THE MODERN CORPORATION—TWENTY YEARS AFTER*

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AS ONE OF THE "GENERATION ON TRIAL"—just old enough to have felt the full force of the crash of 1929 and the mental and economic chaos which followed—a rereading of Berle and Means' famous book has had a special significance to me. For the "Modern Corporation" was one of the "great" books of the early NIRA period—one of the things "everybody" had to read when I was of the elect. And so it is of special interest to ask how it stands up now.

I confess I find the book, today, very difficult to get my teeth into. It seems to me that its significance to us must have been more in its overtones than its actual content. There are a few basic ideas which seem obvious enough now, a great mass of statistical and legal documentation, and some pages of highly dubious economic analysis. I find it hard to deduce from the text a constructive economic philosophy. But scattered through the book are a number of extravagant statements, and Veblenite echoes, scarcely "proved" by the analysis, but nevertheless intriguing to an iconoclastic and disillusioned generation. And these side reflections and suggestions must have given the book its real "kick"—otherwise I am afraid that I cannot now account for it.

I

The book consists of three main theses of fact constantly combined, repeated, and "proved" over and over again. Two of them still seem correct enough, though Berle and Means put them very strongly. That individual stockholders are apt to have very little control over management in large corporations hardly needs elaborate proof today. Was it really news in 1929? Possibly so. Again, that the interests of management and of stockholders are not always identical is also pretty well established now. Perhaps it too may have been news then, though one wonders. The third main thesis, however, is still a matter of fierce debate. Berle and Means maintained that the "concentration of corporate power" had grown and was increasing. This conclusion has been fiercely challenged even today by

* Berle and Means, The Modern Corporation and Private Property (1933).

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economists as far apart in attitude as M. A. Adelman and George Stigler.[1] Large size, we must recall, is one thing and monopoly another. And certainly there never was a golden age of pure competition.[2]

We cannot here enter into the details of the statistical battle other than to refer the reader to some of the main sources. Let us instead concentrate upon the economic conclusions which were deduced in the original book.

II

From the fact that ownership and management have largely been separated in big corporations, Berle and Means deduced three points: (1) "If all profits are earmarked for the security holder, where is the inducement for those in control to manage the enterprise efficiently,"[3] therefore (2) "*if* (italics mine) profits must be distributed either to the owners or to the control, only a fair return to capital should be distributed to the 'owners'; while the remainder should go to the control as an inducement to the most efficient ultimate management. The corporation would thus be operated financially in the interests of control, the stockholders becoming merely the recipients of the wages of capital."[4] Finally, therefore (3) "the passive property right of today must yield before the larger interests of society. ... [I]t seems almost essential if the corporate system is to survive, that the 'control' of the great corporations should develop into a purely neutral technocracy, balancing a variety of claims by various groups in the community and *assigning* (italics mine) to each a portion of the income stream on the basis of public policy rather than private cupidity"[5]—the authoritarian cat thus at last emerging from the institutional bag![6]

In view of the economic illiteracy then and now existing it is not surprising that the first point should have gotten by. And yet it is extremely easily qualified. The manager who earns large profits for his stockholders will tend to receive a higher salary than the one who does not—because of competition for managerial talent. "Good brains," as Schumpeter remarks, "are desperately rare" and people are willing to pay highly for them. Thus there *is* incentive even if the profits go to the stockholders.[7]

[1] See Adelman, The Measurement of Industrial Concentration, 33 Rev. of Econ. & Stat. 269 (1951); Stigler, Five Lectures on Economic Problems (1949).

[2] Cf. Wright, Toward Coherent Anti-Trust, 35 Va. L. Rev. 665 (1949).

[3] Berle and Means, The Modern Corporation and Private Property 343 (1933).

[4] Ibid., at 344. [5] Ibid., at 356.

[6] I say "authoritarian" for the sentence clearly seems to me to imply the possibility of the rule of a managerial elite who from their *own* ethical standards will "assign" income shares. Incidentally, how is this elite to be selected?

