RESPONSE

WEAK SOLUTIONS TO AN ILLUSORY PROBLEM

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In response to Lucian A. Bebchuk & Jesse M. Fried, *Paying for Long-Term Performance*, 158 U. PA. L. REV. 1915 (2010).

In *Paying For Long-Term Performance*, Professors Bebchuk and Fried describe how equity-based compensation in the United States should do a better job of tying top executive pay more closely to long-term performance.[1] The primary assumption the authors and their proposals make is that "standard executive pay arrangements . . . lead[] executives to focus excessively on the short term . . . at the expense of long-term value[,]"[2] and do in fact "reward[] executives for short-term gains that do not reflect long-term performance."[3] They also heavily reference the financial crisis as a motivation for improving compensation.[4]

The recommendations and the article have two major shortcomings. First, Bebchuk and Fried provide little evidence to support their motivating assumption that executive-pay practices reward executives for short-term results that do not reflect long-term performance. One of the "authorities" they cite is Secretary of the Treasury Timothy Geithner,[5] who is not known for his expertise on corporate gover-

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[1] Lucian A. Bebchuk & Jesse M. Fried, *Paying for Long-Term Performance*, 158 U. PA. L. REV. 1915, 1915-16 (2010).

[2] *Id.* at 1917.

[3] *Id.* at 1916.

[4] *See, e.g.*, *id.* at 1956 ("In the aftermath of the financial crisis of 2008–2009, there is a growing recognition among firms, investors, and public officials that equity-based compensation awarded to the top executives of public firms should be tied to long-term results.").

[5] *See, e.g.*, *id.* at 1917 (noting Geithner's urging of corporate boards to structure

nance (or taxation). In reality, there is a great deal of evidence that top U.S. executives are paid for good long-term performance and penalized for poor long-term performance. This is true for firms in general—nonfinancial and financial. Even the claim on which Bebchuk and Fried focus—that top executive compensation was a first-order cause of the financial crisis[6]—is not supported by the evidence.

Second, Bebchuk and Fried tend to overstate the benefits of their proposals while understating the costs. Because top executive pay is already effectively tied to long-term performance, the Bebchuk and Fried proposals, at best, provide marginal improvements to a system that already works well. At the same time, they ignore the additional costs. Their proposals require executives to bear more risk (from a lack of diversification) and are likely to dissuade some of the most talented executives from taking jobs at public companies in the first place. This would be particularly true for top executives who can work for private-equity-funded companies (which do not impose such restrictions) as well as for lawyers who can choose between a law partnership and a general-counsel job. In many cases, the costs of the Bebchuk and Fried proposals likely exceed the benefits.

In this Response, I expand on my arguments and present substantial empirical evidence to support them. Part I assesses the assumption that executive pay practices, in general, reward executives for short-term results that do not reflect long-term performance. Part II assesses whether the assumption holds for financial firms and whether compensation was a first-order cause of the financial crisis. Part III considers whether the Bebchuk and Fried proposals improve on existing compensation arrangements. The last Part concludes.

I. ARE EXECUTIVES REWARDED FOR GOOD AND PUNISHED FOR POOR LONG-TERM PERFORMANCE?

Bebchuk and Fried claim that "standard executive pay arrangements . . . lead[] executives to focus excessively on the short term . . . at the expense of long-term value[,]"[7] and in fact "reward[] executives for short-term gains that do not reflect long-term performance."[8] They do not present empirical evidence that this is the case. Rather, they rely on statements from public officials like Geithner and Special

compensation with an eye to long-term performance).

[6] *Id.*

[7] *Id.* at 1917.

[8] *Id.* at 1916.

Pay Master Kenneth Feinberg,[9] who can hardly be considered serious scholars of corporate governance.

