OUR CONTINUING STRUGGLE WITH THE IDEA THAT FOR-PROFIT CORPORATIONS SEEK PROFIT

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This Essay addresses an issue that, to be candid, perplexes me. That issue is the continuing dismay evidenced in Western, capitalist nations when public corporations that pursue profit for their stockholders take actions that adversely affect the nation's economic stability, the corporation's employees, or the environment.

When a corporation's ardor for profits leads it to take excessive risks that endanger the firm's solvency, commentators react with shock and dismay. How can corporate managers be so blinded by the immediate prospect of profit that they would ignore what, in hindsight, seem like such obvious risks? Likewise, we rent our garments in anger and chagrin when energy companies take environmental shortcuts in drilling for oil or mining coal, surprised that profit-maximizing firms have been less than optimally protective of the environment and their workers, that they did not go beyond what was simply necessary to ensure that regulators allowed them to operate. Similarly, we anguish when the board of a venerable homeland corporate icon reacts receptively to a premium takeover bid from a foreign acquirer. How could the board sell out and undermine the traditional values the firm stands for? It cannot be that the long-term stockholders would put their desire for a one-time, short-term profit ahead of the continued independence of a nationally important institution?

Although I am sympathetic to many of the sentiments and policy concerns that motivate these dismayed reactions, I confess to being weary of the naïveté they manifest. More importantly, the continued failure of our societies to be clear-eyed about the role of

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the for-profit corporation endangers the public interest. Instead of recognizing that for-profit corporations will seek profit for their stockholders using all legal means available, we imbue these corporations with a personality and assume they are moral beings capable of being "better" in the long-run than the lowest common denominator. We act as if entities in which only capital has a vote will somehow be able to deny the stockholders their desires, when a choice has to be made between profit for those who control the board's reelection prospects and positive outcomes for the employees and communities who do not.

In this Essay, I identify some recent instances that reflect our continued inability to view the for-profit corporation with a gimlet eye. These examples track recurrent patterns. I begin with a couple stories in the headlines of corporate greed at BP in connection with the Deepwater disaster in the Gulf of Mexico and at the U.S. banks that were bailed out by the federal government. I then proceed to less obvious stories where courts have affirmed the preeminence of stockholders in the for-profit corporation, the first in an older case challenging Henry Ford's stated preference for employees over stockholders and the second in a recent one challenging Craigslist's attempt to protect its online community from stockholders selling in a takeover. Next, I consider how stockholders have fared in other capitalist countries, looking at Kraft's successful takeover of Cadbury in the United Kingdom and BHP Billiton's failed bid to acquire the Potash Corporation of Saskatchewan. In the end, policy makers should not delude themselves about the corporation's ability to police itself; government still has a critical role in setting the rules of the game.

I. OIL SPILLS AND BAILED-OUT BANKS: RELEARNING OBVIOUS LESSONS OF HISTORY

The first situations I address exemplify the tendency to underestimate the extent to which firms subject to pressures to deliver short-term profits for their stockholders pose a serious risk of generating societally destructive externalities. I will only briefly discuss these examples because they are, at least in my estimation, so obvious.

A. Risk Taking with Underwater Drilling

The first story is the BP oil spill disaster in the Gulf. In the wake of the spill, there was widespread outrage about corporate callousness.[1] How could a corporation drill so deep with no reliable

1. After being criticized for a tepid response toward BP in the wake of the spill, President Obama came out strong against BP as the oil spill neared its third month. *See* Mail Foreign Service, *'Furious' Obama Blasts BP Again as Tony Hayward Gets Set to Shell Out Billions to Investors*, MAIL ONLINE (June 5,

plans as to how to address a leak in the well?[2] How could so many safety features be inoperable?[3] To me, it is to be expected that a corporation that stands to gain large profits from aggressive drilling activity would less than optimally consider the environmental risks and occupational hazards that novel drilling activity posed.[4] BP,

