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# ARTICLES

## The Riddle of Shareholder Rights and Corporate Social Responsibility

*Daniel J. Morrissey*<sup>†</sup>

“Do the dynamics of private capital accumulation inevitably lead to concentration of wealth in ever fewer hands . . . ?”<sup>1</sup>

### INTRODUCTION

Corporations exist primarily to make profit for their shareholders. This has been the black letter rule of law and the reigning orthodoxy of American business for a century.<sup>2</sup> For most of the last 100 years, large corporations<sup>3</sup> have been the prime vehicles for providing needed goods and services while they have continually improved their products to better satisfy their consumers. They have also provided stable jobs for countless workers. Yet through the years certain legal and social theorists have advocated that these business behemoths should

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<sup>1</sup> THOMAS PIKETTY, *CAPITAL IN THE TWENTY-FIRST CENTURY* 1 (Arthur Goldhammer, trans., President and Fellows of Harvard College 2014) (2013)

<sup>2</sup> *See, e.g.*, *Dodge v. Ford*, 170 N.W. 668, 681 (1919); *see also infra* notes 7, 8, 13 and accompanying text.

<sup>3</sup> Today there are approximately 6,700 large public companies whose shares are actively traded. Even though they comprise a small fraction of the 5.8 million U.S. businesses operating in the corporate form, these firms generate the lion’s share of our country’s economic activity. HOWARD M. FRIEDMAN, *PUBLICLY HELD CORPORATIONS: A LAWYER’S GUIDE* 1 (2011).

have a broader mandate. In the last several decades that outlook has grown to a large scale movement called corporate social responsibility (CSR). It asserts that a more expansive corporate mission is needed now more than ever as income inequality has increased to alarming proportions and environmental issues threaten the sustainability of life on our planet.

This Article contends that both these corporate goals, profit and social responsibility, are compatible. Shareholders play an indispensable role in the structure of American business. In addition, economic gain, if widely shared, is a major benefit to our common life. Yet corporate leaders, as stewards of our society's resources, must also be charged with serving the larger interests of their workers and the communities where they do business. A federal law should mandate that obligation.

This Article will begin in Part I with a discussion of the origins of the rule that corporations must be run primarily to make profit for their shareholders. The Article will next explain in Part II the important role that shareholders play in the corporate structure. It will trace how stockholders were initially instrumental in America's industrial development, yet because of the rise of a managerial class they lost their ability to control the enterprises that they owned. Part III will then discuss the role of shareholders in improving corporate governance. Part IV will describe the rise of CSR as a respected corporate objective and conclude with a call for a national corporate law that would provide a structure to hold corporations to a standard consistent with the goals of CSR.

## I. THE RULE OF PROFIT AND SHAREHOLDER PRIMACY

As valuable as shareholders are in our economic system, their rights are not paramount. Such was the approach taken by the pre-industrial common law as Anglo-American cases stressed the communal duties of early corporations.<sup>4</sup> Yet as large scale manufacturing took hold the law began to move in another direction. By the second half of the nineteenth century, it had made the shareholders' right to profit a firm's dominant duty.

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<sup>4</sup> As the leading English jurist of the eighteenth century stated, "[I]t has been found necessary . . . to constitute artificial persons, who may maintain a perpetual succession, and enjoy a kind of legal immortality. These artificial persons are called bodies politics, bodies corporate, (*corpora corporate*), or corporations; of which there is a great variety subsisting, for the advancement of religion, of learning, and of commerce . . ." 2 WILLIAM BLACKSTONE, COMMENTARIES \*467-68 .

One scholar has called that era's approach to the central issue of corporate law "a curious admixture of classical economics, Neo-Calvinism, Social Darwinism, Lockean Political Philosophy and a large component of antistatistism."<sup>5</sup> That was also the time when laissez-faire economics reigned supreme, and an age, correspondingly, when property and contract rights were given strong constitutional protection.<sup>6</sup>

In this high capitalist culture it should not have been a surprise when a court invalidated a contrary business philosophy even when it was practiced by a leading industrialist, Henry Ford, who owned a majority of the stock of his car company and controlled its board.<sup>7</sup> Ford's firm was lushly profitable and he wanted to use part of its surplus to reduce the retail price of its automobiles.<sup>8</sup> Ford had already become a household name for raising his workers base pay to five dollars per day.<sup>9</sup>

When the Dodge brothers, who owned 10 percent of the company's stock, challenged Ford's policy of minimum dividends he expressly defended it with these philanthropic sentiments, "My ambition . . . is to employ still more men; to spread the benefits of this industrial system to the greatest possible number, to help them build up their lives and their homes. To do this we are putting the greatest share of our profits back into the business."<sup>10</sup>

Ford's approach, though daring, was not novel. He was following earlier industrialists from the late nineteenth century such as William Lever, a famed English soap manufacturer, and George Pullman, the American railroad car magnet.<sup>11</sup> Both established company towns near their operations in Liverpool and Chicago where the needs of their workers could be fulfilled.<sup>12</sup> To be sure, self-interest was at work there because such a beneficent and paternalistic strategy was designed to

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<sup>5</sup> See Edwin M. Epstein, *Societal, Managerial, and Legal Perspectives on Corporate Social Responsibility—Produce and Process*, 30 HASTINGS L.J. 1287, 1295 (1979).

<sup>6</sup> See, e.g., *Lochner v. New York*, 198 U.S. 45, 53 (1905).

<sup>7</sup> See Hedrick Smith, *When Capitalists Cared*, N.Y. TIMES, Sept. 3, 2012 at A19, available at <http://www.nytimes.com/2012/09/03/opinion/henry-ford-when-capitalists-cared.html>.

<sup>8</sup> *Dodge v. Ford*, 170 N.W. 668, 683 (1919).

<sup>9</sup> Smith, *supra* note 7. Recent studies, however, show that today those with wealth and power pay scant attention to people without it. Daniel Goleman, *Rich People Just Care Less*, N.Y. TIMES: OPINION PAGES, Oct. 6, 2013 at SR12, available at <http://opinionator.blogs.nytimes.com/2013/10/05/rich-people-just-care-less>.

<sup>10</sup> *Dodge*, 170 N.W. at 671.

<sup>11</sup> N. Craig Smith, *When it Comes to CSR, Size Matters*, FORBES (Aug. 14, 2013), <http://www.forbes.com/sites/insead/2013/08/14/when-it-comes-to-csr-size-matters/>.

<sup>12</sup> *Id.*

quell labor unrest. Yet it was also a forthright plan to share the wealth generated by those companies.

In spite of the clear social good resulting from Ford's philanthropy, the Michigan Supreme Court found that Ford's dividends were too small for a company with such huge profits. The Justices rejected Ford's policies with these forceful remarks that became the definitive law on corporate purpose.

There should be no confusion (of which there is evidence) of the duties which Mr. Ford conceives that he and the stockholders owe to the general public and the duties which in law he and his co-directors owe to protesting, minority stockholders. A business corporation is organized and carried on primarily for the profit of the stockholders. The powers of directors are to be employed for that end.

The discretion of the directors is to be exercised in the choice of the means to attain that end, and does not extend to a change in the end itself, to the reduction of profits, or the non-distribution of profits among stockholders in order to devote them to other purposes.<sup>13</sup>

That attitude, however, was not universal, even in that era. Other cases and statutes permitted corporations to make charitable donations if they served the business in some way,<sup>14</sup> and some social advocates were even arguing for a fuller vision of corporate purpose. As one put it, “[N]ot merely public office but private business is a public trust.”<sup>15</sup> President Theodore Roosevelt railed against the “Malefactors of Great Wealth” and in an address to Congress he asserted, “Great corporations exist only because they are created and safeguarded by our institutions; and it is therefore our right and our duty to see that they work in harmony with these institutions.”<sup>16</sup>

Likewise, Henry Higginson, a prominent Boston businessman, made these remarks in 1911, a time coincident to the “Social Gospel movement”<sup>17</sup> that was pushing American Protestantism to apply Christian principles to questions of social justice.

I do not believe that, because a man owns property, it belongs to him to do with as he pleases. The property belongs to the community, and

<sup>13</sup> *Dodge*, 170 N.W. at 684.

<sup>14</sup> See TEX. REV. CIV. STAT. ANN. art. § 1164 (West 1918); *People v. Hotchkiss*, 120 N.Y.S. 649 (App. Div. 1909); *Steinway v. Steinway & Sons*, 40 N.Y.S. 718 (Sup. Ct. 1896).

<sup>15</sup> Albion W. Small, *Private Business is a Public Trust*, 1 AM. J. SOC. 276, 282 (1895).

<sup>16</sup> President Theodore Roosevelt, First Annual Message to Congress (Dec. 3, 1901). A fine new book on his clash with his hand-picked successor, William Howard Taft, is DORIS KEARNS GOODWIN, *THE BULLY PULPIT: THEODORE ROOSEVELT, WILLIAM HOWARD TAFT, AND THE GOLDEN AGE OF JOURNALISM* (2013).

<sup>17</sup> See, e.g., WALTER RAUSCHENBUSCH, *CHRISTIANITY AND SOCIAL CRISIS* (1907). This is considered one of the leading statements of the Social Gospel philosophy.

he has charge of it, and can dispose of it, if it is well done and not with the sole regard to himself or to his stockholders.<sup>18</sup>

The stock market crash of 1929 and the resulting Great Depression brought about a new public attitude about the social responsibility of business. Even Republican President Herbert Hoover made this telling critique of the American economic system, “The trouble with capitalism is the capitalists; they’re damn greedy.”<sup>19</sup> His successor, Franklin Delano Roosevelt, went further in his first inaugural address, admonishing “conduct in banking and in business which too often has given to a sacred trust the likeness of callous and selfish wrongdoing.”<sup>20</sup>

Roosevelt’s New Deal responded with landmark federal legislation regulating the sale of securities<sup>21</sup> as well as the markets in which they are traded.<sup>22</sup> It established a disclosure regime where public companies were compelled to lay bare all important aspects of their businesses.<sup>23</sup> While those federal securities laws contained little substantive regulation of corporations, they at least established that publicly-held firms would be accountable to their shareholders and society at large by having to truthfully inform them about their operations and financial conditions. In addition, the statutes set up the SEC as a new federal regulatory agency, empowered to make rules delineating the particular disclosures public companies would be required to make in their periodic reports and proxy statements.<sup>24</sup>

Those hard economic times also caused commentators and even business leaders themselves to reassess the duties of public companies. Some urged that corporations undertake civic responsibilities. Professor Merrick Dodd became one of the

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<sup>18</sup> ROBERT N. BELLAH ET AL., *HABITS OF THE HEART* 260 (1985) (quoting Henry Higginson).

<sup>19</sup> David Shipley, *Editorial Notebook; Remembering Herbert Hoover*, N.Y. TIMES (Aug. 10, 1992), <http://www.nytimes.com/1992/08/10/opinion/editorial-notebook-remembering-herbert-hoover.html>.

<sup>20</sup> President Franklin D. Roosevelt, First Inaugural Address (Mar. 4, 1933).

<sup>21</sup> See Securities Act of 1933, 15 U.S.C. §§ 77a-77z (2012).

<sup>22</sup> See Securities Exchange Act of 1934, 15 U.S.C. §§ 78a-78pp (2012) [hereinafter Exchange Act].

<sup>23</sup> See *id.* §§ 13(a), 14(a); 15 U.S.C. §§ 78m(a), 78n(a).

<sup>24</sup> Section 4 of the Exchange Act established the SEC. 15 U.S.C. § 78d. Sections 12(b) and 12(g) of that Act require that companies commonly described as “exchange-listed” and “publicly-held” companies register with the SEC. 15 U.S.C. §§ 781(b),(g). Section 13(a) of the Exchange Act then requires that these “reporting companies” file annual, quarterly, and current reports on forms 10-K, 10-Q, and 8-K respectively. 17 C.F.R. § 240.13a-1, 240.13a-13, 240.13a-11 (2010). Section 14(a) of the Exchange Act empowers the SEC to make rules regarding proxy solicitation by reporting companies. 15 U.S.C. § 78n(a). Using this authority, the SEC has promulgated elaborate rules for disclosure to shareholders. 17 C.F.R. §§ 240.14a-1–240.14a-14.

prime spokespersons for this new vision of “corporate statesmanship.”<sup>25</sup> Managers of firms, he said, should not just be concerned with making profit for stockholders, but ought to consider themselves fiduciaries and act for all who are impacted by their firms. Those constituents would include their workers and the communities where they do business.

Dodd was also the first to speak of what has become the “team” concept of a corporation.<sup>26</sup> As the Latin origin of its name connotes, a corporation is a “body,” not just a collection of individuals.<sup>27</sup> Its leaders should therefore make sure its actions benefit the entity as a whole, rather than just one of its members, the shareholders. Dodd also drew from the new Keynesian economics that was having a profound impact on policy makers.<sup>28</sup> He asserted that actions which serve the interests of a firm’s broader groups, like the payment of good wages to its workers, also redound to the advantage of its shareholders by creating stronger purchasing power for the company’s products.<sup>29</sup>

A prominent case in the immediate post-war era epitomized how Dodd’s more expansive views had taken hold.<sup>30</sup> When a shareholder challenged a corporate contribution to Princeton University by his New Jersey based firm, the highest state court resoundingly affirmed the appropriateness of the donation. It first found that the gift was in the corporation’s “enlightened self-interest” by creating goodwill for the firm and helping to educate its future workers.<sup>31</sup> However, the court went beyond that to uphold the contribution because of the company’s broader obligations to society. Most of America’s wealth, the court observed, is held by corporations and as such it is appropriate for them “to assume the modern obligations of good citizenship in the same manner as humans do.”<sup>32</sup> “[M]odern conditions,” it said, “require that corporations acknowledge and

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<sup>25</sup> Merrick Dodd, *For Whom are Corporate Managers Trustees?*, 45 HARV. L. REV. 1145, 1147-48 (1932).

<sup>26</sup> See, e.g., Margaret M. Blair & Lynn A. Stout, *A Team Production Theory of Corporate Law*, 85 VA. L. REV. 247, 303 (1999).

<sup>27</sup> James Morwood, ed., *Corpus Definition*, OXFORD REFERENCE: POCKET OXFORD LATIN DICTIONARY (2012), <http://www.oxfordreference.com/view/10.1093/acref/9780191739583.001.0001/b-la-en-00001-0002507?rskey=TBld3u&result=1>.

<sup>28</sup> See JOHN MAYNARD KEYNES, *THE GENERAL THEORY OF EMPLOYMENT INTEREST AND MONEY* 3 (1936).

<sup>29</sup> Dodd, *supra* note 25, at 1156.

<sup>30</sup> *A.P. Smith Mfg. Co. v. Barlow*, 98 A.2d 581 (N.J. 1953).

