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Commentary: Achieving corporate transparency

DAVID BROWN, anchor: Some argue these trials offer ample evidence for a bigger case, that we need more corporate transparency. Or do we? We caught our dueling commentators, Ian Ayres and Barry Nalebluff, bickering again.

IAN AYRES:

People think more disclosure is the answer to everything.

BARRY NALEBUFF:

Well, sure. Justice Brandeis got it right when he said sunlight is the best disinfectant.

AYRES: But not always. Think about the secret ballot? It stopped voting corruption. Candidates don't buy votes if they can't find out who voted for them.

NALEBUFF: Ian, what does this have to do with corporate governance?

AYRES: Why not have the board of directors vote secretly? It would be easier with a secret ballot to reject a CEO's proposed pay increase, pet project or misguided merger.

NALEBUFF: Whoa! If the resolution fails unanimously, then the CEO will know exactly who voted no.

AYRES: Yeah? But if everyone votes no, it's going to be hard for the CEO to make an enemy of the entire board. Secret ballots are already the gold standard with regard to shareholder votes on proxy initiatives, but it hasn't happened yet for other shareholder votes, such as approving mergers.

NALEBUFF: Yeah, this is a real issue. In the HP-Compaq battle, people worried that Deutsche Bank's yes vote was coerced. If Deutsche Bank voted their client shares no, they were afraid they would lose HP's underwriting business.

AYRES: Barry, but we should take this further. We can also use secrecy to stop the problem of runaway CEO compensation. We should keep compensation consultants in the dark.

NALEBUFF: Ian, now I'm in the dark. How could a compensation consultant not know who they're evaluating?

AYRES: The trick is to have them evaluate a group of people all at once and then rank them. For example, to evaluate Michael Dell, you'd put him on a peer comparison list with Scott McNeely at Sun, Carly Fiorina at HP, maybe even Steve Jobs at Apple. The big point is that they can't all be ranked at the top of the list.

NALEBUFF: I see, so most everyone wants to think that their CEO is above average, but the forced ranking means that half will have to end up below. But won't the company doing the ranking know who's hired them and thus be subtly or not-so-subtly influenced to put their employer near the top?

AYRES: Barry, that's where lawyers come in. The compensation committee should get some law firm to hire the compensation consultants without telling them who the ultimate client is.

NALEBUFF: Well, this is sounding like the way we test drugs. It's a double-blind experiment. The person doing the evaluation doesn't know which patients got the drug and which got the placebo.

AYRES: It's also the way we hire senior people here at Yale. Other professors are asked to rank the best people in the field without knowing which one is really under consideration for the appointment.

NALEBUFF: Of course, the system can be gained through who you put on the comparison list.

AYRES: That's not perfect, but with companies, the list would be large, and that makes it harder to game.

NALEBUFF: So what do you think about this for you, Ian? You're often hired as an expert witness. Instead of being hired by a plaintiff or defendant, you could be hired by the court.

AYRES: I'd prefer that. You know, I would like to think that I'm on the side of truth, but there's always pressure to please a client. Sometimes keeping people in the dark is the best way to keep them honest.

NALEBUFF: In New Haven, this is Barry Nalebuff.

AYRES: And Ian Ayres for MARKETPLACE.

BROWN: Ian and Barry teach at Yale University and are co-authors of the book "Why Not?"