If Bebchuk and Fried are correct, there should not be much of a relation between long-term stock performance and the pay that top executives realize in a particular year. Joshua Rauh and I posed this exact question and found that, in reality, there is a strong relationship between top executive pay and long-term stock performance.[10]

Rauh and I took all the firms in the Standard & Poor's ExecuComp database and sorted them into five groups based on size (assets) for each year from 1999 to 2004.[11] There are more than 1600 public companies in the ExecuComp database in any particular year.[12] We sorted based on size, because it is well established that pay is tied to firm size.[13] Within each size group for each year, we sorted the CEOs into five groups based on how much compensation they actually realized—salary, bonus, restricted stock, and exercised options.[14] It is worth mentioning that this measure of pay includes gains or losses from any of the gaming Bebchuk and Fried describe.[15] We then looked at how the stocks of each group performed relative to their industry over the previous one, three, and five years.[16]

Actual compensation was highly related to firm stock performance over all three periods. Firms with CEOs in the top quintile of actual pay were the top-performing quintile relative to their industries in every size group.[17] Firms with CEOs in the bottom quintile of actual pay were the worst-performing quintile relative to their industries in every size group.[18] And the magnitudes of the performance differences are large.[19] Figure 1 (Figure 3 in the paper) presents the results graphically for three years of performance. The results are graphical-

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[9] *Id.* at 1917-18.

[10] *See* Steven N. Kaplan & Joshua Rauh, *Wall Street and Main Street: What Contributes to the Rise in the Highest Incomes?*, 23 REV. FIN. STUD. 1004, 1043-45 (2010).

[11] *Id.* at 1044.

[12] *See id.* at 1008 (noting that there were 1747 companies in the database in 1994 and 1722 in 2004).

[13] Xavier Gabaix & Augustin Landier, *Why Has CEO Pay Increased So Much?*, 123 Q.J. ECON. 49, 50 (2008).

[14] Kaplan & Rauh, *supra* note 10, at 1008.

[15] *See* Bebchuk & Fried, *supra* note 1, at 1936 (defining gaming as "springloading, selling on private information, and manipulating the stock price").

[16] Kaplan & Rauh, *supra* note 10, at 1044.

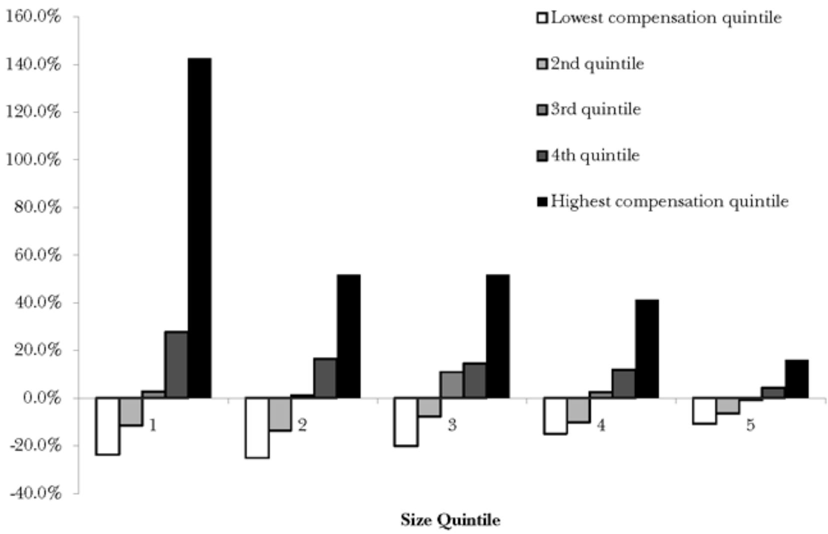
[17] *Id.* at 1044-45.

[18] *Id.* at 1045.

[19] *See id.* at 1044-45 (noting that firms with CEOs in the top quintile of compensation outperform their industries by 61% on average).

ly, qualitatively, and statistically identical for five years[20]—*a period that most would characterize as long-term.*

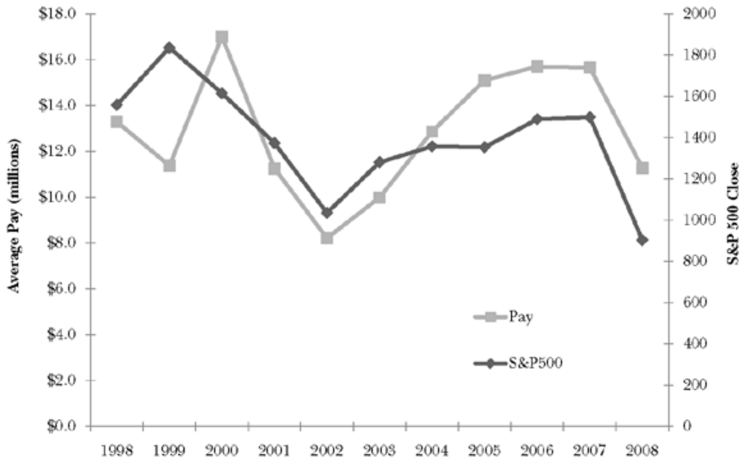
FIGURE 1: THREE-YEAR PERFORMANCE RELATIVE TO VALUE-WEIGHTED INDUSTRY (CEOS ONLY)



