The Transfer of Control in Large Corporations: 1912-19 (Summary)

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Writing in 1905, *Wall Street Journal* editor Sereno S. Pratt found large American corporations "subject to autocratic or oligarchic control" and that "it is not difficult for a small group of financiers to dominate properties worth billions" [11, p. 6704-05]. Twenty-five years later, A. A. Berle and Gardner C. Means found control "ultimately [lay] in the hands of management itself" [1, p. 124]. While all agreed that corporate control has become separated from formal ownership, they disagreed as to whether financiers or managers had succeeded shareholders. Underlying the disagreement was an explicit sequence in the transfer of corporate control. Pratt found a transfer from owners to financiers while Berle and Means assumed one from owners to managers. If, in fact, the sequence encompassed owners, financiers, and managers, then the disagreement loses much of its substance and can be explained as the evolution of corporate control rather than by fundamental empirical differences.

While profuse documentation exists on the separation of ownership from control [1, 4, and 8], little attention has been devoted to the process by which control was transferred from one group to another, apparently because the transfer was assumed to be a mere internal power shift. However, with financiers in control, the transfer ceases to be an internal matter because financiers were usually involved with a number of companies, either as competitors or in unrelated industries. This multiple company interest implies that concerns under financier control cannot be examined as independent entities; instead they must be considered in relation to all those with whom their control is commingled.

Fundamental to this view is the notion of corporate control. Regardless of which group actually retains the power, control must be exercised through the board of directors. This contention has been challenged by a number of authors who maintain that managers (as top officers) effectively control the corporation [5, 6, and 9]. These arguments fail to distinguish daily operating control from ultimate policy control, a difference widely recognized in management circles: "A broad course is plotted by the board, and it is left to the CEO (chief operating officer) to take the com-

pany on this course" [7, p. 47]. While owners, managers, and financiers might attempt to influence company actions, their attempts will never become binding as corporate policy unless they find board representation.

Of course, not all board members are equally active, especially in dealing with other companies and ensuring company survival in a universe of hostile oligopolies. As T. K. Quinn [12] and Henry Morgenthau [10] have indicated, some directors are more able than others to reach agreements and understandings while resolving disputes and conflicts. In this capacity, these directors become corporate diplomats seeking accommodations with suppliers, customers, lenders, and competitors. Perhaps the most positive form of corporate diplomacy is becoming a director of another company, that is, in "interlocking" two concerns. In the years between 1912 and 1919 some directors were so heavily involved in interlocking that they can be typified as "financiers." Although holding numerous directorships, their influence did not arise from any particular position, rather it developed from their ability to link together important companies in such economic sectors as finance, transportation, and manufacturing. This ability, in turn, gave them the power to disproporionately influence the affairs of the companies with which they were affiliated. Although it is difficult to determine the effects of any particular interlock, the overall effect of the activity was to create a complex network of formal relationships among the involved companies.

To determine the composition of this complex network as well as to consider the role of financiers and the transfer of control, interlocks among 167 of the largest American companies were determined for 1912, 1919, and, for comparisons, 1905. (For details see [2].) Between 1912 and 1919 some important changes occurred. In the former year, 12 people holding eight or more directorships, interlocked 68 of the 167 companies included; by the latter year, only three people held eight or more directorships and they interlocked but 27 companies. Between the two years, the number of board positions involving interlocked directors declined from 975 to 919 while the number of direct connections among corporations fell from 1,048 to 780. These changes indicate a decline in the power of financiers since fewer linked fewer companies and an apparent simplification in the relationships among large American corporations.

However, to a considerable extent the changes merely reflected a transfer in control rather than any fundamental alteration in intercorporate affiliations. Between the two years, companies interlocked with each other increased slightly from 140 to 143, the average distance between any two (the smallest number of directors required to interlock directly) changed slightly from 2.3 to 2.5, and the maximum distance between any pair remained unchanged at five. Thus, formal relations among large companies

continued nearly unaltered, despite a sharp decline in the activities of financiers. Similar results were found when examining the stability of particular connections among identical companies at different points in time. Between 1905 and 1912, 63 percent of all connections remained unchanged in order (that is, the number of directors required to link one company with another), 20 percent became more direct, and 16 percent less direct. Between 1912 and 1919, for identical sets of companies, 58 percent remained unchanged, 11 percent became more direct, and 30 percent less direct. Thus, while there was a tendency for companies to become more indirectly interlocked, they nonetheless remained highly connected.

The explanation of how, on the one hand, formal intercorporate relationships continued while, on the other hand, heavily interlocked director-financiers absolutely and relatively declined, is that many separate directors assumed the positions and affiliations that were being vacated. In effect, the activities of a few financiers were transferred to a new class of directors as the control of large corporations passed from one group to another. Berle and Means, identifying these new directors as managers, assumed that they had succeeded owners in controlling corporations whereas in fact they had succeeded financiers. However, since the underlying connections of companies remained virutally unchanged during this transfer of control process, the rise of one controlling group and decline of another had little effect on the basic structure or environment within which large concerns operated.

In conclusion, we have sought to show that the evolution of corporate control was more complex than commonly assumed. Viewing corporations as embedded in an interorganizational network provides a very different picture from one derived from legal standing or hierarchical position. Since between 1905 and 1919 the overwhelming majority of large American corporations were connected together in complete network, we contend that no company can be considered independently from any other. Although the type of control may have changed at the level of the individual firm, the general character of institutional relationships established by major financiers remained virtually stable during the period examined. Thus, while the leadership of Big Business might have changed, its structure remained unaltered.

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