[7] One can still argue over relative adequacy. But Berle and Means are far more sweeping.

The second point is a bit more confusing and may possibly be rendered correct "by definition." If by a "fair wage" of capital one means the amount necessary to call forth *adequate, risk-bearing* capital under the *special* circumstances of each case, then the principle is not wholly wrong, though the special claim of management to surplus elements—rather than any other group—is not immediately evident.[8] But if by "fair wage" one means merely some fixed arbitrary "reasonable" amount—say five per cent—uniformly applied to the shareholders of all corporations regardless of risk, then the results may be very bad from the point of view of society *as a whole* even if the *particular* stockholders happen to be kept quiet. Full evaluation of this problem involves a more careful understanding of the risk-growth dilemma, and this we will take up shortly.

Point number three, to conclude our summary, contains the greatest number of ambiguities. There has not been a reputable economist from Adam Smith on down who did *not* believe that the passive interests of property had to yield to the "larger interests of society" in some cases. In the most ultimate sense, indeed, property rights have *always* been considered subordinate even by the most orthodox. For the orthodox classical economists merely felt that the "larger interests of society" *were* best served, in a number of cases, and in particular surroundings, by protecting property rights. Now what cases and in what surroundings calls for more discussion. But the paramountcy of the *social* welfare in an ultimate sense was never challenged.

On the other hand, however, the mere paramountcy of the social interest is not *ipso facto* a self-evident reason for establishing the rule of an authoritarian group of managers to dole out income payments to this or that group as suits or seems fair to them—no matter how high-minded such managers may be. The second sentence of point (3) I have quoted is obviously an echo of Thorstein Veblen's "Engineers and the Pricing System," of institutional economics, and of technocracy, and to evaluate Veblenism one must again recur to the growth-risk problem. Accordingly we will now turn our attention to that.

III

The writer has long maintained that the fundamental weakness of much left wing thought, especially of Marxism and Veblenism, lies in a failure to understand the problem of economic growth, and before we go any

[8] I say "surplus" for by definition anything over a "fair wage" for both groups must be a surplus.

further let us run over the essentials of that problem as simply and as noncontroversially as possible.[9]

The essential problem of economic growth is that it both comes through change *and* causes change. The change is of three types. In the first place simple expansion, *in and of itself*, will change the *kinds* of goods demanded and the *proportions* in which they are wanted. It is an old Marxian superstition that the pattern of consumer wants only changes when some business man puts on an advertising campaign. Not at all. There would be unpredictable, unsymmetrical changes even if there were never an advertisement permitted. For the man who has lived in one small house will not simply live in two small houses. The man who has drunk one bottle of beer a day will not simply drink a barrel of beer a day. They will spontaneously "redesign" their tastes with growing economic welfare.

A second type of change is also the passive result of simple expansion. Mere growth entails a redesigning of machinery. To build a boat twice as big as the one you have, you can't just take the existing blue print and multiply *everything* by two. An alteration in size may mean a shift in the direction and relative intensity of the forces involved. This type of change is something different from invention. It means merely that, on the basis of *existing* technical knowledge, plant, equipment, and the labor force must be shifted and reorganized as output is increased.

But finally there is the third type of change involved in new inventions —which, over the long pull, are integral parts of the growth process. Without new inventions the law of "diminishing returns" sets in, and it becomes more and more difficult to coax an increase in output.

The crucial point to remember about all this is that the growth process entails at the very least an inevitable minimum of *psychological* insecurity. As we shift technique we must shift and retrain people. And there is no guarantee that those who are being shifted and retrained will always find equally important and equally congenial work in parts of the country that suit them! Full employment for the country doesn't mean security for the individual. The idea that equal money income plus planning will avoid pressure groups is, I have often said, the bastard offspring of "economic man." It springs from an unbelievably narrow view of human motivation. This point is elaborated and documented in the first chapter of the writer's *Capitalism*.[10] The free development of the man with the new idea cannot

[9] For documentation and further explanation of the analysis of this section, see Wright, Capitalism, c. I (1951).