2010), http://www.dailymail.co.uk/news/worldnews/article-1283959/Furious-Barack-Obama-BP-felt-anger-Gulf-Mexico-oil-disaster.html (reporting that Obama, when asked whether he was "angry at BP," responded that he was "furious at this entire situation because this is an example where somebody didn't think through the consequences of their actions"). Other U.S. politicians of both parties also skewered BP's embattled then-CEO, Tony Hayward, and other BP executives in the weeks that followed the spill. *See Rep. Cau Suggests BP Exec Commit 'Hara-Kiri' Over Spill*, FOXNEWS.COM (June 16, 2010), http://www.foxnews.com/politics/2010/06/16/rep-cao-suggests-bp-exec-commit-hari-kari-spill/ (quoting Louisiana Republican House Representative Joseph Cao as telling BP America President Lamar McKay that "in the Asian culture, we do things differently. During the Samurai days, we'd just give you the knife and ask you to commit hara-kiri . . . ."); Kim Landers, *US Congressional Panel Roasts BP Chief*, ABC NEWS (June 18, 2010), http://www.abc.net.au/news/stories/2010/06/18/2930221.htm (quoting Michigan Democratic House Representative Bart Stupak) ("Mr. Hayward I'm sure you'll get your life back and with a golden parachute back to England, but we in America are left with the terrible consequences of BP's reckless disregard for safety . . . ."); Holbrook Mohr, et al., *BP's Gulf Oil Spill Response Plan Lists the Walrus as a Local Species. Louisiana Gov. Bobby Jindal is Furious*, CHRISTIAN SCI. MONITOR (June 9, 2010), http://www.csmonitor.com/From-the-news-wires/2010/0609/BP-s-gulf-oil-spill-response-plan-lists-the-walrus-as-a-local-species.-Louisiana-Gov.-Bobby-Jindal-is-furious ("Look, it's obvious to everybody in south Louisiana that they didn't have a plan, they didn't have an adequate plan to deal with this spill. . . . They didn't anticipate the BOP [(blowout preventer)] failure. They didn't anticipate this much oil hitting our coast. From the very first days, they kept telling us, 'Don't worry, the oil's not going to make it to your coast.'" (quoting Louisiana Republican Governor Bobby Jindal)).

2. My use of the word "reliable" here seems measured in light of public reports about the plans BP apparently had in place to deal with an oil spill in the Gulf. *See* Mohr, *supra* note 1 (noting that BP's 2009 response plan for a Gulf of Mexico oil spill—among numerous other material deficiencies and inaccuracies—included the contact information of a national wildlife expert, Professor Peter Lutz, who died in 2005, and included, under a heading entitled "sensitive biological resources," marine mammals such as walruses, sea otters, sea lions, and seals, "[n]one of which lives anywhere near the Gulf").

3. Daniel Bates, *Oil Worker 'Alerted BP About Rig Fault'—But Bosses Feared Cost of Halting Production, He Says*, MAIL ONLINE (June 25, 2010), http://www.dailymail.co.uk/news/worldnews/article-1288242/Gulf-oil-spill-BP-told-faulty-drill-safety-equipment-weeks-disaster.html (recounting the story of a BP rig worker who claims he told managers that a key blowout preventer was improperly leaking fluid but was ignored, purportedly because it would cost too much to shut down production to deal with the problem); Ian Urbina, *Documents Show Earlier Fears About Safety of Wells*, N.Y. TIMES, May 30, 2010, at N1, N18 (noting that internal BP emails and inspection reports show that the blowout preventer and casing had several problems that would have limited their effectiveness in the event of an actual blowout).

4. *See Little Spent on Oil Spill Cleanup Technology*, ABC ACTION NEWS (June 26, 2010), http://www.abcactionnews.com/dpp/news/state/little-spent-on

after all, stood to gain all the profits from its activities, while the risks to the environment would be borne largely by others.[5]

Not only do corporations have incentives to disregard risks for the sake of profits, but there is a natural tendency to pay attention to short-term profits over long-term risks. In fact, most of us place a higher value on immediate satisfaction than on the long-term risks created by such satisfaction.[6] If we can get all the benefits of the immediate satisfaction for ourselves, and know that the longer-term costs will be shared with a lot of others, we go for today over tomorrow even more. And, when an industry is among the leaders in having lobbyists precisely for the purpose of minimizing governmental regulation of its activity,[7] trusting that industry to

-oil-spill-cleanup-technology (reporting that BP spent $29 *million* on safer drilling operations research in the prior three years while BP and four other major oil drilling companies in the United States spent $33.8 *billion* on oil exploration over the same time period).

5. *See, e.g.*, Henry N. Butler & Jonathan R. Macey, *Externalities and the Matching Principle: The Case for Reallocating Environmental Regulatory Authority*, 14 YALE L. & POL'Y REV. 23, 29 (1996) (noting that the "goal of government regulation of pollution is to force polluters to bear the full costs of their activities," rather than allowing those costs, or "externalities," to be borne by society at large); Margaret Tortorella, *Will the Commerce Clause "Pull the Plug" on Minnesota's Quantification of the Environmental Externalities of Electricity Production?*, 79 MINN. L. REV. 1547, 1549 n.15 (1995) ("Economic theory provides insight into the need for governmental regulation of externalities . . . [in the energy industry because w]hen economic activity affects the external environment, the market mechanism fails to reach the social optim[al allocation of resources] because society, rather than the economic actor, bears the cost of production." (citing WILFRED BECKERMAN, PRICING FOR POLLUTION 24, 25 (2d ed. 1990)).

6. This phenomenon is perhaps most easily observed at crowded American fast-food drive-thru lanes where Big Macs are, in comparison to those who frequently order and consume them, not so big at all.

