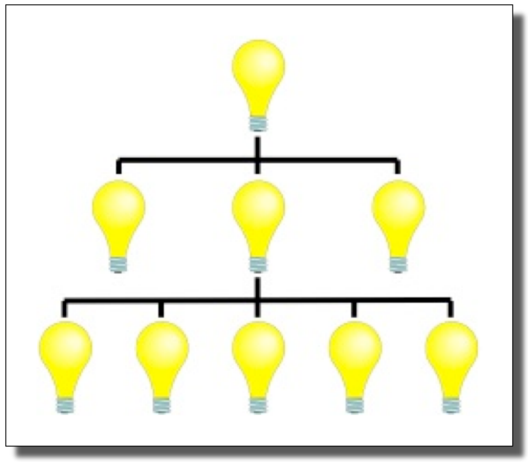

The New Model Corporation

Restoring ethics, decency, responsibility, and accountability to business

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By Karl Albrecht, PhD

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The Problem:

It's time to get the foxes out of the henhouses. Over the last three decades, more and more corporations in America have been hijacked by insiders – greedy executives and boards of directors who place their own financial and political interests above those of the shareholders, employees, and the society at large.

This progressive infection reached a crisis point with the mother of all financial disasters – the Wall Street "meltdown" of 2008.

An unprecedented number of Americans now view banks, and most other large corporations, as generally corrupt; controlled by dishonest, self-serving insiders; and guided by cynical values that benefit the few at the expense of the society at large.

Many social activists are energetically campaigning for corporate reform. The unprecedented "Occupy Wall Street" movement showed a surprising level of intensity – and contagion – even spreading to cities outside the US.

However, most of the activists seeking to change corporate behavior seem to be having difficulty articulating their demands. If they don't get beyond generalities like "honesty," "openness," "fairness," "social responsibility," and "sustainability," they may not accomplish very much. What's needed, I believe, is a concrete agenda – a set of demands for specific reforms that can be seen, touched, and verified.

Based on my experience – of three decades – in studying, working with, and consulting to corporations of many kinds, I've evolved a radical but readily do-able solution for eliminating insider corruption and many of the "corporate crimes" it makes inevitable. This solution goes to a key "leverage point" for inducing change: the *corporate charter*. Every registered corporation has one, and the executives who run the corporation are required by law to follow its provisions.

The Solution:

My proposed solution to the current corporate problem, supported by the discussion that follows, calls for a new, "standard model" corporate charter. Some executives will welcome and embrace this new model corporation (or "NMC") concept as a way to do business. Many, however, will probably resist until it is forced upon them by skillful social activists. The purpose of this paper is to provide activists with a tool for change.

The basic rules of the new model corporation's "standard charter" are:

1. *A clamp on executive compensation*: the ratio of the highest salary received by anyone in the corporation to the lowest salary may not exceed 50:1.
2. *A clamp on incentive compensation*: bonuses, commissions, and other performance-based compensation paid to anyone in the corporation may not exceed 50% of that person's salary.
3. *A limit to non-monetary compensation*: the board of directors and corporate officers may not approve unusually luxurious or expensive perquisites as a means of evading the first two restrictions.
4. *A limit on the size of the board*: the total number of board members may not exceed 15.
5. *Term limits for board members*: each board member will be limited to a five-year term. Expirations of board terms will be staggered evenly at one-year intervals. Board members may serve multiple, non-consecutive terms.
6. *Board independence*. Neither the chief executive officer, nor any member of the executive staff, may occupy a board position.
7. *Employee representation on the board:* at least one board position must be occupied by a full-time, non-managerial, non-union employee of the company.
8. *Union representation on the board*: if more than 50% of the company's workforce is unionized, at least one board position must be occupied by an employee who is a union member.
9. *Restrictions on political spending*: no company funds may be used for political contributions to any person or political party, or knowingly provided to any person or organization that would use them for that purpose.
10. *Three*-year phase-in: if the shareholders approve the new model charter, the board would be required to fully implement the changes within three years.

The Action:

This new model corporation charter could be an effective tool for swarm activism, because it can give activists a standard set of demands or changes, targeting individual corporations one by one.

