Finance and Labor:

Perspectives on Risk, Inequality, and Democracy [*]

2007

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ABSTRACT

Researchers have not paid adequate attention to financial development as a factor causing greater inequality and risk. Yet rather than there being a direct effect, the association between financial and labor markets is mediated by political coalitions at the national and corporate levels. Here we trace the historical interplay between financial markets, corporate governance, regulatory politics, and inequality in the United States. There is close examination of equity-market changes since 1980 and their impact on organized labor's efforts to re-regulate finance.

Institutionalism's insight was that markets are not homeostatic systems floating in timeless hyperspace but instead are embedded in the political and social institutions of a given age. Economic sociologists introduced the modern usage of embeddedness but tend to employ it narrowly as relational contracting. Here the term is treated as a broader construct in which economy and society (the subtitle of the journal *Industrial Relations*) are intertwined to form time- and place-specific institutions that constellate markets. This is an older conception emphasized by American institutionalism. It has resurfaced recently across the social sciences. [1]

Mid-century American institutionalism emphasized the ubiquity of conflict and the practical necessity of devising cooperative mechanisms to reduce it.[2] Institutionalists paid closest attention to labor markets, which left unchallenged the claim that other markets, especially financial markets, were purely competitive and unembedded.

A framework for understanding the interplay between markets and institutions is Polanyi's concept of the "double movement," which is based on two great organizing principles: markets, which claim laissez-faire and contract as their method, and institutions, which "check the action of the market relative to labor, land, and money." The framework is apt at this moment in history. The postwar balance between regulation and markets--a political balance--has tilted decisively in favor of the latter; the 19th century liberal ideology that Polanyi identified as "the myth of the self-regulating market" has resurfaced. This is not to say that history simply repeats itself; this *is* a different world. The cast of players is different; also, institutions created in the past act as constraints on present possibilities. [3]

The focus here is on the workings of the double movement in finance that are generated by the activities of owners, managers, workers, and other groups. Organized labor has applied to finance the same methods it uses to regulate employment: "higgling" and "legal enactment," as the Webbs called them. Higgling over finance includes the restructuring of corporate governance to give labor a voice in corporate rent and risk policies. Usually labor pursues higgling on its own, whereas legal enactment requires alliances beyond the firm. [4]

Finance is vital to all economies to provide capital for investment, credit to sustain households and firms, and mechanisms to diversify risk. The relationship between financial development and growth is ambiguous, however, with effects varying by a nation's GDP level and the type of financial development--credit markets, equity markets, or openness--under consideration. [5] Other aspects of finance are more controversial for several reasons. First, there is the tendency for periods of financial development to end in crises. Some claim that we are at the end of history--that financial crises in advanced economies are a thing of the past. This may be true or it may constitute irrational exuberance. Second, finance has an intimate relationship to the organization of corporations and property rights, which are contested issues. Third, financial development may exacerbate risk and inequality. [6]

The paper has five sections and primarily is about the United States: Part I describes financial trends--focusing on equity markets--since 1870. Part II analyzes the relation between financial markets and labor markets as mediated by regulation and corporate governance. Part III is an historical overview of labor's response to financialization from the 1870s through the 1970s. Parts IV and V discuss changes in ownership since 1980 and how they affect labor's efforts to re-regulate finance.

I. Financialization: Three Phases

In recent years financial markets have grown in size and significance. The phenomenon has caused what critics term the "financialization of daily life." Financialization encompasses a range of phenomena: the salience of stock markets; easy credit and high levels of household debt; growth of financial service industries; waves of mergers and acquisitions; and the establishment of shareholder primacy in corporate governance. [7]

We tend to think that we live in exceptional times and that financial globalization is an unprecedented phenomenon. Yet economic historians well know that there was an earlier period of globalization that rivaled today's. (see Table 1) From 1870 to 1913, trade growth averaged 3.8 percent annually such that the share of trade in GDP for the Western economies reached a high point in 1913 that was not exceeded until the 1970s (and for some countries not until the 1990s). [8] Trade and finance were positively related. In fact, foreign portfolio investments grew more rapidly than trade during the 1870-1913 period. The financial industry became more concentrated, bringing power and profits to The City, Wall Street, and Eastern banks, albeit with occasional panics. Ownership was in the hands of influential blockholders, most of whom were committed to a gold standard. Once adopted, governments committed themselves to parity over popularity. Yet instabilities arising from the gold standard caused political resistance that "hastened the spreading of … protectionist institutions, which were the more welcome the more burdensome fixed exchanges were." [9]

After World War I, trade and finance still were robust. Equity's importance--as measured by stock market capitalization relative to GDP, the percent of capital raised via equity, and the number of listed companies relative to population -- rose in the developed world. (see Table 1) Banks and trusts were drawn to the stock markets; the number of national banks with securities affiliates increased from 10 in 1922 to 114 in 1931. [10]

Stock holding became more diffuse. The initial reason was a tax-induced asset reallocation by the rich into municipal bonds. Wall Street brokers of the 1920s responded with campaigns to persuade less affluent individuals to purchase stock, either directly or through employee stock purchase plans. The 1920s were an era of irrational exuberance. A series of articles in the *Saturday Evening Post* in 1929 described the period as one when "buying [of stock] . . . was not based on reasoning but simply on the fact that prices had risen; a rise led the public to expect more and more returns. The articles warned that excessive anticipation of corporate growth and earnings would lead to depression and unemployment."[11]

Ownership dispersion permitted managers to transform themselves from hired hands to independent decisionmakers. This is not to say, however, that blockholding disappeared. Fifty five percent of the 200 largest U.S. companies were controlled by their owners in 1929, either through private ownership, majority ownership, minority control, or legal devices. Partly as a result, receipt of dividends--and overall stock ownership--were highly concentrated. The top 1 percent of the population in 1927 received 82 percent of dividends, a conservative estimate. For simplicity's sake, we will call this era from 1870 to 1929 "Phase I," although the pre-1913 era was somewhat different from the 1920s. [12]

With the onset of depression, Phase II began. Trade and equity markets plummeted. Wall Street was widely blamed for the Depression and held in low regard. A telling indicator of Wall Street's tainted reputation is the proportion of Harvard Business School graduates choosing the Street as their first position: It fell from 17 percent in 1928 to 1 percent in 1941.[13]

Trade recovered in the 1950s and 1960s as Bretton Woods took hold. However, capital controls and financial regulation constrained financialization. While stock market capitalizations rose between 1950 and 1970, other equity measures--stock market listings and the percentage of fixed capital financed with equity---rose in some countries but stayed flat or declined in others.

It is difficult to date the onset of Phase III because there are different turning points: the end of dollar convertibility and the collapse of Bretton Woods; the decline of postwar productivity growth; the onset of deregulation; and the return of finance. Global equity assets rose from $3 trillion in 1980 to $44 trillion in 2005; equities drove nearly half the rise in global financial assets during those years. Around the world, stock market capitalizations relative to GDP sharply increased, reaching or exceeding levels not attained since previous highs in 1913 and 1929. Savvy MBAs again are a telling indicator: the share of Harvard Business School graduates headed for Wall Street, which had risen modestly from 1.3 percent in 1941 to 10 percent in 1976 (still below 1928 levels), jumped to 30 percent in 1986. [14]

An important change in Phase III was the new prominence of institutional investors, a heterogeneous group including pension funds, mutual funds, trust funds, and insurance companies. Institutional composition varies across nations, with pension funds more important in the US and

UK than other countries. U.S. institutional investors in 1960 owned 12 percent of equities; by 1990 they owned 45 percent and their share rose to 61 percent in 2005. Institutions today own 68 percent of the 1000 largest U.S. corporations. [15]

Institutional owners are different than blockholders. Institutions are diversified; they rarely own more than one percent of a company. Despite their reputation as long-term investors, institutions have myopic tendencies because of the short tenures of in-house fund managers and recent changes in portfolio composition. To notch up returns on indexed assets and diversify beyond them, institutions are putting more money into "alpha"-- riskier investments, some of them leveraged, with anticipated above-average returns. These include private equity, hedge funds, real estate, commodities and micro-cap stocks. Some public pension funds have up to 50 percent of their assets in these alternative investments and, on average, only 30 percent of assets presently are indexed. Institutions actively trade their alpha assets or hold them for finite durations. CalPERS, the giant California public pension fund, aims for an equity portfolio containing 40 percent in alpha. [16]

Economists Raghuram Rajan and Luigi Zingales have brought deserved attention to the U-shape of financial development over the past century. They dub the phenomenon "the great reversals": a flourishing of financial development in Phase I, contraction in Phase II, followed by renewed financial expansion in Phase III. One need not accept Rajan and Zingales' normative interpretations to appreciate the value of their historical and comparative research.

II. Resources, Risk, and Governance

In recent years, economics has produced another comparative and historical research project: empirical studies of income and wealth distribution, especially shares held by top brackets (typically one percent or smaller). Top shares are of interest not only because of their association with financial development but also because they are associated with aggregate income inequality. Top-share recipients also affect social inequality through their ability to avoid the public sector by purchasing private services. Over the past century, one can identify three phases in top income shares. (Table 2) In the Anglo-Saxon world, top shares were relatively large in Phase I, underwent a contraction in Phase II--the great leveling--and remained stable until around 1980. At this point top shares began to steadily expand, so that by 2004 they had attained levels not seen since the 1920s. Top-share trends in continental Europe and Japan parallel the Anglo-Saxon world until Phase III, when something prevented a snap-back to earlier inequality levels. [17]

As for wealth, it too became concentrated during Phase I. The top one percent in 1912 is estimated to have held about 56 percent of U.S. wealth, a much larger share than in 1870. The rich invested their assets through financial intermediaries such as trust banks that grew rapidly after the turn of the century. [18] Over the course of Phase II, however, top wealth shares shrank and then stabilized. (see Table 2) Since the 1970s, top wealth shares have declined modestly, unlike income shares, although wealth holdings remain concentrated. [19]

The evidence showing a finance-inequality link derives from data on advanced countries, which may limit its generality. Also, although it's possible to infer causality running from finance to inequality, the claim requires several caveats. As with other bivariate relationships, one can think of explanations as to why causality might run in the opposite direction or in which the relationship is mediated by other factors. Then there is the null hypothesis that causality is absent. And even if there is a causal relationship, there are other variables than finance that affect inequality, everything from technological change to tax rules to trade. [20]

Note that top shares derive not only from rentier sources but also from business income and from salaries. Whereas capital income was the primary source of top incomes in Anglo-Saxon nations during Phase I, salary income replaced capital at the top in Phase III. In 1926, the top 0.01 percent income bracket received 61 percent of its income from capital, 20 percent from business income, and 19 percent from salaries. In 1999, only 15 percent came from capital, 32 percent from business income, and 53 percent from salaries. [21]

The growing importance of salaries does not mean that the link between finance and top income shares has been severed. The previous figures exclude capital gains, an important source of capital income. Also, top salaries in the U.S. during Phase III were driven, in part, by changes in shareholder preferences in favor of outsider CEOs, which boosted CEO salaries, and in favor of stock options, which were viewed as a tool for aligning CEOs with shareholders. In 1980, fewer than a third of CEOs were granted stock options; by 2000, options had become universal and accounted for the lion's share of executive compensation. Option profits are taxed as income, but there are ways to have them treated as capital gains. One also must also consider salaries and business income earned by collateral beneficiaries of financial development: investment bankers; some commercial bankers; hedge, venture, and private-equity fund managers; attorneys specializing in financial transactions; and more. It is estimated that the share of CEOs and some, but not all, collaterals as a percentage of individuals in the very top brackets is as high as 46 percent and might be higher. From 1972 to 2001, the top .01 percent saw their real earnings rise by 181 percent, whereas real earnings for the median worker fell by 0.4 percent. Thus income shares for the lower quintiles are affected not only by the relative share going to capital but also by changes in the composition of labor's own share related to financial development and tax changes associated with it. [22]

Another labor-market outcome tied to finance is the allocation of risk between owners and corporate stakeholders such as creditors, suppliers, and employees. Some U.S. employers offer policies that insure employees against risk, such as fringe benefits, wage smoothing, and employment security. A firm's financial structure will influence its decisions in this area. For example, debt interferes with cyclical risk sharing. Ownership also matters. Because blockholders are relatively undiversified, their risk preferences will be closer to those of similarly undiversified employees (whose main asset is their illiquid firm-specific human capital) than for more diversified owners.

The relationship between financial markets and labor markets (i.e., risk and inequality) is mediated by politics, which occurs at the national level in disputes over redistribution and regulation, and at the corporate level, where the key players--workers, managers, and owners--press singly or in coalition for alternative forms of governance. Following Gourevitch and Shinn, there are three basic corporate coalitions, each with a winner and loser are: i) owners + managers vs. workers ii) managers + workers vs. owners and iii) owners + workers vs. managers. In the U.S., the first coalition--what Gourevitch and Shinn label "class conflict"-- was dominant during Phases I and III, with workers usually the losers. The second coalition--what I term producerism--was prevalent during Phase II, when managers and workers eschewed class conflict in favor of cooperation to raise productivity; owners got the short end of the stick. The third coalition--institutional capitalism--emerged during Phase III as pension funds pressed managers to focus on share price. The move had unintended consequences and caused managers to fracture into owner-exploiting and owner-friendly groups (and a minority that still espouses producerism). [23]

Corporate governance is the private rules by which owners, managers, and workers influence a firm's strategic decisions, including the distribution of rents and risk. The data in Table 3 show the allocation of value-added under different governance regimes. Labor's share is relatively low in the Anglo-Saxon countries, where governance coalitions changed after 1980 to instantiate shareholder primacy and hostile takeovers. Conversely, labor's share is higher under the producerist systems found on the continent and in Japan. [24]

This is only part of the story behind the divergent post-1980 outcomes shown in Table 2. Another has to do with electoral alliances that press for regulatory change in financial markets and in taxation. These alliances are different--and broader--than those at the corporate level. As we will see, laborist alliances are easier to create in some polities than others. In all countries, however, labor needs middle class support to press for redistributive fiscal policies and for financial regulation. Political factors are difficult to quantify yet that is no reason to give them short shrift in accounting for inequality.

