2015

Income Inequality and Corporate Structure

Matthew T. Bodie
Saint Louis University School of Law, mbodie@slu.edu

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Efforts to address income inequality, such as welfare programs or progressive taxation, are often labeled as wealth redistribution.[1] The original distribution of wealth is viewed as a morally justifiable phenomenon that is dictated by the efficient workings of a massive variety of labor and capital markets.[2] Opponents of wealth redistribution argue that such reallocation improperly infringes upon economic liberty and saps the strength of the "invisible hand" of economic incentives.[3]

 Callis Family Professor, Saint Louis University School of Law. Thanks to Jase Carter for earlier research support on this topic. Special thanks to Jason R. Bent, Dean Christopher Pietruszkiewicz, and the editors of the *Stetson Law Review* for the opportunity to participate in this symposium on income inequality.

1. *See* Christine Jolls, *Behavioral Economics Analysis of Redistributive Legal Rules*, 51 VAND. L. REV. 1653, 1654 (1998) ("Redistributive legal rules are rules chosen for their effects in shifting wealth from high-income to low-income individuals (progressive redistribution)."); Anthony T. Kronman, *Contract Law and Distributive Justice*, 89 YALE L.J. 472, 472 (1980) (describing wealth redistribution as legal efforts to shape transactions "with an eye to their distributional effects in a self-conscious effort to achieve a fair division of wealth among the members of society" (footnote omitted)). Kronman describes two methods of redistributing wealth: through taxation and through regulating permissible contract terms. *Id.* at 498–99.

2. Economists and law and economics scholars focus on maximizing efficiency as the critical decision principle in choosing one set of rules over another. Ideally, a choice is Pareto-superior—namely, at least one party is better off and no parties are worse off. RICHARD A. POSNER, ECONOMIC ANALYSIS OF LAW 12 (7th ed. 2007). However, Kaldor-Hicks efficiency—when the overall sum of efficiency between participants is greater than any alternative rule or outcome, even if some are worse off—has been considered by economists to be "efficient" and thereby sufficient to justify a legal rule. *See* Jolls, *supra* note 1, at 1654 (noting that "[m]any law and economics scholars have urged that legal rules be chosen solely with an eye towards Kaldor-Hicks efficiency"). Louis Kaplow and Steven Shavell have famously argued that any income redistribution should be pursued solely through a tax-and-transfer system. Louis Kaplow & Steven Shavell, *Why the Legal System Is Less Efficient Than the Income Tax in Redistributing Income*, 23 J. LEGAL STUD. 667, 677 (1994) ("[I]t is appropriate for economic analysis of legal rules to focus on efficiency and to ignore the distribution of income . . . ."). *But see* Chris William Sanchirico, *Deconstructing the New Efficiency Rationale*, 86 CORNELL L. REV. 1003, 1068–69 (2001) (arguing that Kaplow and Shavell improperly assume a baseline of efficiency prior to tax redistribution).

3. 2 ADAM SMITH, AN INQUIRY INTO THE NATURE AND CAUSES OF THE WEALTH OF NATIONS, Book IV, at 242 (J. Maynard ed., London 1811) (1776) ("[B]y directing that industry in such a manner as its produce may be of the greatest value, he intends only his own gain; and he is in this, as in many other cases, led by an invisible hand to promote an end which was no part of his intention."). *See, e.g.*, FRIEDRICH HAYEK, THE CONSTITUTION OF LIBERTY 93–102, 133–61 (1961) (arguing that wealth redistribution improperly restricts economic liberty); ROBERT NOZICK, ANARCHY, STATE AND UTOPIA 167–78 (1974) (requiring that property rights should not be overcome by subsequent efforts to reallocate); LUIGI ZINGALES, A CAPITALISM FOR THE PEOPLE:

Many proponents of redistribution, on the other hand, accept the putative efficiency of the original distribution, but argue that income distribution objectives should be met through a tax-and-transfer system.[4]

This Article contends that to a significant extent, the problem of income inequality is not due to our failure to redistribute, but is rather due to our original scheme of income distribution. Specifically, the role of the corporation in wealth distribution is an underappreciated yet significant factor in our increasingly tilted economic picture. The corporation is designed to provide all of the power over the economic firm, and all of the rights to its residual profits, to a set of capital investors. Shareholders control the firm through their right to elect the board of directors,[5] and courts use the "shareholder primacy norm" to judge whether the board has failed in its duty to maximize shareholder wealth.[6] Employees who work at the firm have no employment-related rights to participation or profit.[7] As a result, I argue income has been redirected away from workers and towards capital and those professions that service capital.

Workplace law endeavors to address the consequences of this separation of employment from ownership. Employment laws are generally efforts to set minimum terms and fair-treatment standards on employers in order to protect the employees within. However, efforts to protect workers through labor and employment laws are insufficient to address the underlying power imbalances within the corporate structure.

RECAPTURING THE LOST GENIUS OF AMERICAN PROSPERITY 216–17 (2012) ("Redistribution reduces incentives to work, to invest, to excel.").

4. *See, e.g.*, Kaplow & Shavell, *supra* note 2, at 669 (describing the benefits of addressing income distribution through the income tax system). Opponents of law and economics similarly argue that redistribution is justifiable on equitable grounds, but their acceptance of the underlying efficiency argument is often implicit or begrudging. *See, e.g.*, Guido Calabresi, *The Pointlessness of Pareto: Carrying Coase Further*, 100 YALE L.J. 1211, 1224 n.36 (1991) (arguing that limiting redistribution to a tax-and-transfer system may also not be efficient as well as not being equitable or just).

5. Julian Velasco, *The Fundamental Rights of the Shareholder*, 40 U.C. DAVIS L. REV. 407, 416–17 (2006). *See, e.g.*, DEL. CODE ANN. tit. 8, § 212(a) (2015) (prescribing a one-share, one-vote system).

6. The standard source of the shareholder primacy norm in caselaw is *Dodge v. Ford Motor Co.*, 170 N.W. 668 (Mich. 1919), in which the court stated: "A business corporation is organized and carried on primarily for the profit of the stockholders." *Id.* at 684. For a recent confirmation of this doctrine, see eBay Domestic Holdings v. Newmark, 16 A.3d 1 (Del. Ch. 2010). In *eBay*, the Delaware Chancery Court stated forthrightly: "Having chosen a for-profit corporate form, the craigslist directors are bound by the fiduciary duties and standards that accompany that form. Those standards include acting to promote the value of the corporation for the benefit of its stockholders." *Id.* at 34.

7. *See* Robert Anderson IV, *Employee Incentives and the Federal Securities Law*, 57 U. MIAMI L. REV. 1195, 1202 (2003) (describing various forms of employee incentives). Employees may receive compensation in the form of stock, restricted stock, stock option, or participation in an employee stock ownership plan (ESOP). *Id.* However, there is no right to receive these ownership instruments. *Id.* at 1240 ("[E]mployees normally have no rights in the stock options apart from the employment relationship . . . .").

The National Labor Relations Act (NLRA)[8] is the one workplace statutory regime that endeavors to address the power imbalance within the firm directly. But this effort to develop workplace democracy has stalled, for a variety of reasons, and in some ways was doomed from the start. In order to solve the problems to which labor and employment laws are generally addressed, particularly income inequality, we need to address the structure of the "employer" itself. Workers need more power within the corporation to distribute the wealth generated by the corporation in a more equitable fashion.

This Article will begin by addressing the structure of business enterprises, particularly the corporation, and explain the separation of employment from ownership. It will then provide an overview of how labor and employment law has attempted to address this separation (and its consequences, including income inequality). Finally, it will argue that we need to rethink firm structure and governance if we truly want to address the root causes of income inequality.

I. CORPORATIONS, EMPLOYEES, AND THE DISTRIBUTION OF INCOME

In the United States, we conduct our joint economic enterprises, particularly large-scale ones, through corporations. Although a variety of different business organizational forms exist, such as the partnership, the limited liability company (LLC), and the sole proprietorship, the corporation clearly dominates the economic landscape.[9] The corporation (or company) has been described as "[t]he most important organization in the world . . . : the basis of the prosperity of the West and the best hope for the future of the rest of the world."[10] As Larry Ribstein described it, "The corporation undeniably has driven business growth in the United States since the Industrial Revolution."[11] To a large extent, the United States' approach now represents the global approach.[12]

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8. 29 U.S.C. §§ 151–169 (2012).