As an example: an online activist movement might select one particular corporation for change. By organizing several thousand participants – perhaps even 10,000 or more – each of whom would be willing to buy one share of the corporation's stock, the leaders could build a shareholder bloc that could get the attention of the firm's management.

They would petition the board to place an initiative on the agenda of the firm's annual meeting, amending the charter to include the standard provisions listed above. If adopted by a majority of shareholders, those provisions would become permanently binding, and the officers of the corporation would be legally and civilly liable for violating them, under a legal doctrine known as *ultra vires*.

Pro’s and Con’s:

Many of those who now benefit from the rigged rules for corporate governance will almost certainly oppose any meaningful change to corporate charters, and will offer hyper-capitalist arguments about why the new model corporation will surely destroy America. Among the most common “push-backs” to be expected (and the “swat-backs” to counter them) are:

Push-back #1: “Talented executives are in great demand. High salaries, big bonuses, and expensive perks are necessary to attract capable leaders.”

Swat-back #1: There’s no shortage of leadership talent in this country. And why are there huge differences in executive pay from one firm to another, when their financial performance is about the same? Employees who are not executives get hired based on “market” rates, i.e. the prevailing salary in the competitive marketplace for a particular kind of job. There’s no reason to treat executives any differently. A half-million dollar salary will get you ten highly qualified candidates in a week. And “retention” is just another red herring; few executives leave cushy jobs once they’re there.

Push-back #2: “Executives deserve to be rewarded handsomely if their companies do well under their leadership. Performance-based compensation motivates them to work harder, smarter, and get better results.”

Swat-back #2: A raft of business-school studies have concluded that the correlation between executive pay and company performance is weak at most. And part of the correlation is accounted for by the fact that highly profitable companies just have more money for the insiders to raid. Lots of factors affect company performance, and many of them are beyond the control of the executives. B-school studies also consistently show that most mergers and acquisitions fail to increase overall shareholder value, although most of them enrich the executives of the merged firms. According to an article published by AFL-CIO and Harvard University, “In 1980, *Business Week* magazine estimated that the top executives of the largest U.S. companies made 42 times the pay of factory workers. In 2010, the gap between CEO pay at S&P 500 companies and the median U.S. worker had soared to 343 times.” Something’s out of control.

Push-back #3: “The shareholders automatically benefit when the executives are paid with stock options or bonuses based on profit. Incentive compensation aligns the interests of the executives with those of the shareholders. And, the shareholders can always vote the officers out if they don’t perform well.”

Swat-back #3: This is one of those convenient myths, similar to the idea in American politics: “If you don’t like what they’re doing, vote them out.” You’ll have to search long and hard to find a single instance where the shareholders of any large corporation have replaced the CEO or any of the board members. Insiders depend on the fact that “little” shareholders don’t have enough at stake to take action. The annual meeting and the vote for the slate of corporate officers is a ritual of royalty. A few disgruntled shareholders can show up and make noise, but most of them just sell their shares. Executives pay attention when wealthy mega-shareholders call, but they can safely ignore the small fry.

Push-back #4: “Executives work hard, they endure great stress, and they sacrifice their personal lives for the good of the firm. They deserve the executive luxuries – the grand office, the artwork in the lobby, the company jet, the Manhattan apartment, the chauffeured limousine, the expense account.”

Swat-back #4: Executives are servants and employees, not feudal barons. The corporation and its money are not theirs to do with as they please. They, and the members of the board, are *required by law* to serve as stewards of the interests of the owners of the company – the shareholders. Every dollar (or ten thousand dollars) spent on a painting in the CEO’s office comes out of the pockets of the shareholders. Few people would disagree with compensating executives well and providing them with comfortable accommodations. But too often there are no structural limits or controls on the freedom of insiders to reward themselves from the company treasury, which is the property of the shareholders.

Push-back #5: “The CEO is responsible for building an effective board, and should be free to recruit board members he feels will make the best contribution.”