III. Labor's Response to Finance: Phase I and II

Class Conflict: Space precludes a lengthy discussion of labor's response to financial development since the late 19th century; only a broad overview of events in the United States is presented. [25] From the1870s through the 1890s, labor organizations were active in popular movements opposing the tight credit and deflationary tendencies associated with the gold standard, including Greenbackers, radical Republicans, free silverites, the Knights of Labor, and the People's Party. Labor's initial effort to promote the greenback--the "people's currency"--came through the National Labor Union, the country's first amalgamation of trade unions. In these years, craft workers held to a republican ideology in which direct producers, including small owners, were seen as the source of value while those employed in the money economy were viewed as speculative parasites. As earlier in the 19th century, citizens still embraced the doctrine that banks as well as corporations were subject to regulation because they were public or quasi-public entities whose powers derived from the state. Labor had more than a vague "distrust of concentrations of financial power" as legal scholar Mark Roe says; it saw its interests as antithetical to those of finance. According to historian David Montgomery, "the labor reformers were attempting to impart to the industrial order some values other than purely commercial ones, to impose a moral order on the market economy." Labor opposed monetary stringency, condemned speculation that led to panics and depressions, and loathed the inequities associated with Gilded Age finance. [26]

But the critics of finance--workers, farmers, and small business--could not sustain a unified movement nor muster the resources to win elections. Bryan's 1896 anti-gold campaign was run on a shoestring; Rockefeller and J.P. Morgan each contributed vast sums to the opposition, as did other business leaders. The Republican effort in 1896 was unprecedented in American politics. Millions of pamphlets were printed; hundreds of paid speakers went out into the field. When the Gold Standard Act was passed in 1900, approximately one-third of the Senate's members were millionaires (in 1900 dollars), not a few of them bankers. The Knights of Labor and the Bryan campaign of 1896 were valiant efforts but the Knights' collapse and Bryan's defeat marked the end of organized labor's financial activism. [27]

Labor's sense of moral order faced opposition not only in the electoral realm but in the courts. As against claims that corporations were rooted in the state, the judiciary asserted that they were islands of private property--like land--and had nothing to do with the state or anyone other than owners. "Outside" interference with the corporation was a taking whose harm could be measured by changes in the firm's market value. Eventually the theory developed that corporate power derived from shareholders--the principals--which allowed courts to “disaggregate the corporation into freely contracting individuals.” [28]

During the next three decades, the political baton passed from agrarians and labor to middle-class reformers. Richard T. Ely, Thorstein Veblen, and Louis D. Brandeis were among the Progressive intellectuals who railed against financial and industrial monopoly. Brandeis criticized investment banking --“the money trust”--in a series of essays published as *Other People’s Money and How the Bankers Use It.* His ideas overlapped with another strand in Progressive thought: an enthusiasm for social engineering. In a contemporaneous book, *Business - A Profession*, Brandeis predicted that corporations would become more efficient as a new class of technocratic managers separated itself from owners, eschewed class conflict, and adopted practices such as systematic management and employee participation. [29]

Progressive jurists like Brandeis developed a more realistic conception of corporations that challenged conservative views. Property rights were held to be relative, not absolute; this required a balancing test to weigh claims made by shareholders against those of other claimants. Against the abstraction of a self-regulating market, legal realists offered the view that the market “was a social creation, a creature of law, government, and prevailing conceptions of legitimate exchange,” an instance of embeddedness. The realists drew on the ideas of institutional economists, including those close to the labor movement such as John R. Commons. [30]

Yet organized labor mostly was absent from financial debates of the day, whether the 1912 Pujo investigations or the backroom dealing that led to the Federal Reserve Act. One reason is that after the 1908 *Danbury Hatters* case, the AFL’s political efforts were singled-minded: to undo the judiciary’s repressive interpretations of anti-trust law. Another reason is that organized labor, unlike farmers or small business, had other options than electoral politics to regulate finance. Lloyd Ulman has well described the process by which unions boosted their bargaining power by forming national organization to cope with the extension and interpenetration of markets. In markets were labor was powerful, collective bargaining challenged the corporate governance *status* quo. On the other hand, organized labor was but a fraction of the electorate and politically weak at the national level. Socialists and the AFL-CIO did not form alliances as in Britain, nor did labor ally itself with farmers and the middle class. There were exceptions of course, chiefly at the local and state levels. The urban middle class cooperated with labor in “sewer socialist” cities. In some Midwestern states in the 1920s, farmers and labor formed fusion parties or followed politicians like “Fighting Bob” LaFollette, Jr., who opposed “Wall Street dictatorship” and demanded financial reforms such as bank nationalization. [31]

Lacking allies in a majoritarian electoral system limited labor's ability to achieve financial regulation and social insurance. However, continental Europe's proportional voting provided labor a voice in national politics, which facilitated the creation of a social compact--directly or through preemption-- that mitigated risk and redistributed income via social insurance: for accidents, unemployment, sickness, and old-age indigence. The extensiveness of social insurance enacted before 1913 is positively related to a nation's level of openness in 1913. The United States, with lower levels of working-class power (and openness), remained a social insurance laggard until the New Deal. [32]

Only at the midnight hour--in 1929--did the AFL weigh in on finance. Five months before the crash, its official magazine warned that "growth of speculative credit shall not be permitted to undermine business stability" and that inaction would have deleterious effects on wage-earners When tax figures for 1929 were released, the AFL observed that the bulk of income gains since 1927 had gone to the upper brackets. It blamed three factors: the concentration of stock ownership amongst the rich; stock speculation that benefited the rich; and an uneven distribution of value-added at the corporate level due to excessively high dividends.[33] But these words came late in the game, in fact, after the game was over. [34]

The tremor that was the Great Depression affected everyone from farmers to workers to the middle class. The coalition that failed in 1896 now swept Roosevelt into office. With the New Deal came a myriad of financial investigations and regulations. Roe asserts that labor played at most a minor role in passage of these regulations. But this neglects the larger political canvass against which labor politics were played out. Before the emergence of industrial unionism, the largest popular movements of the 1930s were led by Senator Huey Long ("share the wealth") and by Father Charles Coughlin. In a reprise of 1896, both men attacked the money interests and called for a re-monetization of silver to counteract deflation. [35] Long blasted the nation's unequal distribution of wealth--"concentrated in the hands of a few people"--and tied it to the "God of Greed [worshipped] by Rockefeller, Morgan, and their crowd." Coughlin, too, believed that "bankers and financiers are the chief obstacles to constructive change." The heated rhetoric of Coughlin's populism drew millions of adherents from the same groups that had elected Roosevelt. Coughlin had close ties to the Detroit labor movement, especially to the Homer Martin faction in the UAW. Other labor leaders, such as attorney Frank Walsh, also became Coughlinites. Coughlin was a skilled orator, who could link workers' problems to abstruse financial forces: "Your actual boss, Mr. Laboring Man, is not too much to blame. If you must strike, strike in an intelligent manner not by laying down your tools but by raising your voices against a financial system that keeps you today and will keep you tomorrow in breadless bondage." Coming from

Louisiana, Long had less to do with the labor movement, although his magazine reprinted speeches by the AFL's William Green. [36]

In the Senate, Long threw sand in the wheels of the Glass-Steagall deliberations of 1933, filibustering for three weeks on the Senate floor until the bill included limits on branch banking. Coughlin testified in Congress about the "plutocrats" and demanded a return to silver and nationalization of the Federal Reserve, which led Congressman Wright Patman to sponsor a bill along those lines. Not only demagogues attacked finance. Fiorello La Guardia proposed that dividends be taxed as regular income while the AFL asked that the nation erect safeguards "against speculation that destroys wealth and business structure." [37]

Congress and the Roosevelt administration spun a web of financial regulation: the Securities Act and suspension of gold convertibility in 1933, the Securities Exchange and Banking Acts of 1934, and the Investment Company Act of 1940. One might argue that the new laws were designed by an autonomous "brain trust," although there is little doubt that popular protest--including by labor--bolstered efforts to contain finance. Similar events occurred in Europe, creating what John Ruggie calls "a common thread of social reaction against market rationality." [38] It's difficult to gauge how financial regulation affected the distribution of income and wealth. But limits on Wall Street trading and financial centralization surely curbed financial profits and speculative opportunities. Not for nothing did MBAs avoid Wall Street.

Producerism: A major innovation of the era--one that did not directly involve organized labor --was the Bretton Woods agreement. Nevertheless, union leaders like Sidney Hillman and Walter Reuther publicly endorsed the agreement, which resonated with their producerist beliefs in economic planning. They also saw it a remedy for isolationist and laissez-faire tendencies on the right and for Communist influence on the left. The CIO campaigned to win public support for Bretton Woods, tying the agreement to other forms of economic stabilization such as the Full Employment Act, an instance of Ruggie's "embedded liberalism." Hillman viewed Bretton Woods as a model for international labor coordination. He regretted labor's absence from the Bretton Woods negotiations and attributed this to the lack of a "powerful, united" international labor organization. This led him to create the World Federation of Trade Unions, a global anti-Communist alliance. [39]

The labor movement scored a trifecta of high bargaining, organizing, and political power during the 1940s and 1950s. Its political power derived, in part, from widely shared experiences of depression and war, which narrowed the gap between laborers and the middle class. The depression also made the middle class wary of business and more willing to ally itself with labor as a "countervailing force." Union leaders took advantage of the new environment by promoting legislation that simultaneously reduced risk levels and inequality. One effort was to secure programs as the G.I. bill, minimum wages, and more extensive (and expensive) provision of Social Security. Labor also became familiar with the tax code's arcana: during the war, when it opposed a sales tax in favor of higher taxes on corporations and the wealthy, and after the war, when it demanded progressive tax cuts and the closing of loopholes benefiting the rich. [40]

Organized labor also sought to change governance by giving workers a voice in the allocation of corporate rents and risk. Slichter dated the origins of a shift in labor's share to the 1939-1950 period, when union wage changes became relatively synchronized and unrelated to sectoral variations in productivity. The GM-UAW agreements of 1948 and 1950—the Treaties of Detroit that were proffered by management--sought a cooperative solution to labor militance by basing wages on anticipated productivity and actual inflation. But the treaties had the effect of capping labor's share, an outcome that labor resisted by pressing for wage gains outside the formula when new or reopened contracts were signed. Labor's share continued to rise until the 1970s, driven by pay gains in the union sector. Hence Phase II witnessed the persistence of class conflict alongside cooperative producerism. [41]

Changes in ownership facilitated labor's gains. The basic trend in postwar shareholding was towards dispersion--in 1965 individuals owned 84 percent of U.S. equities--although there is disagreement whether this figure understates the persistence of blockholding. [42] Writing in 1941, legal scholar E. Merrick Dodd thought that the United States had "reached a condition in which the individual interest of the shareholder is definitely made subservient to the will of a controlling group of managers." Fifteen years later, a team of economists found American executives professing producerist principles akin to contemporary European and Japanese models. Executives, it said, believe

> "that they have four broad responsibilities: to consumers, to employees, to stockholders, and to the general public . . . In any case, each group is on an equal footing; the function of management is to secure justice for all and unconditional maxima for none. Stockholders have no special priority; they are entitled to a fair return on their investment but profits above a "fair" level are an economic sin."

The concept of management rights in the industrial relations literature refers to decisions that management reserves for itself free of union influence. In the 1950s, however, management rights acquired an additional meaning. It was "designed to defend for management a sphere of unhampered discretion and authority which is not merely derivative from the property rights of owners." Discretion included decisions regarding the distribution of rents, including retained earnings. [43]

Jurists and economic theorists validated the new conception of governance. An early formulation was offered by Berle and Means, who looked to management rather than the state as a neutral arbiter who would balance competing distributive claims. The idea was consistent with the legal doctrine that managers were fiduciaries for the corporation and should deal with the stockholder "at arm's length as [they] would any outsider." It also was consistent with the Brandeisian claim that large corporations were being run by technocratic experts mindful of their responsibilities to multiple constituencies, labor as well as owners. [44]

Under the new balance of power, dispersed owners had fewer options to assert their claims. Annual dividend yields, for example, showed a downward trend from the late 1930s through the 1960s. Yet most executives did not use their new-found autonomy to plunder. A database of CEOs for the period 1936-2003 finds a decline in real compensation for top executives in the early decades and continued pay sluggishness until the 1970s. In many large companies, rents either were shared with employees or plowed back into retained earnings that became the dominant source of corporate financing. The preference for retained earnings in some circumstances caused "slack" and inefficient spending on corporate empires, as agency theorists later alleged. But in other circumstances, slack facilitated innovation and provided a buffer against short-term pressure from financial markets. [45]

That managers now were more inclined to share rents stemmed not only from labor's militancy and efforts to curb it but from a producerist ethos that spread beyond the union sector and also beyond the United States. The proclivity to share could be found in large nonunion companies employing white-collar professionals who disdained—and would never join--unions. What motivated companies to greater largesse? In one nonunion company, executives believed that "the key to effective employee relations is the presence of trust and confidence between managements and employees. Such a climate is considered desirable for its own sake, and also because it fosters the efficient and effective long-run implementation of corporate strategy." That is, another reason for rent sharing was management's view of value creation as being based on cooperation, a long-term perspective that required restraints on myopic owners. The notion later was rationalized in the literature on the productivity consequences of practices based on long-term employment and on trust: firm-specific training, Lazearian wage profiles, and gift exchanges.[46]

A rising tide did not necessarily lift all boats; labor's share was unevenly distributed. Union workers did especially well, as evidenced by a widening union-nonunion wage gap from 1950 to 1980, when it peaked at 30 percent. The union sector's payroll weight—its share of labor's share--was much larger than its employment weight. In those parts of the nonunion sector where employee turnover was high and firm size modest, wage gains were smaller and less synchronized with union pay trends. Here management lacked an appreciation of “the relation between morale and the efficiency of labor,” as Slichter put it. There were union-to-nonunion spillovers via the threat effect. But evidence of spillovers during Phase II is ambiguous: it occurred in some periods and industries but not others.

Arguably the most important innovation in postwar collective bargaining was the 1955 Ford-UAW agreement, in which the union demanded and won a guaranteed annual wage. This took the form of supplemental unemployment benefits (SUBs) paid by the company and coordinated with unemployment insurance. Not only did this shift risk from owners to workers, it represented an imprimatur on what had become a quasi-permanent relationship. Yet SUBs never spread to the nonunion sector. In fact, they were limited to a few heavily unionized industries--the elite within the working-class elite. In other words, norms established in the union sector were circumscribed. [47]

The SUB agreements illustrate the peculiar structure of social insurance in the United States. It was a two-tier affair in which private benefits sat on top of a relatively sparse public base. Corporate pensions supplemented, and were coordinated with, Social Security; employer medical insurance covered a hole in the safety net. Unions were partly responsible for the two-tier system and their members benefited from it more than for nonunion workers. Unionized workers also were protected from risk through countercyclical labor hoarding and wage smoothing, again less prevalent in the secondary sector. While one might criticize unions for tolerating inequality, they must be credited for effecting a substantial transfer of risks and rents. [48]

During the last decades of Phase II, however, finance staged a comeback. The conglomeration wave of the 1960s and 1970s was one indicator. Conglomerates were hodgepodge organizations built of unrelated businesses, with little more than financial logic and antitrust avoidance holding them together. Unions had been mostly silent about finance during the prosperous 1960s, except to periodically deny that their wage gains were responsible for gold outflows. But organized labor raised complaints against conglomerates because of concerns that their acquisitions were causing layoffs and the transfer of jobs to nonunion regions. [49] A key feature of conglomeration was its elevation of finance’s corporate status. The percentage of CEOs coming out of finance jumped in the 1960s. CFOs brought a financial mindset to management. Decisions now were made by the numbers; CFOs came to dominate the stalwarts of producerism--managers from line-related functions like operations and personnel. Line managers appreciated non-quantitative intangibles such as inimitable resources and employee morale.