9. Andrew Lundeen & Kyle Pomerleau, *Corporations Make up 5 Percent of Businesses but Earn 62 Percent of Revenues*, TAX FOUND. (Nov. 25, 2014), http://taxfoundation.org/blog/corporations-make-5-percent-businesses-earn-62-percent-revenues (noting that only five percent of the organizational entities in the United States are corporations, but sixty-two percent of organizational tax revenues come from corporations).

10. JOHN MICKLETHWAIT & ADRIAN WOOLDRIDGE, THE COMPANY: A SHORT HISTORY OF A REVOLUTIONARY IDEA xv (2005).

11. LARRY E. RIBSTEIN, THE RISE OF THE UNCORPORATION 4 (2010).

12. *See* Henry Hansmann & Reinier Kraakman, *The End of History for Corporate Law*, 89 GEO. L.J. 439, 439 (2001). Hansmann and Kraakman stated,

In the United States, corporations are legal entities that are created through state corporate law.[13] The process of forming a corporation is relatively straightforward. Generally, the incorporating individuals must file a corporate charter, also known as the articles or certificate of incorporation.[14] The articles of incorporation provide the firm's basic structure, including the corporation's name, the incorporators, the corporation's business, and the total number of shares the corporation may issue.[15] Other governance structure provisions are not necessary to the formation of the corporation, but are allowed.[16] Once the corporation is established, control shifts from the entity's incorporators to its board of directors.[17] The board manages the firm and has the ability to bind the corporation through contracts and transfers of property.[18] Shareholders typically select the directors at the annual shareholders meeting.[19] Directors must act in the firm's interests through certain fiduciary duties, such as good faith and loyalty.[20] However, they delegate the actual job of running the business to the officers, primarily through a hierarchy headed by the chief executive officer (CEO).[21] This structure—shareholders select the directors, who in turn select the officers to run the corporation—represents the foundation of corporate law.

Employees find themselves outside of this structure, without any formal legal role in the governance of the corporation.[22] Employees are hired by the corporation itself through officers or other corporate

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> We must begin with the recognition that the law of business corporations had already achieved a remarkable degree of worldwide convergence at the end of the nineteenth century. By that time, large-scale business enterprise in every major commercial jurisdiction had come to be organized in the corporate form, and the core functional features of that form were essentially identical across these jurisdictions.

Id.

13. *Choose Your Business Structure*, U.S. SMALL BUS. ADMIN., https://www.sba.gov/content/corporation (last visited Dec. 14, 2015) ("A corporation is formed under the laws of the state in which it is registered.").

14. *See, e.g.*, DEL. CODE ANN. tit. 8, § 101(a) (2015) (providing the required content for a certificate of incorporation).

15. *Id.* § 102.

16. *E.g.*, *id.* § 102(b)(7) (limiting the liability of directors for breaches of a fiduciary duty); *id.* § 141(d) (staggering the board of directors).

17. Matthew T. Bodie, *Employees and the Boundaries of the Corporation*, *in* RESEARCH HANDBOOK ON THE ECONOMICS OF CORPORATE LAW 86 (Claire Hill & Brett McDonnell eds., 2012).

18. DEL. CODE ANN. tit. 8, § 141(c)(1)–(2).

19. *Id.* § 211(b).

20. Bodie, *supra* note 17, at 86.

21. *See, e.g.*, DEL. CODE ANN. tit. 8, § 142(a) ("Every corporation organized under this chapter shall have such officers with such titles and duties as shall be stated in the bylaws or in a resolution of the board of directors which is not inconsistent with the bylaws . . . .").

22. Bodie, *supra* note 17, at 87.

representatives through a contract.[23] This contract is most commonly terminable at-will.[24] Employees themselves are agents of the corporation, and the corporation is legally responsible for the torts they commit within the scope of employment.[25] The company is also legally responsible to its employees through a myriad of labor and employment laws.[26] However, employees have no direct input into the control of the corporation, nor do they have any claim to its profits.[27]

If we think of the corporation as the legal process through which we engage in joint economic production, those who control the corporation will control the process. The economic distribution of the responsibilities for production, as well as the distribution of the fruits of production, will ultimately rest in the hands of those with organizational power. Much of the debate in corporate law over the last forty years—perhaps even the last century—has concerned the distribution of corporate power between the board, the officers, and the shareholders.[28] Shareholder advocates have pushed for corporate law reforms that provide more direct power to stockholders.[29] On the other side, management and stakeholder advocates have argued that boards need more insulation from shareholders and more unreviewable discretion, even if their ultimate aim remains shareholder wealth maximization.[30] In this second group, there is a subset of advocates who argue that stakeholders such as employees, creditors, consumers, and communities deserve some

23. *Id.*

24. RESTATEMENT OF EMP'T LAW § 2.01 (2015).

25. RESTATEMENT (THIRD) OF AGENCY § 2.04 (2005).

26. *See infra* Part II.

27. *See* Brett H. McDonnell, *Strategies for an Employee Role in Corporate Governance*, 46 WAKE FOREST L. REV. 429, 429 (2011) ("[C]orporate law does nothing to encourage any role for employees in corporate governance." (footnote omitted)).

28. For the beginnings of the debate over the separation of ownership and control, see ADOLF A. BERLE & GARDINER C. MEANS, THE MODERN CORPORATION AND PRIVATE PROPERTY 5–6 (10th ed. 2009). *See also* Michael C. Jensen & William H. Meckling, *Theory of the Firm: Managerial Behavior, Agency Costs and Ownership Structure*, 3 J. FIN. ECON. 305 (1976) (discussing the problem of agency costs in light of the separation of ownership and control).

29. *See, e.g.*, Lucian Arye Bebchuk, *The Case for Increasing Shareholder Power*, 118 HARV. L. REV. 833, 865–69 (2005) (advocating for a system that would allow shareholders to alter a company's charter or state of incorporation).

30. *See, e.g.*, Stephen M. Bainbridge, *Director Primacy: The Means and Ends of Corporate Governance*, 97 NW. U. L. REV. 547, 550 (2003) ("[D]irector accountability for maximizing shareholder wealth remains an important component of director primacy."); Martin Lipton & William Savitt, *The Many Myths of Lucian Bebchuk*, 93 VA. L. REV. 733, 754 (2007) (rebutting the premise that shareholders own corporations); Lynn A. Stout, *The Mythical Benefits of Shareholder Control*, 93 VA. L. REV. 789, 804–09 (2007) (arguing against "the myth that greater shareholder control in public firms benefits shareholders").

protection within the process.[31] However, even within this group, there has been little to no call for changing the corporate electorate; at best, directors are to be given more freedom to consider all stakeholder interests, even though they remain accountable to shareholders.[32]

The allocation of power to shareholders and their representatives has had predictable results. Employees must bargain for purely contractual protections, as opposed to having a say in how the corporation manages its affairs. Directors and officers make the decisions about corporate strategy, dividend policies, stock buybacks, investment in research and development, overall compensation policies—in other words, all the decisions that together create the ongoing business.[33] Employees are costs—they are commodities to be purchased.[34]

It is thus not surprising to see the corporate power structure driving the growing inequality in the distribution of income. Corporations have not only driven down average labor incomes (in real terms); they have also accelerated the rise of the top of the spectrum. As to average incomes, the pressure to maximize shareholder wealth has led to efforts to drive down all firm costs, including (and perhaps especially) wages.[35] The norms of the internal labor market, with its implied lifetime employment contract, disappeared and were replaced with downsizing, layoffs, and outsourcing.[36] These trends accelerated as the market for corporate control took off.[37] As shareholders had new opportunities to sell their stock at higher prices to buyout firms or corporate competitors, companies were pressured to increase dividends by cutting other costs,

31. *See, e.g.*, Margaret M. Blair & Lynn A. Stout, *A Team Production Theory of Corporate Law*, 85 VA. L. REV. 247, 313 (1999) (stating that shareholders are granted limited voting rights because it benefits the interests of the firm's stakeholders).