Swat-back #5: The board and the executive team are supposed to have an “arm’s length” relationship. They’re not pals and playmates. The role of the board is to serve as an independent check on the policies, plans, and performance of the appointed leadership. In American corporate law, *their sole job* is to serve the interests of the shareholders; they advise and guide the CEO only in that capacity. Too often, the CEO “packs” the board with cronies who will agree with and rubber-stamp whatever he proposes. Limiting the size of the board and imposing term limits can prevent the development of a relationship that’s too cozy, and could lead to excessive compensation – possibly as payback for a high-paying board position. Admittedly, boards can sometimes develop an antagonistic relationship to the CEO, or split into internal factions, and that risk is inherent in having an independent board that’s not in the pocket of the CEO.

Push-back #6: “Employees or union members sitting on the board would cause more problems than they solve. They don’t have the knowledge, skills, or business experience to make decisions about the future of the company. Anyway, the executives understand the needs and concerns of the employees, and consider them in their decisions every day.”

Swat-back #6: Most executives seem to be fond of bragging about how they’ve hired the smartest and most capable people to work there. That’s supposed to be the favorite PR story: “Our people make us what we are.” Why, all of a sudden, when we’re looking for one person who can serve on the board, do the employees turn into a bunch of dimwits? This change, perhaps more than any other, would destroy the clubby sense of separation between the “nobility” – the executives - and the “peasant class” – the workers. And it’s understandable that it will be bitterly opposed by many, if not most, insider executives. Many European firms have had employee and union directors for decades, mostly with beneficial results.

Push-back #7: “The US Supreme Court has ruled that corporations have the same rights and freedoms under the Constitution as human beings. They are, for all practical purposes, persons. Giving money to political candidates, office-holders, and lobbying firms to influence laws and government policies is protected by the free-speech clause of the First Amendment."

Swat-back #7: That doesn't make it right, or morally defensible. The 2010 Court ruling, in my view, was one of the most egregious examples of political contamination of the judicial process in US history, and will likely be overturned in time. The lack of a reasonable set of curbs on corporate political spending – which is a modern phenomenon, mostly of the past three decades – has turned the US Congress into a national whorehouse. As philosopher Stanislaw J. Lee observed, "Every snowflake in an avalanche pleads not guilty." There are legitimate ways to be heard that don't involve buying votes and corrupting the political decision making process. Responsible shareholders should not condone such behavior on the part of those who are operating their firms for them, even if those insiders claim they're doing it for the ultimate good of the shareholders themselves. They aren't.

Final Thoughts:

Most of the founders of the American republic were very wary of the increasing concentration of capital and political power in ever larger corporations. Thomas Jefferson reportedly said,

> "I hope we shall crush in its birth the aristocracy of our monied corporations which dare already to challenge our government to a trial by strength and bid defiance to the laws of our country."

He singled out banks for special consideration:

> "I believe that banking institutions are more dangerous to our liberties than standing armies."

I am neither "for" nor "against" the corporation itself as a part of American life. Indeed, the modern corporation, as an economic entity, is one of the most effective mechanisms we have for getting big things done.

A corporation is an abstract entity, a legal and economic fiction. It does not have a heart, a soul, or a conscience. It cannot be "responsible." It makes less sense to talk in terms of "greedy corporations," and more sense to talk about "greedy corporate executives." And certainly not all of them are.

In human beings, some infections go away by themselves, cured by the self-correcting mechanisms of the body; and others become chronic, requiring treatment by a strong antibiotic. So it is with the business environment and the corporations in it.

I believe the current state of affairs will probably not correct itself. Strong medicine will be required. If governments and regulators can't do it, and if the business community can't or won't do it, then I believe there's a legitimate role for social activists. And I believe the new model corporation can be one tool for bringing corporations back to the service of society at large.

In the end, we'll have the corporations we deserve.

About the Author:

Dr. Karl Albrecht is a management consultant, executive coach, futurist, lecturer, and author of more than 20 books on professional achievement, organizational performance, and business strategy.

The Mensa society honored him with its lifetime achievement award, for significant contributions by a member to the understanding of intelligence.

Originally a physicist, and having served as a military intelligence officer and business executive, he now consults, lectures, and writes about whatever he thinks would be fun.

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