CFOs, however, narrowly viewed their objective as the maximization of share price. Hence conglomerates left a legacy of financial hegemony in the corporate order. [50]

In the international arena, British and American policymakers loosened capital controls in the 1960s and began to repudiate Bretton Woods, thereby placing their own domestic interests over international cooperation. The moves came were partly the result of political pressure from financial interests seeking to revive their industry and secure overseas markets for it. As the U.K. and the U.S. deregulated finance, other nations felt compelled to follow. The financial industry pressed more vigorously for repeal of Glass-Steagall and reform of regulatory institutions like the SEC. [51]

Tectonic shifts in politics and ideas occurred during the 1970s: the disintegration of the Keynesian consensus and the New Deal coalition, and the return of an ethos of self-regulating markets. Deregulation--whether in financial, labor, or products markets--came to be seen as a boon to efficiency, with little thought now given to equity. Labor's declining strength facilitated the shift, as evidenced by the ability of a Democratic president, Jimmy Carter, to deregulate unionized strongholds such as transportation and telecommunications. For labor, the bottom fell out in the 1980s: a wave of plant closures and downsizings due to imports and corporate restructuring. Restructuring was promoted by the Republican ascent: the 1981 tax act favored debt, the Justice Department became less stringent in its pursuit of antitrust regulation, and Reagan's actions in the PATCO dispute sanctioned employer anti-unionism. Labor's trifecta transmogrified into a triple defeat. The middle of the labor market was knocked out as the union sector contracted and employment shifted to relatively low-wage jobs. Pay norms in the union sector turned from "pushiness" to passivity. [52]

IV. The Financial Revolution

Cross-border capital flows—their size and ubiquity—rose exponentially during Phase III, as did the equity share of those flows. Relatively open financial markets empowered owners to promote deregulation at home and abroad. But the response to financialization was not the same in the neoliberal and coordinated economies. In continental Europe and Japan, where labor retained a political voice and producerism persisted, liberalization was more akin to "re-regulation" that preserved finance's role as servant, not master, to industry. Europe and to a greater extent Japan (where corporations are not seen as shareholder property) still regard hostile takeovers as controversial and their executive pay lags U.S. levels Going into the 1980s, the United States had some producerist coalitions. But the coalitions grew weaker as unions unraveled and shareholder primacy held out to managers the prospect of becoming rich.. [53]

As during Phase I, Anglo-American economists and jurists formulated theories to guard corporations against non-shareholder intrusion. The crowning achievement of the new law and economics movement was agency theory, which revived earlier ideas about the privileged role of shareholders, this time as residual claimants who pressure agents to maximize shareholder value. Agency theory provided a disciplinary rationale for hostile takeovers and for the re-valorization of share price as a performance criterion. The old distinction between the real economy and the financial economy disappeared. Financial markets, said agency theory, were the linchpin of economic growth. Even the CEA opined in 1985 that takeovers "improve efficiency, transfer scarce resources to higher valued uses, and stimulate effective corporate management." [54]

The justification of shareholder primacy not only was theoretical but empirical. Studies found that weaker shareholder control is associated with lower levels of downsizing and with higher levels of executive and worker compensation. The inference is that these outcomes occur because ineffectually-monitored managers line their pockets and pay excessive rents to employees so as to enjoy a conflict-free quiet life. [55]

But when executives and shareholders seek opposite policies, is it evidence of manager or owner shortcomings? The answer is: probably both. Recent events provide ample evidence of CEOs exploiting owners, often with the acquiescence of boards over whom the CEO has power. But there are other managers--typically insiders committed to the enterprise as a going concern--who understand better than myopic owners how to create value. Evidence supports this interpretation. Downsizing does not boost productivity although it raises shareholder returns, especially when downsizing is aggressive (i.e. during periods when the firm is profitable). As for rent sharing, it is associated with higher productivity, as would be expected from efficiency wages and firm-specific training. When managers oppose takeovers, it may be because they believe that takeovers will not improve efficiency. In fact, the average takeover is not associated with pre-existing performance defects nor with subsequent profitability gains, even nine years after the event. Instead, the average takeover is driven by arbitrage of price imperfections and by tax considerations. [56]

Of course, there are competitive limits to rent sharing. Rent sharing as union-sector pay gains exceeded the amount warranted by U.S. productivity levels in the 1970s. There are, however, limits in the opposite direction, as when firms stint on internal spending to satisfy owner demands, which causes indequate investment in firm-specific assets, including innovation. Financial analysts are concerned that high payouts are depleting internally-generated investment funds. Capital spending increasingly is financed by external credit, which makes firms vulnerable to credit market volatility that can depress investment and productivity. [57]

Thus a different interpretation of Phase III is that restructuring and shareholder primacy not only are about creating value but extracting it. As shareholder payouts have risen since 1980, labor's share of GDP has fallen and is smaller now than at any time since the mid-1960s. During the same period the allocation of labor's share has tilted to the top brackets. True, a portion of shareholder payouts find their way back to households via retirement plans. But even taking the plans into account, the fact is that, among households, the wealthiest 10 percent owns about 80 percent of equities. [58]

As investors press for larger returns, employees faced greater risk. Pension plans have shifted from defined benefit to defined contribution; employer-provided health insurance is disappearing; and wage and employment volatility have risen considerably. However, what is telling is that these volatility effects are greater in public firms; private firms exhibit a *decline* in employment volatility, suggesting an association with financial markets. There also is an association between shareholder power and reduced levels of employee tenure. [59]

Not only conventional politics have driven the return of shareholder primacy. Another factor are social influence processes orchestrated by what Cass Sunstein calls "norm entrepreneurs"--econocrats, think tankers, politicians, and business gurus. They argued in the 1980s and 1990s that U.S companies needed the spur of shareholder control to meet globalization's challenges. The argument was not always disingenuous but some of those making it cloaked distributive goals in efficiency garb. It carried weight because it offered a simple diagnosis and solution to persistent economic stagnation. Subsequently it appeared to be validated as the adoption of shareholder primacy was followed by an improvement in economic performance. That the former induced the latter was a causal stretch but one that was repeatedly invoked to justify events at home and to spur governance reform abroad. With labor weak and financial interests gripping the Democratic Party, there were few challenges to the new financial order or to claims made by the norm entrepreneurs. This is not to say that financial interests had a veto on policymaking, which is semi-autonomous and sensitive to non-business interests. But in the rarified realm of finance, few other concerns were voiced, until recently. [60]

V. Double Movement Redux

Although labor's bargaining power dwindled after 1980, it gradually awoke to the fact that it had an underutilized sword: pension funds. The development of labor's pension activism is a complicated story, involving the interplay between financial markets, state and local pension plans for government employees (SLPFs), and union-affiliated pension plans (UAPFs). SLPFs changed in the 1980s as they were freed of limits on their equity allocations, which permitted them to invest more in equities to accommodate funding gaps and future demographic shifts. In search of higher returns, they became leaders of the shareholder rights movement. UAPFs are pension funds for a union's own employees and Taft-Hartley multiemployer funds that are jointly administered by unions and employers. The UAPFs were slower to activism than the SLPFs and, when it emerged, it took a different, more laborist, approach. [61]

The largest and most active SLPF was CalPERS, which today has assets of almost $250 billion. In the 1980s, CalPERS became the first institutional investor to apply pressure on corporations to be more shareholder-friendly. To foster shareholder primacy it demanded greater board independence, lower takeover barriers, larger payouts to shareholders, and tighter links between CEO pay and firm performance. It relied on a variety of tactics: proxy resolutions, public targeting of underperformers, and alliances with other owners, including corporate raiders. In 1985 CalPERS formed the Council of Institutional Investors (CII) to bolster its clout. The CII's initial members were other SLPFs. It came to include union-affiliated and corporate pension plans, although the UAPFs opposed the corporations' entry and, later on, their leadership role in the CII. After the mid-1990s CalPERS and some other large funds shifted to less visible methods of influence, such as private communications and relational investing.

SLPFs professed to be interested in long-term performance but disgruntled corporate executives said that the funds abandoned their long-term philosophy whenever raiders offered sufficiently juicy premiums for their shares. The SLPFs supplied a good deal of the capital to finance takeovers in the 1980s, which they justified in the same way as the raiders: that they were performing a public service by prodding underperforming companies to maximize shareholder returns. SLPF activism is associated with higher rates of layoff and asset divestiture than in untargeted companies. CalPERS officially was on record that it preferred companies to improve shareholder returns without layoffs. But it was not averse to downsizing. Patricia Macht, a CalPERS official, told the *New York Times* in 1996, "There are companies that are fat, that have not taken a good look at the number of employees they need." [62]

Although many of those enrolled in SLPFs are public-sector union members, workers' influence on SLPF policies is limited because ultimate control of an SLPF resides with the government entities that created it. SLPFs emphatically are not coalitions of workers and shareholders, as claimed by Gourevitch and Shinn. Public-sector employees have limited influence over SLPF policies, and the "workers" covered by SLPFs are not employed by the companies in which their pension funds invest. Private-sector union leaders will state off the record that SLPFs can pursue shareholder primacy because doing so will never hurt their members. (SLPF trustees fire back that UAPFs ignore their fiduciary duties by favoring workers over retirees.) [63]

UAPFs, with combined portfolios worth $400 billion, have less than 10 percent of the SLPFs' assets. But their influence belies their size. UAPFs place greater emphasis than SLPFs on a corporation's employment responsibilities and on the negative aspects of financialization. For example, in 1989 the AFL-CIO opposed having pension funds invest in junk bonds whereas the CII supported it. Although UAPFs and SLPFs both criticize excessive executive pay, the SLPFs focus on damage to owners whereas UAPFs also emphasize harm done to employees. Yet there is overlap between the two types of funds and they work closely on some issues. Also, UAPFs include in-house funds of unions representing public employees, such as AFSCME and SEIU, while SLPFs from liberal regions stake out positions closer to the UAPFs'. [64]

UAPFs in the 1980s were sleepy organizations that failed even to vote their proxies. Some UAPFs, however, began using their pension assets in support of short-term union objectives in organizing, negotiations, strikes, and job creation. The architect of a distinctive UAPF approach was William B. (Bill) Patterson, then field director for ACTWU. During the J.P. Stevens organizing drive, Patterson helped to develop the corporate campaign, whereby unions pressure a company's major shareholders and ask them to restrain anti-union managers. It was a logical progression from pressuring managers via owners to deploying labor's own pension assets for similar ends. Managements strenuously opposed labor's new activism and asked the SEC to ban union-sponsored proxy resolutions during labor disputes. SLPFs did not adopt the UAPF approach, although some refused to invest in firms that benefited from privatization, such as bus companies. [65]

In the early 1990s, Patterson and others were searching for a model of activism that would raise worker concerns while attracting allies from the investing community. As he said in 1993, "It's important to represent workers as stockholders as well as workplace advocates … so employees are engaging companies with their view of shareholder value." What came to be called the "worker-owner" or "capital stewardship" philosophy had four objectives. First was a search for investments that would protect workers while meeting fiduciary guidelines. Second was advocacy of mainstream governance principles that would give labor common ground with other institutional investors. By calling for shareholder rights, labor acquired a more positive public image while at the same time tarnishing management's. Third, UAPFs sought to persuade other investors that worker objectives were positively associated with long-term value. Finally, there was the hope that exercising shareholder power would give labor influence at the corporation's highest levels, a goal that had eluded it since the 1970s. [66]

UAPFs began to adopt more conventional shareholder activism. Like the SLPFs, they demanded that corporations limit executive pay; that they hold binding, not advisory, shareholder votes on proxy resolutions; and that they minimize takeover defenses such as staggered boards. This did not mean, however, that UAPFs automatically favored takeovers. For example, the Teamsters' pension fund mounted a campaign against a private-equity acquisition of Borden. The UAPFs' activism eventually eclipsed that of the SLPFs. By the late 1990s, they were filing more shareholder resolutions than any other group. Active UAPFs at this time included AFSCME, the Carpenters, the Laborers, SEIU, and the Teamsters. Each of these unions, as well as others, hired staff members to handle capital market issues. The honcho at the Teamsters was its new director of national affairs, Bill Patterson. [67]

A turning point came in 1997, when the AFL-CIO created an Office of Investment and a nonprofit Center for Working Capital to educate union trustees about "capital stewardship." The federation hired Patterson to oversee these efforts. Almost overnight, the AFL-CIO became the center of UAPF activism. It created a PayWatch website where workers could compare their earnings to those of their CEO. The site was extremely popular, getting over four million hits in its first year. According to AFL-CIO Secretary-Treasurer Rich Trumka, PayWatch offered workers a way to "vent their anger, anxiety, and outrage." Later the website added a feature called "Pick-a-Pension," which divulged CEO retirement packages and calculated how much health insurance they could buy for uncovered families. [68]

Patterson and others sought to coordinate diverse institutional investors so as to build a coalition in support of worker-owner objectives. The AFL-CIO began issuing Key Votes lists prior to proxy season that described resolutions various UAPFs intended to submit. The lists were circulated not only to UAPFs but to SLPFs and other institutional investors. Another effort at synchronization was the AFL-CIO's Proxy Voting Guidelines, which were disseminated in workshops attended by union trustees. The guidelines espouse good governance practices such as board independence and shareholder accountability but also embody a pro-worker view, what is called "the high road to competitiveness." For example, they assert that long-term performance is a better metric than quarterly or annual equity returns and that corporations have responsibilities to their "constituents" -- not only shareholders but other groups contributing productive assets to the enterprise, a view reminiscent of producerism. [69]

The AFL-CIO catapulted itself into the limelight with the emergence of the corporate scandals epitomized by Enron. In January 2002, the federation's Executive Council was the first group to respond to Enron by demanding that companies refuse to renominate any Enron directors on their boards. Two months later, Damon Silvers, the AFL-CIO's Associate General Counsel, appeared before the Senate Banking Committee to offer recommendations for reform. He called for an omnibus law to insure directorial independence, tighter regulation of accountants and analysts, and cessation of immunity from civil lawsuits for those who had committed securities fraud.