32. *See* Grant Hayden & Matthew T. Bodie, *Shareholder Democracy and the Curious Turn Toward Board Primacy*, 51 WM. & MARY L. REV. 2071, 2113 (2010) (discussing the "strange turn" against stakeholder board representation).

33. *See* PRINCIPLES OF CORP. GOVERNANCE § 3.01 cmt. c (1994) (explaining that senior executives have a management role within the corporation).

34. I say this not to make a "commodification of labor" argument, but instead to describe the legal reality: employees are corporate outsiders. For a discussion of market commodification, see Margaret Jane Radin, *Market-Inalienability*, 100 HARV. L. REV. 1849, 1855–58 (1987).

35. *See, e.g.*, ALLAN A. KENNEDY, THE END OF SHAREHOLDER VALUE: CORPORATIONS AT THE CROSSROADS 91–92 (2000) (explaining how corporations increased their stock values by any means necessary and the resulting impacts on employees).

36. *Id.*; *see also* KATHERINE V. W. STONE, FROM WIDGETS TO DIGITS: EMPLOYMENT REGULATION FOR THE CHANGING WORKPLACE 85–86 (2004) (discussing the implied contract exception to the at-will doctrine and employers' shift away from long-term employment obligations).

37. *See* Steven M. Davidoff, *Takeover Theory and the Law & Economics Movement*, *in* RESEARCH HANDBOOK ON THE ECONOMICS OF CORPORATE LAW 219 (Claire A. Hill & Brett H. McDonnell eds., 2012) ("The 1980s takeover wave transformed the capital markets and was marked by a surge in hostile and unsolicited takeover offers.").

especially labor costs.[38] This pressure continues to this day, with companies continuing to seek less expensive ways of meeting their labor needs.[39]

As to the other end of the spectrum, corporations have enabled executives to elevate their compensation to greater and greater heights.[40] Economists have discovered that the great income divergence is driven not only by a stagnating middle and bottom of the wage spectrum, but also by a huge spike at the top of the spectrum.[41] Although the top ten percent of wage earners have seen their share of national income rise from 34% to 48%, the gains of the mega-rich are much greater.[42] The top one percent of wage earners more than doubled their share of national income (from 10% to 21%), the top 0.1% tripled their share (from 3% to 10%), and the top 0.01% quadrupled their share (from 1.4% to 5%).[43] And who were the folks receiving this larger largesse? According to one study, 42.5% of the top 0.1% were executives, managers, and supervisors at nonfinancial firms.[44] Those who controlled corporations made up almost half of the top 0.1%[45]—the group that saw its share of national income triple.[46]

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38. *See* KENNEDY, *supra* note 35, at 94–102 (describing employers' push to rewrite employment rules and the response of employees).

39. For a thorough and insightful discussion of workplace "fissuring," whereby workers are shed from their parent companies in order to reduce wages and employment responsibilities, see DAVID WEIL, THE FISSURED WORKPLACE: WHY WORK BECAME SO BAD FOR SO MANY AND WHAT CAN BE DONE TO IMPROVE IT (2014).

40. *See* LUCIAN A. BEBCHUK & JESSE M. FRIED, PAY WITHOUT PERFORMANCE: THE UNFULFILLED PROMISE OF EXECUTIVE COMPENSATION 72–75 (2004) (discussing large increases in managers' compensation).

41. Thomas Piketty & Emmanuel Saez, *Income Inequality in the United States, 1913–1998*, 118 Q.J. ECON. 1, 35–37 (2003).

42. TIMOTHY NOAH, THE GREAT DIVERGENCE: AMERICA'S GROWING INEQUALITY CRISIS AND WHAT WE CAN DO ABOUT IT 147 (2012).

43. *Id.*

44. Jon Bakija, Adam Cole & Bradley T. Heim, *Jobs and Income Growth of Top Earners and the Causes of Changing Income Inequality: Evidence from U.S. Tax Return Data* (Williams College Economics Department, Working Paper No. 2010-24, 2010) (manuscript at 49–51, tbls. 1–3), *available at* https://web.williams.edu/Economics/wp/BakijaColeHeimJobsIncomeGrowthTopEarners.pdf, *cited in* NOAH, *supra* note 42, at 151 & 247 n.12. *See also* Lawrence Mishel & Natalie Sabadish, *CEO Pay and the Top 1%: How Executive Compensation and Financial–Sector Pay Have Fueled Income Inequality*, ECON. POL'Y INST. (May 2, 2012), *available at* http://s4.epi.org/files/2012/ib331-ceo-pay-top-1-percent.pdf ("Just as wage inequality is a key driver of income inequality, a key driver of wage inequality is the growth of chief executive officer earnings and compensation and the expansion of and high compensation in the financial sector."). *But see* Steven N. Kaplan & Joshua Rauh, *Wall Street and Main Street: What Contributes to the Rise in the Highest Incomes?*, 23 REV. FIN. STUD. 1004, 1045–46 (2010) (finding that CEOs and top executives of nonfinancial companies comprise a smaller percentage of the top income brackets than generally assumed).

45. *See* Bakija et al., *supra* note 44, at tbl. 3 (listing executives, managers, and supervisors as 42.5% of primary taxpayers in the top 0.1%).

46. James Surowiecki, *Soak the Very, Very Rich*, NEW YORKER (Aug. 16, 2010), http://www.newyorker.com/magazine/2010/08/16/soak-the-very-very-rich.

In the wake of the late 1990s stock boom and the ensuing cavalcade of fraudulent corporate misdeeds in the early 2000s, economics and law professors developed a rich literature on executive compensation. The researchers can be roughly divided into two camps. On one side were those academics that saw the jump in executive compensation as a problem with its roots in a flawed corporate structure.[47] Prominent among this research was the "managerial power" hypothesis, which theorized that high-level executives were not bargaining with the corporation at arms' length, but were rather using their power within the corporation to get excess economic rents.[48] Others have argued that myths about the importance of performance pay for executives, together with the idea that the board's chosen CEO cannot merely be average, resulted in spiraling levels of higher pay.[49] On the other side, adherents to the status quo argued that executive compensation was not really a problem[50] or that efforts to reform the system had exacerbated—and would continue to exacerbate—the disparity.[51] Even if one is an advocate of shareholder power, the rise in executive compensation is a troubling development, as it represents a likely instantiation of the traditional agency-costs concerns raised by Berle and Means.[52] In this respect, the interests of shareholders and the great mass of employees are aligned against opportunism by that small subset of employees that run the company. However, if higher executive pay truly did lead to higher shareholder remuneration, the costs might be worth it to shareholders.[53]

47. *See, e.g.*, BEBCHUK & FRIED, *supra* note 40, at ix (listing defective governance structure as a reason for flawed compensation); MICHAEL B. DORFF, INDISPENSABLE AND OTHER MYTHS: WHY THE CEO PAY EXPERIMENT FAILED AND HOW TO FIX IT 4–5 (2014) (explaining that the common understanding of CEO pay is flawed and that there is little empirical support as to the efficacy of the traditional CEO pay system); Brett H. McDonnell, *Two Goals for Executive Compensation Reform*, 52 N.Y.L. SCH. L. REV. 585, 586 (2008) (citing concerns that excessive executive compensation "both reflects and exacerbates poor corporate governance" and acts "as a source of increasing economic, political, and social inequality").

48. BEBCHUK & FRIED, *supra* note 40, at 61 (introducing the managerial power perspective).

49. DORFF, *supra* note 47, at 265.

50. STEPHEN M. BAINBRIDGE, CORPORATE GOVERNANCE AFTER THE FINANCIAL CRISIS 112 (2012) (arguing that "regulating executive compensation is an inapt and unfair approach" to the broader problem of wealth and income inequality).