The previous analysis is across firms within a given year. It also is possible to see the relationship across time. Figure 2 presents the average pay realized by S&P 500 CEOs (adjusted for inflation) against the level of the S&P 500 from 1998 to 2008. It is difficult to miss the strong relationship between pay and the overall stock market.

[20] *See also* Gian Luca Clementi & Thomas F. Cooley, *Executive Compensation: Facts* 13-15 (Nat'l Bureau of Econ. Research, Working Paper No. 15426, 2009) (finding qualitatively similar results). A recent *Wall Street Journal* article also reaches a similar conclusion. *See* Scott Thurm, *Measuring Bang for the Buck: Best-Paid Corporate Chiefs Tend to Deliver Above-Average Shareholder Returns*, WALL ST. J., Apr. 1, 2010, at B5.

FIGURE 2: REALIZED CEO PAY AGAINST THE S&P 500 (INFLATION-ADJUSTED)



The Bebchuk and Fried analysis also assumes that CEOs are not penalized much for poor performance. Jenter and Lewellen studied this issue by examining CEO turnover for companies in the S&P ExecuComp database and found that boards aggressively fire CEOs for poor performance.[21]

For example, in a CEO's first five years, 59% of CEOs in the bottom quintile of industry-adjusted stock performance (over those five years) lose their jobs, compared to 17% of CEOs in the top quintile of performance.[22] Jenter and Lewellen find similar results for the fourth quintile versus the second quintile, with 51% of CEOs in the fourth quintile turning over, compared to 20% in the second quintile.[23]

The penalty for poor performance is even greater in companies with what Jenter and Llewellen refer to as "higher quality" boards—smaller boards with fewer insiders and higher board stock ownership. CEO turnover is 83% in the bottom quintile versus 10% in the top quintile.[24]

The result for higher-quality boards is particularly interesting because boards have gotten smaller and have included fewer insiders

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[21] Dirk Jenter & Katharina Lewellen, Performance-Induced CEO Turnover 18-26 (Feb. 2010) (unpublished draft), *available at* http://www.stanford.edu/~djenter/CEO_Turnover_February_2010.pdf.

[22] *Id.* at 26.

[23] *Id.* at 36 fig.2.

[24] *Id.* at 37 fig.3.

over the last twenty years, suggesting that governance has improved.[25] Again, the performance measure is not short-term stock performance, but performance over a five-year period.

To summarize the results in this Part, there is strong evidence that CEOs are compensated—both positively and negatively—for long-term stock performance.

II. Did Poor Top-Executive Incentives Precipitate the Financial Crisis?

Bebchuk and Fried propose their solutions for two types of firms—financial and nonfinancial. Their motivation, however, focuses heavily on financial firms and the financial crisis. Bebchuk and Fried claim that the financial crisis has led to "widespread recognition that pay arrangements that reward executives for short-term results can produce incentives to take excessive risks."[26] The previous Part argued that there is little evidence that this is a systemic problem for firms in general. In this Part, I argue that it is even questionable whether poor top-executive incentives at financial firms played an important role in precipitating the financial crisis.

The poor-pay-practice explanation for the financial crisis implies that "[t]op bank executives were rewarded for short-term results with large amounts of up-front cash pay," "[b]ank executives did not hold sufficiently large amounts of stock to align their interests with those of shareholders," and "[e]xecutives with more short-term pay and less stock ownership should have had the greatest incentive to take bad and excessive risks, and, so, should have performed worse in the crisis."[27]

Fahlenbrach and Stulz tested these implications by studying the CEOs of almost 100 large financial institutions from 2006 to 2008.[28] In 2006, the mean CEO took home $3.6 million in cash compensation

[25] *See also* Steven A. Kaplan & Bernadette A. Minton, *How Has CEO Turnover Changed? Increasingly Performance Sensitive Boards and Increasingly Uneasy CEOs* 25 (Nat'l Bureau of Econ. Research, Working Paper No. W12465, 2008), *available at* http://papers.ssrn.com/sol3/papers.cfm?abstract_id=924751 (finding a stronger relationship between turnover and performance than previous empirical studies).