Several of Silvers' proposals were included in the Sarbanes-Oxley Act of July 2002. One legal expert dubs SOX "the most sweeping securities law reforms since the New Deal." The AFL-CIO hailed the act and said that the scandals were the result of markets that "once were well-regulated but are now trapped in a destructive cycle where short-term financial pressures combine with the greed of corrupt corporate insiders." Harking back to the 1890s, it condemned financial markets for being "rigged to entrench and enrich speculators . . . at the expense of employees, shareholders, and communities." [70]

In the years since Enron's implosion, UAPFs have moderated their emphasis on worker issues so as to foster alliances with other groups. Yet the UAPFs have not tossed out distinctive concerns, such as continuing efforts to persuade companies formerly headquartered in the U.S. to "come home to America." Several items on their agenda promote worker interests but do so in harmony with the institutional mainstream. UAPFs currently are pursuing five main issues. Two of them--executive pay and board structure--are old chestnuts of mainstream shareholder activism. The others are proxy access, scrutiny of investment managers, and regulation of private equity and hedge funds. The UAPFs rely on higgling--using bargaining power conferred by their investments--and on legislative enactment. [71]

Pay: Ever-higher executive compensation and scandals such as options backdating have kept pay issues at the forefront of UAPF activism. The AFL-CIO was quick to call for regulation of options backdating and for rules that would force executives to return part of their pay if earnings are revised. The proposals tap into public dismay over stratospheric executive pay levels. In a recent survey of American households, seventy percent agreed with the statement, "When corporations are profitable, the benefits are not shared with workers but go only to the top." Even President George W. Bush has acknowledged the prevailing political winds. During a 2007 visit to Wall Street, Bush told the audience to "pay attention to the executive pay packages that you approve." Amazingly, he tied finance to inequality and made a point previously contested by conservatives. "Income inequality," he said, "is real. It has been rising for more than 25 years." [72]

The SEC's revision of executive pay disclosure rules--for which the AFL-CIO lobbied--provides informational ammunition for criticizing executive pay levels and perks such as personal use of corporate jets (permitted by 70 percent of companies). The *New York Times* said that the disclosure rules brought to mind Brandeis's quip that "sunlight is said to be the best of disinfectants" (from Brandeis's post-Pujo book, *Other People's Money*). In the 2006 and 2007 proxy seasons, UAPFs sponsored the vast majority of advisory pay resolutions. Some sought limits on golden parachutes and executive retirement benefits; others demanded that executive bonuses be awarded only if performance was superior to a peer group. (PayWatch now carries case studies of egregious option grants and severance packages.) By far the most popular of the UAPFs' resolutions are those urging a "Say on Pay" by permitting advisory votes on the board's pay recommendations. Say on Pay proposals have garnered an average positive vote of 43 percent, which is on the high side for shareholder resolutions. The House in 2007 approved a bill backed by both SLPFs and UAPFs requiring say on pay. The bill was sponsored by the new Democratic chair of the House Financial Services Committee, Barney Frank, who is sympathetic to the labor movement's financial agenda. Damon Silvers attributed the vote to "increasing discontent in our country about income inequality generally and CEO pay specifically." Although Silvers' words echoed Bush's, the White House opposes the bill.

The combination of higgling and political pressure occasionally has brought labor influence at strategic corporate levels. For example, AFSCME and CalPERS recently joined with ten major corporations in a working group on advisory pay voting. As one union official said, "Five years ago we would never have gotten in a corporate boardroom. Now we're regularly meeting with corporate directors about substantive issues." [73]

Boards: Less dramatic but no less important has been the continuing emphasis on board reform. UAPF proposals include long-standing demands to limit board interlocks, separate the CEO and chairman positions, and require boards to seek shareholder approval of poison pills. A new issue is majority voting, instead of plurality voting, for corporate directors. In the past two proxy seasons, UAPFs again took the lead in sponsoring resolutions for majority voting. The idea is popular with other institutional investors and received more than 70 percent support in the 2007 proxy season. Bowing to the inevitable, more than half the proposals were withdrawn after companies agreed to adopt the rule. [74]

Proxy access: Related to majority voting is proxy access. Under current rules, shareholders are unable to nominate directors whose names would appear on the proxy. UAPFs propose that long-term owners holding a minimum percentage of shares be given this right. Other institutional investors are allied with UAPFs on this issue; they see proxy access as the most effective way to hold management accountable by placing on the board truly independent directors. It is also a way for shareholders to make boards more transparent. As an AFL-CIO official says of proxy access, "You're opening up the kitchen inside these companies. That's a dark secret. That's a place where the insiders really play inside ball." [75]

AFSCME, the AFL-CIO, and the CII submitted petitions to the SEC in 2003 seeking a rule on proxy access. When the SEC issued a staff report later in the year, it identified two issues for consideration: Should proxy access be adopted and, if so, what ought to be the requirements for shareholders to obtain it? If adopted, the key issue to be decided is the threshold of support from shareholders to initiate a proxy access vote. [76]

The SEC report brought vociferous opposition from the business community. An executive at Fidelity Investments said that investors already had sufficient tools to pressure management. The Business Roundtable warned that proxy access was "a thinly veiled attempt by labor unions and public pension funds to increase their influence over corporate America in order to further private agendas." But pension funds are not the only group seeking proxy access; socially responsible mutual funds and religious trust funds also support the change. If proxy access succeeds, the AFL-CIO hopes that owners will nominate directors who are knowledgeable about the industry, have a long-term view, and support the AFL-CIO's critique of capital markets. Rich Trumka, a feisty former president of the Mine Workers, is more ambitious. He wants directors who are "worker-friendly," which might include workers themselves, who, he notes, are likely to be independent of management. [77]

To press the issue, UAPFs have proposed proxy access at major companies. AFSCME, for example, filed resolutions at AIG, Citigroup, and Hewlett Packard. AIG, a scandal-ridden insurance company, took AFSCME to court on the grounds that SEC rules prohibit a proxy access resolution. But the courts ruled in AFSCME's favor in 2006. AFSCME came close to getting proxy access at HP, with only 52 percent of shares voting against the proposal. The issue is still in the air. The SEC--facing a court order to clarify its stance on proxy access--offered alternative proposals in July 2007. Democratic commissioners support a plan to require shareholder votes on proxy-access resolutions that are supported by 5 percent of investors. Republican commissioners want to forbid proxy access entirely. [78]

Mutual Funds and Investment Managers: Labor's activism now includes not only corporations but also mutual funds. Because pension funds are minority owners they need allies Mutual funds--whose share of U.S. equities is 25 percent and rising--are a logical place to look. Mutuals have not been shareholder activists, with the exception of a few "social" funds. Most are part of companies that sell financial services to business: administration of benefit plans, record keeping, and provision of investment options (usually their own mutual funds) for retirement plans. This creates an obvious conflict of interest. Funds do not vote against management, which protects the other side of their business. Trumka calls this "a rigged system" and alleges that financial companies have told prospective clients, "make me your mutual fund for your 401(k) … and I guarantee you the vote." The evidence supports Trumka's claim: the more business an investment services firm does with a client company, the less likely are the firm's mutual funds to vote against the client's wishes. [79]

Until recently, mutual funds did not disclose their proxy votes nor were they required to do so. In response to a request from the AFL-CIO, the SEC in 2000 considered to adopt a proxy disclosure policy. Investment companies selling mutual funds were opposed, even TIAA-CREF. To turn up the heat, Bill Patterson organized a demonstration outside Fidelity headquarters, protesting the firm's adamant refusal to disclose its votes. The timing was auspicious--mutuals were then being hit by scandals of their own--and in 2003 the SEC adopted a disclosure rule. [80]

UAPFs also have targeted financial companies that provide funds to politicians and political groups seeking privatization of Social Security and termination of defined-benefit (DB) pension plans in the public sector. In 2005, unions organized demonstrations at several financial giants in this camp, including Schwab and Wachovia. UAPFs sent letters warning the companies that they would lose union pension business unless they backed off. "We're seeking to pull Wall Street money out of the debate," said Bill Patterson. "Wall Street's covert funding of the drive to privatize Social Security is a conflict of interest because they stand to gain billions of dollars." [81]

Now that proxy disclosure is required, the AFL-CIO publishes annual reports analyzing how mutual funds vote for items on the UAPFs' agenda. Sixty percent of the items are mainstream "good governance" issues; twenty percent have to do with the environment and the poor; and another twenty percent reflect the UAPF's distinctive concerns. The AFL-CIO publishes a different report identifying investment managers who support privatization of Social Security and DB elimination. The UAPFs' effort signals to other institutional investors that labor supports their agenda and that, via the reciprocity norm, those investors should support labor's agenda. [82]

An important side show are firms offering proxy advice and other services to pension funds. The dominant player in the proxy business is Institutional Shareholder Services, which has a near-monopoly. ISS tailors its recommendations by institutional segment--including corporate, union, and public pension funds--which means that different parts of ISS can take contrary positions, not always in labor's interests. There also is a variety of specialized companies that provide investment services to UAPFs, such as the Marco Group. Marco has the lion's share of the UAPF market (140 clients with $75 billion in assets). It seeks investments that meet fiduciary standards while creating collateral benefits for unionized workers. Because of its size, Marco is a private-sector complement to efforts to synchronize UAPF voting patterns. [83]

The labor movement knows that its ability to influence finance is declining as DB plans gradually disappear. Already more than 40 percent of AFL-CIO members have defined-contribution (DC) plans, usually as substitutes for their DB plans. In the public sector, elected officials are proposing conversion of SLPFs from DB to DC, as California governor Arnold Schwarzenegger unsuccessfully attempted in 2004. Although the labor movement has been critical of DC plans, it sees the handwriting on the wall. It is quietly developing proposals for hybrid pensions that would pool risk, integrate with Social Security, and provide portability. Whether or not hybrids come to pass, 401(k) s surely will expand and mutual funds will be the recipients of their funds. To keep its agenda alive, the labor movement must build ties to mutual funds and align them with labor's emphasis on long-term value. Efforts to make mutuals more transparent and apolitical are one step in this direction. Another is Trumka's proposal to have investor representatives sit on the mutuals' boards, the same "voice" philosophy as proxy access. A third option is to sell labor's own mutual funds through a union-affiliated entity. [84]

Private Equity and Hedge Funds: Private equity funds (PE) are today a major part of financial markets. PE is a throwback to earlier eras: to the takeovers of the 1980s and, because of their collection of unrelated assets, to the conglomerates of the 1960s. The differences, however, involve scale and the source of capital--junk bonds then, easy credit now. PE's *modus operandi* is to leverage its funds via debt, buy undervalued companies, take them private, and later bring them back to the public markets. Buyouts in 2006 involved more money than was being put into mutual funds. How PE funds make money is a matter of dispute. PE funds say that, because they are blockholders aiming for a future IPO, they have an incentive to manage corporate assets to maximize long-term productivity. Critics charge that that the productivity effects of PE are undemonstrated and that PE profits are based on tax-advantaged income (debt and capital gains) and aggressive cash withdrawals that damage long-term performance. For example, a coalition of PE firms bought Hertz for $15 billion and paid themselves a dividend of $1 billion six months later. Other PE funds buy and flip within a year or less. PE is a leading example of how changes in capital markets affect labor markets. The funds currently employ 7 percent of the U.S. workforce and have lingering effects on employees of post-IPO companies. [85]

The great irony is that pension plans are the largest source of capital for PE. SLPFs alone account for 26 percent of PE funds raised in 2006. CalPERS has 7 percent of its assets in PE; other SLPFs have as much as 17 percent invested. The returns are too high to ignore for underfunded SLPFs, who find themselves between a rock and a hard place. CalPERS gets a return rate on PE of 20 percent. Because returns are higher than for other asset classes, the significance of PE to pension plans is greater than its portfolio weight. As a result, SLPFs have been wary of UPLF proposals to raise taxes on PE and an association of SLPFs publicly opposed the idea (although it later recanted). [86]

UAPFs were slow to enter the PE market because they associated PE with layoffs and because PE funds were reluctant to do business with them. In 1999, only 0.1 percent of UAPF assets were in PE. At this point, labor-friendly investment managers began encouraging UAPFs to place some of their assets in PE. Later, the AFL-CIO issued PE guidelines for UAPFs: to seek funds that respect worker rights and are committed to preserving or expanding jobs. With this encouragement, and faced with their own underfunding, the UAPFs turned to PE, although they currently have a smaller share invested than SLPFs. [87]

PE's first critics were European and transnational unions. In Britain, the largest PE market in Europe, unions have been vocal in their opposition to PE. One of their bête noires is Permira, Europe's largest PE fund. After Permira purchased a British company in 2004, it laid off 3,500 workers and cut vacation time for survivors. Elsewhere, Permira announced a plant closure one month after buying the parent firm. Another target is KKR, from which British unions extracted a pledge to invest and add jobs after KKR bought Boots. A recent TUC report to the government charges that PE funds with exacerbate inequality and threaten long-term growth. It urges an end to PE's tax advantages and seeks measures to protect employees in buyouts. [88]

The U.S. labor movement was slow to criticize PE in part because it found itself on both sides of the table. UAPFs not only invest in PE but some unionized workers are the beneficiaries of PE investments. There is a part of the PE industry that specializes in buyouts of heavily unionized firms in troubled industries such as auto parts, coal, steel, and textiles. The best known investor here is Wilbur L. Ross, a wealthy billionaire and donor to the Democratic Party. Ross makes his buyouts profitable by declaring bankruptcy, terminating the union's pension plan, and shifting its liabilities to the government's PBGC. He obtains job cuts by offering severance bonuses to dismissed workers; to survivors he offers profitsharing. Says Ross, "We found that if you approach with a realistic request -- in that you are not cutting them [union members] just so management can live in the lap of luxury - and if you have a quid pro quo so that they can share in the profits, you get along reasonably well." But not all unions are able to strike deals with Ross. In steel, the unions have been successful; in coal, where unions are weaker, Ross refused to negotiate. It remains to be seen what kind of deal the UAW can strike with Cerberus, the PE fund that purchased Chrysler. Cerberus has a reputation for making deep job cuts. It is yet another irony that Cerberus counts among its investors several large SLPFs. [89]

