seriously) about why

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15. See generally Sarbanes-Oxley Act, Pub. L. No. 107-204, 116 Stat. 745 (codified in scattered sections of 11, 15, 18, 28, and 29 U.S.C.).

levels of executive compensation have grown so explosively in recent years would require a more nuanced analysis of the contemporary economy, and particularly, the market for CEOs and other top executives. Leaving questions of social causality to one side, we should at least be aware of the range of political decisions that have accompanied the rise in executive compensation, and that have shaped this economy more generally. While there is no space in this Essay for detailed historical analysis of how we reached our present positions, we might sketch a few directions such analysis might take.

First, while bonuses are as old as the hills, only in 1993 was the tax code amended to ensure that all executive compensation above \$1 million be linked to performance. That is, as economic and social history goes, a fairly recent development. Widespread adoption of payment schemes that were essentially grants of property had the effect of giving managers of established businesses the financial upside of entrepreneurs who found businesses. As law professor Charles Elson put it, "Exxon was there long before Mr. Raymond was there and will be there long after he leaves. Yet he received Rockefeller returns without taking the Rockefeller risk."<sup>16</sup>

Second, once executive compensation grew into a complicated business involving stock options, severance practices, complex perquisites (which needed to be disclosed, or not, in various ways) and the like, it was clear that what the world needed was another consultant, namely a compensation consultant. An entire industry sprang up to help corporate boards figure out how to put together compensation packages that would be attractive to prospective CEOs and at least publicly perceived as affordable to the company.

Third, the SEC sensibly enough has wanted the details of executive compensation to be made publicly available, because how someone is paid presumably affects how they

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16. Mouawad, *supra* note 8. Rephrased, to argue with Michael Eisner's 1997 payout of \$577 million from Walt Disney is different from arguing with Steven Jobs \$775 million from Apple, which he founded. If, of course, you think what Jobs was doing was creating/owning, and what Eisner was doing was "working." But my whole point is it is ridiculous to think of Eisner's case that "work" is what is significant here.

work, and it also affects the cost structure of the company, which is the sort of thing that prudent investors would like to know.

Note what these developments come to: individual executive (particularly CEO) pay arrangements are now complex, and fairly public—at least among the CEOs and corporate boards and investment analysts that care about such things. And there is reason to believe that interest in these matters is broader; we all know the names of many top executives, who are the subject of incessant stories in the *Times*, the *Wall Street Journal*, and elsewhere in the middlebrow press. In short, CEO pay went from being private business, to public business, to being celebrated.

In a parallel but relevant development, the idea of what an executive does has shifted over the last two generations. What had once been “run *the* business” became more like “run *a* business.” Rather than rise through the ranks, midlevel executives increasingly swap companies, even whole markets, in which they work. The management function became separated from the business context. This is not entirely new, of course. Harvard and other business schools have been preaching this for a long time, and it has started to sink in. If schools can teach management in general, then management can be commoditized, can become a marketable skill. We can speak of a market for executives, or in the law school jargon, a market for corporate control. The old saying at Pepsi was when you start at the company, a gun is fired—and you run until the bullet catches you. That was then. An executive today is likely to step sideways, make a lateral move to another company. Pepsi’s new CEO, Indra Nooyi, held strategic planning positions at Asea Brown Boveri (now ABB), Motorola, and the Boston Consulting Group before joining Pepsi’s management.

To add another relatively recent wrinkle: in the 1980s, and in a different form, the 1990s, the U.S. economy underwent a wave of takeovers, which resulted in the wholesale firing of a lot of people, including a lot of managers. Even when no takeover is imminent, the threat of a takeover can spur boards of directors to seek new management. As a result, the tenure of executives has come down, and CEOs seem to view their jobs as somewhat unreliable. Therefore, in order to leave a good position,

executives demand substantial pay upfront, and in case things do not work out for one reason or another, they demand “downside protection.” None of this, of course, has much to do with how the company is performing.

Putting these things together, CEOs have come to view their earning potential much like professional athletes do. Like athletes, CEOs justifiably believe that they can make enormous amounts of money so long as they are perceived to be on top of their games, but they must cash in quickly because life, and particularly the life of perceptions, is uncertain. There are of course differences. How an athlete is performing at a given moment is almost always easier to assess objectively than how an executive is performing. Even in the case of athletes, however, scouting is a substantial industry, and perception matters. In the world of sponsorship—where the real money is made—perception is all, and wealth is a function of celebrity, however deserved.

Understanding CEOs to be like professional athletes goes a long way toward explaining the otherwise perverse behavior of corporate boards in voting for stratospheric executive compensation, thereby raising the company’s costs. If we understand that CEOs are acquired in what amounts to a public auction market, then executive compensation becomes a prestige item, nicely expressed in sports by the phrase “marquee” player. In getting a flashy CEO, and paying him accordingly, boards are not so subtly complimenting themselves and their company, and bragging to the world. We might call this the Steinbrenner effect. Rephrased, part of what one is buying, when buying the services of Derek Jeter, or a Ferrari, is the ability to say (not to have to say) that I paid a *lot* of money for this player, or this car. The “cost” in practice is an “asset.” And here we are very close indeed to Veblen: economic rationality or irrationality is not the point—the point is status.

Understanding CEOs as professional athletes explains something else otherwise odd, but also familiar from sports: a considerable gap is emerging between CEO pay and the pay of the next rung of management. Pay of treasurers, for example, while no doubt generous, has not exhibited the stratospheric rise of CEO pay. Why? Similarly, in sports, the rise in salaries of journeyman professional athletes has

not paced the rise in “compensation” paid to stars. The treasurer, like the journeyman athlete, is not a marquee player.

If CEOs are sports stars, compensation consultants are brokers and social arbiters. The work of compensation consultants is not suggesting how to structure pay packages (accountants and lawyers could do that), but instead reporting on “what is competitive,” that is, what did the other guy get? The question asked by both CEOs and boards is “what is prestigious,” not “what would it be reasonable to pay to get somebody competent in the executive suite?” In short, the recent rise in CEO pay is due to competition for prestige within the class of folks that controls companies. Unsurprisingly, the dynamics have all the sobriety of real estate in Newport during the gilded era, or these days, Martha’s Vineyard or Telluride.

Let me close with three remarks. First, by using equity—property—in enterprises as the basis of compensation, executive compensation has gone far toward creating a class in the old sense of folks with a specific relationship to the means of production guaranteed by a regime of property rights. Second, and in some tension with the first, there are reasons to doubt that executives will ever constitute a class in the traditional sense of a hereditary social position. While one might date the emergence of “contemporary” executive compensation practices in various ways, by all accounts the regime has not been around for very long. It remains to be seen how successful the current cohort of top executives will be at transmitting their positions to their children. But tax politics, specifically hostility to corporate and inheritance taxes, and the increasing irrelevance of the income tax on wages, suggests that this administration is interested in trying to make current disparities hereditary. What these two remarks might mean for our children’s understanding of the United States I leave for another day.

Third, turning back to corporate governance, I do not mean to suggest that executive compensation is absolutely irrelevant to the running of companies. But I do think it fair to say that executive compensation has very little to do with general corporate health, productivity, shareholder equity, or anything else internal to the company, and I am skeptical that efforts to get performance based compensation “right” will be more than window dressing, though perhaps



nonetheless worth doing. The problem for corporate governance is not so much the cost of compensation. The problem here is that regardless of the way executive performance is measured, achieving compensation that a man can be proud of requires justification, even while other aspects of the enterprise are neglected. Executive compensation distorts the perspective of management, a once familiar phenomenon that used to be called class bias, which is probably not a good thing for our economy, or our society.