51. Kevin J. Murphy, *The Politics of Pay: A Legislative History of Executive Compensation*, *in* RESEARCH HANDBOOK ON EXECUTIVE PAY 11, 37–38 (Randall S. Thomas & Jennifer G. Hill eds., 2012) (arguing that efforts to regulate executive pay have been fruitless or counterproductive). *See* BAINBRIDGE, *supra* note 50, at 122–37 (examining the failures of Dodd-Frank and Sarbanes-Oxley to correct executive compensation).

52. BERLE & MEANS, *supra* note 28, at 124 (discussing how the corporation's "controlling group is in a position to serve its own interests").

53. Bebchuk and Fried fall into this camp. BEBCHUK & FRIED, *supra* note 40, at 8 ("We would accept compensation at current or even higher levels as long as such compensation, through its incentive effects, actually serves shareholders.").

But such a result could be disastrous to employees, particularly if executives improved share performance by cutting labor costs.

Rising share prices, executive incomes, and income inequality have all contributed to what some are calling the "New Gilded Age."[54] An income phenomenon has become a cultural phenomenon, with an elite group of corporate leaders, investment bankers, and hedge fund managers pulling away from the rest of society into a mega-wealthy bubble.[55] This bubble depends on control of the corporation to fuel its inflation. Much of the income divergence can be laid at the feet of the financial interests within the economy.[56] These interests service management and shareholders—in other words, those who currently control the business and finances of the corporation. The mix of financial professionals and corporate leaders—often listed under the moniker of "Wall Street"—has a wide range of overlapping economic, business, and personal interests and experiences.[57] These cultural connections exacerbate the power dynamics and compensation norms that result in diverging incomes. It becomes a back-scratching culture. In just one example of the interrelations between these groups, Goldman Sachs rewarded eBay executives for funneling their initial public offering (IPO) business to the firm by giving those executives thousands of shares in other lucrative IPOs that were also handled by Goldman Sachs.[58] Further, eBay CEO Meg Whitman also happened to be on the Goldman

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54. Paul Krugman, *Why We're in a New Gilded Age*, N.Y. REV. BOOKS (May 8, 2014), http://www.nybooks.com/articles/archives/2014/may/08/thomas-piketty-new-gilded-age/ (explaining that an incredible surge in the "one percent's" share of national income has marked the second Gilded Age).

55. Chrystia Freeland, *The Rise of the New Global Elite*, ATLANTIC (Jan.–Feb. 2011), http://www.theatlantic.com/magazine/archive/2011/01/the-rise-of-the-new-global-elite/308343/ (finding that the super-rich are "becoming a transglobal community of peers who have more in common with one another than with their countrymen back home").

56. *See, e.g.*, LAWRENCE E. MITCHELL, THE SPECULATION ECONOMY: HOW FINANCE TRIUMPHED OVER INDUSTRY 4–6 (2008) (discussing how finance and the stock markets became the driving forces in the economy); NOAH, *supra* note 42, at 156 ("In effect, Wall Street ate the economy.").

57. *See In re* Oracle Corp. Derivative Litig., 824 A.2d 917, 930–35 (Del. Ch. 2003) (discussing academic, social, and philanthropic connections between the Oracle board's special litigation committee and the executives charged with insider trading); BEBCHUK & FRIED, *supra* note 40, at 31–34 (explaining certain psychological and social factors that contribute to directors' decisions regarding CEO compensation); *About*, THEY RULE, http://www.theyrule.net/drupal/about (last visited Dec. 14, 2015) (illustrating alleged connections between corporate executives, directors, government, and allowing users to search companies and boards).

58. *In re* eBay, Inc. S'holders Litig., No. C.A. 19988-NC, 2004 WL 253521, at *1 (Del. Ch. Jan. 23, 2004). eBay CEO Meg Whitman herself received shares in over 100 IPOs. *Id.* The Delaware Chancery Court noted: "Because the IPO market during this particular period of time was extremely active, prices of initial stock offerings often doubled or tripled in a single day." *Id.*

Sachs board of directors—a position she resigned once the scandal broke.[59]

Something needs to break the cycle. The clear trends over the last two decades (after a brief blip during the financial crisis) are that corporate profits are continuing to diverge from labor income, and that compensation for the top income percentiles are continuing to diverge from the lower percentiles.[60] For some, the answer lies in the law of labor and employment regulation.

II. WORKPLACE LAW AND INCOME INEQUALITY

The myriad laws governing the workplace largely endeavor to mitigate the inequalities engendered by the structure of the business corporation. These laws are often seen as regulatory in nature, akin to consumer safety or environmental protection laws,[61] or as part of the country's overall social safety net.[62] Although these regimes may have varying degrees of effectiveness regarding various social and economic problems, they are largely ineffective in addressing the income inequality that comes through corporate distribution.

A broad swath of workplace protections focus on providing a minimum level of protections or endowments to employees. As to protections, employers are liable for the torts of their employees not only when the victims are third parties, but also when the victims are fellow employees.[63] When an employee harms another employee as a result of tortious behavior, the employer is liable if that tort was committed within the scope of employment or if the employer later ratified the conduct.[64]

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59. *eBay CEO Quits Goldman Board*, CNN MONEY (Dec. 20, 2002, 7:15 AM EST), http://money.cnn.com/2002/12/20/news/whitman/.

60. *See* Emmanuel Saez & Gabriel Zucman, *Wealth Inequality in the United States Since 1913: Evidence from Capitalized Income Tax Data* (NBER Working Paper No. 20625, 2014), *available at* http://gabriel-zucman.eu/files/SaezZucman2014.pdf (discussing diverging income inequality); Floyd Norris, *Corporate Profits Grow and Wages Slide*, N.Y. TIMES (Apr. 4, 2014), http://www.nytimes.com/2014/04/05/business/economy/corporate-profits-grow-ever-larger-as-slice-of-economy-as-wages-slide.html (discussing the rise in corporate profits and fall of employee compensation).

61. *See* Cynthia Estlund, *Labor Law Reform Again? Reframing Labor Law as a Regulatory Project*, 16 N.Y.U. J. LEGIS. & PUB. POL'Y 383, 383 (2013) (reframing labor law as "one field of regulation among others, alongside regulation of the environment, product safety, and financial integrity").

62. For an argument that common-law nations tend to have stronger shareholder-primacy policies when they have stronger social welfare policies, see CHRISTOPHER M. BRUNER, CORPORATE GOVERNANCE IN THE COMMON-LAW WORLD: THE POLITICAL FOUNDATIONS OF SHAREHOLDER POWER 9 (2013) ("[S]tronger stakeholder protections outside the corporate governance system allow it to focus more exclusively on the shareholders' interests by blunting political resistance . . . .").

63. RESTATEMENT OF EMP'T LAW § 4.03 cmt. f (2015).

64. *Id.* § 4.03(a)–(b) (2015).

An employer also faces liability if its supervisor or manager commits a tort outside the scope of employment, unless the employer had taken reasonable care to prevent the conduct and the employee failed to take advantage of this care.[65] A similar rule applies to sexual harassment: the employer has responsibility for a hostile work environment when that environment was created by a supervisor or supervisors with authority over the employee.[66] The sexual harassment protections are part of a set of federal antidiscrimination statutory schemes that protect employees against adverse employment actions because of race, ethnicity, sex, religion, age, or disability.[67] Employers also have a common-law duty to exercise care in selecting, retaining, and supervising their employees,[68] and they are liable for harm to employees caused by the breach of this duty.[69] Employers also have a common-law duty to provide a reasonably safe workplace for employees and to provide warning of dangerous working conditions.[70] The common-law duty has been supplemented by the federal Occupational Safety and Health Administration (OSHA) regime, in which employers similarly have a general duty to provide safe working conditions.[71] When workers suffer injuries on the job that require medical treatment and may result in employee disability, state workers'

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65. *Id.* § 4.03(c).