Low-wage service workers are especially vulnerable during PE buyouts. They are easier to replace and consequently have less bargaining than industrial workers. One of the first American unions to target PE was SEIU, whose members are employed in a variety of low-wage service industries affected by PE. Blackstone, the largest PE fund, owns nearly 600 large office buildings; Cerberus and other PE funds are major players in the hotel industry; and Carlyle owns nursing-home giant Manor Care. SEIU's public awareness campaign is aimed at giving workers more say and more money during buyouts. SEIU started a website to track Blackstone and published a report analyzing major PE deals that resulted in large layoffs, including at Hertz and KB Toys. There is method to the SEIU's public campaign. Andy Stern, head of SEIU (and of Change to Win, the AFL-CIO's competitor) has privately approached PE firms offering them political cover if they agree to treat workers fairly. [90]

What galvanized the AFL-CIO was Blackstone's 2007 announcement of its IPO. Trumka filed two statements with the SEC criticizing the IPO as an effort to avoid taxes. The AFL-CIO is working with its friends in Congress to regulate PE. Barney Frank, whose committee has held several hearings on PE, says that the funds are causing "gross imbalances" and notes that a recent buyout of Tommy Hilfiger led to the replacement of unionized janitors making $19 per hour by nonunion workers earning $8 per hour. Both the House and the Senate are considering bills to raise tax rates on PE managers and investors. With the Democrats controlling Congress, it is an auspicious time. Democrats, at least some of them, and the labor movement hope to show an anxious middle class that they are forcing the rich to play by the rules; it is an economic wedge issue. Using the threat of regulation as leverage, U.S. and foreign union leaders have held meetings with Blackstone to seek a pro-worker deal. The AFL-CIO and Change to Win have other reasons for speaking out. They fear that some of their affiliates have dangerously large amounts invested in, and are too enthusiastic about, PE. Says Damon Silvers, "What we are trying to do in this environment is to put some distance between the labor movement and the hunger of our funds for return." Another idea being batted about is to have UAPFs invest directly in PE rather than through intermediaries, the approach of some Canadian UAPFs. [91]

Congress and the labor movement also have targeted hedge funds. Like PE, they are an unregulated segment of the capital markets. Hedge funds have enormous assets--over $ 1.5 trillion --and account for more than half of all trades on the NYSE. They have broadened their base from hedging stocks to riskier assets like subprime debt, which recently went sour in real estate.. Hedge funds have branched out into PE, blurring the line between them. [92] Hedge funds have short time horizons--often less than a second--yet they have attracted considerable money from pension funds. Again, SLPFs have invested more than UAPFs, although both have less allocated to hedge funds than PE. Efforts to regulate hedge funds are moving quickly. The AFL-CIO contacted the Senate Banking Committee in 2006, to urge legislation covering transparency, trading tactics, and risk. The advice was prescient. Two months later came the collapse of Amaranth, a giant hedge fund in which SLPFs had invested several hundred million dollars. Four months later was the revelation of widespread share lending, wherein investors temporarily loan their shares to hedge funds seeking to throw a proxy contest in the direction of their bets. (It emerged that CalPERS had earned $130 million in a single year through this practice.) Frank's committee held its first hearings in March 2007, when the SEIU released a study showing that the 25 highest-paid hedge fund managers earned an average of $570 million in 2006. Lest one think that these earnings entirely reflect returns to skill, bear in mind that fund managers consistently receive 2 percent in management fees and 20 percent of earnings ("carried profit"). "You see this extraordinary accumulation of wealth in the hands of a relatively small group of people," said one SEIU staffer. "It's just not healthy for society." In 2007, the AFL-CIO urged support for Frank's legislation to increase transparency of, and tax rates on, hedge funds. [93]

Conclusions

The coalitions forming around financial issues are, in a word, complex. At the corporate level, owners--many of them institutions--seek shareholder primacy and minimal regulation. They do so unilaterally or with owner-oriented executives. However, here and there are executives and investors--like Jim Goodnight of SAS and John Bogle of Vanguard--who rail against short-termism while endorsing a revivified stakeholder approach. Labor federations and their UAPFs are steering a middle ground between owner and worker interests. Lacking market power, labor seeks support from SLPFs and a middle class anxious about inequality. [94]

The efforts of the labor movement may seem a Sisyphean attempt to overturn contract law and economic logic. Yet as in Phase I a new legal realism is emerging that supports labor's efforts. The legal neo-realists are at pains to point out that under law shareholders are neither the corporation's owners nor its sole residual claimants. Focusing on how the firm actually is organized, they observe that corporations are cooperative teams rather than the nexus of contracts portrayed in agency theory. To produce wealth, team members invest in firm-specific assets that are worthless if the firm goes bust. Hence all team members--not only shareholders--bear residual risk. With illiquid investments and little diversification, employees have the greatest incentive to monitor agents and may be best placed to do so. [95]

There is also a new realism in economics. It questions the rationality assumptions of agency theory and other models of abstract contractualism. Behavioral finance, as the field is called, offers evidence that investors are prone to cognitive distortions such as myopia, overconfidence, and biased self-attribution. The findings undermine the claim that share price is a reliable criterion of firm performance. Behavioral finance also justifies practices previously condemned by agency theory, such as insider boards and takeover defenses. In short, the double movement is waxing in the realm of ideas as well as politics. [96]

These developments have not gone unchallenged. Modern classical liberals have pursued several strategies to defend the financial status quo against charges that it produces undesirable results. One strategy is to claim that market forces, such as technology-driven skill biases, are driving income and wealth accumulation on Wall Street. There is no evidence, they say, that deregulation and deunionization have anything to do with the explosion of top shares. But the record shows that financial development is deeply embedded in a political matrix. [97]

Rajan and Zingales acknowledge a connection between finance and politics, if only in a negative sense. For them, financial development occurs when markets triumph over vested interests and the state. Yet if we consider Phase I as an example, what we see is that finance flourished *because* vested interests influenced the state and expanded its administrative powers. Such was the case with the gold standard, banking reform, creation of the Federal Reserve, and the design of antitrust regulation. Vested interests did not retard financial development; they expedited it. The same is occurring today. Clinton's Treasury Secretary Robert Rubin, previously the CEO of Goldman Sachs, promoted a variety of financial reforms such as interstate banking and Glass-Steagall's repeal. The Business Roundtable, a vested interest if ever there was one, is currently lobbying for regulatory changes in corporate governance and financial markets. Unlike labor, it has access to, and meets with, officials from the White House, OMB, the SEC, and the Treasury. On the ideological front, Wilbur Ross is funding a bipartisan group, the Committee on Capital Markets Regulations, which has proposed limits on "runaway" litigation and a rollback of SOX. The Committee is a blue-ribbon group whose roster includes prominent financiers, business leaders, and academics--R. Glenn Hubbard (Columbia), Hal C. Scott (Harvard), and Luigi Zingales (Chicago). One corporate law scholar describes the committee as "an escalation of the culture war against regulation." [98]

A second strategy is to claim that the benefits of finance outweigh its costs. As Rajan and Zingales say, "financial development is so beneficial that it seems strange that anyone would oppose it." They attribute financial regulation to vested interests or to exogenous shocks such as depression or hyperinflation. But it is not shocks nor an elite that have caused the double movement's recurrence. Instead it arises when citizens perceive the economic and social costs of finance to outweigh its benefits. There are benefits, of course. Financial development facilitates consumption smoothing to counteract income volatility. But the ability of sub-median households to smooth is less than that of wealthier households with larger asset cushions. As a result, consumption inequality has risen along with income inequality since the 1980s. Sub-median households face particular difficulties when volatility spikes due to job loss. The median high-school dropout facing unemployment has liquid assets worth only 5 percent of the income loss from unemployment versus 124 percent for college graduates. For sub-median households, it is government safety nets--progressive taxation, unemployment insurance, food stamps--that facilitate smoothing. But the safety nets are frayed. Hence a perception that financial costs outweigh benefits is not strange nor is it evidence of an anti-liberal conspiracy.[99]

The third strategy is to underweight the benefits of stakeholder governance--what Rajan and Zingales call "relational capitalism"--and assert that it was and is incompatible with rapid technological change. Yet coordinated market economies--which the United States resembled during Phase II--are as capable of producing wealth as the liberal market economies preferred by Rajan and Zingales. Another issue is normative efficiency: what sort of arrangements best match citizen preferences. In the past, relational capitalism sustained private and social compacts to share risk in return for openness. Today, however, the compacts offer less in return for openness than in the past. As the compacts grow weaker, so does democratic support for liberalization. [100]

To their credit, Rajan and Zingales recognize the importance of democracy. They believe that finance has an inherently egalitarian spirit: "The financial revolution is opening the gates of the aristocratic clubs to everyone…it puts the human being at the center of economic activity." Perotti and von Thadden, also finance enthusiasts, make the same point in a different way: the recent spread of share ownership has brought equities to the masses and created broad political support for finance. Examining data on shareholding by quintiles, they identify nations in which the median household has a propensity to own shares. Because these nations--the U.K. and the U.S.--have relatively free financial markets, they infer that "the existence of a financially solid median class may be essential for democratic support for a market environment." [101]

How can one square these claims with the evidence presented here? Is there a hidden popular groundswell for freer financial markets? The problem is that Perotti and von Thadden examine neither the value of the middle quintile's shareholdings nor its debt. In the U.S. the middle quintile owns shares--directly or indirectly via retirement plans--worth $7500, which account for 5 percent of its assets. Debt--three-quarters of which is mortgages--stands at $74,000. Now take the top 1 percent. It holds $3.3 million in shares, which account for 21 percent of its assets. Debt stands at $566,000. So let's compare: the median has a debt/equity ratio of 9.9; the top 1 percent's ratio is 0.17. One need not be an economist to predict which group will be risk-averse and which will welcome financial risk. [102]

The citizenry is not deluded, nor are parallels to the past coincidental. As the *New York Times* recently put it, we are in the midst of a new Gilded Age and a new populism, one whose fires are being stoked by rising instability and inequality. [103] Deregulation of financial markets and lax supervision during Phase III--especially in the U.S. and U.K.-- has come back to haunt those countries through the recent meltdown of mortgage markets and credit instruments built upon them. For the first time since the 1930s, a run occurred on a major bank, Britain's Northern Rock. Despite its weakness, the labor movement is building investor and electoral coalitions to mitigate these problems. Labor's use of its pension capital is not without paradoxes. In the main, however, its efforts are consistent: to forge a new compact that will weaken the link between financial and labor markets. Will the effort prove successful? It's too early to say. As in the past, much depends on the balance of power in markets and politics.

Table 1: Global Trade and Finance, 1870-2003 [1]

	World Export Growth Rates	Stock Market Capitalization/GDP (US)	Fixed Capital Investment Funded by Equity Issues
Phase I			
1870-1913	3.8%		
1900-1913	4.5		
1913		0.40 (.39)	0.13 (.04)
1924-29	6.0		
1929		0.53 (.75)	0.34 (.38)
Phase II			
1929-38	0		
1950		0.27 (.33)	0.03 (.04)
1950-73	7.0		
1970		0.42 (.66)	0.02 (.07)
Phase III			
1973-92	4.0		
1990-2005	6.0		
1999		1.08 (1.52)	0.18 (.12)
1999-2003		0.86 (1.42)	

[1] Column 1: Merchandise exports as share of GDP in 1990 prices from Angus Maddison, T*he World Economy*, vol. 2 (Paris, 2006), 362. Columns 2 and 3: Rajan and Zingales, "Great Reversals," 13-15; data for 1999-2003 from Simeon Djankov, Rafael La Porta, Florencio Lopez-de-Silanes, and Andrei Shleifer, "The Law and Economics of Self-Dealing," December 2005, SSRN.

Table 2: Top 1 percent Income Shares [2]

	UK	US	US Wealth	Austl	Swd	Fr	Grm	NL	Jp
c. 1900-1913		18			21	19	20	21	16
1920	19	15	38	12	14	18	20	21	17
1925	20	20	36	11	13	18	13	18	18
1952	10	11	23	9	8	9	11	13	8
1980	7	10	19	5	5	8	11	6	7
c. 1999-2004	13	17	21	9	7	8	10	5	9
1980/ 1925	.35	.50	.53	.45	.38	.44	.85	.33	.39
1999-2004/ 1980	1.86	1.70	1.11	1.80	1.40	1.00	.91	0.83	1.29

[2] U.K: A.B. Atkinson, "Top Incomes in the UK over the 20th Century" 168 *J.R. Statistic. Soc.*(2005). U.S. income: Thomas Piketty and Emmanuel Saez, "Income Inequality in the United States" in A.B. Atkinson and T. Piketty (eds.), *Top Incomes over the Twentieth Century* (New York, 2007). U.S. wealth: Wojciech Kopczuk and E. Saez, "Top Wealth Shares in the United States, 1916-2000," NBER Working Paper 10399 (2004). Australia: A.B. Atkinson and A. Leigh, "Understanding the Distribution of Top Incomes in Anglo-Saxon Countries over the 20th Century," Working paper, Australian National University (2004). Sweden: Jesper Roine and Daniel Waldenstrom, "Top Incomes in Sweden over the 20th Century," Stockholm School of Economics, working paper 602 (2005). France: Thomas Piketty, "Income Inequality in France,1901-1998" CEPR Working Paper 2876 (2001) and Emmanuel Saez, "Income and Wealth Concentration in a Historical and International Perspective" in Alan Auerbach, David Card, and John Quigley, *Public Policy and Income Distribution* (New York, 2006). Germany: Fabien Dell, "Top Incomes in Germany and Switzerland over the 20th Century," 3 *Journal of the Eur. Econ. Assoc.* (2005). Netherlands: A.B. Atkinson and Wiemer Salverda, "Top Incomes in the Netherlands and the U.K. over the 20th Century," 3 *Journal of the Eur. Econ. Assoc.* (2005). Japan: Chiaki Moriguchi and Emmanuel Saez, "The Evolution of Income Concentration in Japan, 1886-2005," working paper, Northwestern University (2007). N.B. 1900 figures shown for U.S. and Netherlands are for 1913-14, for Sweden for 1906, and for France for 1900-1910. 1999-2004 figures are for most recent year available in that period. Some figures are interpolated.

Table 3: Distribution of Net Value Added in Large European Corporations, 1991-1994 [3]

	Labor	**Capital**	**Government**	**Retained**	**Dividends**
Anglo-Saxon	62.2	23.5	14.3	3.2	15.0
Germanic	86.1	8.8	5.1	5.2	3.0
Latinic	80.3	14.4	5.3	3.0	4.7
Average	79.0	13.7	7.3	3.6	6.1

[3] Dividends and retained earnings do not equal the capital share because net interest payments and third-party shares are not included. Henk Wouter De Jong, "The Governance Structure and Performance of Large European Corporations," 1 *Journal of Management and Governance* (1997).