<sup>31</sup> See ROBERT C. CLARK, *CORPORATE LAW* 681-84 (1986).

<sup>32</sup> *A.P. Smith*, 98 A.2d at 586.

discharge social as well as private responsibilities as members of the communities within which they operate.”<sup>33</sup>

The post-war era however saw little real movement to define or embrace CSR beyond limited philanthropic activity. It was a time of collective complacency when the tradition “shareholder primacy” paradigm was generally accepted without question. One notable exception was the far-sighted management expert Peter Drucker. He argued that business leaders should also be concerned with political or social issues that might be important to their “alternative constituencies,” like workers and consumers.<sup>34</sup>

Even most liberals then believed that the “regulatory state” established by the New Deal was sufficient to guarantee that corporations would not harm the public interest.<sup>35</sup> The business elite seemed to go along with that system by not challenging those bureaucracies. It was thus no surprise that in that era of relative good feeling, corporate law did nothing to particularly prescribe how businesses must act.

As one commentator said, corporate codes then were just a “black box,” a series of rules governing the technical operation of those firms, having no real effect on what public companies actually did.<sup>36</sup> In the same vein, another legal scholar of that period said corporate law had become “trivial,”<sup>37</sup> and one more described it with rhetorical flourish as “great empty corporation statutes—towering skyscrapers of rusted girders, internally welded together and containing nothing but wind.”<sup>38</sup> In sum, corporate law then contained no requirements pertaining to how businesses should behave, and it prescribed no goals for them other than profit-making.

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<sup>33</sup> *Id.* at 585-86.

<sup>34</sup> Jerome J. Shestack, *Corporate Social and the Lawyer in the 21st Century*, in *CORPORATE SOCIAL RESPONSIBILITY* 403 (2011); *see also* LORRAINE TALBOT, *PROGRESSIVE CORPORATE GOVERNANCE FOR THE 21ST CENTURY* 105 (2013).

<sup>35</sup> *See generally* HENRY M. HART, JR. & ALBERT M. SACKS, *THE LEGAL PROCESS: BASIC PROBLEMS IN THE MAKING AND APPLICATION OF LAW* (1994). *But see* David G. Yosifon, *The Public Choice Problem in Corporate Law: Corporate Social Responsibility After Citizens United*, 89 N.C. L. REV. 1197 (2011). The author argues that because of the Supreme Court’s decision in *Citizens United*, which struck down laws limiting political spending by corporations, those firms will be much more able to influence government. As a result it will be less able to restrict corporate excesses that are visited on non-shareholding stakeholders such as workers and consumers. Boards must therefore play that role, the author urges, and be attentive to the needs of those groups.

<sup>36</sup> Ronald J. Gilson, *Corporate Governance and Economic Efficiency: When Do Institutions Matter?*, 74 WASH. U. L. Q. 327 (1996).

<sup>37</sup> Bernard S. Black, *Is Corporate Law Trivial?: A Political and Economic Analysis*, 84 NW. U. L. REV. 542, 544 (1990).

<sup>38</sup> Bayless Manning, *The Shareholder’s Appraisal Remedy: An Essay for Frank Coker*, 72 YALE L. J. 233, 245 n.37 (1962).



All that would change, however, in the period of unrest that became known as the 1960s. The civil rights and anti-war movements of that time inspired an idealistic youth culture that brought about a generalized discontent with the status quo.<sup>39</sup> As concern for the historically disadvantaged and the environment took center stage, corporations became the focal point of much of that dissatisfaction.<sup>40</sup> Reformers like Ralph Nader claimed that corporations were responsible for a number of significant evils.<sup>41</sup> Those evils included industrial pollution, unsafe products, deceptive advertising, and discriminatory employment practices.<sup>42</sup> In addition, critics attacked the dominant corporate culture as alienating and stressful.<sup>43</sup>

One early response to that dissatisfaction was the growth of in-house corporate foundations. Some firms, such as Dayton-Hudson, Levi Strauss, and Cummins Engines, began giving up to five percent of their pre-tax earnings to eleemosynary efforts.<sup>44</sup> But an even more significant result was the beginning of the CSR movement.<sup>45</sup> CSR's influence reached its first high-point in the mid-1970s when prominent legal scholars joined with social activists to urge that the federal government replace states as the ultimate source of corporate law.<sup>46</sup>

Federal chartering of corporations, they argued, should displace state-based regimes where jurisdictions like Delaware had won the race to the bottom with their lax standards for management's conduct.<sup>47</sup> The ensuing federal law would then require better governance practices and mandate that corporations engage in socially beneficial activity that would be enforced by public interest directors.<sup>48</sup> Such a mandate would put pressure on corporations to act in a more socially responsible manner.

Those fervent efforts at reform, however, met strong immediate resistance from laissez-faire economists, most

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<sup>39</sup> See TODD GITLIN, *THE SIXTIES: YEARS OF HOPE, DAYS OF RAGE* 12-14 (1987).

<sup>40</sup> See Phillip I. Blumberg, *The Politicization of the Corporation*, 51 B.U. L. REV. 425, 426 (1971).

<sup>41</sup> See generally RALPH NADER ET AL., *TAMING THE GIANT CORPORATION* (1976).

<sup>42</sup> *Id.* at 17-24.

<sup>43</sup> See *id.* at 27.

<sup>44</sup> Craig Smith, *The New Corporate Philanthropy*, HARV. BUS. REV., May-June 1994, at 105, 107.

<sup>45</sup> Douglas M. Branson, *Corporate Social Responsibility Redux*, 76 TUL. L. REV. 1207, 1211-12 (2002).

<sup>46</sup> TALBOT, *supra* note 34, at 113.

<sup>47</sup> William L. Cary, *Federalism and Corporate Law: Reflections Upon Delaware*, 83 YALE L. J. 663, 705 (1974).

<sup>48</sup> Branson, *supra* note 45, at 1213-14.

prominently Nobel Laureate Milton Friedman.<sup>49</sup> He countered that a corporate official is merely an employee of its shareholders—the owners of the business. As such, he wrote:

[A corporate executive] has direct responsibility to his employers. That responsibility is to conduct the business in accordance with their desires, which generally will be to make as much money as possible while conforming to the basic rules of the society, both those embodied in law and those embodied in ethical custom.<sup>50</sup>

For Friedman, non-profit activity was not the business of business, but of government and private charity. In addition, as other defenders of the traditional view noted, if corporate goals other than profit-maximizing were legitimate, boards would be divided and distracted from achieving the highest return on the capital entrusted to them.<sup>51</sup> The rights of other corporate “constituents,” such as employees and creditors should therefore be set only by the contracts they make with the firm.<sup>52</sup> Management, they argued, should just be attentive to the wishes of its masters, the shareholders.

These attitudes were quickly re-enforced by two new developments, one in politics and the other in legal scholarship. By the late 1970s, a resurgence of conservatism was taking hold, first signaled by the taxpayers’ revolt of Proposition 13 in California.<sup>53</sup> Part of its agenda was to deregulate business. That was at first tentatively embraced by the Carter administration and then welcomed without reserve by President Reagan after his election in 1980. Reagan’s presidency ushered in a new, full-throated form of capitalism that became the “Greed is Good,”<sup>54</sup> era—hardly an attitude that would be friendly to any diversions of business from its profit-making goals.

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<sup>49</sup> Milton Friedman, *A Friedman Doctrine—The Social Responsibility of Business is to Increase Its Profits*, N.Y. TIMES MAG., Sept. 13, 1970, at 32.

<sup>50</sup> *Id.*

<sup>51</sup> See Bayless Manning, *Thinking Straight About Corporate Law Reform*, 41 LAW & CONTEMP. PROBS. 3, 10 (1977).

<sup>52</sup> See Oliver Williamson, *Corporate Governance*, 93 YALE L.J. 1197, 1198 (1984).

<sup>53</sup> Officially titled the “The People’s Initiative to Limit Property Taxation,” Proposition 13 was approved by a California voter referendum in 1978 and is now Article 13A of the Constitution of the state of California.

<sup>54</sup> Financier Ivan Boesky made that signature statement at a business school commencement speech shortly before he was indicted for insider trading. PATRICK DILLON & CARL M. CANNON, *CIRCLE OF GREED: THE SPECTACULAR RISE AND FALL OF AMERICA’S MOST FEARED AND LOATHED LAWYER* 108 (2010). It was the template for Gordon Gekko’s famous declaration in Oliver Stone’s 1987 movie, *WALL STREET* (20th Century Fox Film Corp. 1987). Michael Douglas won an academy award for his role as Gekko.

Going hand in hand with those political events was a new school of jurisprudence, law and economics.<sup>55</sup> Legal rules, it held, should promote the efficient allocation of society's resources, and the best way to do that was to encourage market forces. Any laws which interfered with that pricing mechanism were considered harmful to wealth enhancement. Private ordering by contract was therefore the preferred mode of business organization and a corporation was seen as a mere "nexus" of those relationships.<sup>56</sup> This highly individualist approach left all members of the corporate community except stockholders to fend for themselves and prescribed no other duties for corporate officials other than maximizing the value of their shares.<sup>57</sup> In doing so they would benefit the holders of those instruments—the owners of their firms.

## II. THE INDISPENSABLE SHAREHOLDER

The law governing for-profit corporations provides that there must be some group that has the final claim on their wealth<sup>58</sup> and there also must be someone to whom their directors are accountable.<sup>59</sup> Common shareholders occupy both positions. They supply a firm's risk capital and therefore have the ultimate entrepreneurial stake in the company. They are also the residual owners of its profits and thus the ones to whom its managers must be responsible. Shareholders are therefore fundamental constituents of a for-profit corporation.

Such a system of private investing has many virtues. It can channel economic resources to their most efficient uses because it rewards intelligent risk-takers with the profits from their investments. It is also an altogether good idea to encourage wide-spread holdings in the equity of our country's businesses. Half of American households are shareholders; either directly or through their retirement plans.<sup>60</sup> Since stock

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<sup>55</sup> The founding text in that school is RICHARD POSNER, *THE ECONOMIC ANALYSIS OF LAW* (1973).

<sup>56</sup> Jeffrey Bone, *Legal Perspective on Corporate Responsibility: Contractarian or Communitarian Thought?*, 24 *CAN. J. L. & J.* 277, 285 (2011) (contrasting this viewpoint to a more communal notion of the corporation).

<sup>57</sup> See Frank H. Easterbrook & Daniel R. Fischel, *The Proper Role of a Target's Management in Responding to a Tender Offer*, 94 *HARV. L. REV.* 1161, 1164, 1190-92 (1981); Ronald J. Gilson, *A Structural Approach to Corporations: The Case Against Defensive Tactics in Tender Offers*, 33 *STAN. L. REV.* 819 (1981).

<sup>58</sup> See, e.g., MODEL BUS. CORP. ACT § 6.01(b)(2) (2002).

<sup>59</sup> See *id.* § 6.01(b)(1).

<sup>60</sup> Annie Lowrey, *Top 10% Took Home Half of U.S. Income in 2012*, *N.Y. TIMES*, Sept. 11, 2013, at B4, *version available at* <http://economix.blogs.nytimes.com/2013/09/10/the>

ownership returns more over time than fixed obligations like bonds or bank deposits, it allows investors to maximize the growth of their savings.

A. *The Shareholder's Role in Early American Corporate History*

When the American industrial revolution got started in earnest in the first part of the nineteenth century, the United States was already a country with a prosperous middle class. Since those folks had some savings and were generally eager to share in the profitability of new firms, businesses found it advantageous to secure capital from them.<sup>61</sup>

The corporate form aided that process.<sup>62</sup> Limited liability for shareholders was already one of its standard features and, by the time of the Civil War, obtaining a corporate charter had become a simple process.<sup>63</sup> By then, entrepreneurs no longer needed a specific legislative act to create a corporation but could bring such a separate legal entity into existence by merely filing certain documents with a public official.<sup>64</sup> The opportunities those developments afforded business people in the latter decades of the nineteenth century were aptly described by two leading legal historians.

In the Gilded Age, decades after the Civil War, it was the device of the corporation that made possible the growth of the new commercial empires including railroads, steel, iron, rubber, automobiles, food process, and oil. The corporation allowed for the pooling of vast sums of capital, an essential requirement for industries with large, fixed-cost components: track, locomotives, railway cars, buildings, factories, furnaces, and machines. With enormous sums of capital at risk, the limitation on liability worked as the perfect inducement of investors.<sup>65</sup>

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rich-get-richer-through-the-recovery/. A large percentage of that stock ownership, however, is now held by the richest Americans. Most working people, with little disposable income, have been unable to participate in the recent stock market gains. James Surowiecki, *The Pay is Too Damn Low*, FIN. PAGE: NEW YORKER (Aug. 12, 2013), <http://www.newyorker.com/magazine/2013/08/12/the-pay-is-too-damn-low>.

<sup>61</sup> See JOHN STEELE GORDON, AN EMPIRE OF WEALTH 107 (2004) (recounting, for instance, how most of the money to build the Erie canal came from small New York investors while the labor was mostly provided by recent Irish immigrants).

<sup>62</sup> Daniel J. Morrissey, *Toward a New/Old Theory of Corporate Social Responsibility*, 40 SYRACUSE L. REV. 1005, 1006-09 (1989).

<sup>63</sup> See J. HURST, THE LEGITIMACY OF THE BUSINESS CORPORATION IN THE LAW OF THE UNITED STATES 1780-1970, at 26-27, 44, 50-51 (1970).

<sup>64</sup> See *id.* at 70.

<sup>65</sup> STEPHEN B. PRESSER & JAMIL S. ZAINALDIN, LAW AND JURISPRUDENCE IN AMERICAN HISTORY: CASES AND MATERIALS 359 (6th ed. 2006).

Nicholas Murray Butler, the renowned president of Columbia University, spoke for many in the early part of the twentieth century when he praised the privileged status enjoyed by shareholders and described how it benefited society. “[I]n my judgment,” he said, “the limited liability corporation is the greatest single discovery of modern times . . . even steam and electricity are far less important than the limited liability corporation, and they would be reduced to comparative impotence without it.”<sup>66</sup>

In large enterprises, the corporation’s structure also provided a distinct governance advantage. It would obviously be impractical to follow the partnership model there and allow each of the numerous and far-flung shareholder owners to make legally binding commitments for the business. Happily, the corporation solved that problem by centralizing management in a board of directors and by establishing shareholders who are the residual owners of corporations. Shareholders elect directors who have the ultimate managerial power. The directors in turn select officers to run the day to day affairs of the business. Under “[t]he basic and [long-standing] principle of U.S. corporate law”<sup>67</sup> stockholders elect the board, but after that they have no right to make decisions for the business. In addition, the business judgment rule makes it difficult for shareholders to challenge actions by directors about corporate policy, including those that implicate its social responsibility.