7. John M. Broder, *Coal Industry Spending to Sway Next Congress*, N.Y. TIMES, Oct. 29, 2010, at A12 (reporting that the coal industry is spending millions of dollars in lobbying and campaign donations to influence the makeup of the next Congress in an effort to stave off tightened health and safety regulations); Dan Eggen & Kimberly Kindy, *Three of Every Four Oil and Gas Lobbyists Worked for Federal Government*, WASH. POST, July 22, 2010, at A1 ("With more than 600 registered lobbyists, the [oil and gas] industry has among the biggest and most powerful contingents in Washington."); Anne C. Mulkern, *Obama's SOTU Nod Unleashes Lobbying on Clean-Power Goal*, N.Y. TIMES GREENWIRE (Jan. 26, 2011), http://www.nytimes.com/gwire/2011/01/26/26greenwire-obamas-sotu-nod-unleashes-lobbying-on-clean-pow-3140.html?pagewanted=1 (reporting that the American Coalition for Clean Coal Electricity's lobbying efforts have focused on stopping the U.S. EPA from regulating greenhouse gas emissions); *see also Lobbying: Oil and Gas Industry Profile*, OPENSECRETS.ORG, http://www.opensecrets.org/lobby/indusclient.php?lname=E01&year=a (last updated Dec. 11, 2011) (reporting, based on publicly available information from the Senate Office of Public Records, that oil and gas lobbyists spent a mere $146,296,424 on lobbying efforts in 2010, down from nearly $175 million in 2009).

balance environmental concerns and worker safety responsibly against the prospect of immediate profit would seem even more naïve.

B. Risk Taking with Now Underwater Mortgages

The other rather obvious example of silly surprise is the recent financial crisis. This crisis was in no small measure caused by the signing of trillions of dollars in risk-shifting transactions, the bulk of which had at their root packages containing subprime mortgages.[8] The parties who wrote these mortgages did not act or think as typical lenders.[9] They did not expect the borrowers to pay off the mortgage contracts as written.[10] Instead, the idea was that the

8. *See, e.g.*, William Poole, *Causes and Consequences of the Financial Crisis of 2007–2009*, 33 HARV. J.L. & PUB. POL'Y 421, 424–26 (2010) (describing collateralized debt obligations backed by subprime mortgages as the leading cause of the financial crisis); *see generally* Atif Mian & Amir Sufi, *The Consequences of Mortgage Credit Expansion: Evidence from the U.S. Mortgage Default Crisis*, 124 Q.J. ECON. 1449 (2009) (conducting an analysis of the mortgage default crisis in the United States by empirically examining subprime mortgages in the years leading up to the financial crisis, and observing the sharp increase in mortgage defaults in areas of the country that represent a disproportionately large share of subprime borrowers and that the period between 2002 and 2005 is the only time in the last eighteen years when income and mortgage credit growth were negatively correlated). *But see* Lynn A. Stout, *The Legal Origin of the 2008 Credit Crisis* 24–25 (UCLA Sch. of Law, Working Paper No. 11-05, 2011), *available at* http://ssrn.com/abstract=1770082 (admitting that subprime mortgages often undergirded the derivatives whose value plummeted, but making the point that the value of all U.S. subprime mortgages was only slightly over $1 trillion and noting that it was the writing of speculative contracts worth many times that amount related to those mortgages that required the U.S. government to make emergency loans of over $3 trillion and to take other actions to alleviate some of the harm and economic dislocation arising when the value of those contracts plummeted).

9. *Cf.* Giovanni Dell'Ariccia et al., *Credit Booms and Lending Standards: Evidence from the Subprime Mortgage Market* (Int'l Monetary Fund, Working Paper No. 08/106, 2008), *available at* http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1153728 (associating the rapid expansion in the subprime mortgage market predating the financial crisis with relaxed lending standards and further observing that the areas hardest hit by the crisis were those where lending standards declined the most); Ken Kupchik, *Regrets of a Subprime Mortgage Lender*, SALON (Feb. 1, 2011), http://www.salon.com/news/mortgage_crisis/?story=/mwt/pinched/2011/02/01/confessions_of_a_subprime_lender_open2011 (chronicling the author's experience working for a subprime mortgage company and confessing that company policy was to make the sale, regardless of whether the loan put the borrower in a better financial position, which in the author's opinion, it rarely did).

10. *See* THE FIN. CRISIS INQUIRY COMM'N, 111TH CONG., THE FINANCIAL CRISIS INQUIRY REPORT xxiii (2011) [hereinafter FIN. CRISIS REPORT] ("Many mortgage lenders set the bar so low that lenders simply took eager borrowers' qualifications on faith, *often with a willful disregard for a borrower's ability to pay*.") (emphasis added); *id.* (noting that in 2005, 68% of so-called "option ARM"

mortgages would be refinanced again as already inflated real estate prices continued to rise.[11] Even better, of course, the loans were securitized so the underwriters—the first-instance "lenders"—could pass the risk down the line.[12] Buyers of these securities were plentiful. Most of these transactions were motivated by a desire to

loans (Adjustable Rate Mortgage) originated by Countrywide and Washington Mutual had "low- or no-documentation requirements").