[26] Bebchuk & Fried, *supra* note 1, at 1917.

[27] Steven N. Kaplan, *Should Banker Pay Be Regulated?*, THE ECONOMIST'S VOICE, Dec. 2009, at 1, http://www.bepress.com/ev/vol6/iss11/art6/ .

[28] Rüdiger Fahlenbrach & René M. Stulz, *Bank CEO Incentives and the Credit Crisis* (Ohio St. U. Working Paper No. 2009-03-013, 2009).

(representing less than half of total compensation).[29] The larger share of pay was in restricted stock and options. At the same time, the mean CEO held $88 million worth of the firm's equity and options.[30] In other words, the average CEO took home $3.6 million in cash while leaving more than twenty-four times as much money in his or her firm. It seems unlikely that up-front cash pay provided much of an incentive for the average CEO to knowingly take bad or excessive risks that would jeopardize his or her much larger equity stakes and his or her job. CEOs lost a great deal in the crisis. *From 2006 to 2008, the average CEO lost $31 million in stock value, dwarfing any gains from cash compensation. CEOs lost large amounts on their options as well.*[31]

These (and additional) results lead Fahlenbrach and Stulz to conclude that bank "CEO incentives . . . cannot be blamed for the credit crisis or for the performance of banks during that crisis."[32]

Kevin Murphy presents a similar analysis for TARP and non-TARP banks, as well as quantitatively similar results, in his Congressional testimony.[33]

David Yermack agrees that many prominent financial executives lost "small fortunes" in 2008.[34] He adds that "farther down the ladder, most mid- and upper-level managers of financial companies also lost a significant amount of their net worth in 2008."[35] Yermack concludes that "[t]he recent scrutiny of executive pay seems to stem from an odd mix of envy and vengeance, unsupported by facts or theories."[36]

Murphy and Yermack, noted researchers on CEO pay, have written articles highly critical of specific CEO compensation practices. Nevertheless, their conclusions on the relation of CEO pay to the financial crisis are diametrically opposed to those of Bebchuk and Fried.

Benjamin J. Keys et al. studied mortgage loan origination and "d[id] not find any relationship between the quality of loan originations and top management incentives."[37] Instead, they found that "a proxy of relative power of the risk manager is associated with loans

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29 *Id.* at 34 tbl.3.

30 *Id.*

31 *Id.* at 24.

32 *Id.* at 25.

33 *Compensation Structure and Systemic Risk: Hearing Before the H. Comm. on Fin. Servcs.*, 111th Cong. 3-10 (2009) (testimony of Kevin J. Murphy, Chair in Finance, University of Southern California, Marshall School of Business).

34 David Yermack, *Keeping the Pay Police at Bay*, WALL ST. J., Oct. 11–12, 2009, at W1.

35 *Id.*

36 *Id.*

37 Benjamin J. Keys et al., *Financial Regulation and Securitization? Evidence from Subprime Loans*, 56 J. MONETARY ECON. 700, 719 (2009).

that have lower default rates." They interpreted this result to suggest "that the moral hazard problem is less severe for lenders in which the risk management department has greater bargaining power within the firm."[38]

To be fair, one paper is modestly favorable to Bebchuk and Fried. Cheng, Hong, and Scheinkman studied whether short-termism leads to excessive risk taking in financial firms.[39] Partially because the traditional and intuitive measure of incentives Fahlenbrach and Stulz use is not correlated with excessive risk, Cheng et al. created a somewhat complicated and unintuitive measure of residual compensation. They found that financial firms that paid higher residual compensation had modestly higher stock volatility and lower stock returns from 2001 to 2008.[40] The results on returns were driven largely by insurance firms.[41] Even in their conclusion, however, Cheng et al. were not willing to agree with the Bebchuk and Fried assumption and concluded that the modest relationship was not necessarily causal.[42]

Bebchuk and Fried do not mention any of these studies that fail to support their assumptions. Rather, the only relevant evidence they cite is from Bebchuk, Cohen, and Spamann: that executives at Bear Stearns and Lehman cashed out almost $2 billion of equity from 2000 to 2008, an amount (slightly) greater than the value of their holdings at the start of 2008.[43] The inference they intend to make is that the Bear Stearns and Lehman executives knowingly behaved in a short-term manner and were able to cash out.