An area where vigilant stockholders can provide an important service for society is by taking an active role in corporate governance. Two leading authorities describe the ideal function of corporate governance when “the three key players—the executives, the board of directors, and the shareholders—provide through a system of checks and balances a system for a transparent and accountable system for promoting objectively determined goals and benchmarks.”<sup>68</sup>

Problems occur when top executives of public companies do not act responsibly to promote the interests of their shareholders and other constituents. Such wrongdoing is often compounded because their supervisors, the directors, fail to prevent those transgressions. Officers, in the worst case, may

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<sup>66</sup> WILLIAM M. FLETCHER, 1 CYCLOPEDIA OF THE LAW OF PRIVATE CORPORATIONS § 21 (1917).

<sup>67</sup> Lucian Arye Bebchuck, *The Case for Increasing Shareholder Power*, 118 HARV. L. REV. 833, 844 (2005).

<sup>68</sup> ROBERT A.G. MONKS & NELL MINOW, CORPORATE GOVERNANCE, at xiii (5th ed. 2011).

enrich themselves through self-dealing with the corporation. *Guth v. Loft* is a good example of that harmful behavior where a corporate executive usurped an opportunity of the corporation.<sup>69</sup> A leading shareholder advocate recently described other substantial wrongdoing that boards condone:

Is it fair that CEOs make 700 times what the average worker makes, even if the chief executive is doing a terrible job and thousands of workers are laid off? Why do CEOs get awarded huge bonuses by friendly boards when the share prices are down by double digits and then get their options reset to lower levels as an “incentive”?<sup>70</sup>

To a lesser, but also troubling extent, executives may shirk their duties<sup>71</sup> or engage in empire-building that benefits themselves at the expense of their shareholders.<sup>72</sup> Alternatively, they may follow excessively conservative strategies that protect their positions but do not serve their stockholders well. That wrongful conduct may ultimately be just as harmful to the corporation and society as outright looting.<sup>73</sup> Yet it is once again harder to challenge because corporate officials have the protection of the business judgment rule, which embodies the reluctance of courts to review situations where only a board’s duty of care is implicated.<sup>74</sup>

### B. *Shareholders Lose Their Voice*

As large corporations were achieving their pre-eminent status in the American economy, a new development changed the nature of how shareholders related to their companies. In

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<sup>69</sup> See generally *Guth v. Loft, Inc.*, 5 A.2d 503 (Del. 1939).

<sup>70</sup> Carl Icahn, Challenging the Imperial Boardroom, WALL ST. J., Sept. 19, 2013, at A19, available at <http://online.wsj.com/news/articles/SB10001424127887324665604579081703521362462>. This explosion of wealth at the upper levels of our society has exacerbated income inequality. See Daniel J. Morrissey, *Executive Compensation and Income Inequality*, 4 WM. & MARY BUS. L. REV. 1 (2013). It has also led to new ostentatious displays of riches, Paul Krugman, *The Show-Off Society*, N.Y. TIMES, Sept. 26, 2014, at A31, available at <http://www.nytimes.com/2014/09/26/opinion/paul-krugman-the-show-off-society.html>.

<sup>71</sup> See FRANKLIN A. GEVURTZ, CORPORATION LAW 236 (2d ed. 2010).

<sup>72</sup> See ROBERT CHARLES CLARK, CORPORATE LAW 536 (1986).

<sup>73</sup> See GEVURTZ, *supra* note 71, at 236-37.

<sup>74</sup> As the Delaware Supreme Court put it, “A board of directors enjoys a presumption of sound business judgment, and its decisions will not be disturbed if they can be attributed to any rational business purpose.” *Sinclair Oil Corp. v. Levien*, 280 A.2d 717, 720 (Del. 1971). That discretion has been reinforced by the famous Delaware “raincoat” provision, which allows corporations to amend their articles to exculpate their officers and directors for improper conduct unless it involves activities like those done in bad faith, intentional wrongdoing, breaches of duties of loyalty, or knowing violations of law. DEL. CODE ANN. tit. 8, § 102(b)(7) (1974); see also MODEL BUS. CORP. ACT § 8.31(a) (2014) (explaining standards of liability for directors of corporations).

the early years of corporate prominence, large stockholders were typically the directors of their firms.<sup>75</sup> As stock became more widely-held after sale to the public, however, ownership became diffuse and far-flung. By 1932, as Professors Berle and Means demonstrated in a well-regarded study, it was rare in large companies that one shareholder held more than one percent of the outstanding stock.<sup>76</sup> In the mid-1980s Professor John Coffee summed up those landmark findings with the following remarks:

A little over fifty years ago, Berle and Means reported that the separation of ownership and control in the modern corporation had left shareholders effectively powerless, as managers could neither be ousted from office by shareholders who were widely dispersed, and therefore incapable of coordinated action, nor disciplined effectively by the capital market—at least so long as managers could rely on internal cash flow to finance corporate expansion.<sup>77</sup>

Yet in the prosperous post-World War II era, no one, except perhaps the occasional shareholder gadfly, seemed particularly concerned that stockholders were powerless. De facto supremacy had gone to a managerial class that perpetuated its authority by soliciting shareholder proxies to elect its nominees to the board.<sup>78</sup> Yet who could fault the business elite, which were then guiding the country to unparalleled productivity and growth?<sup>79</sup>

As America moved through the twentieth century, the achievements of its large public companies became legendary. They developed all kinds of products that promoted higher

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<sup>75</sup> Andrei Schleifer & Robert Vishny, *Large Shareholders and Corporate Control*, 94 J. POL. ECON. 461, 462 (1986). In their treatise on Corporate Governance, A.G. Monks & Nell Minow explain how the great industrialists of that time like John D. Rockefeller, Andrew Carnegie, Andrew Mellon, and Cornelius Vanderbilt sold shares of their companies to the public but continued to dominate them. MONKS & MINOW, *supra* note 68, at 20; see also TALBOT, *supra* note 34, at 222 (critically describing ownership patterns, stating, “[i]n the United States, controlling shareholders in the 19th century sought to dominate the economy through legal mechanisms such as special charters and trusts”).

<sup>76</sup> ADOLF A. BERLE, JR. & GARDINER C. MEANS, *THE MODERN CORPORATION AND PRIVATE PROPERTY* 47 (1933).

<sup>77</sup> John C. Coffee, Jr., *Shareholders Versus Managers: The Strains in the Corporate Web*, 85 MICH. L. REV. 1, 15 (1986).

<sup>78</sup> Monks and Minow attribute this “disenfranchisement” of shareholders to “management’s vastly superior access to the proxy, both procedurally (in terms of resources) and substantively (in terms of appropriate subject matter).” MONKS & MINOW, *supra* note 68, at 125.

<sup>79</sup> “In 1965, America’s big companies had a hell of a year. The stock market was booming. Sales were rising briskly, profit margins were fat, and corporate profits as a percentage of G.D.P. were at an all-time high.” James Surowiecki, *Open Season*, FIN. PAGE: NEW YORKER (Oct. 21, 2013), <http://www.newyorker.com/magazine/2013/10/21/open-season-3>.

standards of living and became places where vast numbers of employees could anticipate steady, profitable employment. They constructed our infrastructure and financed scientific research that led to further increases in our standard of living. Professor Lawrence Mitchell aptly laid out their successes:

The modern American business corporation has been a subject of wonder . . . for innovative and risky projects that create technological miracles and human comforts . . . Wonder, because in these ways modern American business corporations have created material well-being that allows so many people to live the eighteenth-century liberal ideal on which America was founded, an ideal of individual freedom, autonomy, and choice.<sup>80</sup>

Other observers just as forcefully described the predominant status that the modern corporation had achieved:

Corporations are such a pervasive element in everyday life that it can be difficult to step back far enough to see them clearly. Corporations do not just determine what goods and services are available in the marketplace, but, more than any other institution, corporations determine the quality of the air we breathe and the water we drink, and even where we live.<sup>81</sup>

### C. *The Time of Tender Offers*

The post-war era of corporate complacency ended when a new type of shareholder activism took hold during the 1970s and 1980s. Hostile take-overs then began shaking up the corporate world. Corporate raiders, as these unwelcomed purchasers were pejoratively called, tried to gain control of companies by making public proposals to shareholders to buy their stock at a premium in cash over their current market prices.<sup>82</sup> According to the emerging law and economics school, however, these tender offers were really a form of shareholder empowerment where the true owners could regain a measure of control over the unaccountable managers of their corporations.<sup>83</sup> Inefficient management, they

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<sup>80</sup> LAWRENCE E. MITCHELL, *CORPORATE IRRESPONSIBILITY: AMERICA'S NEWEST EXPORT 1* (2001).

<sup>81</sup> MONKS & MINOW, *supra* note 68, at 9.

<sup>82</sup> During that time, the author wrote extensively about that phenomenon. See Daniel J. Morrissey, *Defensive Tactics in Tender Offers-Does Anything Go?*, 534 TENN. L. REV. 103, 103-05 (1985); Daniel J. Morrissey, *Law, Ethics, and the Leveraged Buyout*, 65 U. DET. L. REV. 403, 406 (1988); Daniel J. Morrissey, *Safeguarding the Public Interest in Leveraged Buyouts*, 69 OR. L. REV. 47 (1990).

<sup>83</sup> See Frank H. Easterbrook & Daniel R. Fischel, *The Proper Role of a Target's Management in Responding to a Tender Offer*, 94 HARV. L. REV. 1161, 1168-69 (1981); Ronald J. Gilson, *A Structural Approach to Corporations: The Case Against Defensive Tactics in Tender Offers*, 33 STAN. L. REV. 819, 841 (1981).



wrote, fails to make proper use of a firm's resources, which causes its stock price to go down.<sup>84</sup> The underperforming company then attracts a hostile bidder who wants to gain control so he can dismiss the firm's management and restructure it to achieve more profitability. Such a result is good for everyone, according to the theory, except the officers and directors who are replaced. Shareholders have their wealth enhanced, the new owner gains from better deployment of the firm's resources, and the overall economy is enriched by a more productive use of corporate wealth. Even the possibility of a tender offer disciplines an underachieving management to increase share value to ward off such undesired advances.<sup>85</sup>

A series of judicial rulings from the Delaware Supreme Court, however, failed to follow that logic. Instead, they deferred to the business judgment of incumbent boards and allowed them to employ various defensive tactics, like poison pills, to deter unwanted tender offers.<sup>86</sup> Yet those decisions also represented an overall victory for shareholder rights. While condoning the short-range, anti-takeover strategies of management, the court also recognized a board's ultimate duty to increase shareholder value. That would become a compelling consideration when a decision was made to sell the company because management would then have to actively seek the highest bid for its firm.<sup>87</sup>

The tender offer movement re-empowered shareholders by affording them more lucrative offers for their stock than existed in the trading market.<sup>88</sup> The potential for such hostile take-overs would, according to law and economics theory, lead incumbent managements to make their firms more profitable. As a consequence, a corporation might have to forgo socially beneficial activity that could reduce its bottom line.

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<sup>84</sup> Easterbrook, *supra* note 83, at 1196-97.

<sup>85</sup> In the same vein, Judge Henry Friendly called takeovers "the sharpest blade for the improvement of corporate management." See Henry J. Friendly, Senior Judge, U.S. Court of Appeals, Speech to the ALI-ABA (May 4-6, 1978), in 3 ALI-ABA COURSE MATERIALS J. 128 (1978).

<sup>86</sup> Chief among those were *Unocal Corp. v. Mesa Petroleum Co.*, 493 A.2d 946 (Del. 1985) and *Moran v. Householder Int'l, Inc.*, 500 A.2d 1346 (Del. 1985).

<sup>87</sup> See *Smith v. Van Gorkom*, 488 A.2d 858 (Del. 1985); see also *Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc.*, 506 A.2d 173 (Del. 1986).

<sup>88</sup> As one author wrote of that phenomenon, "[d]uring the 1980s, nearly half of all U.S. companies were restructured, more than 80,000 were acquired or merged, and over 700,000 sought bankruptcy protection in order to reorganize and continue operations." ANDREW J. SHERMAN, *MERGERS AND ACQUISITIONS FROM A TO Z*, at xii (3d. ed. 2010).

D. *The Court Protects More Than Profit Maximizing Corporate Decisions*

That unfortunate result, however, was blunted by a series of decisions from Delaware affirming management's prerogative to adopt defensive measures that could, up to a point, thwart hostile bids. In one such leading opinion, *Unocal v. Mesa Petroleum*, the Delaware Supreme Court held that directors facing a tender offer could consider the effect that it might have on constituencies other than its shareholders.<sup>89</sup> Those would include "creditors, customers, employees, and . . . the community."<sup>90</sup> This helped CSR because it gave management some leeway to make decisions based on factors other than profit.

Likewise, that High Court stated a year later that so long as the directors have not made a decision to sell the company, "[a] board may have regard for various constituents . . . provided there are rationally related benefits accruing to the stockholders."<sup>91</sup> Three years later the Delaware Supreme Court refined that position, giving the board the power to reject even a high priced offer if it was not "offered by a reputable and responsible bidder."<sup>92</sup> A board might make that determination based at least in part on concerns for corporate constituents other than shareholders.<sup>93</sup>

The same year, in *Paramount Communications v. Time, Inc.*, Delaware Chancellor William T. Allen refused a shareholder's request to enjoin a merger entered into to forestall a hostile takeover.<sup>94</sup> The plaintiff stockholder argued that the combination should be stopped because it would frustrate the immediate maximization of share value.<sup>95</sup> The Chancellor, however, ruled that management is allowed to engage in such strategic maneuvers even at the expense of

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<sup>89</sup> *Unocal*, 493 A.2d at 955-56.

<sup>90</sup> *Id.* at 955.

<sup>91</sup> *Revlon*, 506 A.2d. at 182. For comment on how that might impact CSR issues, see JAMES ROSELLE, *The Triple Bottom Line: Building Shareholder Value, in CORPORATE SOCIAL RESPONSIBILITY: THE CORPORATE GOVERNANCE OF THE 21ST CENTURY* 132 (Ramon Mullerat, ed., 2d ed. 2011); see also Anthony Bisonti, *The Double Bottom Line: Can Constituency Statutes Protect Socially Responsible Corporations Stuck in Revlon Land?*, 42 LOY. L.A. L. REV. 765 (2009).

<sup>92</sup> *Mills Acquisition Co. v. MacMillan, Inc.*, 559 A.2d 1261, 1282 (Del. 1989).

<sup>93</sup> RADU MARES, *THE DYNAMICS OF CORPORATE SOCIAL RESPONSIBILITY* 39 (2008) (citing D. Gordon Smith, *The Shareholder Primacy Norm*, 23 J. CORP. L. 277 (1998)).

<sup>94</sup> See *Paramount Commc'ns, Inc. v. Time, Inc.*, Nos. 10866, 10670 and 10935, 1989 WL 79880 (Del. Ch. July 14, 1989), *aff'd*, 571 A.2d 1140 (unpublished).