11. *See, e.g.*, William W. Bratton & Michael L. Wachter, *The Case Against Shareholder Empowerment*, 158 U. PA. L. REV. 653, 717 (2010) (observing that the burst of the housing bubble in 2007 exposed banks that were heavily invested in the residential mortgage sector to severe losses and that the initial reason for the banks' decision to invest heavily in that market was the "assumption that the price of real estate securing the loans would continue to rise," an assumption based in part on the "increasing demand for housing fueled by ever-riskier real estate financing"); Peter Grier, *Commission: Three Reasons Why the Financial Crisis Happened*, CHRISTIAN SCI. MONITOR (Jan. 14, 2010), http://www.csmonitor.com/USA/2010/0114/Commission-three-reasons-why-the-financial-crisis-happened (noting that the financial industry in the United States, in the years leading up to the financial crisis, "did not consider that it was possible housing prices could decline"); Brent T. White, *Underwater and Not Walking Away: Shame, Fear, and the Social Management of the Housing Crisis*, 45 WAKE FOREST L. REV. 971, 988 (2010) (arguing that homeowners in the years before the crisis suffered from "selective perception" that caused them to fail to see evidence that the value of their home was not rising but falling, and that "many homebuyers . . . ignore[d] signs of the impending housing-market collapse in the first place, and optimistic overconfidence may have caused many homeowners to take out interest-only adjustable-rate mortgages . . . in the misplaced belief that they . . . would refinance as their home's value grew exponentially"). But not everyone was drinking the home price Kool-Aid. Indeed, some, years before the crisis, almost prophetically questioned the propriety of the assumption that housing prices would continue an upward climb indefinitely. *See, e.g.*, *House Prices: After the Fall*, THE ECONOMIST, June 18, 2005, at 11 (observing that American and global house prices "have reached dangerous levels" and that a devastating drop in prices is inevitable that "could decide the course of the entire world economy over the next few years").

12. Private securitization, or structured finance securities, had two key benefits from both the standpoint of the financial institutions creating and selling them and the investors that bought them: pooling and tranching. FIN. CRISIS REPORT, *supra* note 10, at 43. By pooling many mortgage loans, a few defaults would have minimal effect. By tranching the same loans, sellers of the securities could fine tune them to meet particular investor preferences based on the investor's desired level of risk it wished to take on. *Id.* At the same time, however, pooling and tranching greatly reduced an investor's ability to understand and price these securities because to do so required the calculation of the statistical probability that certain types of mortgages would default and the lost revenues attributable to those defaults. *Id.* This difficulty, according to the National Commission on the Causes of the Financial and Economic Crisis in the United States, brought the leading credit rating agencies—Standard & Poor's, Moody's, and Fitch—to prominence. *Id.* It became a common practice by the packagers of these mortgage-backed securities, i.e., financial institutions, to pay "handsome fees to the rating agencies to obtain the desired ratings." *Id.* at 44.

make speculative trading profits, not to hedge risks.[13] And the willingness of rating agencies to give the packages a triple-A rating[14] allowed fiduciaries[15]—so-called "sophisticated investors"—to buy them for pension funds.[16]

Now, how any loan tranche dependent on subprime loans could be rated triple A—the very best—is difficult for a definitionally disciplined mind to grasp, but men and women of finance, making bets largely with other people's money, did not hesitate over the linguistic or even financial illogic of such labeling. Nor mind you, did very real risk indicators give them pause, such as the need for the American credit card industry to secure the passage of a bill making it harder for their increasingly defaulting clients to file for bankruptcy.[17] Nay, that bill encouraged this risk-taking as sub-

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13. *See* Stout, *supra* note 8, at 20–21 (observing that most of the OTC derivative trading in the years leading up to the financial crisis was "dominated by speculative trading," not by investors seeking to hedge their market positions).

14. "From 2000 to 2007, Moody's rated nearly 45,000 mortgage-related securities as triple-A. This compares with six private-sector companies in the United States that carried this coveted rating in early 2010. In 2006 alone, Moody's put its triple-A stamp of approval on 30 mortgage-backed securities every working day. . . . 83% of the mortgage securities rated triple-A that year ultimately were downgraded." FIN. CRISIS REPORT, *supra* note 10, at xxv. Of course, Moody's and the rest of the ratings agencies made nice profits for their services. In 2005, 2006, and 2007, for example, the rating of structured finance products made up nearly half of Moody's rating revenues, representing a fourfold increase from levels in 2000. *Id.* at 118.

15. *See* JOHN C. COFFEE JR., GATEKEEPERS: THE PROFESSIONS AND CORPORATE GOVERNANCE 303 (2006) ("[F]or over a century institutional investors have been found by courts to have satisfied their due diligence obligation as fiduciaries when they relied on 'investment grade' ratings from the ratings agencies.").