Unfortunately, that analysis leaves out one extremely important detail—taxes. Most compensation in those firms was in the form of restricted stock. When restricted stock vests, the executive owes taxes on the award. For New York residents (including many of the executives), the combined federal and state marginal tax rate over this period was well over 40% and as high as 50%.[44] Is it surprising then, that

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[38] *Id.*

[39] Ing-Haw Cheng, Harrison Hong & Jose A. Scheinkman, *Yesterday's Heroes: Compensation and Creative Risk-Taking* 1 (Nat'l Bureau of Econ. Research, Working Paper No. 16176, 2010).

[40] *Id.* at 3.

[41] *Id.* at 15-16.

[42] *Id.* at 28.

[43] Lucian A. Bebchuk, Alma Cohen & Holger Spamann, *The Wages of Failure: Executive Compensation at Bear Stearns and Lehman 2000–2008*, 27 YALE J. ON REG. 257, 267-73 (2010).

[44] The top federal tax rate was 39.6% in 2000, 39.1% in 2001, 38.6% in 2002 and 35% from 2003-2008. TAX FOUND., U.S. FEDERAL INDIVIDUAL INCOME TAX HISTORY, 1913–2010 (2010), http://www.taxfoundation.org/publications/show/151.html. The Medicare tax rate is

the executives sold a little more than 50% of their shares over the period? A large fraction of those sale proceeds undoubtedly went to pay taxes.

To see this, suppose that an executive is awarded $100 million in restricted stock. When the award vests, the executive owes $45 million in taxes. Now, let's say the executive sells $50 million of the $100 million vested stock. In that case, $45 million would go to pay taxes and the executive would retain $5 million in cash. At the same time, the executive would still hold $50 million in vested stock. Net of taxes, then, the executive still has an extremely strong incentive to maximize long-term shareholder value. Her remaining stock is worth ten times the cash she has realized.

The Bebchuk et al. analysis inexplicably ignores taxes. They assume that the executive gets to keep the $50 million he sold (*not the $5 million the executive really ends up with*) while retaining $50 million in stock. In their analysis, the executive has an incentive to take risks because he takes a lot of money out of the company.[45] By ignoring taxes, Bebchuk and Fried greatly overestimate the amount of money executives actually realize. At a 45% tax rate, they overestimate the amount by a factor of ten.

In other words, an after-tax analysis would likely find that the Bear Stearns and Lehman executives' after-tax realizations from stock sales were on the order of 10% of what they lost on their remaining shares—not the roughly equal amount claimed by Bebchuk et al. This, by the way, is a general point applicable to the entire Bebchuk and Fried analysis. In ignoring taxes, they overstate the extent of the problem.

If front-loaded incentives did not play a major role in the crisis, what did? Taylor points to the highly expansionist monetary policy in the years leading up to the crisis.[46] Diamond and Rajan cite the so-called capital glut—large inflows of external capital from much of the

1.45% for employees and 2.9% for people who are self-employed. Social Security Online, http://www.ssa.gov/OACT/ProgData/taxRates.html (last visited Oct. 18, 2010). As of February 1, 2010, the New York State top marginal tax rate was 6.85% to 7.7%. TAX FOUND., STATE INDIVIDUAL INCOME TAX RATES, 1913-2010 (2010) http://www.taxfoundation.org/taxdata/show/228.html. In 2009, the New York City top marginal tax rate was 3.65%. NYC Finance, http://www.nyc.gov/html/dof/html/services/business_tax_nys_income.shtml (last visited Oct. 18, 2010).

[45] *See* Bebchuck et al., *supra* note 43, at 271 (characterizing the value of remaining shares for Bear Stearns and Lehman executives as "relatively modest" and "non-existent" respectively).

[46] *See* John B. Taylor, *The Financial Crisis and the Policy Responses: An Empirical Analysis of What Went Wrong* 2-5 (Nat'l Bureau of Econ. Research, Working Paper No. 14631, 2009) (noting deviations by the Federal Reserve from traditional monetary policies employed during long periods of strong growth).

developing world.[47] Calomiris highlights the role that the political system played in inflating the banking sector and real estate prices, particularly the subprime sector, through mandates implemented by Fannie Mae, Freddie Mac, and others to promote low-income housing.[48] Ruling out compensation practices hardly leaves us at a loss for culprits in the recent debacle.