66. *See* 42 U.S.C. § 2000e-2(a) (2012) (stating that an employer may not classify, limit, or segregate an employee in a way that would deprive that employee of employment opportunities, or otherwise adversely affect the individual's employment status, on the basis of sex); Burlington Indus., Inc. v. Ellerth, 524 U.S. 742, 765 (1998) (holding that an employer is open to vicarious liability when a supervisor with immediate authority over an employee creates a hostile work environment by making threats based on the employee's sex). A similar duty has been found in tort. *See, e.g.*, Ford v. Revlon, Inc., 734 P.2d 580, 584–85 (Ariz. 1987) (holding that a company's failure to investigate a complaint of sexually abusive treatment is independent of the abusive treatment itself and that a company may be liable for failing to stop the abusive treatment regardless of whether the treatment itself rises to the level of an actionable tort).

67. *See* 29 U.S.C. § 623(a) (2012) (prohibiting discrimination against employees based on age); 42 U.S.C. § 2000e-2 (prohibiting discrimination against employees based on race, sex, ethnicity, or religion); *id.* § 12112(a) (prohibiting discrimination against employees based on disability).

68. RESTATEMENT OF EMP'T LAW § 4.04.

69. *See, e.g.*, Retherford v. AT & T Commc'ns of Mountain States, Inc., 844 P.2d 949, 973 (Utah 1992) (describing the elements of a claim of negligent employment as "(i) [employer] knew or should have known that its employees posed a foreseeable risk of retaliatory harassment to third parties, including fellow employees; (ii) the employees did indeed inflict such harm; and (iii) the employer's negligence in hiring, supervising, or retaining the employees proximately caused the injury" (footnote omitted)); Kerans v. Porter Paint Co., 575 N.E.2d 428, 432 (Ohio 1991) ("[B]oth federal and state courts have held that an employer may be liable for failing to take appropriate action where that employer knows or has reason to know that one of its employees poses an unreasonable risk of harm to other employees.").

70. RESTATEMENT OF EMP'T LAW § 4.05. The duty has been recognized in all United States jurisdictions. *Id.* rptr. n. cmt. a.

71. *See* 29 U.S.C. § 654(a)(1) (requiring an employer to "furnish to each of his employees employment and a place of employment which are free from recognized hazards that are causing or are likely to cause death or serious physical harm to his employees").

compensation statutes require employers to cover the compensation even if the employer was not at fault.[72]

Employers are also responsible for providing a minimum level of wealth distribution to employees. The federal minimum wage is a familiar duty placed on employers to provide a certain monetary compensation level.[73] The same statute provides that employees must receive at least one-and-a-half times their hourly wages if they work over forty hours per week.[74] These federal requirements are supplemented by a plethora of state and local wage requirements, which can go well above the federal minimums.[75] As for benefits, employers must provide their employees with up to twelve weeks of unpaid leave per year for family or medical leave and allow the employee to return to an equivalent position.[76] Pension plans need not be provided, but if they are, they must comport with extensive federal regulations on their legal and financial structures.[77] The Affordable Care Act's employer mandate now requires employers of a certain size to purchase health insurance for their employees or provide funding for employees to buy their insurance on state exchanges.[78] If employers fail to do so, they must pay a tax penalty.[79]

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72. *See* MARK A. ROTHSTEIN & LANCE LIEBMAN, EMPLOYMENT LAW 757–61 (7th ed. 2011) ("Employers meet their statutory obligation to compensate injured workers through various forms of insurance.").

73. *See* 29 U.S.C. § 206 (establishing the minimum wages all employers must pay each employee).

74. *Id.* § 207.

75. For example, in 2013, voters in SeaTac, Washington, home to the Seattle-Tacoma International Airport, increased the region's minimum wage to $15. Kirk Johnson, *Voters in SeaTac, Wash., Back $15 Minimum Wage*, N.Y. TIMES (Nov. 26, 2013), http://www.nytimes.com/2013/11/27/us/voters-in-seatac-wash-back-15-minimum-wage.html. *See also* Dana Milbank, *Raising the Minimum Wage Without Raising Havoc*, WASH. POST (Sept. 5, 2014), http://www.washingtonpost.com/opinions/dana-milbank-no-calamity-yet-as-seatac-wash-adjusts-to-15-minimum-wage/2014/09/05/d12ba922-3503-11e4-9e92-0899b306bbea_story.html (discussing the wage increase's effects).

76. 29 U.S.C. §§ 2612, 2614.

77. The Employee Retirement Income Security Act (ERISA) does not require that employers provide pension benefits, but it does set forth mandatory standards for these benefits if provided, particularly in the pension context. *See* Conkright v. Frommert, 559 U.S. 506, 516 (2010) ("Congress enacted ERISA to ensure that employees would receive the benefits they had earned, but Congress did not require employers to establish benefit plans in the first place."); DANA SHILLING, THE COMPLETE GUIDE TO HUMAN RESOURCES AND THE LAW 202 (1998) ("ERISA gives employers a choice. There is no requirement that an employer maintain any pension plan at all.").

78. 26 U.S.C. § 4980H(a), (c)(2)(A). *See* Suja A. Thomas & Peter Molk, *Employer Costs and Conflicts Under the Affordable Care Act*, 99 CORNELL L. REV. 56, 58 (2013) ("Employers with fifty or more full-time employees or the equivalent must either offer insurance to full-time employees or pay a fine to the federal government." (footnote omitted)).

79. *See* Thomas & Molk, *supra* note 78, at 58. ("Employers can trigger the fine in two ways. First, employers can refuse to offer *any* health insurance to employees, in which case the employer must pay $2,000 per full-time employee in excess of thirty employees. Second, employers can offer 'inadequate' health insurance (insurance that is either not sufficiently comprehensive or too expensive) to employees. In that case, the employer must pay the lesser of the above fine or $3,000

Further, although the "at will" doctrine frames the employment relationship as terminable at any time, with or without cause, employers still owe a duty under the state-provided (but federally subsidized) unemployment insurance system to provide unemployment compensation for their employees.[80]

These protections and distributions all contribute to creating a "floor" of minimal levels of welfare for employees. Such required thresholds play an important role in establishing a baseline for economic participation that all employees can be expected to enjoy.[81] However, the baseline protections do very little to address the income inequality problem. Although the required minimums do provide some degree of adjustment upward to those at the bottom of the income spectrum, particularly if benefits are considered as part of the equation, they are designed to be minimums. As such, they address the growing disparity in incomes only by bumping up the bottom, not by addressing the inherent causes of inequality across the income spectrum.

The only workplace statute that could, in theory, more directly address the disparity in income is the NLRA.[82] Under the NLRA, employees can select a collective representative to negotiate terms and conditions of employment, and the employer must bargain with this representative in good faith.[83] A complex array of subsidiary obligations flow from this central obligation, such as the prohibition against discipline or discharge for an employee's protected concerted activity.[84] Federal labor law forces employers to engage with groups of their employees on wages, hours, benefits, and job responsibilities.[85] The employer need not agree to any specific set of terms, but it must bargain in good faith and abide by the complex legal system for managing this bargaining relationship.[86] The NLRA enables employees to exercise

per eligible employee who opts for, and receives, individual coverage subsidized by the federal government through a state health insurance exchange.").

80. *See* ROTHSTEIN & LIEBMAN, *supra* note 72, at 1051 (providing an overview of the system).

81. That, of course, assumes enforcement of the minimums. For a discussion of one program designed to create a voluntary self-policing mechanism for the enforcement of employment minimums, see Matthew T. Bodie, *The Potential for State Labor Law: The New York Greengrocer Code of Conduct*, 21 HOFSTRA LAB. & EMP. L.J. 183, 185–200 (2003).

82. 29 U.S.C. §§ 151–159.

83. *Id.* § 158(a)(5) (setting forth the duty to bargain); *id.* § 159 (establishing the process to select the employees' collective representative).

84. *See id.* § 158(a)(1), (3) ("It shall be an unfair labor practice for an employer—(1) to interfere with, restrain, or coerce employees in the exercise of the rights guaranteed in section 157 of this title; [or] . . . (3) by discrimination in regard to hire or tenure of employment or any term or condition of employment to encourage or discourage membership in any labor organization . . .".).

85. *Id.* § 158(a), (d).