16. *See* Margarita S. Brose & Bill Nichols, *Toxic Assets: Untangling the Web*, BYU INT'L L. & MGMT. REV., Winter 2009, at 1, 16 ("In a process that now looks to be a tragic combination of magic and wishful thinking, some of these tranches somehow ended up with AAA investment ratings and were marketed as high quality investments, which dramatically broadened the base of potential investors to include pension funds and asset managers."); Charles W. Murdock, *Why Not Tell the Truth?: Deceptive Practices and the Economic Meltdown*, 41 LOY. U. CHI. L.J. 801, 868 (2010) (observing that many investors in mortgage-backed securities were "fiduciaries subject to fiduciary standards as to the instruments in which they could invest" and that therefore, "[t]he only way these investments could be sold was to receive the imprimatur [i.e. a triple AAA stamp] of the credit agencies"); Greg Farrell, *SEC Slams Credit-Rating Agencies over Standards*, USA TODAY, July 11, 2008, at 3B ("Because many institutional investors [and pension funds] can put money into only investment-grade bonds (i.e., bonds with a rating of 'AAA'), investment banks scrambled to win the highest rating for the mortgage-backed securities they developed during the real estate bubble.").

17. The bill was named the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005. Pub. L. No. 09-8, 119 Stat. 23 (codified as amended in scattered sections of 11 U.S.C.).

prime mortgages were marketed to people on the idea that the new mortgage would provide cash needed to pay off credit card debt, buy a new big screen TV, and come with a great feature—no need to pay principal for five years at a time of unprecedentedly low interest rates.[18] This was the real blue-chip stuff, the obvious triple A. But on top of it was built an Everest of money, much of it backed in the end by AIG, which at one point was contractually responsible for $2.7 trillion in potential risk.[19]

As Professor Lynn Stout has recently pointed out, there was an even bigger warning sign. In 2008, the $67 trillion credit default swap market was made up almost exclusively of credit default swaps written on mortgage-backed bonds in a market in which the total value of all underlying asset-backed and corporate bonds in the United States that year was a mere $15 trillion.[20] Rank speculation was thus the rule, not the exception.[21]

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18. *See, e.g.*, Kevin T. Jackson, *The Scandal Beneath the Financial Crisis: Getting a View from a Moral-Cultural Mental Model*, 33 HARV. J.L. & PUB. POL'Y 735, 762 (2010) (noting Countrywide Financial Corporation's "practice of predatory lending, which involves entering into unsound secured loans for inappropriate purposes" through the use of "a bait-and-switch technique, advertising low interest rates for home refinancing[s]" that would tout a 1% or 1.5% interest rate but swap out an adjustable rate mortgage contract at closing that would allow the homeowner "to make interest-only payments, yet the interest charged is more than the amount of interest paid"); *see also* Mark Brown, *Countrywide Wasn't Really on Your Side*, CHI. SUN-TIMES, June 26, 2008, at 8 (reporting that one of Countrywide's most popular mortgage products was the "PayOption ARM," an adjustable rate mortgage, that allowed consumers to "pay the monthly minimum on their credit cards as the balance owed g[ot] bigger and bigger and bigger" and that Countrywide, in selling these mortgages, was "indifferent to whether homeowners could afford to repay its loans," often "ignoring the fact that the borrowers . . . didn't make enough money to repay the loans, especially the higher payments that would later come due on adjustable rate mortgages").

19. Carol J. Loomis, *AIG's Wind-Down Has $1.6 Trillion Left*, CNNMONEY (Mar. 26, 2009), http://money.cnn.com/2009/03/25/news/companies/loomis_aig.fortune/index.htm (noting that AIG's exposure on derivatives was, at its height in 2008, $2.7 trillion); Rick Newman, *7 Surprises Buried Beneath AIG Bonuses*, U.S. NEWS & WORLD REP. (Mar. 20, 2009), http://money.usnews.com/money/blogs/flowchart/2009/03/20/7-surprises-buried-beneath-the-aig-bonuses (noting that at its highest point before the bailout, AIG faced exposure on its derivatives in the amount of $2.7 trillion). Interestingly, AIG's public disclosures noted that AIG was on the hook for a shockingly large $527 billion. Am. Int'l Grp., Inc., Annual Report (Form 10-K) (Dec. 31, 2007), *available at* http://www.sec.gov/Archives/edgar/data/5272/000095012308002280/y44393e10vk.htm.

20. *See* Stout, *supra* note 8, at 21 (noting that the value of all asset-backed securities and corporate bonds in the United States was $15 trillion in 2008 and yet there were $67 trillion in outstanding credit default swap ("CDS") contracts written that were backed only by a small fraction of those bonds).

21. *See id.* at 19–25 (arguing that reductions in legal regulations that limited the ability to use hedging contracts for the purpose of speculation fueled the huge increase in speculative trading in credit default swaps and other derivatives that resulted in the financial crisis).