[10] Ibid.

be the condition for the free development of the man who wishes to keep on in the old routine.

IV

We thus see that modern radical, and, indeed, much liberal thought suffers from a split personality. If "continuity" and serene routine are to be our highest values then we cannot have economic growth. Nor can we permit our scientists to make practical use of their discoveries. Nor can we allow independent opportunity to individuals—for if we do allow independent opportunity we will find someone "rocking the boat" by trying to introduce some new idea. A technological inquisition, as in Samuel Butler's *Erewhon*, is essential.

For this reason the writer has often pointed out that Veblen's attitude toward technical change is highly inconsistent. He at once blames the business man for *not* using new methods and at the same time criticizes him for interrupting the *continuity* of production. Whether Veblen ever quite recognized the fact or not his real goal is a *stationary* society ruled by Platonic guardians. Such a goal (from my point of view, fortunately) is not yet the aim of most Americans. The writer's *Democracy and Progress* gives some of the difficulties involved.[11]

V

It is time to pull together our argument and explain why "The Modern Corporation" no longer seems to me convincing. As explained in *Democracy and Progress* just referred to, the writer's basic values are neither those of the pig, the epicurean, nor the yogi, but the *artist!*[12] And startling though it may be to say so, I suggest that there is a certain fundamental similarity of temperament between the artist, the scientist, and the active businessman (entrepreneur, in Schumpeter's special language). For all three of them are believers in satisfaction *through activity*, and through the *creation of novelty*. Capitalist cultures have helped to foster work of this sort because by their competitive decentralization no single massive "official" school of art, or science, or technology has been able to obtain control and force art and science into a strait jacket as was done by the Nazis and is now being increasingly done in Communist Russia. But this emphasis upon novelty-creation, and Whiteheadian "adventure" cannot

[11] Wright, Democracy and Progress at 23 especially (1949); see also Wright, Capitalism, c. IV (1951).

[12] Wright, Democracy and Progress (1949).

be combined with perfectly continuous process.[13] I believe that we can maintain a reasonable degree of aggregate stability but, as already explained, this does not mean security in routine for all individuals.

The question next arises whether the emergence of some large scale business and some owners who do not control makes the values just stated unattainable under modern conditions. It is submitted that it does not. Much liberal thought is hopelessly mixed up by the confusion of *fluidity* with *equality*. Adequate competition does not necessarily imply a mere swarm of little business of equal size.[14] It implies some big business, some middle sized business, and some little business and a reasonable amount of bankruptcy and turnover.

Now to bring our argument down to earth, and to the terms of Berle and Means' book, the adventurous technological progress which is the core of capitalism must imply a willingness to run risks. Furthermore this willingness must exist not *merely* on the part of the managers but also on the part of the lenders. A society in love with smooth routine, and heavily loaded with bonded debt, is not likely to show the requisite vigor. And when disturbances come—and *some* disturbances are obliged to come, short of absolutely centralized economic despotism, and probably even then—such a society is likely to be very unadaptable and vulnerable.

Now the fact that a few big firms keep running "automatically" does not mean that we will necessarily find ourselves having an adequate *margin of risky new expansion and turnover*. Today we hear a constant complaint regarding the shortage of "equity capital," i.e., risk-taking stockholders. This shortage, I submit, comes directly from policies which we have adopted, based directly upon reasoning similar to that of Berle and Means, and founded upon the idea that the risk-bearing stockholder has little function and deserves little respect. I refer to the double and triple taxation of corporate profits, to the attempts of the unions to restrict them to some conventional minimum and so on. "Risk, Uncertainty and Profit," in the words of a great Chicago professor, still go together. And when we take out one, we should not be surprised to find the others suffering too. The fact that *some* corporations continue to run with little profit for shareholders does not mean that *as many* risk-bearing investors can be found as we need; it may even be the reason why they cannot be found.

[13] Whitehead, Adventures of Ideas, c. V (1933).

[14] Wright, Some Pitfalls of Economic Theory as a Guide to the Law of Competition, 37 Va. L. Rev. 1083 (1951).