In sum, Bebchuk and Fried's claim that short-term top executive incentives led to excessive risk taking and strongly contributed to the financial crisis is not supported by the preponderance of the empirical evidence. At best, it is debatable.

III. DO THE BEBCHUK-FRIED PROPOSALS DELIVER BENEFITS IN EXCESS OF COSTS?

In the first two Parts, I presented evidence that the problem Bebchuk and Fried assume is overstated. Top executive compensation and turnover are, in fact, tied to long-term performance. As a result, adopting the Bebchuk and Fried proposals can provide, at best, modest marginal benefits to the existing governance arrangements that already work well. At the same time, their proposals also impose additional costs. This Part weighs the marginal benefits of the recommendations against the potential costs. Bebchuk and Fried make recommendations in three general areas: unwinding, hedging, and timing. I address each area below.

A. *Unwinding*

Bebchuk and Fried recommend that executives should be restricted from unwinding equity-based awards and allowed to do so only gradually after vesting, subject to aggregate unwinding limitations. The idea is to make sure that executives have incentives to focus on the long-term stock price.

Such restrictions might make sense for some executives at some companies. But that Bebchuk and Fried claim a benefit fails to estab-

[47] *See* Douglas W. Diamond & Raghuram Rajan, *The Credit Crisis: Conjectures About Causes and Remedies* 2 (Nat'l Bureau of Econ. Research, Working Paper No. 14739, 2009) (explaining that many emerging-market countries became net lenders of capital during the late 1990s).

[48] *See* Charles Calomiris, *Banking Crises and the Rules of the Game* 55 (Nat'l Bureau of Econ. Research, Working Paper No. 15403, 2009) (suggesting that housing policies exacerbated incentives for subprime risk taking).

lish that there is a marginal benefit to this policy—and ignores the potential costs.

First, Bebchuk and Fried argue that by reducing unwinding, firms will not have to replenish equity grants and therefore can pay their executives less.[49] This makes no sense in a world where there is a functioning market for top executives. Top executives will see to it that they are paid the going market wage. It is not clear there is any marginal benefit here.

Second, they acknowledge that many companies now impose some type of ownership guidelines on top executives.[50] They criticize these other ownership guidelines as ineffective, but do not provide any supporting evidence. For example, Bebchuk and Fried criticize the guideline that executives must hold stock worth a multiple of their annual compensation. They argue that these requirements are often too low and cite Procter & Gamble and Verizon as requiring their CEOs to hold too little company equity.[51] But even those two specially chosen examples contradict the Bebchuk and Fried criticisms. The CEO of Procter & Gamble, A.G. Lafley, in fact, owned more than $100 million in stock and options[52] while the CEO of Verizon, Ivan Seidenberg, owned more than $60 million.[53] For both, the ownership stakes arguably provided substantial incentive to manage for the long term. It is hard to see much of a marginal benefit to making it more difficult to unwind those positions than it already is.

Bebchuk and Fried also criticize guidelines that require executives to hold a certain amount of stock until retirement.[54] They argue that this may encourage executives to retire early.[55] While this may matter in a small number of cases, it is not clear that it matters much. More importantly, it is not clear the Bebchuk and Fried proposal is any better. By requiring executives to remain undiversified for a long time, the Bebchuk and Fried solution also gives executives strong incentives to leave their current employers to work elsewhere. Under their proposal, a job-switching executive obtains the same total compensation,

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[49] Bebchuk & Fried, *supra* note 1, at 1933.

[50] *Id.* at 1934.

[51] *Id.* at 1934-35.

[52] Procter & Gamble Co., Definitive Proxy Statement (Schedule 14A), at 42 (Aug. 28, 2009).

[53] Verizon Commc'ns, Inc., Definitive Proxy Statement (Schedule 14A), at 43 (Mar. 23, 2009).

[54] Bebchuk & Fried, *supra* note 1, at 1925-28.

[55] *Id.* at 1927.

obtains diversification, and probably is able to unwind more quickly from his or her first company.