NOTES

[*] Thanks to Steve Foresti, Dana Frank, John Logan, James Livingston, David Montgomery, Grace Palladino, Hugh Rockoff, Richard Sylla, Ryan Utsumi, Fred Whittlesey, Robert Zieger, and various interviewees, especially Dan Pedrotty, who generously offered their time and ideas. The usual disclaimer applies. I am grateful for support from the Price Center at the UCLA Anderson School and from the Institute for Technology, Enterprise, and Competitiveness at Doshisha University. This paper is dedicated to Lloyd Ulman: scholar, teacher, mensch.

[1] Sanford M. Jacoby, "The New Institutionalism: What Can It Learn from the Old?" 29 *Industrial Relations* (1990): 316-340; Daron Acemoglu and James Robinson, *Economic Origins of Dictatorship and Democracy* (Cambridge, UK, 2005); Peter A. Hall and David Soskice, *Varieties of Capitalism: The Institutional Foundations of Comparative Advantage* (New York, 2001); Mary Brinton and Victor Nee, *The New Institutionalism in Sociology* (Stanford, 2001); Kathleen Thelen, *How Institutions Evolve* (Cambridge, UK, 2004).

[2] Lloyd Ulman, “Cost Push and Some Policy Alternatives,” 62 *American Economic Review* (1972); Jack Barbash, *The Elements of Industrial Relations* (Madison 1984).

[3] Karl Polanyi, *The Great Transformation* (New York 1944):76; Arthur M. Schlesinger, Jr., *The Cycles of American History* (Boston 1986).

[4] In this paper finance refers to financial institutions and to owners. The growth of financial markets is termed financial development or financialization. Labor usually connotes organized labor, although in other places it means the non-executive workforce.

[5] Regarding growth, Levine and Zervos find that stock market liquidity is positively associated with growth but that stock market size has no effect. Arestis et al. (2001, 2006) find that the contribution of stock markets to growth is modest and that the effect attenuates in developed countries. An IMF (2006:16) review of the evidence on openness concludes that “it remains difficult to find robust evidence that financial integration systematically increases growth, once other determinants of growth are controlled for.” Ross Levine and Sara Zervos, “Stock Markets, Banks, and Economic Growth,” 88 *American Economic Review* (1998); Philip Arestis et al., “Financial Development and Economic Growth,” 33 *Journal of Money, Credit, and Banking* (2001); Arestis et al., “Financial Development and Productive Efficiency in OECD Countries,” 74 *The Manchester School* (2006); M. Ayan Khose, Eswar Prasad, Kenneth Rogoff, and Shang-Jin Wei, “Financial Globalization: A Reappraisal,” IMF working paper 189 (2006).

[6] Philip T. Hoffman, Gilles Postal-Vinay, and Jean-Laurent Rosenthal, et al., *Surviving Large Losses* (Cambridge, 2007); David Skeel, *Icarus in the Boardroom* (New York 2005).

[7] Randy Martin, *Financialization of Daily Life* (Philadelphia 2002).

[8] Angus Maddison, *The World Economy*, vol. 2 (Paris, 2006), 362; Paul Bairoch and Richard Kozul-Wright, “Globalization Myths,” UNCTAD discussion paper 113 (1996).

[9] Richard F. Bensel, *The Political Economy of American Industrialization, 1877-1900* (Cambridge, UK, 2000): 418-442; Polanyi, *Great Transformation*, 214.

[10] Barry Eichengreen, *Globalizing Capital: A History of the International Monetary System* (Princeton 1996); Raghuram Rajan and Luigi Zingales, “The Great Reversals: The Politics of Financial Development in the 20th Century,” 69 *Journal of Financial Economics* (2003); Randall Kroszner and Raghuram Rajan, “Is the Glass-Steagall Act Justified?” 84 *Amer. Ec. Rev.* (1994). Rajan and Zingales measure financial development as the sum of the three equity measures plus the ratio of deposits to GDP, which is not discussed here.

[11] Cedric B. Cowing, *Populists, Plungers, and Progressives* (Princeton 1965): 170.

[12] Even under dispersed ownership, practical control could be exercised by relatively small stakes. Adolf A. Berle and Gardiner C. Means, *The Modern Corporation and Private Property* (New York 1932): 106; Robert A. Gordon, *Business Leadership in the Large Corporation* (Washington, DC 1945); Dennis Leech, “Concentration and Control in Large U.S. Corporations,” 35 *Journal of Industrial Economics* (1987); Gardiner C. Means, “The Diffusion of Stock Ownership in the U.S.,” 44 *QJE* (1930): 599.

[13] Rajan and Zingales, “Great Reversals’: Steve Fraser, *Every Man a Speculator: A History of Wall Street in American Life* (New York 2005): 444-7; 473.

[14] Diana Farrell et al., “Mapping the Global Capital Market,” McKinsey Global Institute (2007): 8; Fraser, *Every Man*, 552.

[15] Margaret Blair, *Ownership and Control* (Washington DC 1995): 46; Conference Board, “2007 Institutional Investment Report” (2007): IMF, *Global Financial Stability Report* (2005): 68.

[16] Gary Gorton and Matthias Kahl, “Blockholder Identity, Equity Ownership Structures, and Hostile Takeovers,” NBER working paper W7123 (1999); *Pensions & Investments* (hereafter *P&I*), Nov. 15, 2004, April 17, 2006, Aug. 21, 2006; *Bus. Wk.*, Sept. 17, 2007; Stephen J. Choi and Jill E. Fisch, “On Beyond CalPERS: Survey Evidence on the Developing Role of Public Pension Funds in Corporate Governance,” working paper, Fordham Law School, 2007.

[17] A.B. Atkinson, “Measuring Top Incomes: Methodological Issues” in A.B. Atkinson and T. Piketty (eds.), *Top Incomes over the Twentieth Century* (New York, 2007), 18-42. Atkinson finds a close relationship between top shares and the aggregate Gini coefficient in the United States from 1947 to 2002. According to his estimates, a rise of 8 points in the top share--which occurred in the U.S. during Phase III--theoretically can account for most of the Gini

coefficient's rise during this period, although this does not prove that the former actually caused the latter. Roe finds a positive association between a nation's stock market capitalization and its Gini coefficient Mark J. Roe, "Political Preconditions to Separating Ownership from Control," 53 *Stanford L.R.* (2000): 564.

[18] Jeffrey Williamson and Peter Lindert, *American Inequality: A Macroeconomic History* (New York, 1980): 50; Kevin Phillips, *Wealth and Democracy* (New York 2002): 43; Irving B. Kravis, "Relative Income Shares in Fact and Theory," 49 *Am. Econ. Rev.* (1959); 1959; Wojciech Kopczuk and Emmanuel Saez, "Top Wealth Shares in the United States, 1916-2000," NBER Working Paper 10399 (2004); Larry Neal, "Trust Companies and Financial Innovation," 45 *Bus. Hist. Rev.* (1971). In 1914, Scott Nearing, a socialist economist then teaching at the Wharton School, found similarity of labor's share in France, Germany, Switzerland, the U.K., and the United States; it was about 60 percent This is consistent with the data in Table 2 and close to Kravis's figures. Nearing, "Service Income and Property Income," 14 *Publics. of the Amer. Stat. Assoc.* (1914).

[19] Kopczuk and Saez, "Top Wealth Shares;" Lawrence Mishel, Jared Bernstein, and Sylvia Allegretto, *The State of Working America* (Ithaca 2006): chap. 5.

[20] Much of the literature on finance and distribution is concerned with developing, not developed, countries. Clarke (2006) and Beck et al. (2007) find a negative association between financial development and inequality, although they examine credit provision, not equity markets. Baddeley (2006) finds a positive association between financial development and inequality. Das (2003) finds that stock market liberalization boosts inequality, especially through its positive effects on top-income shares. Goldberg and Pavcnik (2007) analyze trade openness, which is correlated with financial openness, and finds that openness is positively associated with inequality. Growth does boost average incomes levels, of course, but growth can be hampered by inequality, according to Aghion (1999). As for the determinants of top shares, Atkinson and Leigh (2004) find that top 1 percent shares are sensitive to marginal tax rates and to the return on equities. Of various income sources, it is only the return on equities that is significantly related to top shares. Note that tax rates themselves are endogenous, as discussed below and as evidenced by the fact that two-thirds of the decline in progressivity between 1960 and 2004 occurred during the Reagan years. George Clarke et. al, Finance and Income Inequality: What Do the Data Tell US?" 72 *Southern Economic Journal* (2006); Thorsten Beck, Asli Demirguc-Kunt, and Ross Levine, "Finance, Inequality, and the Poor," working paper (2007); Michelle Baddeley, "Convergence or Divergence? The Impacts of Globalisation on Growth and Inequality in Less Developed Countries," 20 *Intl. Rev. of Applied Econs.* (2006); Mitali Das and Sanket Mohapatra, "Income Inequality: The Aftermath of Stock Market Liberalization in Emerging Markets," 10 *Journal of Empirical Finance* (2003); Pinelopi Goldberg and Nina Pavcnik, "Distributional Effects of Globalization in Developing Countries," *J. of Econ. Lit.* (2007); Philippe Aghion et al., "Inequality and Economic Growth," 37 *J. of Econ. Lit.* (1999); A.B. Atkinson and A. Leigh, "Understanding the Distribution of Top Incomes in Anglo-Saxon Countries over the 20th Century," Working paper, Australian National University (2004); Thomas Piketty and Emmanuel Saez, "How Progressive is the U.S. Federal Tax System?" 21 *J. of Economic Perspectives* (2007).

[21] Thomas Piketty and Emmanuel Saez, "Income Inequality in the United States" in A.B. Atkinson and T. Piketty (eds.), *Top Incomes over the Twentieth Century* (New York, 2007).

[22] Lucian Bebchuk and Jesse Fried, *Pay without Performance: The Unfulfilled Promise of Executive Compensation* (Cambridge 2006); Gerald Epstein and Arjun Jayadev, "The Rise of Rentier Incomes in OECD Countries," in Epstein (ed.), *Financialization and the World Economy* (Cheltenham, UK 2005); Steven N. Kaplan and Joshua Rauh, "Wall Street and Main Street: What Contributes to the Rise in the Highest Incomes?" NBER working paper 13270 (2007); Ian Dew-Becker and Robert J. Gordon, "Where did the Productivity Growth Go? Inflation Dynamics and the Distribution of Income," NBER working paper 11842 (2005); Richard Freeman, *America Works* (New York 2007): 39.

[23] Peter Gourevitch and James Shinn, *Political Power and Corporate Control: The New Global Politics of Corporate Governance* (Princeton 2005).

[24] Regarding the negative effect of takeovers on labor rents, see Andrei Shleifer & Lawrence H. Summers, "Breach of Trust in Hostile Takeovers" in Alan J. Auerbach, ed., *Corporate Takeovers: Causes and Consequences* (Chicago 1988); Jagadeesh Gokhale, Erica Groshen, and David Neumark, "Do Hostile Takeovers Reduce Extramarginal Wage Payments," 77 *REStat* (1995). Since the mid-1990s, Germany modestly has shifted shares from labor to capital but Japan has not, as discussed in Gregory Jackson, "Stakeholders Under Pressure: Corporate Governance and Labour Management in Germany and Japan," 13 *Corporate Governance* (2005). Note that the view taken here is that corporate governance is endogenous and interrelated with technology, politics, regulation, market structure, and other factors. Sanford M. Jacoby, "Convergence by Design: The Case of CalPERS in Japan," 55 *Amer. J. of Comp. Law* (2007).

[25] There was variation across the industrialized world in the timing of labor's response to financialization. International patterns "rhymed" but were not precisely synchronized. The subject is addressed in a forthcoming book, *Labor and Finance.*

[26] Louis Hartz, *Economic Policy and Democratic Thought* (Cambridge 1948); Mark Roe, *Strong Managers, Weak Owners: The Political Roots of American Corporate Finance* (Princeton 1994): 68; David Montgomery, *Beyond Equality: Labor and the Radical Republicans, 1862-1872* (Urbana 1967): 445.

[27] Lawrence Goodwyn, *The Populist Movement* (New York 1978): 278-84; Phillips, *Wealth and Democracy*, 239; Bensel, *American Industrialization,* passim; Kim Voss, *The Making of American Exceptionalism: The Knights of Labor and Class Formation in the Nineteenth Century* (Ithaca 1994).