86. *Id.* § 158(d).

collective power to improve the terms that they secure from the employer, no matter where on the income spectrum they fall.[87]

Because of the duty to bargain, labor law is really the only tool in the current workplace's legal toolbox that might plausibly address income inequality. Although the exact economic ramifications are contested, there is a consensus that collective bargaining increases wages amongst employees on an individual firm level.[88] On a societal level, relative income equality's "golden era" in the 1950s is often attributed to the power of unions to demand a greater share of the economic pie.[89] However, it is unrealistic to expect unions to put much of a dent in the current and widening income gap. For a variety of contested reasons, the percentage of unionized private-sector employees has been steadily shrinking since its 1950s heyday, from a high of about 35% to the current 6.6%.[90] Furthermore, despite the continual hope of unions and their allies, there is not much chance for that trend reversing. The failure of labor-friendly legislation in the first Obama Administration, when Democrats controlled both houses of Congress, indicates the improbability of pro-union statutory change.[91] If anything, the current political climate seems more likely to further erode private-sector union

87. For example, professional sports players are unionized and are at the top of the income distribution spectrum. VisualNews, *Visualizing the Yearly Salary of Professional Athletes, NBA Players Average $5+ Million a Year*, HUFFINGTON POST (Nov. 1, 2013, 11:12 AM EDT), http://www.huffingtonpost.com/visualnewscom/visualizing-the-yearly-sa_b_ 4184716.html.

88. *See* RICHARD B. FREEMAN & JAMES L. MEDOFF, WHAT DO UNIONS DO? 43–60 (1984) (discussing studies of the union wage effect); David G. Blanchflower & Alex Bryson, *What Effect Do Unions Have on Wages Now and Would Freeman and Medoff Be Surprised?*, 25 J. LAB. RES. 383, 391 (2004) (finding a 17% private-sector union wage effect and a 14.5% public-sector union wage effect in the late 1990s).

89. *See* NOAH, *supra* note 42, at 128 (discussing unions' role in ameliorating income inequality); Harwell Wells, *U.S. Executive Compensation in Historical Perspective*, *in* RESEARCH HANDBOOK ON EXECUTIVE PAY 41, 55 (Randall S. Thomas & Jennifer G. Hill eds., 2012) ("The years during which executive pay was restrained were, after all, also the years during which much of the American political economy operated within an informal concordat between labor unions, big business, and the Federal government, an era in which average workers' wages rose relatively rapidly, as political and economic institutions (notably unions) encouraged wide distribution of the fruits of economic growth . . . .").

90. *Union Membership (Annual) News Release*, U.S. BUREAU LAB. STAT. (Jan. 23, 2015, 10:00 AM), http://www.bls.gov/news.release/union2.htm. *See also* NOAH, *supra* note 42, at 128 (discussing the decline in union membership). At their peak in the 1950s, unions are estimated to have represented more than a third of the private and nonagricultural workforce. MICHAEL GOLDFIELD, THE DECLINE OF ORGANIZED LABOR IN THE UNITED STATES 10 tbl.1 (1987); LEO TROY & NEIL SHEFLIN, U.S. UNION SOURCEBOOK: MEMBERSHIP, STRUCTURE, FINANCE, DIRECTORY app. A, A-1 (1985).

91. *See* Harold Meyerson, *Under Obama, Labor Should Have Made More Progress*, WASH. POST (Feb. 10, 2010), http://www.washingtonpost.com/wp-dyn/content/article/2010/02/09/AR2010020902465.html (discussing the failure of the Employee Free Choice Act).

membership even more, as states such as Michigan and Wisconsin change to right-to-work regimes.[92]

Moreover, there is a larger structural problem with labor law when it comes to addressing the corporate power structure that enables income inequality. The federal labor law regime enacted under the NLRA clearly creates zones of power and influence that leave the underlying business organizational structure intact. Employers are only required to bargain on specific topics that could be considered "mandatory" subjects of bargaining.[93] The idea behind mandatory subjects is that the employer need only engage with its employees on the terms of the employment contract.[94] Bigger issues such as product development, executive compensation, financial structuring, and internal firm governance are not within the ambit of the union's responsibilities or concerns, and the employer has no duty to discuss such issues.[95] The idea that the "core of entrepreneurial control"[96] is reserved to the employer itself is central to the federal system of collective bargaining. Employers may be forced to talk with the employees' representatives about the employees' bargain with the firm, but employers have no duty to talk about how they run the business.[97] Plus, the union may not insist on talking about these issues, either; to do so would be a failure to bargain in good faith.[98]

Unions were able to change the income-distribution dynamics in the mid-twentieth century by economic force.[99] They collectivized employees in entire industries, such as auto-manufacturing, truck driving, and steel

92. Monica Davey, *Unions Suffer Latest Defeat in Midwest with Signing of Wisconsin Measure*, N.Y. TIMES (Mar. 9, 2015), http://www.nytimes.com/2015/03/10/us/gov-scott-walker-of-wisconsin-signs-right-to-work-bill.html. Right-to-work is just one of the policy changes that are making public-sector union membership more difficult and less desirable. *See, e.g.*, Paul M. Secunda, *The Wisconsin Public-Sector Labor Dispute of 2011*, 27 A.B.A. J. LAB. & EMP. L. 293, 293–94 (2012) (describing Wisconsin's "unprecedented attack on public-sector bargaining").

93. NLRB v. Wooster Div. of Borg-Warner Corp., 356 U.S. 342, 349 (1958) (discussing the mandatory subjects of collective bargaining).

94. *Id.*

95. *See id.* (emphasizing a party's freedom to bargain or not bargain over other subjects).

96. Fibreboard Paper Prods. Corp. v. NLRB, 379 U.S. 203, 223 (1964) (Stewart, J., concurring) (discussing mandatory subjects' limitations, including how managerial decisions lie outside the scope of mandatory subjects). *See also* James Gray Pope, *Class Conflicts of Law II: Solidarity, Entrepreneurship, and the Deep Agenda of the Obama NLRB*, 57 BUFF. L. REV. 653, 658 (2009) ("The doctrine [of entrepreneurial control] provides the focal point for a coherent and positive conception of employer interests that has come to permeate the labor law." (footnote omitted)).

97. *See Fibreboard Paper Prods. Corp.*, 379 U.S. at 223 (explaining how every decision made that may affect job security does not trigger mandatory bargaining).

98. Local Union 189, Amalgamated Meat Cutters v. Jewel Tea Co., 381 U.S. 676, 689 (1965) (citing *Wooster Div. of Borg-Warner Corp.*, 356 U.S. at 349).

99. *See* Nicholas Kristof, *The Cost of a Decline in Unions*, N.Y. TIMES (Feb. 19 2015), http://www.nytimes.com/2015/02/19/opinion/nicholas-kristof-the-cost-of-a-decline-in-unions .html (describing how unions have been integral to maintaining the middle class and suggesting that the decline in unions has led to income inequality).

production, and they used strikes and other forms of economic pressure to push up their wages and benefits.[100] The NLRA is based on this notion of economic battle, and in fact the Supreme Court has taken special concern to balance each side's "weapons" of economic conflict.[101] In creating this divided battlefield, however, the NLRA fenced employees and their representatives out of any real participation in the firm's management. "Management," which under the NLRA's statutory scheme includes low-level supervisory employees,[102] has control of the firm, and "labor" can only try to pressure management into giving up some of the economic spoils. When a union can achieve something close to monopoly power over the workers in an industry, it can exercise sufficient power to change the income dynamics. But those days seem well behind us.

Rather than forcing employees (as "labor") to engage in a locked, eternal struggle with management to achieve some share of the firm's resources, the law should reorient corporate law to include employees in the governance of the firm. Rather than having to fight back on the outside, labor should be on the inside, working with the firm's equity contributors to run the ongoing business. Such an approach would be a dramatic change, not only in our approach to labor and employment law, but also in our approach to corporate law.