<sup>95</sup> *Id.* at \*21.

short-term shareholder gain.<sup>96</sup> The Delaware Supreme Court affirmed, holding that absent a limited set of circumstances management “is not under any *per se* duty to maximize shareholder value in the short-term.”<sup>97</sup>

The tender offer epoch also led many state legislatures to enact so-called “Constituency Statutes” as part of their corporate codes. These took a broad view of corporate welfare and specifically gave boards a mandate to consider the effects of any corporate action upon its non-shareholders stakeholders such as employees, suppliers, and customers of the corporation.<sup>98</sup> Directors were also allowed to take into account the effects of their decisions on the “communities in which offices or other establishments of the corporation are located, and all other pertinent factors.”<sup>99</sup> States amended their corporate codes allowing boards to adopt a variety of anti-takeover provisions.<sup>100</sup> These varied in content but their intended result was to allow management to impede or delay a hostile bid. The constituency and anti-takeover statutes were thus designed to give boards both explicit grounds and specific tactics that they could use to deter and resist tender offers. As Professor Elhauge has pointed out, this enhanced respect for a board’s business judgment allows directors to make non-profit making decisions that support the goals of CSR.<sup>101</sup>

<sup>96</sup> *Id.* at \*30.

<sup>97</sup> *Paramount Commc’ns, Inc. v. Time, Inc.*, 571 A.2d. 1140, 1142 (Del. 1989).

<sup>98</sup> See generally Stephen M. Bainbridge, *Interpreting Nonshareholder Constituency Statutes*, 19 PEPP. L. REV. 971 (1992); Lawrence E. Mitchell, *A Theoretical and Practical Framework for Enforcing Corporate Constituency Statutes*, 70 TEX. L. REV. 579 (1992); Eric W. Otis, *Beyond Shareholders: Interpreting Corporate Constituency Statutes*, 61 GEO. WASH. L. REV. 14 (1992).

<sup>99</sup> MARES, *supra* note 93, at 38.

<sup>100</sup> See *id.*

<sup>101</sup> See generally Einer Elhauge, *Sacrificing Corporate Profits in the Public Interest*, 80 N.Y.U. L. REV. 733 (2005). As renowned venture capitalist Peter Thiel points out, however, only firms that have some insulation from competitive markets may have this room to maneuver. From his perspective in Silicon Valley he writes:

The problem with a competitive business goes beyond lack of profits. Imagine you’re running one of those restaurants in Mountain View. You’re not that different from dozens of your competitors, so you’ve got to fight hard to survive. If you offer affordable food with low margins, you can probably pay employees only minimum wage . . . . A monopoly like Google is different. Since it doesn’t have to worry about competing with anyone, it has wider latitude to care about its workers, its products, and its impact on the wider world. Google’s motto—“Don’t be evil”—is in part a branding ploy, but it’s also characteristic of a kind of business that’s successful enough to take ethics seriously without jeopardizing its own existence.

Such initiatives did not sit well with business groups and law and economics theorists. They challenged those state provisions as specifically geared to inhibit contests for corporate control, which they claimed would promote more efficient commercial operations and be wealth enhancing for stockholders.<sup>102</sup> Advocates of that position went even further and claimed that their version of laissez-faire economics was required by the Commerce Clause of the United States Constitution.<sup>103</sup> The United States Supreme Court, however, turned aside those arguments finding that absent express federal pre-emption, corporate law is state law.<sup>104</sup> Under the internal affairs doctrine, states were therefore free to prescribe the governing rules for businesses that are incorporated in their jurisdictions.<sup>105</sup>

CSR advocates also achieved a partial victory during the 1980s when the American Law Institute adopted Section 2.01 of its *Principles of Corporate Governance: Analysis and Recommendations*.<sup>106</sup> It began by reaffirming the traditional purpose of a corporation as profit and shareholder gain.<sup>107</sup> In succeeding paragraphs, however, it qualified that by approving of other corporate activity although it might not be remunerative for the firm.<sup>108</sup>

In subpart (b)(2), the ALI stated that in the conduct of its business a corporation “[m]ay take into account ethical considerations that are reasonably regarded as appropriate to the responsible conduct of business.”<sup>109</sup> In subpart (b)(3), the ALI went even further and said that a corporation “[m]ay devote a reasonable amount of resources to public welfare, humanitarian, educational, and philanthropic purposes.”<sup>110</sup> In similar fashion, Section 302(13) of the Revised Model Business Corporations Act, adopted at about the same time, lists among a corporation’s general powers, “to make donations for the public welfare or for charitable, scientific, or educational purposes.”<sup>111</sup>

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<sup>102</sup> *CTS Corp. v. Dynamics Corp. of Am.*, 481 U.S. 69, 91-92 (1987).

<sup>103</sup> U.S. CONST. art. 1, § 8, cl. 3; see *CTS Corp.*, 481 U.S. at 93.

<sup>104</sup> *CTS Corp.*, 481 U.S. at 93.

<sup>105</sup> *Id.* at 86-87.

<sup>106</sup> 1 AM. LAW INSTITUTE, PRINCIPLES OF CORPORATE GOVERNANCE: ANALYSIS AND RECOMMENDATIONS, pt. II, § 2.01 (1992). For a good description of the history of this project, see Douglas M. Branson, *Proposal for Corporate Governance Reform: Six Decades of Ineptitude and Counting*, 48 WAKE FOREST L. REV. 673, 683-86 (2013).

<sup>107</sup> AM. LAW INSTITUTE, *supra* note 106, § 2.01.

<sup>108</sup> *Id.*

<sup>109</sup> *Id.*

<sup>110</sup> *Id.*

<sup>111</sup> MODEL BUS. CORP. ACT § 3.02(13) (2002).

### III. SHAREHOLDER CONTRIBUTIONS TO IMPROVED CORPORATE GOVERNANCE

#### A. *Options for Increasing Shareholder Power*

For shareholder governance rights to be effective they must overcome several traditional drawbacks. First is the “rational apathy” that discourages most stockholders from reviewing management conduct in the firms where they invest. Such activity hardly seems worth the effort when a limited percentage of ownership means there is so little at stake for a particular stockholder. Better to follow the “Wall Street rule” and sell, goes the logic, rather than challenge improper practices by corporate officials.<sup>112</sup> Such departures by disgruntled shareholders may drive down share prices but they do little to remedy harmful managerial conduct.<sup>113</sup>

Another long-standing barrier to shareholder engagement is management’s control over the mechanism for soliciting proxies to elect directors.<sup>114</sup> Top executives always have their own slate for those lucrative positions, and a shareholder who puts forth her competing candidates must pay the significant expense of garnering support from other stockholders. Several years ago, the SEC made a rule that would change that by allowing a significant shareholder to propose her own nominees for directors and have them sent out at the company’s expense.<sup>115</sup> The Court of Appeals, however, invalidated that initiative to foster shareholder democracy on the grounds that the Commission did not do a proper study of its costs and benefits.<sup>116</sup>

Yet the push for shareholder participation in corporate governance continues to gain ground. Commentators keep assailing the “[d]omination of public companies by self-serving and ineffective executives [that] costs America billions of dollars every year and contributed to the current economic meltdown.”<sup>117</sup> The exposure of those abusive practices has propelled new corporate governance models designed to reform

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<sup>112</sup> GEVURTZ, *supra* note 71, at 232.

<sup>113</sup> See MONKS & MINOW, *supra* note 68, at 129-30.

<sup>114</sup> See GEVURTZ, *supra* note 71, at 233.

<sup>115</sup> See *Business Roundtable v. SEC*, 647 F.3d 1144, 1147 (D.C. Cir. 2011).

<sup>116</sup> See *id.* at 1150-51.

<sup>117</sup> George W. Dent Jr., *The Essential Unity of Shareholders and the Myth of Investor Short-Termism*, 35 DEL. J. CORP. L. 97 (2010).

the “old boy” network of boards that has been all too inclined to rubberstamp decisions of dominant chief executives.<sup>118</sup>

At the heart of the models are measures for independent directors who would serve on audit and compensation committees to make sure there are meaningful internal checks on fraud and other illegal activity by management. Several leading academics have lent their support here, arguing that to counter those abuses shareholders must be given increased rights to guard against improper management conduct<sup>119</sup> or at least be empowered to exercise the rights they already have in a more meaningful way.<sup>120</sup>

Professor Lucien Bebchuck points out that the interests of management often are not aligned with those of its shareholders.<sup>121</sup> Consequently, corporate officials may engage in various self-dealing activities, reject beneficial acquisition offers, or engage in empire-building.<sup>122</sup> To counter that, Bebchuck persuasively contends that shareholders should be given more rights to approve or disapprove those major corporation actions.<sup>123</sup> The Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010’s Say-on-Pay provision<sup>124</sup> is a step toward such enhanced shareholder voting rights. It gives shareholders the right to express their views on management compensation, but this required referendum is non-binding.

Professor Julian Velasco differs from Bebchuck, by not calling for more measures empowering shareholders.<sup>125</sup> What is really needed, he says, is just that stockholders take their current rights seriously and be supported in that by legal authorities.<sup>126</sup> For instance, Section 14(a) of the Securities Exchange Act of 1934 already charges the SEC with regulating proxy solicitations, and the legislative history of that provision

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<sup>118</sup> Critics also point to the homogeneity of American boards that lack women or minority group members and are thus overwhelmingly “male, pale, and stale,” Gretchen Morgenson, *Choosing Not to Walk the Walk*, N.Y. TIMES, June 1, 2014, at B1. For an upcoming article that discusses this issue in the context of European Law, see Catherine M.A. McCauliff & Catherine Savio, *Gender Consideration on the Board of European Corporations: Lessons for U.S. Corporations or a Cautionary Tale?*, 16 GEO. J. GENDER & L. (forthcoming 2015).

<sup>119</sup> See Bebchuck, *supra* note 67, at 913.

<sup>120</sup> See Julian Velasco, *Taking Shareholder Rights Seriously*, 41 U.C. DAVIS L. REV. 605, 631 (2007).

<sup>121</sup> See Bebchuck, *supra* note 67, at 912-13.

<sup>122</sup> *Id.* at 914.

<sup>123</sup> *Id.*

<sup>124</sup> Dodd-Frank Wall Street Reform and Consumer Protection Act, 12 U.S.C. § 951 (2010).

<sup>125</sup> See Velasco, *supra* note 120, at 631.

<sup>126</sup> *Id.* at 634.

states that regulation must occur for the benefit of investors.<sup>127</sup> No doubt Professor Velasco would rue the Court of Appeals' decision discussed above that struck down the SEC's proxy access rule. That would have made it less expensive for shareholders to nominate their own slate of directors but it fell victim to a judicial ideology excessively sensitive to management's prerogatives.<sup>128</sup>

In other areas, however, Professor Velasco sounds more like Professor Bebchuck. Velasco points out that shareholder rights to vote on important matters like mergers and by-law amendments are severely restricted because directors must first approve those initiatives.<sup>129</sup> He also calls for other reforms that activist shareholders are already including in settlements of derivative suits as ways to remedy wrongful management conduct.<sup>130</sup> One of these new requirements is that directors must receive a majority of all votes cast. Unlike the traditional rule that a director is elected by plurality vote, the majority requirement would give shareholders a greater power to prevent the election of undesirable candidates.<sup>131</sup> Velasco also recommends the elimination of staggered boards of directors.<sup>132</sup> In that system directors have multi-year terms and are classified so that they do not all stand for election every year. Annual election of directors, by contrast makes them less entrenched and more accountable to shareholders. It might also remove a deterrent to a tender offer that could return increased value to shareholders. A potential bidder then would not be put off by having to wait more than a year to gain control of a board once she has achieved majority stock ownership.

Along those lines, Velasco points out that corporate law is mostly geared toward enabling a firm's activity and does not

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<sup>127</sup> *Id.* at 614.

<sup>128</sup> *See* Business Roundtable v. SEC, 647 F.3d 1144, 1154 (D.C. Cir. 2011).

<sup>129</sup> *See* Velasco, *supra* note 120, at 677.

<sup>130</sup> *Id.* at 641-61. Since derivative suits are equitable in nature, the Court has broad discretion in granting relief. DEBORAH A. DEMOTT & DAVID F. CAVERS, SHAREHOLDER DERIVATIVE ACTIONS: LAW AND PRACTICE § 7.6 (2013); *see also generally* Bert S. Prunty, *The Shareholders' Derivative Suit Notes on its Derivation*, 32 N.Y.U. L. REV. 980 (1957); *see, e.g., In re Pfizer Inc. S'holder Derivative Litig.*, 780 F. Supp. 2d 336 (S.D.N.Y. 2011) (approving a settlement involving the creation of a new board-level regulatory committee); *see also* Memorandum of Understanding, *In re News Corp. S'holder Derivative Litig.*, No. 6285 (Del. Ch. Apr. 17, 2013), *available at* <http://www.newscorpderivativesettlement.com/pdf/mou.pdf>; *In re Johnson & Johnson Derivative Litig.*, 900 F. Supp. 2d 467 (D.N.J. 2012) (containing significant provisions geared to enhance board-level responsibility for legal and regulatory compliance).

<sup>131</sup> In 2012, directors at 41 public companies failed to gain 50% shareholder approval for their reelection, yet they have remained in office. James B. Stewart, *When Shareholder Democracy is Sham Democracy*, N.Y. TIMES, Apr. 13, 2013, at B1, *available at* <http://www.nytimes.com/2013/04/13/business/sham-shareholder-democracy.html>.

<sup>132</sup> Velasco, *supra* note 120, at 647.

mandate its substantive conduct.<sup>133</sup> The statutory rules for corporate governance therefore are only default provisions and can be changed.<sup>134</sup> In that regard he points to shareholder initiated reforms that more corporations are accepting such as the requirement that each director be elected by a majority of the shareholders.<sup>135</sup>

Professor Velasco also notes the increasing dominance of institutional shareholders with large holdings in particular stocks.<sup>136</sup> He sees that as a likely counterweight to traditional shareholder apathy.<sup>137</sup> He also dismisses an argument which is often made to deprecate the legitimate rights of shareholders—that stockholders will only use their power opportunistically to advance their own interests.<sup>138</sup>

Two well-known corporate authorities, Chancellor Leo Strine<sup>139</sup> and Professor Steven Bainbridge,<sup>140</sup> have recently asserted that position, arguing that stockholders often have viewpoints that are inconsistent with the long-term best interests of their corporations.

Professor George Dent, however, goes even further than Velasco in refuting that often-made case against shareholder empowerment. He contends that those misgivings are exaggerated and have no empirical basis.<sup>141</sup> For the most part, shareholders are not short-term oriented but instead want their officers to maximize the long-term value of their firms.<sup>142</sup>

Dent also convincingly asserts that shareholder choices are entitled to respect in the same manner as those of voters in a political democracy. Citizens may not be capable of statecraft, but they are appropriately given the power to elect those who will run their government. By the same logic, shareholders should be able to choose directors to manage the companies that they own. There is no reason that enhanced federal regulation could not further the goal of shareholder democracy

<sup>133</sup> See Velasco, *supra* note 120, at 656.