[28] Morton J. Horwitz, *The Transformation of American Law, 1870-1960: The Crisis of Legal Orthodoxy* (New York 1992): 90. The claim of absolute property rights was the basis for judicial application of the labor injunction, previously a remedy restricted to physical--usually maritime--property.
[29] Louis D. Brandeis, *Other People's Money and How the Bankers Use It* (New York 1914); Brandeis, *Business - A Profession* (Boston 1914); Samuel Haber, *Efficiency and Uplift: Scientific Management in the Progressive Era* (Chicago 1964).
[30] Horwitz, *Transformation,* passim.
[31] Lloyd Ulman, *The Rise of the National Trade Union: The Development and Significance of Its Structure, Governing Institutions, and Economic Policies* (Cambridge 1955); James Weinstein, "Radicalism in the Midst of Normalcy," 52 *Journal of American History* (1966); Cedric Cowing, "Sons of the Wild Jackass and the Stock Market," 33 *Bus. Hist. Rev.* (1959).
[32] Michael Huberman and Wayne Lewchuk, "European Economic Integration and the Labour Compact," 7 *European Review of Economic History* (2003). An interesting question is why the social compact did not translate into smaller top shares prior to the 1930s. The answer is that the first compacts came cheap. In 1920, social spending as a share of national income in the European nations shown in Table 2 was 1.1 percent. For four of those countries--the U.K., Sweden, Netherlands, and France-- it was 1.4 percent, whereas for those same four countries in 1965 it was 19 percent and probably higher because the 1965 figures omit items included in the 1920 data. Peter Lindert, "The Rise of Social Spending, 1880-1930," 31 *Explorations in Econ. Hist.* (1994); Jens Alber, "Is There a Crisis of the Welfare State?" 4 *European Sociological Review* (1988): 190.
[33] According to the AFL, between 1927 and 1928 capital gains rose by 70 percent, dividends by 7 percent, and manufacturing wages by 1.5 percent. At International Harvester--a bellwether corporation in its day--wages barely budged during the 1920s despite the firm's record profits. 36 *American Federationist* (May 1929): 535; 37 *American Federationist* (March 1930): 339-41; Cowing, *Populists, Plungers,* 155-186; Robert Ozanne, *Wages in Practice and Theory* (Madison 1968): 49.
[34] The timing of events in Britain was different. Britain's 1925 return to the prewar parity rate had deflationary effects, including wage cuts. These were one cause of the 1926 General Strike, in which 2.5 million workers walked off their jobs. As Ernest Bevin recalled twenty years later, responsibility for the strike was the government's because the gold standard forced a "miserable attack on the standard of life of men in a basic industry." Melvin C. Shefitz, "The Trade Disputes and Trade Unions Act of 1927: The Aftermath of the General Strike," 29 *Review of Politics* (1967): 405.
[35] Roe, *Strong Managers,* 42. Couglin urged, "Forward to Christ all ye people! God wills it -- this religious crusade against the pagan of gold. Silver is the key to prosperity -- silver that was damned by the Morgans." William E. Leuchtenberg, *Franklin D. Roosevelt and The New Deal* (New York 1963): 101.
[36] Ibid., 103; Alan Brinkley, *Voices of Protest: Huey Long, Father Coughlin, and the Great Depression* (New York 1982): 140, 150, 171
[37] Ibid., 54-56; Cowing, *Populists, Plungers,* 223; Leuchtenberg, *Roosevelt*, 60; Charles R. Geisst, *Undue Influence: How the Wall Street Elite Puts the Financial System at Risk* (New York 2005): 68; Paul Studenski and Herman E. Kroos, *Financial History of the United States* (New York 1952): 363; Herbert M. Bratter, "The Silver Episode: II," 46 *JPE* (1938); Ellis Hawley, *The New Deal and the Problem of Monopoly* (Princeton 1966): 307; *New York Times* (hereafter *NYT*) Dec. 13, 1937.
[38] John G. Ruggie, "Ínternational Regimes, Transactions, and Change: Embedded Liberalism in the Postwar Economic Order," 36 *International Organization* (1982): 387; Vincent Carosso, "Washington and Wall Street: The New Deal and Investment Bankers," 44 *Bus. His. Rev.* (1970); Barry Eichengreen, *Golden Fetters: The Gold Standard and the Great Depression, 1919-1939* (New York 1992).
[39] *NYT* Jan. 1, 1945, April 13, 1945, Feb. 13, 1945.
[40] *NYT* April 8, 1943, Feb. 12, 1943, April 8, 1943, Feb. 12, 1943, April 22, 1944; Studenski and Kroos, *Financial History,* 471; William L. Cary, "Pressure Groups and the Revenue Code," 68 *Harvard L.R.* (1955); Boris Shiskin, "Organized Labor and the Veteran," 238 *Annals of the Amer. Acad. of Pol. and Soc. Sci.* (1945); Robert M. Collins, "The Economic Crisis of 1968 and the Waning of the 'American Century'", 101 *Amer. Hist. Rev.* (1996).
[41] Robert Ozanne, "Impact of Unions on Wage Levels and Income Distribution," 73 *QJE* (1959); Sumner H. Slichter, "Do the Wage-Fixing Arrangements in the American Labor Market Have an Inflationary Bias?" 44 *American Econ. Rev.* (1954); Alan B. Krueger, *Measuring Labor's Share,* 89 *Amer. Ec. Rev.* (1999); Harry C. Katz, *Shifting Gears: Changing Labor Relations in the U.S. Automobile Industry* (Cambridge 1985); Frank Levy and Peter Temin, "Inequality and Institutions in 20th Century America," MIT working paper, 2007.
[42] Jonathan Baskin and Paul J. Miranti, Jr., *A History of Corporate Finance* (Cambridge, UK 1997): 232; Blair, *Ownership and Control,* 46. The TNEC investigations of the late 1930s showed blockholding persisting in many companies. The extent to which blockholders lost control over the course of Phase II is disputed. Much depends on choice of an ownership criterion conferring control as well as assumptions regarding the control conferred by bank ownership and board memberships. Using a 10 percent criterion, Larner claimed that 84 percent of the top 200 nonfinancial corporations in 1963 were under management control. On the other hand, Burch found 40 percent under management control because of holdings by families, trusts, and estates. Gordon, *Business Leadership*, 38; 157; Marco Becht and J. Bradford DeLong, "Why Has There Been So Little Blockholding in America?" working paper (2004);

Philip Burch, *The Managerial Revolution* (Lexington, MA 1972); Maurice Zeitlin, "Corporate Ownership and Control," 79 *American Journal of Sociology* (1974).
[43] E. Merrick Dodd, "The Modern Corporation, Private Property, and Recent Federal Legislation," 54 *Harvard LR* (1941): 924; Francis X. Sutton et al., *The American Business Creed* (Cambridge 1956): 64-5.
[44] Berle and Means, *Modern Corporation*, 199.
[45] G. W. Schwert, "Indexes of U.S. Stock Prices from 1802 to 1987," 63 *The Journal of Business* (1990); Mary O'Sullivan, "Living with the U.S. Financial System: The Experiences of General Electric and Westinghouse in the Last Century," 80 *Bus. Hist. Rev*. (2006); Carola Frydman and Raven Saks, "Historical Trends in Executive Compensation," MIT working paper (2005); Nitin Nohria and Ranjay Gulati, "Is Slack Good or Bad for Innovation?" 39 *Acad. of Mgt. J.* (1996). Dependence on retained earnings in the postwar decades is reflected in the low rate of equity funding for fixed capital shown in Table 1.
[46] Charles Maier, "The Politics of Productivity: Foundations of American International Economic Policy After World War II," 31 *Intl. Org.* (1977); Fred Foulkes, *Personnel Policies in Large Nonunion Companies* (Englewood Cliffs 1980): 325.
[47] Richard Freeman and James Medoff, *What Do Unions Do?* (New York 1982): 53; Sanford Jacoby and Daniel J.B. Mitchell, "Measurement of Compensation: Union and Nonunion," 27 *Industrial Relations (*1988); Sumner H. Slichter, "The Current Labor Policies of American Industries," 43 *Qrt. J. of Econ.* (1929): 398; Daniel J.B. Mitchell, *Unions, Wages, and Inflation* (Washington, DC 1980); Sumner H. Slichter, James Healey, and E. Robert Livernash, *The Impact of Collective Bargaining On Management* (Washington DC 1960). In the 1970s, SUBS covered 10 percent of unionized workers and none in the nonunion sector. Freeman and Medoff, *What Unions Do.*
[48] Robert Hart and James Malley, "Excess Labour and the Business Cycle," 63 *Economica* (1996); Robert J. Flanagan, "Implicit Contracts, Explicit Contracts, and Wages," 74 *Am. Econ. Rev.*(1984); David M. Gordon, Richard Edwards, and Michael Reich, *Segmented Work, Divided Workers* (Cambridge, UK 1982). In the mid-1970s, pension coverage among union workers was 91 percent; for nonunion workers it was 47 percent. Union workers were 14 percent more likely to have medical insurance and their benefit levels were more generous. Freeman and Medoff, *What Do Unions Do?*
[49] Baskin and Miranti, *History of Finance,* ch. 7; *NYT* Feb. 16, 1961. Feb. 13, 1970, July 1, 1973. In fact, there is evidence to support the association between conglomerates and the "going South" strategy. Anil Verma and Thomas A. Kochan, "The Growth and Nature of the Nonunion Sector within a Firm" in Kochan, ed., *Challenges and Choices Facing American Labor* (Cambridge 1985).
[50] David Halberstam, *The Reckoning* (New York 1986); Dirk Zorn, Frank Dobbin, Julian Dierkes, and Man-Shan Kwok, "Managing Investors: How Financial Markets Reshaped the American Firm" in K.K. Cetina and A. Preda, *The Sociology of Financial Markets* (New York, 2006); Neil Fligstein, "The Intraorganizational Power Struggle," 52 *American Soc. Review* (1987).
[51] Eric Helleiner, *States and the Emergence of Global Finance* (Ithaca 1994): 81-122; Geisst, *Undue Influence*, 174-77.
[52] Martha Derthick and Paul Quirk, *The Politics of Deregulation* (Washington DC 1985); Daniel J.B. Mitchell, "Union vs. Nonunion Wage Norm Shifts," 76 *Amer. Ec. Rev.* (1986).
[53] Steven K. Vogel, *Freer Markets, More Rules* (Ithaca 1996); Jacoby, "Convergence by Design."
[54] Michael C. Jensen and William Meckling, "Theory of the Firm: Managerial Behavior, Agency Costs, and Ownership Structure," 3 *Journal of Financial Economics* (1976); Connie Bruck, *The Predators" Ball* (New York, 1988): 261.
[55] Marianne Bertrand and Sendhil Mullainathan, "Enjoying the Quiet Life? Corporate Governance and Managerial Preferences," 111 *Journal of Political Economy* (1999); Henrik Cronqvist and Rudiger Fahlenbrach, "Large Shareholders and Corporate Policies," Fisher College, Ohio State University, working paper 14 (2006); Michael C. Jensen, "Agency Costs of Free Cash Flow, Corporate Finance, and Takeovers," 76 *Amer. Econ. Rev.* (1986). Note that the "lazy manager" claim is an analogue to the view that employees are shirkers. Both assume that the pursuit of self-interest leads uncontrolled individuals to the sub-optimal quadrant of the prisoner's dilemma. The idea originates in classical liberalism, from Hobbes to Smith to Mills. For a different, and more empirical, view, see Robert M. Axelrod, *The Evolution of Cooperation* (New York 1984). Also note that Jensen recently recanted his faith in conventional stock options. See http://papers.ssrn.com/sol3/papers.cfm?abstract_id=480401.
[56] Bebchuk and Fried, *Pay without Performance;* William J Baumol, Alan Blinder, and Edward N. Wolff, *Downsizing in America* (New York 2003): 261; Gunther Capelle-Blancard and Nicolas Couderc, "How Do Shareholders Respond to Downsizing?" SSRN working paper 952768 (2007); David I. Levine, "Can Wage Increases Pay for Themselves? Tests with a Production Function," 102 *Economic Journal* (1992); Julian Franks and Colin Mayer, "Hostile Takeover and the Correction of Managerial Failure," 40 *J. of Fin. Econ.* (1995); Andrei Shleifer and Robert Vishny, "Stock Market Driven Acquisitions," 70 *Journal of Financial Economics* (2003); William W. Bratton, "Is the Hostile Takeover Irrelevant? A Look at the Evidence," working paper, Georgetown Law Center, 2007; Lynn Stout, "Do Antitakeover Defenses Decrease Shareholder Wealth?" 55 *Stanford L.R.* (2002); Frederick Reichheld, *The Loyalty Effect* (Boston 1996).
[57] Barry T. Hirsch, *Labor Unions and the Economic Performance of Firms* (Kalamazoo 1991); Bronwyn Hall, "Corporate Restructuring and Investment Horizons in the U.S., 1976-1987," 68 *Bus. Hist. Rev.* (1994); Brian J. Bushee, "The Influence of Institutional Investors on Myopic R&D Investment Behavior," 73 *The Accounting Review* (1998);

Julian Franks and Colin Mayer, "Capital Markets and Corporate Control," 5 *Economic Policy* (1990); Clayton Christensen and Scott Anthony, "Put Investors in Their Place," *Business Week* (May 28, 2007); *The Economist*, April 23, 2005, 71.

[58] Cash distributions by the S&P 500 rose from $300 billion in 2003 to $836 billion in 2006 and aggregate dividend payments have risen steadily since 1990. Meanwhile, wages and salaries as a percentage of GDP are at their lowest level since 1947 as is total compensation (with the exception of a dip in the mid-1990s). *Financial Times*, Feb. 22, 2007; *Global Financial Stability Report* (Washington DC 2006): 19; Harry De Angelo et al., "Are Dividends Disappearing?" 72 *Journal of Financial Economics* (2003); *NYT,* Aug. 28, 2006; Krueger, *Measuring Labor's Share;* Mishel et al., *State of Working America,* 258.

[59] Michael Firth, "The Impact of Institutional Investors and Managerial Interests on the Capital Structure of Firms," 16 *Managerial and Decision Economics* (1995); Steven J. Davis et al., "Volatility and Dispersion in Business Growth Rates: Publicly Traded vs. Privately Held Firms," NBER working paper 12354 (2006); Robert A. Moffitt and Peter Gottschalk, "Trends in the Transitory Variance of Earnings in the U.S.," 112 *The Economic J.* (2002) ; Clair Brown, John Haltinger, and Julia, Lane, *Economic Turbulence: Is a Volatile Economy Good for America?* (Chicago 2006); Boyd Black, Howard Gospel, and Andrew Pendleton, "Finance, Corporate Governance, and the Employment Relationship," 46 *Industrial Relations* (2007).

[60] Cass Sunstein, "Social Norms and Social Roles," 96 *Columbia L.R.* (1996); ; Colin Mayer, "Corporate Governance, Competition and Performance," 24 *Journal of Law & Society* (1997); Sanford M. Jacoby, *The Embedded Corporation: Corporate Governance and Employment Relations in Japan and the United States* (Princeton 2005); Susan Strange, *The Retreat of the State* (Cambridge UK 1996); Beth A. Simmons, "The International Politics of Harmonization: The Case of Capital Market Regulation," 55 *International Organization* (2001). On policy autonomy in financial regulation, see Rawi Abdelal, *Capital Rules: The Construction of Global Finance* (Cambridge 2007).

[61] Teresa Ghilarducci. *Labor's Capital: The Economics and Politics of Private Pensions* (Cambridge 1992).

[62] Note that studies do not find an association between the CalPERS governance principles and firm performance, with the exception of low takeover barriers, although the latter finding has been contested. *P & I*, Feb. 6, 1989; Jacoby, "Convergence by Design," 249. Also see note 57, supra.

[63] Sean Harrigan, former president of CalPERS, found out the hard way that SLPFs are not "worker" funds. At the time of his appointment to the CalPERS board by Governor Gray Davis, Harrigan was a union official. He staked out a laborist path for CalPERS during his tenure on its board (1999-2004), which included a stint as board president. But when Harrigan led CalPERS into conflict with California companies such as Disney and Safeway, Governor Arnold Schwarzenegger had him removed from the board.

[64] *P & I*, Feb. 6, 1989; *NYT,* April 1, 1996.

[65] Paul Jarley and Cheryl Maranto, "Union Corporate Campaigns," 43 *ILRR* (1990); Stewart Schwab and Randall Thomas, "Realigning Corporate Governance: Shareholder Activism by Labor Unions," 96 *Mich L.R.* (1998); *P&I*, April 4, 1994; *P&I* Sept. 29, 2003; Teresa Ghilarducci et al., "Labour's Paradoxical Interests and the Evolution of Corporate Governance," 24 *Journal of Law & Society* (1997).