III. ADDRESSING INCOME INEQUALITY THROUGH STRUCTURAL CORPORATE LAW CHANGE

In earlier works, I have argued that corporate law has improperly fenced out employees from participation in corporate governance.[103] Employees deserve a role in that governance because they participate in the ongoing business of the firm in a manner similar to equity participants. In fact, Ronald Coase based his theory of the firm on the relationship between employers and employees.[104] There is thus an

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100. *See* JAKE ROSENFELD, WHAT UNIONS NO LONGER DO 1–2 (2014) (describing how unions were "*the* core equalizing institution" for income equality (emphasis in original)).

101. NLRB v. Ins. Agents' Int'l Union, 361 U.S. 477, 489 (1960) ("The presence of economic weapons in reserve, and their actual exercise on occasion by the parties, is part and parcel of the system that the Wagner and Taft-Hartley Acts have recognized.").

102. 29 U.S.C. § 152(11) (2012) (defining "supervisor").

103. *See* Bodie, *supra* note 17, at 100 (arguing that corporate law "has divorced the employees from the firm").

104. R. H. Coase, *The Nature of the Firm*, 4 ECONOMICA 386, 403 (1937) ("We can best approach the question of what constitutes a firm in practice by considering the legal relationship normally called that of 'master and servant' or 'employer and employee.'" (footnote omitted)). For a lengthier discussion on the importance of employment to Coase's theory of the firm, see Matthew T. Bodie,

independent set of economic and structural reasons why employees should have a role in firm governance related to the firm's structure. This Article, however, focuses on a separate policy justification for employee participation in governance: namely, the role that employee participation would play in making income distributions more equal. By addressing the initial inequality in income distributions, we would not need to rely on secondary efforts to ameliorate the divergence, such as tax transfers. Instead, firms themselves would more equitably allocate the gains from economic production.

Employees have traditionally participated in firm governance through collective bargaining or through some form of employee ownership.[105] As discussed above,[106] unions likely played a significant role in equalizing incomes in the mid-twentieth century, but they are unlikely to repeat that success for a variety of reasons. Employee ownership, on the other hand, directly involves employees in the governance of the firm by placing them in the driver's seat. The most direct way for employees to participate in governance would be to purchase a controlling percentage of the outstanding stock in the company. For almost all sets of employees, however, this option will be unrealistic: the capital necessary to make the purchase is likely to be well beyond the reach of most employees, barring special restructuring of the firm's finances or an extremely long time horizon.[107] Even if employees could accumulate the capital, it would be extremely risky for them to sink their savings into the same company in which they work.[108] This lack of risk diversification would also represent extremely poor financial

Participation as a Theory of Employment, 89 NOTRE DAME L. REV. 661, 695–97 (2013) (discussing certain theoretical aspects of the firm and employees' role within the firm).

105. *See supra* Part II.

106. *See supra* Part II.

107. *See* LOUIS O. KELSO & MORTIMER J. ADLER, THE CAPITALIST MANIFESTO 188–89 (1958) (explaining how ownership of capital can be interrupted).

108. Brett H. McDonnell, *Employee Primacy, or Economics Meets Civic Republicanism at Work*, 13 STAN. J.L. BUS. & FIN. 334, 351 (2008) ("If employee primacy is tied to employee share ownership, then employees may wind up putting too many eggs in one basket. If their employer fails, not only do they lose their jobs, but they also lose the value of their shares."). Susan Stabile has written extensively and persuasively on the financial risks associated with employer securities. *See* Susan J. Stabile, *Enron, Global Crossing, and Beyond: Implications for Workers*, 76 ST. JOHN'S L. REV. 815 (2002) [hereinafter Stabile, *Enron, Global Crossing, and Beyond*] (explaining how workers suffer disproportionately compared to executives when stocks fall); Susan J. Stabile, *Another Look at 401(k) Plan Investments in Employer Securities*, 35 J. MARSHALL L. REV. 539, 546–47 (2002) (describing the danger of over-investment in employer securities by employee pension plans); Susan J. Stabile, *Pension Plan Investments in Employer Securities: More Is Not Always Better*, 15 YALE J. ON REG. 61, 64–65 (1998) (examining major problems posed by excessive retirement plan investments in employer securities).

planning—as many former Enron employees can attest.[109] Finally, it makes sense for companies to avail themselves of global capital markets in order to finance at least a portion of their operations.

Of course, it will still make sense for some firms, at some moments in time, to be employee-owned; even skeptics of employee ownership agree on that.[110] But even traditional methods of employee ownership often fail to give employees significant control. The employee stock ownership plan (ESOP) provides a tax-favored financial vehicle, in which a trust owns the company's shares on behalf of the employee–shareholders.[111] The trust is administered by a trustee who must act in the interests of the beneficiaries.[112] This trustee, however, need not consult employees or endeavor to assay their wishes; instead, the trustee is only obligated to pursue what the trustee believes is in the employees' best financial interests.[113] Thus, ESOPs can often shut out rank-and-file employees from actual participation in the firm's governance. Not surprisingly, ESOPs have a reputation for being a refinancing tool that is responsive to managerial interests, rather than of a process that provides

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109. *See* Stabile, *Enron, Global Crossing, and Beyond*, *supra* note 108, at 824–27 (discussing Enron employees' difficulties in protecting themselves financially).

110. HENRY HANSMANN, THE OWNERSHIP OF ENTERPRISE 91 (1996) (discussing how employee ownership is most likely to be successful when employees have similar status and economic interests).

111. *See* Jeffrey M. Hirsch, *Labor Law Obstacles to the Collective Negotiation and Implementation of Employee Stock Ownership Plans: A Response to Henry Hansmann and Other "Survivalists*,*"* 67 FORDHAM L. REV. 957, 959 (1998) ("Typically, [ESOPs] create a trust for employees that borrows money, then loans the borrowed money to the employer while obtaining stock from the employer as repayment for the loan.").

112. *See* JOHN H. LANGBEIN ET AL., PENSION AND EMPLOYEE BENEFIT LAW 53 (4th ed. 2006) ("ESOP assets are held in trust and managed by a trustee, who is usually selected by the employer."). ESOP trustees have fiduciary duties to the ESOP's beneficiaries. 29 U.S.C. § 1104(a) (2012) (discussing fiduciary duties under ERISA for pension plans, including ESOPs). *But see* Meredith L. Gray, Comment, *A Presumption Without Prudence: Replacing* Moench v. Robertson *with a Prudent "When in Doubt, Don't" Standard for ESOP and 401(k) Company Stock Fund Fiduciaries*, WIS. L. REV. 907, 921 (2010) ("Since Congress intended that ESOPs invest primarily in company stock, it also exempted fiduciaries from the duty to diversify ESOP investments and from ERISA's prudence requirement, but '*only to the extent that it requires diversification*.'" (emphasis in original) (footnote omitted)).

113. *See* Hirsch, *supra* note 111, at 960 ("Employee ownership plans typically do not have to 'pass-through' voting rights to the employee-owners, and even with pass-through voting, a trustee may vote in place of actual workers." (footnote omitted)).

employees with participation in the firm.[114] It is unusual for an ESOP even to place any representatives on the board.[115]

Moving to a system of complete or majoritarian employee ownership would be moving from one extreme to another: from a system of shareholder primacy to a system of employee primacy. Even putting aside the sheer financial impossibility of transferring all current shares from their current holders to employees (absent a government-imposed system of redistribution),[116] shareholders would be vulnerable to employee opportunism if they lacked meaningful participation in firm governance. Such opportunism may, certainly, operate to diminish income inequality by distributing the firm's resources to employees. But in an era of global capital mobility, companies rife with shareholder exploitation cannot maintain access to equity capital for long. Thus, while employee stock ownership is an important (and perhaps underutilized) piece of the puzzle, it should not be the only mechanism for employee participation.[117]

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114. Sean M. Anderson, *Risky Retirement Business: How ESOPs Harm the Workers They Are Supposed to Help*, 41 LOY. U. CHI. L.J. 1, 16 (2009) ("Choosing an ESOP, then, reflects either a misunderstanding of the workers' best interests or a deliberate subordination of those interests to the interests of the company and the insiders."); Julie Lynn Kaufman, *Democratic ESOPs: Can Workers Control Their Future?*, 5 LAB. LAW. 825, 825 (1989) (arguing that "the majority of ESOPs are structured to skew stock ownership heavily towards management" and "ESOP trusts thus become a means of perpetuating and entrenching current managerial control").