In hindsight, this is the kind of stuff Planters® honey roasts and sells in a can. There were many who knew enough financial history to be very nervous about a system that combined core banking with speculative trading, that hid greatly relaxed capital requirements, and that allowed outright speculative gambling in the form of unregulated credit default swaps.[22] In the typical credit default swap, a kind of insurance contract, the party providing the insurance neither had to have an insurable interest in the matter[23] nor, more importantly, sufficient capital to make good on the insurance protection it had sold. As it turns out, AIG's riskiest insurance operation was its writing of trillions of credit default swaps, contracts it was not capitalized to fulfill and which were outside the province of state regulators. Similarly absurd was the idea that swap protection was purchased from hedge funds,[24] whose only obligation to make good was to issue capital calls to its investors. Good luck with that.

The mismatch between immediate reward and the bearing of ultimate risk could not have been more extreme, as speculation ran wild in the wake of the erosion of key legal barriers to gambling of this kind.[25] But legislators and regulators had become drunk on their own cocktails, having naïvely (or worse) assumed that markets would "price" these risks. So, indeed, had many academics, such as many of my law and economics scholar-friends in the academy who

22. *E.g.*, Elaine Lafferty, *The Woman Who Predicted the Mortgage Crisis Goes on the Record About the Future*, WOMEN'S VOICES FOR CHANGE (Apr. 30, 2008), http://womensvoicesforchange.org/the-woman-who-predicted-the-mortgage-crisis-goes-on-the-record-about-the-future.htm (reporting on Karen Weaver, a Wall Street analyst who voiced concern in 2005 about the artificial and unsustainable rise in home prices underlying many mortgage-backed securities); Cyrus Sanati, *How Value Investing Paid Off in the Crisis*, N.Y. TIMES DEALBOOK (Mar. 16, 2010), http://dealbook.nytimes.com/2010/03/16/how-value-investing-paid-off-in-the-meltdown/ (reporting that Michael Burry of Scion Capital made $100 million by betting against mortgage-backed securities (i.e., purchasing credit default swaps on pools of mortgages), and that Burry did so because "he knew [subprime mortgage-backed securities] were troubled").

23. *See, e.g.*, Stout, *supra* note 8, at 5 ("Neither the 'buyer' nor the 'seller' of a CDS contract on a particular corporate or mortgage-backed bond needs to actually own the underlying bond in question." (citing MICHAEL LEWIS, THE BIG SHORT: INSIDE THE DOOMSDAY MACHINE 29 (2010)).

24. *See* David Evans, *Hedge Funds in Swaps Face Peril With Rising Junk Bond Defaults*, BLOOMBERG (May 20, 2008), http://www.bloomberg.com/apps/news?pid=newsarchive&sid=aCFGw7GYxY14 (noting that although hedge funds have provided 31% of all credit default swap protection, such protection is not likely to be of any value because few hedge funds have the cash available to meet bankers' requests and the law does not require sellers of protection to set aside reserves).

25. *See* Stout, *supra* note 8, at 19–25 (arguing that reductions in legal regulations that limited the ability to use hedging contracts for the purpose of speculation fueled the huge increase in speculative trading in credit default swaps and other derivatives that resulted in the financial crisis).

confidently told me in the years before the meltdown that my worries over the credit bubble and increased leverage in the financial sector reflected my inadequate appreciation of the keen ability of current financial and capital markets to price risks accurately.

Nor, of course, did one need worry that financial institutions that had regularly received government bailouts because of their systemic importance would be less than optimally incentivized to prudently assess risks. And the growing complexity of financial institutions themselves was no worry, again, for the same reasons. Markets would take care of it and price it, ignoring of course that the capital markets themselves had grown in complexity and churned like a meth-fueled gerbil's wheel.[26] Whatever these capital markets were driven by, a deep examination of the long-term risks of transactions generating large short-term profits did not, in the end, turn out to be high on the list.[27]

And when it all crashed down, the first to receive treatment were those who had profited most. No doubt they felt pain, but not enough that one can confidently believe they are worse off today than if they had not behaved recklessly. Most obviously, though, the importance of these institutions to our economies made it impossible not to bail them out. And bailed out they were, given huge subsidies, partly comprised of free money to borrow in order to make profitable trades and return to health.[28]

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26. As I observed in an earlier article dealing with activism by institutional shareholders:

> Responsible commentators estimate hedge fund turnover at around 300 percent annually. What is even more disturbing than hedge fund turnover is the gerbil-like trading activity of the mutual fund industry which is the primary investor of Americans' 401(k) contributions. The average portfolio turnover at actively managed mutual funds, for example, is approximately 100 percent a year. Median turnover is in the 65 percent range. . . . [The] annual[] turnover of stocks traded on the New York Stock Exchange [is] well over 100 percent, with turnover approaching 138 percent in 2008. And . . . market capitalization data from the U.S. Statistical Abstract reveals that turnover across all U.S. exchanges reached approximately 311 percent in 2008.

Leo E. Strine, Jr., *One Fundamental Corporate Governance Question We Face: Can Corporations Be Managed for the Long Term Unless Their Powerful Electorates Also Act and Think Long Term?*, 66 BUS. LAW. 1, 10–11 (2010) (footnotes omitted).