<sup>134</sup> *Id.* at 656 n.250.

<sup>135</sup> *Id.* at 643.

<sup>136</sup> *Id.* at 623, 628.

<sup>137</sup> *Id.* at 622-24.

<sup>138</sup> *Id.* at 635-37.

<sup>139</sup> Leo E. Strine, Jr., *Toward a True Corporate Republic: A Traditionalist Response to Bebchuk's Solution for Improving Corporate America*, 119 HARV. L. REV. 1759, 1769-70 (2006). At the time of the writing of this piece Leo Strine held the office of Vice-Chancellor, but was subsequently appointed the Chief Justice of Delaware.

<sup>140</sup> Stephen M. Bainbridge, *Director Primacy and Shareholder Disempowerment*, 119 HARV. L. REV. 1735, 1735-37, 1745, 1749-51 (2006).

<sup>141</sup> Dent, *supra* note 117, at 122-28.

<sup>142</sup> *Id.*



and empowerment as well as mandate that corporations act in a socially responsible manner.

*B. Hopeful Signs of Shareholder Activism*

The need for greater accountability by corporate officials is a compelling objective. There have to be effective checks on their innate tendencies to enrich themselves at the expense of various corporate constituents and society itself. Investigations after the Watergate scandal revealed a widespread pattern of illegal campaign contributions and other improper activity by a large number of major corporations.<sup>143</sup> In response, the SEC began demanding more disclosure of the composition and workings of public boards.<sup>144</sup> The American Law Institute followed suit with a 16-year project that culminated in its “Principles of Corporate Governance.”<sup>145</sup> It included “good practice” guidelines for the make-up and operation of boards.<sup>146</sup>

Then, after the dot-com bubble burst at the turn of the century, prominent financial frauds like Enron and WorldCom came to light.<sup>147</sup> They resulted in the loss of billions of dollars of shareholder wealth and precipitated the Sarbanes-Oxley Act of 2002, creating stringent requirements for disclosures about the governance practices of public corporations.<sup>148</sup> The required disclosures included whether the firms had watchdog board committees to oversee audits, executive compensation, and the nomination of new directors.<sup>149</sup> The Act also demanded transparency about whether the directors on those panels were independent from the top executives of their companies.<sup>150</sup> The major stock exchanges soon followed with their own

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<sup>143</sup> See M. Thomas Arnold, “*It’s Déjà vu All Over Again*”: Using Bounty Hunters to Leverage Gate Keeper Duties, 45 TULSA L. REV. 419, 427 (2009).

<sup>144</sup> See GEVURTZ, *supra* note 71, at 241.

<sup>145</sup> *Id.*

<sup>146</sup> *Id.*

<sup>147</sup> For two good books about the Enron scandal, see generally BETHANY MCLEAN & PETER ELKIND, THE SMARTEST GUYS IN THE ROOM: THE AMAZING RISE AND SCANDALOUS FALL OF ENRON (2003); REBECCA SMITH & JOHN R. EMHWILLER, 24 DAYS: HOW TWO WALL STREET JOURNAL REPORTERS UNCOVERED THE LIES THAT DESTROYED FAITH IN CORPORATE AMERICA (2003). For a good description of the WorldCom accounting fraud, see Peter Elstrom, *How to Hide \$3.8 billion in Expenses*, BLOOMBERG BUSINESSWEEK (June 27, 2002), <http://www.businessweek.com/stories/2002-06-27/how-to-hide-3-dot-8-billion-in-expenses>.

<sup>148</sup> Sarbanes-Oxley Act of 2002, Pub. L. No. 107-204, 116 Stat. 745 (codified in scattered sections of 15 U.S.C. and 18 U.S.C. (2002)).

<sup>149</sup> *Id.* at § 301 (codified at 15 U.S.C. § 78f).

<sup>150</sup> *Id.*

“independence” standards for the boards of companies whose shares are listed there.<sup>151</sup>

The newly required disclosures were geared towards making the leaders of public companies more accountable to their shareholders and the public. Sadly, they did little to stop the devastating financial meltdown of 2008. As one commentator observed after, “The recent financial crisis makes clear that the directors and officers of public corporations have not internalized Enron’s lessons.”<sup>152</sup>

Congress responded with more legislation, Dodd-Frank,<sup>153</sup> that, among other things, provided additional requirement for shareholder participation in governance. The law requires disclosure about situations where the same individual is both CEO and Chair of the Board<sup>154</sup> and, with its “Say-on-Pay” provision, also gave shareholders an advisory vote on executive compensation.<sup>155</sup>

Shareholders are increasingly involved in movements to challenge traditional corporate goals. When he points out the entrenchment of wealth perpetuated through the traditional corporate structure, Carl Ichan, a major investor and shareholder activist, puts it bluntly, “[I]n the middle ages, feudal lords asserted the ‘divine right’ of royalty to justify their lordly positions while plundering the peasants. Today’s boards act like they are vested with similar powers.”<sup>156</sup> Ichan then notes how formerly disconnected shareholders can be united by social media and other communication tools and he pledges to use them “to make more shareholders aware of their rights and what can be done to keep those rights from being trampled on.”<sup>157</sup> Other shareholder activists have put out similar calls for unified action.<sup>158</sup>

<sup>151</sup> GEVURTZ, *supra* note 71, at 242.

<sup>152</sup> Hillary A. Sale, *The New “Public” Corporation*, 74 LAW & CONTEMP. PROBS. 137 (2011).

<sup>153</sup> See Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, 124 Stat. 1376 (codified in scattered sections throughout the U.S.C. (2010)); see generally Daniel Morrissey, *Reining in Wall Street: Dodd-Frank Provides a Needed Mechanism to Bridle the Animal Spirits that Drive the Financial Community*, NAT’L L. J. OPINION (Aug. 30, 2010), <http://www.nationallawjournal.com/id=1202471121556/Reining-in-Wall-Street?slreturn=20150205135812>.

<sup>154</sup> See Dodd-Frank Wall Street Reform and Consumer Protection Act § 972.

<sup>155</sup> See *id.* § 951.

<sup>156</sup> Ichan, *supra* note 70, at 1.

<sup>157</sup> *Id.*

<sup>158</sup> These efforts appear to be bearing fruit as some boards are inviting activist shareholders to join them as directors. David Benoit, *Companies, Activists Declare Truce in Boardroom Battles: Corporate Executives, Directors Find it Cheaper to Negotiate than Fight*, WALL ST. J. (Dec. 9, 2013, 8:01 PM), <http://online.wsj.com/news/articles/SB10001424052702303330204579248501076906672>.

John Liu, New York City's comptroller oversees the city's pension funds that own a large stake in Cablevision.<sup>159</sup> Expressing outrage at directors who lost elections but remained on the company's board Liu said, "As fiduciaries, we can't sit by and let the board make a mockery of our fundamental right to elect directors."<sup>160</sup> He urged a proxy fight against such "zombie directors," stating, "Share owners need accountable directors who will ensure the company isn't being run for the benefit of insiders at our expense."<sup>161</sup>

Activist stockholders are also becoming effective at controlling excessive executive compensation. Approximately 128,000 shareholders of Verizon who are retirees of its predecessor companies achieved a partial victory last year when the company agreed to cut back performance-based stock awards for its officials if Verizon's stock does not do well.<sup>162</sup> The group has also moved against any severance awards at the company that are more than three times the retiring officers' base pay and incentives.<sup>163</sup> In similar fashion, investment officers at the California State Teachers' Retirement System (CalPERS) are questioning peer group standards for executive pay that are out of line with compensation paid at truly comparable companies.<sup>164</sup> Activist stockholders are also using the shareholder proposal mechanism in the federal securities laws<sup>165</sup> to prod their companies to undertake socially responsible activities. In 2014, 56% of shareholder proposals concerned environmental and social issues.<sup>166</sup>

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<sup>159</sup> Stewart, *supra* note 131, at 1.

<sup>160</sup> *Id.*

<sup>161</sup> *Id.*

<sup>162</sup> Gretchen Morgenson, *As Shareholders Say 'Enough Already,' Some Boards Are Starting to Listen*, N.Y. TIMES, Apr. 7, 2013, at BU1, available at <http://www.nytimes.com/2013/04/07/business/shareholders-can-slow-the-executive-pay-express.html>.

<sup>163</sup> *Id.*

<sup>164</sup> See Gretchen Morgenson, *A Better Way to Compare C.E.O. Pay*, N.Y. TIMES, Sept. 22, 2013, at BU1, available at <http://www.nytimes.com/2013/09/22/business/a-better-way-to-compare-ceo-pay.html>.

<sup>165</sup> See 17 C.F.R. § 240.14a-8 (2012).

<sup>166</sup> Emily Chasan, *More Companies Bow to Investors With a Social Cause*, THE CFO REPORT: WALL ST. J. (Apr. 1, 2014, 2:44 AM), <http://blogs.wsj.com/cfo/2014/04/01/more-companies-bow-to-investors-with-a-social-cause/>.

#### IV. ACHIEVING THE TRIPLE BOTTOM LINE

##### A. *CSR at the Close of the Century*

In a famous address delivered in 1992, Chancellor Allen acknowledged how “turbulent” the 1980s had been for corporate law.<sup>167</sup> Two different and contradictory approaches to a corporation’s *raison d’être*, he said, had peacefully co-existed for decades.<sup>168</sup> One which he called the “property conception” was premised on shareholder primacy and held that the board’s paramount duty was to maximize profits.<sup>169</sup> The other, which he labeled the “social entity conception,” charged the corporation with broader obligations.<sup>170</sup> This conflict, he said, had been “papered over”<sup>171</sup> by the general acceptance that corporate philanthropy could be justified as being in the long term best interest of the firm and its shareholders.

Such an approach, said the Chancellor, had worked when American companies were free from global competition and impervious to hostile take-overs.<sup>172</sup> The dynamic world economy and the rise of tender offers, however, had exposed the inconsistencies of that position and forced the law to grapple with issues pitting CSR against shareholder value. Courts, he said, were hardly eager to decide those questions because there was “no widely accepted doctrine [that] offered a clear guide.”<sup>173</sup>

With landmark decisions like *Paramount Pictures*,<sup>174</sup> Allen said, the Courts had punted the problem back to corporate boards.<sup>175</sup> Conscientious directors now have to grapple with them.<sup>176</sup> It all comes down, the Chancellor wisely observed, to a fundamental clash between one notion of corporations as

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<sup>167</sup> William T. Allen, *Our Schizophrenic Conception of the Business Corporation*, 14 CARDOZO L. REV. 261, 263 (1992). As one commentator said of Chancellor Allen’s particular expertise, “Especially during the late 1980s and early 1990s, when Chancellor Allen was deciding cases, the Delaware Court of Chancery was the center of the corporate law universe.” D. Gordon Smith, *Chancellor Allen and the Fundamental Question*, 21 SEATTLE U. L. REV. 577, 578 (1998).

<sup>168</sup> Allen, *supra* note 167, at 264-65.

<sup>169</sup> *Id.*

<sup>170</sup> *Id.*

<sup>171</sup> *Id.* at 272.

<sup>172</sup> *Id.* at 266.

<sup>173</sup> *Id.* at 275.

<sup>174</sup> See *Paramount Commc’ns Inc. v. Time Inc.*, Nos. 10866, 10670, and 10935, 1989 WL 79880 (Del. Ch. July 14, 1989), *aff’d*, 571 A.2d 1140 (unpublished).

<sup>175</sup> See Allen, *supra* note 167, at 276.

<sup>176</sup> See *id.*

economic and financial entities as opposed to another which sees them as institutions of political and social significance.<sup>177</sup>

As most Americans experienced increasing economic insecurity during the latter part of the twentieth century,<sup>178</sup> advocates for CSR became even more forceful. Accelerating ecological concerns contributed to its increasing prominence as well. It was thus in the early 1990s that a well-known environmentalist, John Elkington, coined the term “triple-bottom-line.”<sup>179</sup> It succinctly asserted that in a system of sustainable capitalism a corporation’s profit-making goals had to be both eco-friendly and tempered by a commitment to a fair distribution of the world’s resources.<sup>180</sup>

A report from the John F. Kennedy School of Government at Harvard aptly described how different movements were then coalescing in this drive for an enhanced corporate mandate.<sup>181</sup> It found that reformers were demanding corporations serve not just their shareholders’ interests for financial gain but also attend to the needs of their employees, consumers, communities, and society as a whole.<sup>182</sup> The report described these varied efforts in this fashion:

The term [CSR] is often used interchangeably with corporate responsibility, corporate citizenship, social enterprise, sustainability,

<sup>177</sup> *Id.* at 264-65.

<sup>178</sup> This is perhaps the most pressing problem facing the United States and has been written extensively about in Morrissey, *supra* note 70. Among the many fine studies on this important issue, HEDRICK SMITH, WHO STOLE THE AMERICAN DREAM (2012) is one the best. As the author there wrote of that disturbing trend which began in the late 1970s:

The soaring wealth of the super-rich has brought the unraveling of the American Dream for the middle class—the dream of a steady job with decent pay and health benefits, rising living standards, a home of your own, a secure retirement, and the hope that your children would enjoy a better future.

*Id.* at xvi. The harmful psychological effect of this insecurity on American workers is described in a series of articles that appeared in the September/October 2013 issue of AMERICAN PROSPECT under the apt title, *Work in the Age of Anxiety*. The lead piece presents the effects of the decline in real wages since 1974. See generally Harold Meyerson, *The Forty-Year Slump*, in AMERICAN PROSPECT: WORK IN THE AGE OF ANXIETY (Sept./Oct. 2013), available at <http://prospect.org/article/40-year-slump>. The impact of this poor compensation on workers’ commitments to their jobs is predictable. The Gallup poll reports that “52% of workers are mentally ‘checked out’ and an additional 18% are actively disengaged.” John Stancavage, *A Cure for Workplace Zombies is Possible*, TULSA WORLD, Aug. 11, 2013 at E1, available at [http://www.tulsaworld.com/business/john-stancavage-managers-need-to-find-a-cure-for-workplace/article\\_0546d971-aead-55a8-aca4-37ce3456d158.html](http://www.tulsaworld.com/business/john-stancavage-managers-need-to-find-a-cure-for-workplace/article_0546d971-aead-55a8-aca4-37ce3456d158.html).

<sup>179</sup> MICHAEL KERR ET AL., CORPORATE SOCIAL RESPONSIBILITY: A LEGAL ANALYSIS 24 (2009).

<sup>180</sup> *Id.*

<sup>181</sup> *Id.* at 7-8.