Furthermore, the Bebchuk and Fried pay proposals—increasing the period between the time stock is issued as compensation and the time it can be sold net of taxes[56]—would not have stopped the executives at Bear Stearns, Lehman, Merrill, and elsewhere from selling many of their shares before the crisis. As I mentioned above, a large fraction of the selling by those executives was likely driven by tax payments which Bebchuk and Fried acknowledge are allowed under their proposal. Under the Bebchuk and Fried proposals, many of the executives—Cayne (Bear Stearns), Fuld (Lehman), and Lewis (Bank of America)—would have been eligible to sell a substantial amount of their remaining equity because they had long tenures and received large amounts of restricted stock and options in the 1990s and 1980s.

The foregoing argues that there is unclear or little marginal benefit to the Bebchuk and Fried unwinding proposals over current practice. In addition, there are (at least) two important costs to the proposals that Bebchuk and Fried do not mention.

First, as already mentioned, the unwinding proposals (and to some extent the timing proposals) make it more difficult for executives to diversify their personal portfolios. This imposes additional (but difficult to quantify) costs on the executives. One suspects some executives would choose to diversify by going to work for other companies.

Second, it also seems likely that the restrictions would dissuade some of the most talented executives from taking jobs at public companies in the first place. This would be particularly true for top executives who can work for private-equity-funded companies (which do not impose such restrictions upon exit) and lawyers who can choose between a law partnership and a general counsel job.

On the whole, then, Bebchuk and Fried fail to make a convincing case that their unwinding proposals improve much, if at all, upon current practice.

B. Hedging

Bebchuk and Fried recommend that top executives be restricted from hedging their equity positions.[57] This recommendation is sensible but, again, addresses a problem that hardly exists. The net benefit

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[56] *Id.* at 1928-30.
[57] *Id.* at 1954.

is negligible. Bebchuk and Fried claim that "[a] recent empirical study by Bettis, Bizjak, and Kalpathy confirms the significance of the problem."[58] The fact is that Bettis et al. confirm the opposite: very few companies now allow their top executives to hedge. To see this, one has only to look at table 1 of Bettis et al. In 2005 and 2006, the last two years they studied, an average of fewer than fifty firms each year allowed their executives to hedge.[59] And roughly 20% of those hedges used exchange funds that the authors find have no negative timing attributes.[60] The paper, therefore, finds potentially costly hedging behavior in roughly forty public firms a year out of the more than 5000 companies publicly traded on U.S. exchanges. This is a rate of less than 1%. I would not call this significant.

C. Timing

Bebchuk and Fried recommend making it more difficult for top executives to affect the timing of equity-based grants and equity-based realizations.[61] Those recommendations are sensible and do not have any obvious costs. But many companies already follow these recommendations, suggesting there is a small marginal benefit to existing practices. Many companies award options at set dates. Many require equity sales to occur over time through 10b5-1 plans. Fewer companies appear to require predisclosure of such sales. To the extent companies do not follow these recommendations yet, they are well advised to consider them.

CONCLUSION

On the whole, the Bebchuk and Fried proposals address a problem that is already largely solved. Boards and compensation committees already pay a great deal of attention to motivating top executives to manage for long-term shareholder value. Accordingly, most firms already implement policies that deliver most of the benefits of the Bebchuk and Fried proposals. This is reflected in the strong empirical relation of top executive compensation and turnover to performance—a relation Bebchuk and Fried do not acknowledge.

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[58] *Id.* at 1951 (citing Carr Bettis, John Bizjak & Swaminathan Kalpathy, Why Do Insiders Hedge Their Ownership and Options? An Empirical Examination (Mar. 2010) (unpublished manuscript), *available at* http://ssrn.com/abstract=1364810.

[59] Bettis et al., *supra* note 58, at 53 tbl.1.

[60] *See id.* at 6 ("[T]he evidence suggests that exchange funds are more likely to be used purely as a diversification strategy.").

[61] Bebchuk & Fried, *supra* note 1, at 1937-41.

The cost of these proposals (and articles like Bebchuk and Fried's) is that they continue to treat CEOs and boards with more skepticism and hostility than is justified by the empirical evidence. That hostility diffuses to the media and the political arena, where it can have real and negative effects in leading to costly and unnecessary regulations. Although it is difficult to quantify, there also can be little doubt that the hostility dissuades able executives from taking on top executive roles at public companies.

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