27. *See generally* Bratton & Wachter, *supra* note 11, at 653–54, 720–21 (demonstrating that financial institutions that engaged in the speculation activities that triggered firm failures and the financial crisis had received a stock market premium over institutions that had not in the years before the crisis).

28. Binyamin Appelbaum, *Bailout Overseer Says Banks Misused TARP Funds*, WASH. POST, July 20, 2009, at A6 (noting that according to a report from the special inspector general charged with overseeing the government's

The borrowers, who share a good deal of responsibility, too, but whose need to take risks was perhaps easier to rationalize as moral—a house to live in and bills paid off versus the ability to buy an even cooler sports car—got a rawer deal. Rawest of all, though, was the deal for millions of hard working people who were paying their bills until the calamity destroyed economic growth and resulted in double-digit, persistent unemployment.[29] They continue to suffer as do many others who have retained their jobs but endured furloughs, benefit cuts and pay freezes, and seen their local taxes increase as services by budget-crunched governments diminish.

For now, however, the important lesson is simple. For-profit businesses have incentives toward current profit-maximization that make them poorly positioned to evaluate risk and be safe regulators. The environmental wreckage in the Gulf of Mexico and the global human wreckage caused by the financial sector's imprudence should be rather plain evidence of that truth.

II. "COMMUNITY VALUES" ON THE ASSEMBLY LINE AND IN ONLINE CLASSIFIEDS: RECOGNIZING THE INCENTIVES IN THE STOCKHOLDER-FINANCED CORPORATION

Another enduring myth is that there exist "special" for-profit corporations, ones that will behave differently from others over the long-run because they are controlled by visionaries who will place some idea of the public good ahead of profit. In saying this is a myth, I don't mean to imply that there are not very talented entrepreneurs who figure out how to do well by doing good. There are, thankfully, a number of businesses that do pay good wages, provide safe working environments and livable weekly hours, treat the environment with respect, and play the competitive game fairly. Instead, my point is that managers in stockholder-financed corporations are inevitably answerable to the stockholders, whatever the "community values" articulated by the corporation's

financial rescue program, many banks that received federal TARP money that was supposed to be used for increased lending instead used a portion of that money to make new investments, repay debts, or buy other banks).

29. At its high point, U.S. unemployment reached 10.1% in October 2009. As of December 2011, it remains at 8.5%, a figure that may be understated due to the way unemployment statistics are calculated. U.S. BUREAU OF LABOR STATISTICS, http://data.bls.gov/timeseries/LNS14000000 (last visited Feb. 27, 2012); *see also* Vincent Del Giudice & Thomas R. Keene, *U.S. Unemployment Probably Higher Than Reported, Silvia Says*, BLOOMBERG (Oct. 2, 2009), http://www.bloomberg.com/apps/news?pid=newsarchive&sid=aYxjmA7Mh96Q (noting that the unemployment rate in the United States is probably higher than reported because many laid off people who have been out of work for a long period of time have given up the search for jobs and are therefore no longer factored in to the unemployment calculation).

founders or others, which is why regulations designed to protect against the externality risks inherent in profit-seeking are critical.

A. A Taste of History: Henry Ford's Social Vision for Ford Motor Company

Ultimately, any for-profit corporation that sells shares to others has to be accountable to its stockholders for delivering a financial return. This is not a new notion. An American entrepreneur by the name of Henry Ford tested that proposition and lost some ninety-three years ago in a famous case.[30] In that case, Ford brazenly proclaimed that he was not managing Ford Motor Company to generate the best sustainable return for its stockholders.[31] Rather, he announced that the stockholders should be content with the relatively small dividend they were getting and that Ford Motor Company would focus more on helping its consumers by lowering prices and on bettering the lives of its workers and society at large by raising wages and creating more jobs.[32]

To simplify, the Michigan Supreme Court held that Ford could not justify his actions that way, and that although he could help other constituencies such as workers and consumers, as an instrument to the end of benefiting stockholders, he could not subordinate the stockholders' best interest.[33] This holding was central, in my view, to the court's embrace of what we call the

30. Dodge v. Ford Motor Co., 170 N.W. 668 (Mich. 1919).

31. *Id.* at 683–84.

32. *Id.* at 671; *see also* Thomas A. Edison, *Henry Ford Explains Why He Gives Away $10,000,000*, N.Y. TIMES, Jan. 11, 1914, § 5, at 3, *available at* http://query.nytimes.com/mem/archive-free/pdf?res=F2091EFE355D13738DDD A80994D9405B848DF1D3 (explaining that Henry Ford advocated for a more direct role for businesses to play in improving social welfare not by paying higher wages, but by "dividing profits with his employees"). Ford is also quoted as having said that he "believe[s] it is better for the nation, and far better for humanity, that between 20,000 and 30,000 should be contented and well fed than that a few millionaires should be made." *Id.* Of course, given that his litigation adversaries were the Dodge brothers, Ford's desire to deny them dividends that could be used to fund their own eponymous car manufacturing operations might have also contributed to Henry Ford's high-mindedness.