<sup>182</sup> *Id.*

sustainable development, triple-bottom line, corporate ethics, and in some cases corporate governance. Though these terms are different, they all point in the same direction: throughout the industrialized world and in many developing countries there has been a sharp escalation in the social roles corporations are expected to play.<sup>183</sup>

Thus, increased tension between the shareholder's goal to maximize profit and the increasing concern and awareness of the need for socially responsible corporations is begging for a solution. One is for a uniform federal regulation of corporations that would establish such a mandate.

### B. *CSR Today*

In the years since the twenty-first century began, the push for CSR has continued to gain momentum. The phenomenon is attributable at least in part to the global rise of social and environmental awareness that quite naturally focuses on corporate behavior. For instance, business was first made responsible for making development sustainable at the United Nations Conference on Environment and Development held in Rio de Janeiro in 1992. The follow-up conference held in Johannesburg 10 years later not only re-enforced CSR goals of the prior conference but called for "continuous improvement in corporate practices" to achieve it.<sup>184</sup> The United Nations continued this momentum with another environmental conference in New York City in September 2014.

Such agendas are fostered by concerned groups that have sprung up over the last several decades to address social ills. There are now thousands of these non-governmental organizations (NGOs) and many of them focus on activities by business, especially those that operate on a world-wide scale. Their attention is on labor, environmental, and human rights issues and those that involve corrupt conduct. CorpWatch, an American organization, is a good example. Its mission is "to expose multinational corporations that profit from war, fraud, environmental, human rights and other abuses, and to provide critical information to foster a more informed public and an effective democracy."<sup>185</sup> Even an editorially conservative

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<sup>183</sup> *Id.* (alteration in original).

<sup>184</sup> *Id.* at 18-19.

<sup>185</sup> *About CorpWatch*, CORP WATCH, <http://www.corpwatch.org/article.php?id=11314> (last visited Feb. 25, 2015).

newspaper like the Wall Street Journal has continued to focus on these corporate abusers.<sup>186</sup>

Such activity has engendered a favorable response from business. A majority of Fortune 500 companies now publish a CSR or sustainability report, a significant increase from the small handful that did so 10 years ago.<sup>187</sup> Internationally the result is much the same.<sup>188</sup>

Many of these moves have been initiated by business leaders themselves. In a famous speech at the World Economic Forum in Davos, Switzerland in 2008, Bill Gates called for a new system of “creative capitalism” to tackle problems like the eradication of malaria.<sup>189</sup> To that end Gates later wrote, “It is mainly corporations that have the skills to make technological innovations work for the poor. To make the most of those skills, we [must] stretch the reach of market forces so that more companies can benefit from doing work that makes more people better off.”<sup>190</sup>

In that vein, John Mackey, the president of Whole Foods, has recently co-authored a book called *Conscious Capitalism: Liberating the Heroic Spirit of Business*.<sup>191</sup> As its title states, Mackey believes most business people are motivated not just to make profit but at least in part to do good for others.<sup>192</sup> Mackey and Gates’s efforts are two prime examples of what some have called, “[p]hilanthrocapitalism . . . a more self-consciously innovative and entrepreneurial effort to tackle the world’s most urgent social problems.”<sup>193</sup>

<sup>186</sup> See, e.g., Eva Dou, *China’s Tech Factories Turn to Student Labor*, WALL ST. J. (Sept. 25, 2014), <http://online.wsj.com/articles/chinas-tech-factories-turn-to-student-labor-1411572448>.

<sup>187</sup> Knowledge@Wharton, *Why Companies Can No Longer Afford to Ignore Their Social Responsibilities*, TIME.COM (May 28, 2012), <http://business.time.com/2012/05/28/why-companies-can-no-longer-afford-to-ignore-their-social-responsibilities/>.

<sup>188</sup> Approximately “seventy percent of the companies listed on the Toronto Stock Exchange” now issue such reports annually. Craig Kielburger & Marc Kielburger, *The Rise of Corporate Social Responsibility*, HUFFINGTON POST (May 25, 2011), [http://www.huffingtonpost.com/craig-kielburger-and-marc-kielburger/the-rise-of-corporate-soc\\_b\\_85395.html](http://www.huffingtonpost.com/craig-kielburger-and-marc-kielburger/the-rise-of-corporate-soc_b_85395.html). More than 8,000 businesses world-wide have signed on to the UN Global Compact promising responsible action in the areas of human rights, labor standards, and environmental protection. See Knowledge@Wharton, *supra* note 187.

<sup>189</sup> Bill Gates, Chairman, Microsoft Corp., *A New Approach to Capitalism in the 21st Century*, Address at the World Economic Forum (Jan. 24, 2008), *available at* <https://www.youtube.com/watch?v=Ql-Mtlx31e8>.

<sup>190</sup> Bill Gates & Barbara Kiviat, *Making Capitalism More Creative*, TIME (July 31, 2008), <http://content.time.com/time/magazine/article/0,9171,1828417,00.html>.

<sup>191</sup> JOHN MACKEY & RAJ SISODIA, *CONSCIOUS CAPITALISM: LIBERATING THE HEROIC SPIRIT OF BUSINESS* (2013).

<sup>192</sup> See *id.*

<sup>193</sup> Chrystia Freeland, *Plutocrats vs. Populists*, N.Y. TIMES, Nov. 3, 2013, at SR1, *available at* <http://www.nytimes.com/2013/11/03/opinion/sunday/plutocrats-vs-populists.html>.

Those nobler purposes should be specifically acknowledged, says Mackey, and business should therefore take into account the interests of all their stakeholders, like their employees and the communities that they serve.<sup>194</sup> The founders of Google professed a similar commitment to the common good in their prospectus when the company went public in 2004 stating, “We believe strongly that in the long term, we will be better served—as shareholders and in all other ways—by a company that does good things for the world even if we forgo short term gains.”<sup>195</sup>

Such sentiments resonate with the public at large. Approximately 77% of consumers now say it is important for business to be socially responsible<sup>196</sup> and 50% of them take that into consideration when they buy things.<sup>197</sup> Such concerns are even stronger among young people. Approximately 85% of them say they are interested in how corporations act<sup>198</sup> and 70% of Millennials, those ages 18 to 26, tell opinion researches that they want to work at a company that is dedicated to improving its community.<sup>199</sup>

Religious leaders and public intellectuals have also given CSR momentum. Pope Francis made this forceful statement in his November 2013 Apostolic Exhortation, “How can it be that it is not a news item when an elderly homeless person dies of exposure, but it is news when the stock market loses two points?”<sup>200</sup> In addition he criticized those who defend unfettered laissez-faire capitalism with these pointed remarks:

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<sup>194</sup> See Alan Murray, *Chicken Soup For a Davos Soul: Successful Companies Serve a Purpose Beyond Making Money*, WALL ST. J. (Jan. 16, 2013, 4:46 PM), <http://online.wsj.com/news/articles/SB10001424127887324235104578243673073627726> (reviewing MACKAY & SISODIA, *supra* note 191).

<sup>195</sup> 2004 Founders’ IPO Letter: “An Owner’s Manual” for Google’s Shareholders, GOOGLE, <https://investor.google.com/corporate/2004/ipo-founders-letter.html> (last visited Feb. 25, 2015).

<sup>196</sup> Knowledge@Wharton, *supra* note 187; see also David Brooks, *How to Leave a Mark*, N.Y. TIMES (Jan. 27, 2015), [http://www.nytimes.com/2015/01/27/opinion/david-brooks-how-to-leave-a-mark.html?\\_r=1](http://www.nytimes.com/2015/01/27/opinion/david-brooks-how-to-leave-a-mark.html?_r=1) (discussing the recent mainstream emergence of “impact investing” where investors “seek out companies that are intentionally designed both to make a profit and provide a measurable and accountable social good”).

<sup>197</sup> Kielburger, *supra* note 188.

<sup>198</sup> *Id.*

<sup>199</sup> Knowledge@Wharton, *supra* note 187. Another survey cited in an article in the editorially conservative Wall Street Journal found that 61% of those responding want corporate leaders to help solve social problems and 59% want them to be responsible for the welfare of their employees. Donald A. Baer, *The West’s Bruised Confidence in Capitalism*, WALL ST. J. (Sept. 22, 2014), <http://online.wsj.com/articles/donald-baer-the-wests-bruised-confidence-in-capitalism-1411358403>.

<sup>200</sup> VATICAN PRESS, APOSTOLIC EXHORTATION EVANGELII GAUDIUM OF THE HOLY FATHER FRANCIS TO THE BISHOPS, CLERGY, CONSECRATED PERSONS AND THE LAY FAITHFUL OF THE PROCLAMATION OF THE GOSPEL IN TODAY’S WORLD 45 (2013), *available*



Some people continue to defend trickle-down theories which assume that economic growth, encouraged by a free market, will inevitably succeed in bringing about greater justice and inclusiveness in the world. This opinion, which has never been confirmed by the facts, expresses a crude and naïve trust in the goodness of those wielding economic power and in the sacralized workings of the prevailing economic system.<sup>201</sup>

The 2012 presidential election even served as a referendum of sorts on this outlook. Republican presidential candidate Mitt Romney had made a large fortune at Bain capital, a firm that specialized in financing corporate restructuring that displaced many workers and hurt local communities. As one commentator said, it was a “cutthroat form of capitalism . . . [that] sent unheard-of profits toward the prosperous few while threatening the jobs and eroding the wages of the rest.”<sup>202</sup> President Obama made an issue of Romney’s business background, especially in key battle ground states like Michigan and Ohio that he carried on the way to his reelection.<sup>203</sup>

If the CSR movement is not yet the dominant theme in business, it has at least become an important one. Even its critics attest to that. As Clive Crook, the then deputy editor of *The Economist* acknowledged in 2005, “[t]he movement for corporate social responsibility has won the battle of ideas . . . CSR commands the attention of executives everywhere . . . and it would be a challenge to find a recent annual report of any big international company that justifies the firm’s existence merely in terms of profits rather than service to the community.”<sup>204</sup>

Part of that surge in support may be attributable to the self-interest of business itself that recognizes the goodwill it

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at [http://w2.vatican.va/content/francesco/en/apost\\_exhortations/documents/papa-francesco\\_esortazione-ap\\_20131124\\_evangelii-gaudium.html](http://w2.vatican.va/content/francesco/en/apost_exhortations/documents/papa-francesco_esortazione-ap_20131124_evangelii-gaudium.html) (click “Download PDF”).

<sup>201</sup> *Id.* at 46. For a similar take from a leading American philosopher who has advocated our collective responsibilities to one another, see MICHAEL J. SANDEL, WHAT MONEY CAN’T BUY: THE MORAL LIMITS OF MARKETS 6-11 (2012).

<sup>202</sup> Eduardo Porter, *At the Polls Choose Your Capitalism*, N.Y. TIMES, Oct. 31, 2012, at B1, available at <http://www.nytimes.com/2012/10/31/business/choose-your-capitalism.html>.

<sup>203</sup> George Will, *Status Quo Preserved in U.S. Politics*, TULSA WORLD, Nov. 9, 2012, at A20; see also Sabrina Siddiqui, *Mitt Romney Wants Business Record Removed from Obama Campaign Attacks*, HUFFPOST POLITICS (Aug. 10, 2012, 4:41 PM), [http://www.huffingtonpost.com/2012/08/10/romney-business-record-attack-ads\\_n\\_1765601.html](http://www.huffingtonpost.com/2012/08/10/romney-business-record-attack-ads_n_1765601.html).

<sup>204</sup> KERR, *supra* note 179, at 33.

can generate from this socially responsible activity<sup>205</sup> or conversely the ill-will that can come from its neglect. Two recent examples are the devastating BP oil spill in the Gulf of Mexico<sup>206</sup> and the horrible fires and sweat-shop conditions in Bangladesh factories that make clothes sold by U.S. retailers.<sup>207</sup>

Along those lines, many businesses have also profited by cost savings resulting from changes designed to benefit the environment. Dow Chemical is a good illustration of that.<sup>208</sup> Likewise companies like Gap, Inc. are proud to boast how their employee friendly policies have led to increased profitability.<sup>209</sup> As the company stated in its 2005-06 *Social Responsibility Report*, “[w]hen factories treat workers well, they also tend to produce higher-quality product and deliver it on time. The more we respect and empower our own employees, the more creative and innovative our products and marketing tend to be.”<sup>210</sup>

Institutional investors have led the way here too. CalPERS with its \$264 billion fund, has identified 111

<sup>205</sup> See Mark Pfitzer et al., *Innovating for Shared Value*, HARV. BUS. REV., Sept. 2013, at 101; Michael E. Porter & Mark R. Kramer, *Strategy and Society, The Link Between Competitive Advantage and Corporate Social Responsibility*, HARV. BUS. REV., Dec. 2006, at 78; see also JEFFREY D. SACHS, *THE PRICE OF CIVILIZATION* 42-48 (2011) (arguing the efficiency and fairness may reinforce each other); Forest L. Reinhardt et al., *Corporate Social Responsibility Through an Economic Lens*, 2 REV. ENVTL. ECON. & POL’Y 152 (2008) (questioning whether CSR requires companies to sacrifice profits).

<sup>206</sup> Jeffrey Hollender, co-founder of the American Sustainable Business Council and the Sustainability Institute had these harsh words for BP’s shortsightedness in 2010:

If British Petroleum was an authentically responsible corporation, would the Gulf be in the mess it is now . . . . An oil company driven by a mission of genuine responsibility would have voluntarily installed the non-required safety gear . . . . Yes these things can take money. An automatic switch that closes off the blowouts, for example, runs about \$500,000. But compared to the \$30 billion drop in market value of BP stock has experienced since the spill, not to mention what it might cost to clean up the entire Gulf, that’s a drop in the bucket.

Gerald Milward-Oliver, *The Soul of the Corporation*, in *CORPORATE SOCIAL RESPONSIBILITY: THE CORPORATE GOVERNANCE OF THE 21ST CENTURY*, *supra* note 91, at 77-78.

<sup>207</sup> See Julfikar Ali Manik & Jim Yardley, *Bangladesh Finds Gross Negligence in Factory Fire*, N.Y. TIMES (Dec. 17, 2012), <http://www.nytimes.com/2012/12/18/world/asia/bangladesh-factory-fire-caused-by-gross-negligence.html> (describing a November 24, 2012 fire, in which 112 workers lost their lives at the Tazreen Fashion Factory, which made clothing for global retailers like Walmart and Sears); see also Mark Anner et al., *Toward Joint Liability in Global Supply Chains: Addressing the Root Causes of Labor Violations in International Subcontracting Networks*, 35 COMP. LAB. L. & POL’Y J. 1 (2013).

<sup>208</sup> Because of energy reducing initiatives, Dow Chemical said in 2004 that it had achieved approximately \$3 billion in savings. KERR, *supra* note 179, at 42.