[66] *P&I* April 5, 1993; Thomas Kochan, Harry Katz, Robert McKersie, *The Transformation of American Industrial Relations* (New York, 1986); Schwab and Thomas, "Realigning." Under Secretary Robert Reich, the Labor Department issued guidelines in 1994 that supported activism so long as the benefits to the pension fund outweighed the cost. Department of Labor, Pension & Welfare Benefits Administration, "Interpreting Bulletin 94-2 Relating to Written Statements of Investment Policy Including Proxy Voting Policy" (Washington DC 1994).

[67] Schwab and Thomas, "Realigning." *Houston Chronicle* April 17, 1994; *P&I* April 3, 1995; *NYT* March 12, 1996.

[68] *P&I* April 23, 1998; Trumka in *Wash. Post* April 11, 1997; *Bus. Wk.* Sept. 29, 1997, Dec. 8, 1997.

[69] Interview with Rich Trumka, AFL-CIO, March 26, 2007; *IRRC Corporate Governance Bulletin*, April 2001; *P&I* March 23, 1998; AFL-CIO, *AFL-CIO Proxy Voting Guidelines: Exercising Authority, Restoring Accountablility* (2003); *Bus. Week,* April 15, 1993; Ron Blackwell and Bill Patterson, "The Crisis of Confidence in American Business," draft working paper, March 2003. In 1999, John Sweeney issued a statement opposing Vodafone's hostile bid for Mannesman. "The AFL-CIO," he said, "believes value is created over the long-term by partnerships among all of a corporation's constituents--workers, investors, customers, suppliers, and communities. Mannesman, and the European model of corporate governance under which it is structured, has allowed just those kinds of value creating partnerships to flourish." "Statement by AFL-CIO President John Sweeney on Mannesman Takeover", Nov. 22, 1999; *The Economist* July 14, 2007.

[70] *FT* Jan. 26, 2002; Damon A. Silvers, Testimony, to the U.S. Sen. Comm. on Banking, Housing, and Urban Affairs, "Hearing on Accounting and Investor Protection Issues Raised by Enron and Other Public Companies," 107th Cong., 2d. Sess., March 20, 2002; Skeel, *Icarus,* 175; Blackwell and Patterson, "Crisis of Confidence,"; John C. Coates, "The Goals and Promise of the Sarbanes-Oxley Act," 21 *J. of Econ. Perspectives* (2007). Labor's effort to capitalize on the scandals was momentarily hurt by the revelation that Robert Georgine, a long-time building trades official, personally profited from Ullilco's investment in an IPO for Global Crossing, one of the firms caught up in the scandals. *Bus. Wk.* March 18, 2002.

[71] Schwab and Thomas, "Realigning"; Damon Silvers, William Patterson, and J.W. Mason, "Challenging Wall Street's Conventional Wisdom," in Archon Fung, Tessa Hebb, and Joel Rogers, ed., *Working Capital: The Power of Labor's*

Pensions (Ithaca 2001). Unions affiliated with Change to Win (CTW) have moved in the same direction as the AFL-CIO's. Although Bill Patterson left the AFL-CIO for CTW, good working relationships exist between capital stewardship staff in both federations.

[72] *San Diego Union Tribune,* Jan. 31, 2007. Concerned about declining support for financial and trade openness, the Financial Service Forum, representing the nation's twenty largest financial institutions, recently issued a report urging the government to do more to reduce risk and inequality in U.S. labor markets. Peter Gosselin, *L.A. Times,* Aug. 20, 2007.

[73] *Bus. Wk.* Dec. 28, 2006; *NY Times,* April 8, 2007; Brandeis, *Other People's Money*, 92; AFL-CIO, "Key Votes Survey: How Investment Managers Voted in the 2006 Proxy Season," (2006); *L.A. Times* April 21, 2007; *Atlanta Constitution* June 6, 2007; *Fin. Times* April 1, 2007; quote in *Bus. Wk.* June 11, 2007.

[74] Ibid.; "Key Votes."

[75] Damon Silvers and Michael Garland, "The Origins and Goals of the Fight for Proxy Access," in Lucian Bebchuk, ed., *Shareholder Holder Access to the Proxy Ballot* (Cambridge 2005); Interviews with Ron Blackwell and with Damon Silvers, AFL-CIO, March 26, 2007.

[76] Lucian Bebchuk, "The Myth of the Shareholder Franchise," *93 Va. L.R.* (2007); Silvers interview.

[77] *Daily Deal*, Oct. 20, 2003; Silvers and Garland, "Fight for Proxy Access"; Interview with Daniel Pedrotty, AFL-CIO, March 26, 2007; Trumka interview.

[78] Bebchuk, "The Myth,"; *L.A. Times* Feb. 17, 2003, July 26, 2007; *Fin. Times* April 1, 2007; Conference Board, "2007 Report." The SEC also has proposed doing away with nonbinding shareholder resolutions, which would eliminate advisory votes on executive pay and other issues.

[79] Trumka interview; AFSCME, "Failed Fiduciaries: Mutual Fund Proxy Funding on CEO Compensation," (Wash. DC 2007); Gerald F. Davis and E. Han Kim, "Business Ties and Proxy Voting by Mutual Funds," 85 *J. of Fin. Econs.* (2007).

[80] *Boston Herald*,, Dec. 3, 2002.

[81] *Fin. Times,* March 8, 2005; *NYT* March 17, 2005.

[82] AFL-CIO, "Key Votes"; AFL-CIO, "Retirement Security: How Do Investment Managers Stack Up?" May 11, 2006.

[83] *P&I* Nov. 13, 1989, Feb. 23, 2004, April 2, 2007.

[84] *P&I,* Sept. 9, 2006; *WSJ,* March 3, 2003.

[85] Patrick A. Gaughan, "How Private Equity and Hedge Funds Are Driving M&A," *Journal of Corp. Acctg. and Finance* (2007); *Economist* Feb. 10, 2007; *Bus. Wk.* Feb. 10, 2007, Oct. 30, 2006; *Wash. Post* April 4, 2007; *WSJ*, July, 25, 2007.

[86] Several of CalPERS' PE investments are controversial. In 1993 it entered into its largest-ever PE deal by investing $250 million in Enron's Joint Energy Development (JEDI) limited partnership. After selling the investment back to Enron (actually Chewco) for a large profit, CalPERs made a second investment in 1997 of $156 million in a JEDI fund in 1997. These were the off-book entities that helped cause Enron's collapse. Another sensitive CalPERS investment is in the Carlyle Group, a PE fund of which CalPERS owns 6 percent. Carlyle's main holdings are in the defense industry, where Carlyle is alleged to have profited inside information about the planning of the Afghanistan and Iraq invasions. *San Francisco Gate,* Dec. 2, 2001; *The Nation,* April 1, 2002; *San Francisco Chron.* March 21, 2004.

[87] *P&I* May 4, 1998, Dec. 25, 2000, Sept. 29, 2003, Aug. 21, 2006; Dec. 11, 2006; *WSJ*, Feb. 28, 2007, Aug. 27, 2007; *Buyouts* Aug. 2, 1999; 5-3-99; *Bloomberg* News, Sept. 5, 2007; AFL-CIO, "Investment Product Review: Private Capital," (2002); *Bus. Wk.* Oct. 30, 2006; *Economist* Feb. 10, 2007; *Fin.* Times, Aug. 28, 2006; *Bus. Wk.,* Sept. 17, 2007. State pension plans in 2006 held 4.4 percent of their assets in private equity, a 25 percent increase since 2001. Wilshire Consulting, "Report on State Retirement Systems," (2007).

[88] *Daily Teleg.* Feb. 27, 2007; *The Guardian* March 27, 2007; *P&I* May 14, 2007; TUC, "Private Equity: TUC Evidence to the Treasury Committee Inquiry," (May 2007).

[89] *NYT* Sept. 18, 2005; *Wash. Post* June 10, 2007; *IHT* May 15, 2007; *Labor Notes*, June 2007.

[90] *Workforce Mgt*. May 7, 2007; *The Independent* April 2, 2007; SEIU, "Behind the Buyouts: Inside the World of Private Equity," April 2007; Andrew L. Stern to U.S. House, Committee on Financial Services, May 16, 2007; *Wash. Post* April 4, 2007. Yet another irony: The Chinese government recently purchased a $3 billion stake in Blackstone.

[91] Richard L. Trumka to John White (SEC) and Andrew Donohue (SEC), May 15, 2007 and June 12, 2007; *NYT* May 17, 2007; *Inv. News* May 29, 2007; *Fin. News* May 28, 2007; *Wash. Post* April 4, 2007; Silvers interview; *NYT* Sept. 6, 2007. Slated for future IPOs are PE giants Och-Ziff and Kohlberg Kravis Roberts. As with Blackstone, the AFL-CIO is demanding that the SEC classify these IPOs as investment companies, which means that they would pay corporate, not partnership, tax rates, as called for in the Senate's Baucus-Grassley bill. More stringent legislation is being proposed by Barney Frank and other House members that would tax a manager's carried interest as ordinary income instead of capital gains. However, prospects for quick action in the Senate are fading because of heavy lobbying by PE funds. *LAT* Oct. 10, 2007.

[92] For example, hedge funds own 55 percent of Stelco, a unionized steel producer in Canada, hedge funds. The CEO is a former associate of Wilbur Ross, causing the union to fear that a recent acquisition will lead to pension and job terminations. *Toronto Star,* June 2, 2007.

[93] IMF, *Global Financial Stability Report* (2007): 57; Richard L. Trumka to Senators Richard C. Shelby and Paul Sarbanes, Senate Banking Committee, July 25, 2006; *WSJ* Jan. 26, 2007; *NYT* March 15, 2007; *L.A. Times* July 12, 2007; Henry T.C. Hu and Bernard Black, "The New Vote Buying," 79 *USC L.R.* (2006).
[94] Sanford Jacoby, "Corporate Governance and Society," 48 *Challenge* (2005); John C. Bogle, *The Battle for the Soul of Capitalism* (New Haven 2005).
[95] See, for example, Margaret Blair and Lynn Stout, "A Team Production Theory of Corporation Law," 85 *Virginia L.R.* (1999); Simon Deakin, "The Coming Transformation of Shareholder Value," 13 *Corporate Governance* (2005); Lynn LoPucki, "The Myth of the Residual Owner," 82 *Wash. Univ. L.Q.* (2004); Bruno Amable et al., "New Answers to an Old Question," IZA working paper 2731 (2007).
[96] A sampling of behavioral finance includes: Russell Korobkin and Thomas Ulen, "Law and Behavioral Science: Removing the Rationality Assumption from Law and Economics," 88 *Cal. L.R.* (2000); Andrei Shleifer, *Inefficient Markets: An Introduction to Behavioral Finance* (Oxford, UK 2000); Robert J. Shiller, *Irrational Exuberance* (Princeton 2000); Ray Fisman et al., "Governance and CEO Turnover: Do Something or Do the Right Thing?" SSRN working paper (2005). The institutionalists, too, brought behavioral realism to economic theory. Jacoby, "The New Institutionalism."
[97] Kaplan and Rauh, "Wall Street and Main Street."
[98] Raghuram G. Rajan and Luigi Zingales, *Saving Capitalism from the Capitalists* (Princeton 2003); Marco Pagano and Paolo Volpin, "The Political Economy of Finance," 17 *Oxford Review of Economic Policy* (2001); Robert Kuttner, "Friendly Takeover," *The American Prospect*, March 18 2007; *Bus. Wk.* June 14, 2004; *NYT* Oct. 20, 2006, Dec. 1, 2006.
[99] Rajan and Zingales, "Great Reversals," 18; Enrico C. Perotti and Ernst-Ludwig von Thadden, "The Political Economy of Corporate Control and Labor Rents," 114 *Journal of Political Economy* (2006).
Susan Dynarski and Jonathan Gruber, "Can Families Smooth Variable Earnings?" *Brookings Papers on Economic Activity* (1997), 229-03; David Cutler and Lawrence Katz, "Macroeconomic Performance and the Disadvantaged," *Brookings Papers on Economic Activity* (1991:2), 1-74.
[100] Rajan and Zingales, *Saving* Capitalism, ch. 11; David Soskice, "Reinterpreting Corporatism and Explaining Unemployment: Coordinated and Uncoordinated Economies," in Renatta Brunetta and Carlo Dell'Arringa, eds., *Labour Relations and Economic Performance* (1990); Jonas Pontusson, *Inequality and Prosperity: Social Europe vs. Liberal America* (Ithaca 2005); Dani Rodrik, *Has Globalization Gone Too Far?* (Washington DC 1997): 62-63; Geoffrey Garrett and Deborah Mitchell, "Globalization, Government Spending, and Taxation in the OECD," 39 *European Journal of Political Research* (2001); Kenneth Scheve and Matthew Slaughter, "A New Deal for Globalization," *Foreign Affairs* (2007).
[101] Rajan and Zingales, *Saving Capitalism*, 92; Perotti and von Thadden, "Corporate Control," 169.
[102] Mishel et al., *Working America*, 261.
[103] *NYT* July 15, 2007.

I find that democratic regimes reduce risks for multinational investors, specifically through increasing constraints on the executive. Utilizing qualitative evidence from investors, insurers, and location consultants, I explore the mechanisms linking democratic regimes with lower levels of political risk. Details. Figures. References. Cited by. The Journal of Politics. Volume 70, Number 4October 2008. 4. See Sanford M. Jacoby, Finance and Labor: Perspectives on Risk, Inequality, and Democracy, 30 COMP. Lab. L. & pol'y j. 17, 19-20, 32 (2008).Â RESEARCH AT BOSTON COLL., THE FINANCIAL CRISIS AND PRIVATE DEFINED BENEFIT PLANS 2 (2008), availableat http://crr.bc.edu/images/stories/Briefs/ib-8-18.pdf; Ste-. Vol. 4 no. 2 2009. The legacy of deregulation and the financial crisis. This paper considers the association between financial development and labor-market outcomes such as risk and inequality. The relationship is not straightforwar.Â Politics spurs financial development, which sets in motion countervailing efforts to restrain the effect of finance on inequality and risk. The empirical analysis relies on historical, comparative, and contemporary evidence. Emphasis is given to recent events in the United States: the political origins of contemporary financial development and attempts by organized labor and its allies to re-regulate finance and reshape corporate governance. Keywords: labor, shareholders, financial regulation, pensions, risk, corporate governance, unions, inequality. JEL Classification: D23, D63, G23, G34, J32 This paper considers the association between financial development and labor-market outcomes such as risk and inequality. The relationship is not straightforward, however. It is mediated by politics at the national and corporate levels. Politics spurs financial development, which sets in motion countervailing efforts to restrain the effect of finance on inequality and risk. The empirical analysis relies on historical, comparative, and contemporary evidence. Emphasis is given to recent events in the United States: the political origins of contemporary financial development and attempts by organ