115. *See* Hirsch, *supra* note 111, at 960 ("[A]n employer can create an ESOP that owns a majority of the company but gives employees virtually no voice in managerial policy-making."). As one example, during its existence as an ESOP-owned company, Avis did not have any employee representatives on its board. James S. Hirsch, *Avis Employees Find Stock Ownership Is Mixed Blessing*, ASSOCIATED PRESS (May 2, 1995, 9:19 AM ET), http://www.apnewsarchive.com/1995/Avis-Employees-Find-Stock-Ownership-Is-Mixed-Blessing/id-fc7b2b373d85cd1c193da5078c5ee1dc. In its 1994 restructuring, United Airlines did in fact put employee representatives on the board after an ESOP, which was funded by the airline's pilots and management employees, purchased fifty-five percent of the company. Jeffrey N. Gordon, *Employee Stock Ownership in Economic Transitions: The Case of United Airlines*, 10 J. APPLIED CORP. FIN. 39, 52 (1998). However, these representatives made up only one-quarter of the board—far less than a controlling percentage. *Id.* at 54 ("The board consist[ed] of [twelve] members: five 'public directors,' four 'independent directors,' two 'union directors,' and one 'salaried and management' director (the latter three directors known collectively as 'employee directors').").

116. The current ESOP structure is already a system of redistribution, given the tax benefits it provides. *See* Robert Hockett, *What Kinds of Stock Ownership Plans Should There Be? Of ESOPs, Other SOPs, and "Ownership Societies*,*"* 92 CORNELL L. REV. 865, 890 (2007) ("The leveraged ESOP as currently constituted is essentially a public benefit conferred through private channels.").

117. *See id.* at 931–33 (discussing a new credit strategy to provide for employee–ownership financing, similar to home mortgages and student loan financing). In the interest of brevity, I am giving short shrift to the many thoughtful treatments of the possibilities for greater employee ownership. *See, e.g.*, JOSEPH BLASI ET AL., IN THE COMPANY OF OWNERS: THE TRUTH ABOUT STOCK OPTIONS 223 (2003) (arguing that "most corporations in America would enjoy more motivated workers and larger profits if they embraced partnership capitalism centered around employee stock options").

Another approach is to integrate workers into firm governance in a substantial but not dominating way. If employee representatives were placed onto boards of directors, the boards' deliberations would change in a meaningful way.[118] Rather than acting simply in the interests of shareholders, directors would need to consider the impact on all those who participate in the ongoing business of the firm: equity contributors and labor contributors. The firm would not be governed with a monolithic pursuit of shareholder wealth maximization; instead, the firm would need to account for workers' interests as well.[119]

What would employee representation mean for income inequality? Employee representatives would be in a position to demand more for workers. In the heyday of unionization, employee representatives were able to secure significant wage gains through suasion, bargaining, and collective economic power.[120] Having actual power within the corporate governance structure would enable those representatives to exercise their rights of governance in support of workers. If shareholder primacy and an energized shareholder electorate have tilted the playing field in equity's favor over the last four decades, a shared governance regime between workers and equity would balance the division of spoils. Changing the electorate to include a new group would make the decision-making process more favorable to that group.

Moreover, employee representatives would also change norms about the acceptability of sky-high compensation for CEOs, high-level executives, and those advisors and professionals who service the corporation's financial needs. Shareholder advocates and union pension fund representatives have been on the forefront of criticizing excessive executive compensation and have advocated for measures such as say-on-pay referenda.[121] It serves both groups' interests to tamp down on

118. Troy A. Paredes, *Too Much Pay, Too Much Deference: Behavioral Corporate Finance, CEOs, and Corporate Governance*, 32 FLA. ST. U. L. REV. 673, 757–61 (2005). Paredes has argued for a devil's advocate or "chief naysayer" on corporate boards to advocate against groupthink and challenge the decision-making processes of boards and CEOs. *Id.* at 740–41 ("At bottom, considering the opposite results in a more balanced and presumably more accurate assessment of a course of conduct."). I am making a similar argument as to employee representation on boards: they would ask directors to consider the ramifications of their decisions on workers, which would change the decision-making process.

119. *But see* HANSMANN, *supra* note 110, at 89–91 (arguing that employee ownership fails because of the heterogeneity of employee interests).

120. *See supra* Part II.

121. *See* Stephen M. Bainbridge, *Dodd-Frank: Quack Federal Corporate Governance Round II*, 95 MINN. L. REV. 1779, 1808 (2011) (noting that Council of Institutional Investors, the AFL-CIO, and AFSCME all supported the say-on-pay provisions in the Dodd-Frank Act). *See also* Stewart J. Schwab & Randall S. Thomas, *Realigning Corporate Governance: Shareholder Activism by Labor Unions*, 96 MICH. L. REV. 1018, 1023 (1998) (claiming that "much union-shareholder activity represents an

managerial pay. The managerial power generated in the absence of strong shareholder oversight would be diminished in the presence of directors representing employees who are on the ground and have a greater interest in policing such matters. With employees voting for their own directors, powerful CEOs would have much more difficulty assembling an entire board of sycophants and cronies.[122] The culture of compensation would be changed, both at the top and the bottom.

In an earlier article, I advocated for a small yet tangible step in the direction of employee empowerment: a nonbinding employee vote on transformative corporate transactions.[123] This referendum would be held whenever shareholders had the right to vote to approve a merger, acquisition, or other large-scale corporate combination.[124] The company's employees would have the right to vote prior to the shareholder vote, not to bind the shareholders but rather to inform them.[125] The vote would be a signaling device, which could bridge the common interests of shareholders and employees.[126] But it would also provide the independent benefit of giving employees a voice—albeit a nonbinding one—in the future of their corporation.[127]

Workers have been fenced out of meaningful participation in corporate governance. Because of their participation in the ongoing business enterprise, they deserve to play a part in the management of the business. An important byproduct of this participation would be a change in the control over the allocation of compensation. By addressing the distribution of income in the first place, these reforms to the corporate structure would ameliorate the need to redistribute that income through a secondary process.

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alignment of shareholder and worker interests that attempts to prod management to increase the overall worth of the firm").

122. *See In re* Walt Disney Co. Derivative Litig., 907 A.2d 693, 762–63 (Del. Ch. 2005) (describing former Walt Disney CEO Michael Eisner's manipulation and control of Walt Disney's board of directors), *aff'd*, 906 A.2d 27 (Del. 2006). Eisner was famously described as "having enthroned himself as the omnipotent and infallible monarch of his personal Magic Kingdom." *Id.* at 763.

123. Matthew T. Bodie, *Workers, Information, and Corporate Combinations: The Case for Nonbinding Employee Referenda in Transformative Transactions*, 85 WASH. U. L. REV. 871, 878 (2007).

124. *Id.*

125. *Id.* at 878–79.

126. *Id.* at 898–913 (discussing how the referendum would benefit shareholders and employees).

127. The referendum could be required under state corporate law. *See id.* at 926 (acknowledging that the referendum is designed to work within the state law system and explaining its advantages). Alternatively, the referendum could be required through a shareholder-proposed bylaw. Matthew T. Bodie, *The Case for Employee Referenda on Transformative Transactions As Shareholder Proposals*, 87 WASH. U.L. REV. 897, 898 (2010).

IV. CONCLUSION

Proponents of greater income equality must contend with the claim that they are interfering with the natural order of the markets. But the legal structure of the corporation allows high-level executives and shareholders to siphon off the lion's share of the firm's economic surplus. If employees had rights to participate in the ongoing governance of the business, they would be empowered to claim a larger share of the enterprise's gains. This shift in distributional outcomes would go a long way in addressing the growing divergence in economic outcomes across our society. It is one more reason to change the corporate structure to incorporate employee participation in firm governance.