<sup>209</sup> *Id.*

<sup>210</sup> *Id.*

initiatives that focus on issues such as green energy and regions that are “underserved’ by investment capital.”<sup>211</sup> In addition, a new surge of student activism with roots in the 1960s anti-war protests and the 1980s movement to end apartheid has been agitating on-campus, calling on universities to divest their holdings in fossil fuel companies.<sup>212</sup>

All these undertakings have been substantially assisted by the rise of social media that can link people immediately in ways never before imagined. As one observer put it so well:

The billions of cell phones in the world will increasingly be used to record, upload, forward, and display corporate and other abuses, whether of sweatshops employing child labor, pipeline leaks, trafficking of women and children, or corporate resources [being] used to support crimes against humanity or genocide . . . . These new, powerful, ubiquitous, and interactive communication technologies . . . empower rapid, bottom-up democratic “WikiAdvocacy” by individuals, “citizen journalists” bloggers, and self-organiz[ed] coalitions, while simultaneously allowing greater scrutiny and pressure from investors, consumers, communities, established NGOs, and other market monitors.<sup>213</sup>

### C. *CSR’s Increased Sophistication*

As it has grown in strength and influence, the CSR movement has sharpened the theories that support its agenda. Two major themes now stand out. First, corporations must combine their profit making efforts with environmental and social concerns. Second, they must give appropriate consideration to the interests of all their stakeholders.<sup>214</sup> In doing this, companies must go beyond minimal legal requirements and conventional

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<sup>211</sup> Randall Smith, *A New Divestment Program Focus on Campus: Fossil Fuels*, N.Y. TIMES: DEALBOOK (Sept. 5, 2013, 3:53 PM), <http://dealbook.nytimes.com/2013/09/05/a-new-divestment-focus-fossil-fuels/>.

<sup>212</sup> Christen Graham, *From Campus Protests to Your Retirement Fund, How Divesting from Fossil Fuels and Investing in ESGs Work*, BANGOR DAILY NEWS (Mar. 18, 2013), <http://changeup.bangordailynews.com/2013/03/18/social-responsibility/from-campus-protests-to-your-retirement-fund-how-divesting-from-fossil-fuels-and-investing-in-esgs-work/>.

<sup>213</sup> Joe W. (Chip) Pitts III, *Corporate Social Responsibility: Current Status and Future Evolution*, 6 RUTGERS J.L. & PUB. POL’Y 334, 336 (2009) (footnotes omitted).

<sup>214</sup> KERR, *supra* note 179, at 11-12. *But see Burwell v. Hobby Lobby Stores, Inc.*, No. 13-354, slip op. at 31 (U.S. June 30, 2014), where the Supreme Court ruled that the owners of a closely-held corporation did not have to consider the wishes of their employees when they refused on religious grounds to offer them health insurance with certain forms of birth control required by the Affordable Care Act.

philanthropy<sup>215</sup> and stake out positive commitments to these broader concerns.<sup>216</sup>

Books and articles on these topics now abound and with their proliferation have come new ideas about how companies can balance profit with larger principles.<sup>217</sup> In the school of Progressive Corporate Law, American professors Lawrence Mitchell<sup>218</sup> and Douglas Branson<sup>219</sup> have led the way and Canadian legal scholar Joel Balkan has made a significant contribution with his work, *The Corporation: The Pathological Pursuit of Profit and Power*. Though Balkan acknowledged that a corporation is a “remarkably efficient wealth-creating machine” he argued that it should be committed to social welfare as well as profit.<sup>220</sup> “Though individualistic self-interest and consumer desires are core parts of who we are and nothing to be ashamed about,” he wrote, “they are not all of who we are.”<sup>221</sup> By extension the ethical mandate which applies to each person should therefore also control the actions of such significant human institutions as corporations.

Part of the theory supporting CSR has also targeted short-termism, which pushes corporations to externalize the costs of their demand for quick profits on the rest of society. This can take the form of worker mistreatment, environmental pollution, and a general failure to provide for the sustainability of the enterprise.<sup>222</sup> There is an obvious overlap between corporate governance and CSR.<sup>223</sup>

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<sup>215</sup> Chris Howells, *When it Comes to CSR, Size Matters*, FORBES.COM (Aug. 14, 2013, 2:28 AM), <http://www.forbes.com/sites/insead/2013/08/14/when-it-comes-to-csr-size-matters/>.

<sup>216</sup> Greg Hills et al., *Anti-Corruption as Strategic CSR: A Call to Action for Corporations*, FSG SOCIAL IMPACT ADVISORS, May 2009, at 2.

<sup>217</sup> See KERR, *supra* note 179; CORPORATE SOCIAL RESPONSIBILITY: THE CORPORATE GOVERNANCE OF THE 21ST CENTURY, *supra* note 91; DOREEN MCBARNET ET AL., *THE NEW CORPORATE ACCOUNTABILITY: CORPORATE SOCIAL RESPONSIBILITY AND THE LAW* 282-83 (2007); MARES, *supra* note 93.

<sup>218</sup> See LAWRENCE E. MITCHELL, *PROGRESSIVE CORPORATE LAW* (1995).

<sup>219</sup> DOUGLAS M. BRANSON, *CORPORATE GOVERNANCE* (1993).

<sup>220</sup> JOEL BAKAN, *THE CORPORATION: THE PATHOLOGICAL PURSUIT OF PROFIT AND POWER* 159 (2004).

<sup>221</sup> *Id.* at 166.

<sup>222</sup> LAWRENCE E. MITCHELL, *The Board as a Path to Corporate Social Responsibility*, in *THE NEW CORPORATE ACCOUNTABILITY: CORPORATE SOCIAL RESPONSIBILITY AND THE LAW*, *supra* note 217.

<sup>223</sup> Mark Walsh & John Lowry, *CSR and Corporate Governance*, in *CORPORATE SOCIAL RESPONSIBILITY: THE CORPORATE GOVERNANCE OF THE 21ST CENTURY*, *supra* note 91, at 45.

It is ultimately up to the board to be the corporate conscience and restrain this short-sightedness.<sup>224</sup> The business judgment rule, which affords directors discretion in running a corporation, gives them legal support to follow such a balanced approach.<sup>225</sup> Chancellor Allen explained the justification for that deference with these comments, “Resolving the often conflicting claims of these various corporate constituencies calls for judgment, indeed calls for wisdom, by the board of directors of the corporation.”<sup>226</sup>

As another commentator put it:

In recent years, a growing number of public companies have come to recognize that sustainable corporate profit does not result from the single-minded pursuit of financial gain. Rather sustainable growth and shareholder value are best achieved by working through a broad framework of economic, social, environmental and ethical values and shared objectives that involve constant interaction between the company and its various stakeholders.<sup>227</sup>

In much the same vein, CSR theorists have been increasingly focusing a more direct attack on Milton Friedman’s classic one dimensional definition of corporate purpose—to only maximize profits for shareholders.<sup>228</sup> McBarnet pointed out that as opposed to the holistic response of CSR, Friedman’s view represented “the atomising perspective of the traditional individualist approach.”<sup>229</sup> Another picked up on Friedman’s concession that corporations should obey laws and “ethical custom.”<sup>230</sup> Since social responsibility is certainly a moral norm for individuals, why shouldn’t it also be one for corporate citizens?<sup>231</sup> In Mitt Romney’s famous dictum, “corporations are people.”<sup>232</sup>

<sup>224</sup> See generally Kenneth E. Goodpaster & John R. Matthews, Jr., *Can a Corporation Have a Conscience?* 60 HARV. BUS. REV. 132 (1982).

<sup>225</sup> See *supra* note 116 and accompanying text.

<sup>226</sup> Allen, *supra* note 167, at 271.

<sup>227</sup> ROSELLE, *supra* note 91, at 129.

<sup>228</sup> See Friedman, *supra* note 49 and accompanying text.

<sup>229</sup> AURORA VOICULESCU, *Changing Paradigms of Corporate Criminal Responsibility: Lessons for Corporate Social Responsibility*, in THE NEW CORPORATE ACCOUNTABILITY: CORPORATE SOCIAL RESPONSIBILITY AND THE LAW, *supra* note 217, at 416.

<sup>230</sup> FRIEDMAN, *supra* note 3, at 17.

<sup>231</sup> KERR, *supra* note 179, at 53-54.

<sup>232</sup> Philip Rucker, *Mitt Romney says ‘Corporations are People’*, WASH. POST (Aug. 11, 2011), [http://www.washingtonpost.com/politics/mitt-romney-says-corporations-are-people/2011/08/11/gIQABwZ38I\\_story.html](http://www.washingtonpost.com/politics/mitt-romney-says-corporations-are-people/2011/08/11/gIQABwZ38I_story.html). In two landmark cases the Supreme Court has recently ruled that corporations can be seen as moral agents with rights to free speech and free exercise of religion. See *Burwell v. Hobby Lobby Stores, Inc.*, No. 13-354 (U.S. June 30, 2014); see also *Citizens United v. Fed. Election Comm’n* 558 U.S. 10 (2010); see generally IMMANUEL KANT, THE METAPHYSICS OF MORALS (1797).

Leading corporate scholars like Hillary Sale and Margaret Stout have also written of this communal notion of corporate identity. Sale points out that the adjective “public,” which modifies large companies with many shareholders, implies that those firms should serve all people in a society.<sup>233</sup> Stout’s concept of the corporation as a “team,” which connotes that it needs the talents of many players to make it successful, also speaks to the broader ideas that underlie CSR theory.<sup>234</sup>

In addition, the rise of a new legal form that a business may take, the “Benefit” or “B” corporation, addresses those aspirations even more directly. Such a company may state in its charter that in addition to making profit it may engage in less remunerative activity that will produce social good. Such an innovation is in line with diverse approaches to corporate governance taken in other countries.<sup>235</sup>

One prominent and successful example of that is the Workers’ Councils of Germany. They collaborate with management in that highly productive and prosperous country and lead their firms to embrace broad social goals.<sup>236</sup> Such a new corporate model might even have some resonance with the state capitalism of China where a new generation of leaders speaks openly of the need to pay better wages to factory workers so they can afford to buy the products they make.<sup>237</sup> The rapid growth of the CSR movement during the last several decades can be explained, at least in part, as a response to the

<sup>233</sup> See Sale, *supra* note 152, at 1.

<sup>234</sup> See Blair & Stout, *supra* note 26, at 275-76. This “team” concept of the corporation, however, received a set-back in the recent Hobby Lobby case. There the Supreme Court held that the owners of a closely-held corporation did not have to consider the wishes of their employees when they refused on religious grounds to offer them health insurance with certain forms of birth control required by the Affordable Care Act. *Hobby Lobby*, slip op. at 31.

<sup>235</sup> See generally Christopher Lacovara, *Strange Creatures: A Hybrid Approach to Fiduciary Duty in Benefit Corporations*, 2011 COLUM. BUS. L. REV. 815 (2011); Judd F. Sneirson, *Green is Good: Sustainability, Profitability, and a New Paradigm for Corporate Governance*, 94 IOWA L. REV. 987 (2009). The author there cleverly parodied Gordon Gekko’s notorious “Greed is Good” speech to the board of a paper producing company, in this fashion: “The point is, ladies and gentlemen, that green, for lack of a better work, is good. Green is right. Green works. Green clarifies, cuts through, and captures the essence of the evolutionary spirit. Green in all of its forms—green for life, for money, for love, knowledge—has marked the upward surge of mankind. And green, you mark my words, will not only save Teldar Paper, but that other malfunctioning corporation called the U.S.A.” *Id.* at 989.

<sup>236</sup> For a fine book that makes this point while discussing the disadvantages American workers face in comparison with their much better off German counterparts, see THOMAS GEOGHEGAN, *WERE YOU BORN ON THE WRONG CONTINENT?: HOW THE EUROPEAN MODEL CAN HELP YOU GET A LIFE* (2010).

<sup>237</sup> James Fallows, *Mr. China Comes to America*, THE ATLANTIC (Nov. 28, 2012), <http://www.theatlantic.com/magazine/archive/2012/12/mr-china-comes-to-america/309160/>.

increasing disparity in income and wealth among Americans. In the decades after World War II, most firms in our country paid high wages. That in turn led to robust consumer spending that spurred the economy to even more productivity. Such widely shared affluence thus engendered a virtuous cycle of strong business activity.<sup>238</sup>

Yet despite significant gains in productivity over the last thirty years, wage growth has been stagnant.<sup>239</sup> During that time, technology and globalization<sup>240</sup> have destroyed many manufacturing and clerical jobs in this country—leaving behind only poorly paying service jobs.<sup>241</sup> By contrast, those in the upper echelons of society, principally financiers and executives, have grown ever richer.<sup>242</sup>

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<sup>238</sup> See Jordan Weismann, *60 Years of American Economic History, Told in 1 Graph*, THE ATLANTIC (Aug. 23, 2012, 3:17 PM), <http://www.theatlantic.com/business/archive/2012/08/60-years-of-american-economic-history-told-in-1-graph/261503>.

As Hedrick Smith writes of that era: “In the heyday of the middle class, for thirty years after World War II, America’s great companies paid high wages and good benefits. Tens of millions of families had steady income, and they spent it, generating high consumer demand.” SMITH, *supra* note 178, at xxiv. Robert Reich’s recent movie, *INEQUALITY FOR ALL* (72 Productions 2013), contrasts that era of widespread prosperity to the current time when the disparities in income have grown to alarming proportions. It was favorably reviewed by Nicolas Rapold, *Chasm Between the Very Rich and Everybody Else*, N.Y. TIMES, Sept. 26, 2013, at C16, available at <http://www.nytimes.com/2013/09/27/movies/robert-reich-stars-in-the-documentary-inequality-for-all.html>.

<sup>239</sup> William A. Galston, *Behind the Middle-Class Funk*, WALL ST. J. (Aug. 6, 2013, 6:29 PM), <http://online.wsj.com/articles/SB10001424127887324653004578650460173879732>. This is so even while American workers are more productive than those in European countries. Discussing the substantial wealth increase in America during the last several decades, Thomas Geoghegan writes: “Technically we seem far ahead, but don’t drool. The U.S. superrich gobble well over two-thirds of the increase. In 2005, the real hourly wage for production workers in America was approximately eight percent lower than it was in 1973, while our national output per hour is 55 percent higher. So it’s dubious whether most Americans have gained even a penny in purchasing power since 1989.” GEOGHEGAN, *supra* note 236, at 13.

<sup>240</sup> Nobel-prize-winning economist Joseph E. Stiglitz aptly described this phenomenon. “[L]aborsaving technologies have reduced the demand for many “good” middle-class, blue-collar jobs. Globalization has created a worldwide marketplace, pitting expensive, unskilled workers in America against cheap unskilled workers overseas. Social changes have also played a role—for instance, the decline of unions, which once represented a third of American workers and now represent about 12 percent.” Joseph E. Stiglitz, *Of the 1%, by the 1%, for the 1%*, VANITY FAIR (May, 2011), <http://www.vanityfair.com/society/features/2011/05/top-one-percent-201105>.

<sup>241</sup> In an earlier piece, the author has marshalled a number of statistical measurements to substantiate this income inequality and wealth concentration. Morrissey, *supra* note 70, at 4-8.

<sup>242</sup> Morrissey, *supra* note 70, at 13-16. In the last two years, despite substantial criticism of exorbitant corporate compensation, the pay of top executives has continued to soar. See Gretchen Morgenson, *The Unstoppable Climb in C.E.O. Pay*, N.Y. TIMES, June 30, 2013, at BU1, available at <http://www.nytimes.com/2013/06/30/business/an-unstoppable-climb-in-ceo-pay.html>; Nelson D. Schwartz, *The Infinity Pool of Executive Pay*, N.Y. TIMES, Apr. 7, 2013, at BU1, available at <http://www.nytimes.com/2013/04/07/business/executive-pay-shows-modest-2012-gain-but-oh-those-perks.html>.

The gap between the wealthiest Americans and almost everyone else has continued to accelerate.<sup>243</sup> Even worse, this general decline in the American economy was masked by an illusory prosperity. It came first in a run-up of high-tech dot-com stocks,<sup>244</sup> and then in a surge in real estate prices. When the latter bubble finally burst in 2008 it brought on the worst financial panic since 1929.<sup>245</sup>

Thanks to fiscal and monetary bailouts by the federal government, the nation avoided a depression and the stock market rebounded, soaring again to new heights.<sup>246</sup> Yet hardly any of that “created” money trickled down to middle income Americans who work for wages. Statistics continue to pour out showing that the gap between the wealthiest Americans and almost everyone else keeps growing. Last year, for instance, the richest 10 percent got over one-half the income our country produced.<sup>247</sup> Even recent job gains that have come as the country has slowly emerged from this great recession have been almost entirely in the low-paid service and retail sectors.<sup>248</sup> Another recent report states that the real income of middle class Americans has declined by 8% since the Great Recession began in 2007.<sup>249</sup> As one commentator sadly put it, “we have become a nation of hamburger flippers.”<sup>250</sup>

That very troubling trend is best exemplified by the disparity between the pay of top corporate officials and that of

<sup>243</sup> Even conservatives are acknowledging this growing income inequality, while blaming it on government policies. See David Malpass, *How Big Government Drives Inequality: Stifling Economic Growth and Benefiting Insiders with Washington Access Do Not Help the Middle Class*, WALL ST. J. (Jan. 16, 2014), <http://online.wsj.com/news/articles/SB10001424052702303848104579312422581164580>.

<sup>244</sup> The 1990s saw astounding gains in the stock market. The Dow Jones Industrial Average increased from 2753.20 to 11224.70 and the NASDAQ went from 454.82 to 3620.24. *Rollicking, Rocketing Stock Markets*, WALL ST. J., Dec. 13, 1999 at C1, C23.

<sup>245</sup> For the author's take on the meltdown and its impact on the economy see Daniel J. Morrissey, *After the Meltdown*, 45 TULSA L. REV. 393, 393-97 (2009).

<sup>246</sup> The stock market had its best year in 2013 since 1997. The Standard and Poor's 500 Stock index rose 29.6%. Adam Shell, *Stocks End Red-Hot 2013 at All-Time Highs*, USA TODAY (Dec. 31, 2013), <http://www.usatoday.com/story/money/markets/2013/12/31/stocks-soar-in-2013/4204327/>.

<sup>247</sup> Lowrey, *supra* note 60.

<sup>248</sup> Ross D. Franklin, *New Jobs Disproportionately Low-pay, Part-time*, NEWS-JOURNAL.COM (Aug. 3, 2013), [http://www.news-journal.com/news/nation/new-jobs-disproportionately-low-pay-part-time/article\\_10536eec-5421-5db4-86b2-cc8a29158a47.html](http://www.news-journal.com/news/nation/new-jobs-disproportionately-low-pay-part-time/article_10536eec-5421-5db4-86b2-cc8a29158a47.html).

<sup>249</sup> Rakesh Kochhar and Rich Morin, *Despite Recovery, Fewer Americans Identify as Middle Class*, PEW RESEARCH CENTER, available at <http://www.pewresearch.org/fact-tank/2014/01/27/despite-recovery-fewer-americans-identify-as-middle-class/>.

<sup>250</sup> Aaron Task, “We Have Become a Nation of Hamburger Flippers”: Dan Alpert Breaks Down the Jobs Report, THE DAILY TICKER (Aug. 2, 2013, 10:58 AM), <http://finance.yahoo.com/blogs/daily-ticker/become-nation-hamburger-flippers-dan-aperlt-breaks-down-145831220.html>.



average workers. In 1965 it was 24 to one, but by 2010 at the 300 largest companies it had sky-rocketed to 343 to one.<sup>251</sup> The discontent spawned by that huge inequality is evident in the Occupy Wall Street movement.<sup>252</sup> As one union official said in endorsing those work stoppages, “We think it’s important to back low-wage workers who are willing to stand up and have the courage to strike to make the case that the economy is creating jobs that people can’t support their families on.”<sup>253</sup>

All this has had a real effect on our social fabric, particularly the promise of upward mobility that generations of Americans have taken for granted which is now vanishing.<sup>254</sup> As the renowned social historian Francis Fukuyama has recently stated,

The fact is, however, that rates of intergenerational social mobility are far lower in the United States than many Americans believe them to be . . . Over time elites are able to protect their positions by gaming the political system, moving their money off-shore to avoid taxation, and transmitting these advantages to their children through favored access to elite institutions.<sup>255</sup>

Another author made much the same point, saying, “Most of Western Europe today is both more equal in incomes *and* more economically mobile than the United States.”<sup>256</sup> More and more Americans are becoming aware of that painful reality. A survey recently found that only 55% of those asked said they

<sup>251</sup> Jennifer Liberto, *CEOs Earn 343 Times More than Typical Worker*, CNN MONEY (Apr. 20, 2011, 7:46 AM), [http://money.cnn.com/2011/04/19/news/economy/ceo\\_pay/](http://money.cnn.com/2011/04/19/news/economy/ceo_pay/); David Owens, *The Pay Problem: What’s to be Done About C.E.O Compensation?*, NEW YORKER, Oct. 12, 2009, at 58, available at <http://www.newyorker.com/magazine/2009/10/12/the-pay-problem>.

<sup>252</sup> Erick Eckholm & Timothy Williams, *Anti-Wall Street Protests Spreading to Cities Large and Small*, N.Y. TIMES, Oct. 4, 2011, at A18, available at <http://www.nytimes.com/2011/10/04/us/anti-wall-street-protests-spread-to-other-cities.html>.

<sup>253</sup> Steven Greenhouse, *A Day’s Strike Seeks to Raise Fast-Food Pay*, N.Y. TIMES, July 31, 2013, at A1, available at <http://www.nytimes.com/2013/08/01/business/strike-for-day-seeks-to-raise-fast-food-pay.html>.

<sup>254</sup> President Obama has taken this as a major theme in his second term. See Gerald F. Seib, *Obama’s Second-Term Agenda: Progressive Ideas, Populist Packaging*, WALL ST. J.: CAP. J. (July 26, 2013), <http://online.wsj.com/news/articles/SB10001424127887323971204578627940606382774>.

<sup>255</sup> FRANCIS FUKUYAMA, *THE ORIGINS OF POLITICAL ORDER* 9 (2011).

<sup>256</sup> Timothy Noah, *The Mobility Myth*, NEW REPUBLIC (Feb. 8, 2011), <http://www.newrepublic.com/article/politics/magazine/100516/inequality-mobility-economy-america-recession-divergence>.

believed that their children will have a better life than they have, the lowest percentage since the survey began in 1987.<sup>257</sup>

*D. Renewing the Call for National Corporate Law*

It is time to go beyond sporadic efforts at reform and enact comprehensive national legislation regulating large public companies. This is not a new idea. At least three times during the last century, during the presidencies of Theodore Roosevelt, Franklin Roosevelt, and Jimmy Carter, serious efforts were made to require that large companies be federally chartered.<sup>258</sup>

The ensuing legal framework should not endanger the innovative edge American corporations have long enjoyed in the global economy. Nor should it diminish the personal responsibility of each worker to use her or his talents skillfully for the common good. But it should serve to not only protect investors more fully from wrongdoing by corporate insiders but also to mandate a broader purpose for these highly productive enterprises to make sure they serve the larger public interest.

Such regulation would require, among other things, that corporations adopt more balanced compensation structures narrowing the egregious difference that now exists between the pay of top executives and front-line workers.<sup>259</sup> It would also mandate that these companies make meaningful efforts to expand their work forces and pay them good wages thus creating a prosperity that would be shared by a large majority of our citizens, many of whom are now in danger of falling into

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<sup>257</sup> Emily Alpert, *Amid Slow Economic Recovery, More Americans Identify as Lower Class*, L.A. TIMES (Sept. 18, 2013), <http://www.spokesman.com/stories/2013/sep/18/lower-class-descriptor-rising/>.

<sup>258</sup> Mark J. Roe, *Delaware's Competition*, 117 HARV. L. REV. 588, 597 (2003).

<sup>259</sup> Cf. Eduardo Porter, *Seeking New Tools to Address a Wage Gap*, N.Y. TIMES, Nov. 4, 2014, at B1. There the author asserts that the wage gap between executives and workers can best be addressed by corporations themselves and not the government. He further states that 36% of Republicans say major companies are most responsible for narrowing the income gap—significantly more than say it is the job of the poor themselves or the government to do it. Howard Schultz, CEO of Starbucks, has committed to have his company hire 10,000 veterans over the next five years. He stated that the company will employ a recruiter who is a veteran and “understands the language, understands the anxiety and can bridge the gap.” Susan Page, *Starbucks CEO: Honor Vets with a Concert—And a Job*, USA TODAY (Nov. 11, 2014), <http://www.wusa9.com/story/news/nation/2014/11/11/capital-download-howard-schultz-veterans-day-concert-and-book/18840931/>. Companies are spending huge amounts of money Wall Street “mega-mergers,” but companies “are not spending money in other areas. Wage growth remains sluggish, and hiring is growing only modestly.” Even worse, it is questionable whether these big take-overs benefit the economy as these mergers “often create redundancies which can lead to job cuts.” David Gelles, *Mega Mergers Popular Again on Wall Street*, N.Y. TIMES, Nov. 17, 2014, at A1.

a permanent underclass. Such an approach can be justified on both principled and pragmatic grounds.

First, it is eminently sensible that these large firms with countrywide and international operations be regulated by our national government. Observers have long pointed out that the preeminence of Delaware law in corporate regulation is a historical anomaly.<sup>260</sup> The internal affairs doctrine has allowed that small, non-industrial state to be the de facto law-giver for corporate America with continuing charges that firms flock there to incorporate because of its lax regulation.<sup>261</sup> In addition, there is ample warrant for a national mandate that corporations have a broader purpose than just profit.

Firms that do business in the corporate form receive substantial support from the larger community. Shareholders, who have the ultimate claim on the accumulated wealth of those companies, are given the privilege of limited liability and perpetual existence for their business.<sup>262</sup> Such businesses are also granted the legal rights afforded natural persons under the constitution<sup>263</sup> and they are supported by political institutions in myriad ways. Those include tax breaks, infrastructure construction, education of their workforce, government contracts, and financial bailouts. It is therefore only right that large public companies owe reciprocal duties to society as a whole.

From a practical perspective, corporate executives have substantial resources under their control. They also have the expertise to use them to expand the productive capacities of their enterprises so that they can give meaningful employment to a larger workforce. In addition, the executives can distribute the revenue of their firms in ways that both reduce the egregious income inequality that now threatens the stability of our society and also promote widespread purchasing power that will secure a market for their products.

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<sup>260</sup> In the first part of the 20th century, Delaware copied the corporate act of New Jersey, which was then the leading jurisdiction for incorporations. When a reforming Governor named Woodrow Wilson tightened New Jersey's law, many of the firms incorporated there migrated to Delaware and never left. See Cary, *supra* note 47, at 664. Wilson's reform agenda as governor of New Jersey is described at length in a fine new biography, *Wilson*, by A. Scott Berg. See A. SCOTT BERG, *WILSON* 189-212 (2013).

<sup>261</sup> Cary's famous observation that "there is no public policy left in Delaware corporate law except the object of raising revenue." Cary, *supra* note 47, at 684.

<sup>262</sup> See *supra* note 105 and accompanying text.

<sup>263</sup> See generally *Citizens United v. Fed. Election Comm'n*, 558 U.S. 310 (2010), which is the most notorious example of this where the High Court ruled that a corporation's free speech rights prohibited any restrictions on contributions it might make to political campaigns; see also *Burwell v. Hobby Lobby Stores, Inc.*, No. 13-354 (U.S. June 30, 2014).

As this Article has pointed out, some business leaders have acknowledged the need for this more pervasive mandate. A large percentage of the general population recognizes that personal satisfaction comes from working in enterprises that not only provide a good living for their employees but also serve the larger purposes of society.

In addition, a large number of state legislatures have already led the way here by adding provisions to their corporate codes that directors may take the interests of an array of corporate constituents into account.<sup>264</sup> More recently, many states have also allowed for the chartering of so-called “benefit corporations” that can be set up to not just make profit but also to achieve broader social goals.<sup>265</sup> Those efforts represent a platform upon which to build national legislation.

## CONCLUSION

For the last several decades two seemingly incompatible ideas have been moving forward in corporate law. One is shareholder rights and the other is CSR. Yet even the conservative economist Milton Freedman, the prime spokesperson for the shareholder primacy approach, conceded that corporations are bound not only to obey the law but also to abide by ethical customs. As that sense of public morality has expanded to include many of the ideas found in CSR, there appears to have emerged a new “reflective equilibrium” on this issue.

The highly respected social philosopher, John Rawls,<sup>266</sup> used that term to describe an adjustment to previously-held principles brought about by a more complete understanding of the demands of justice. Now that CSR theory has achieved its maturity such equipoise may have arrived. Corporate law no longer need be “schizophrenic” as Chancellor Allen claimed,<sup>267</sup> but can embrace as its goals both shareholder rights and CSR. As this Article has argued, both are important for our society. If, either by the wise choices of corporate boards or by legislative mandate, business leaders accept those responsibilities, our nation and the world will be much the better for it.

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<sup>264</sup> See *supra* note 100 and accompanying text.

<sup>265</sup> See *supra* note 235 and accompanying text.

<sup>266</sup> JOHN RAWLS, A THEORY OF JUSTICE 49 (1971).

<sup>267</sup> Allen, *supra* note 167, at 261.