33. *Dodge*, 170 N.W. at 684 ("A business corporation is organized and carried on primarily for the profit of the stockholders. The powers of the directors are to be employed for that end. The discretion of 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 to the non-distribution of profits among stockholders in order to devote them to other purposes."); *see also* M. Todd Henderson, *Everything Old Is New Again: Lessons from* Dodge v. Ford Motor Company, *in* CORPORATE LAW STORIES 37, 66 (J. Mark Ramseyer ed., 2009) (noting that the Michigan Supreme Court's concern in *Dodge* was that a majority stockholder might use his control to "divert[] resources [of the corporation] to self-serving ends").

business judgment rule.[34] Under that rule, the judiciary does not second-guess the decision of a well-motivated, non-conflicted fiduciary.[35] Fundamental to the rule, however, is that the fiduciary

34. It is, of course, accepted that a corporation may take steps, such as giving charitable contributions or paying higher wages, that do not maximize corporate profits currently. They may do so, however, because such activities are rationalized as producing greater profits over the long-term. *See, e.g.*, Shlensky v. Wrigley, 237 N.E. 776, 780 (Ill. App. Ct. 1968) (rejecting a plaintiff shareholder's allegation of mismanagement against the corporation's directors for their refusal to install lights at Wrigley Field because the court was "not satisfied that the motives assigned [to the directors] are contrary to the best interests of the corporation and the stockholders" when adding lights for night baseball games might have reduced surrounding property values and that the "the long run interest of the corporation in its property value at Wrigley Field might demand all efforts to keep the neighborhood from deteriorating"); Melvin Aron Eisenberg, *Corporate Conduct That Does Not Maximize Shareholder Gain: Legal Conduct, Ethical Conduct, The Penumbra Effect, Reciprocity, The Prisoner's Dilemma, Sheep's Clothing, Social Conduct, and Disclosure*, 28 STETSON L. REV. 1, 14–15 (1998) (explaining that sometimes business decisions that appear to be profit-nonmaximizing, such as charitable donations, can in fact be justified on a "straight maximizing basis" and in fact, "frequently a corporation can earn greater profits by appearing to be philanthropic than by appearing to maximize [profits]"); Ian B. Lee, *Efficiency and Ethics in the Debate About Shareholder Primacy*, 31 DEL. J. CORP. L. 533, 555–56 (2006) ("Similarly, few would disagree . . . with the claim that eliminating . . . discretion [to make profit-sacrificing decisions] would be counterproductive even from the standpoint of shareholder profit-maximization."). The Delaware Supreme Court's contrasting treatment of the consideration directors can give to other constituencies in its famous *Unocal* and *Revlon* decisions makes this point. When a corporation is ongoing, it may consider the interests of other constituencies in pursuing a long-term course to maximize profits. Unocal v. Mesa Petroleum Co., 493 A.2d 946, 955 (Del. 1985) (holding that a board, in considering a threat that a hostile bid poses to the corporation, may consider "the nature of the takeover bid and its effect on the corporate enterprise" which entails, among other things, an analysis of "the inadequacy of the price offered, [the] nature and timing of the offer, questions of illegality, the impact on 'constituencies' other than shareholders (i.e., creditors, customers, employees, and perhaps even the community generally), the risk of nonconsummation, and the quality of securities being offered in the exchange"). But when there is no long-term, as when a sale is inevitable, directors must maximize value for the stockholders immediately. Revlon Inc. v. MacAndrews & Forbes Holdings, Inc., 506 A.2d 173, 182 (Del. 1986) ("A board may have regard for various constituencies in discharging its responsibilities, *provided there are rationally related benefits accruing to the stockholders*. However, such concern for non-stockholder interests is inappropriate when an auction among active bidders is in progress, and the object no longer is to protect or maintain the corporate enterprise but to sell it to the highest bidder.") (emphasis added) (internal citation omitted). These cases, when read together, mean stockholders' best interest must always, within legal limits, be the end. Other constituencies may be considered only instrumentally to advance that end.

35. Aronson v. Lewis, 473 A.2d 805, 812 (Del. 1984) ("[The business judgment rule] is a presumption that in making a business decision the directors of a corporation acted on an informed basis, in good faith and in the honest belief that the action taken was in the best interests of the company.");

be motivated by a desire to increase the value of the corporation for the benefit of the stockholders.[36] By confessing that he was placing his altruistic interest in helping workers and consumers over his duty to stockholders,[37] Henry Ford made it impossible for the court to afford him business judgment deference.

B. History Repeats Itself: Craigslist as a "Community" Corporation

In 2010, Chancellor Chandler decided a case in Delaware with some striking similarities to *Dodge v. Ford Motor*. The case[38] pitted the founder of Craigslist, the online classifieds firm, against eBay, the well-known online auction giant. As with the Dodge brothers and Ford, eBay (the suing stockholder) was also a competitor of the firm being sued. Also, as in *Dodge v. Ford Motor*, the firm being sued had a leader who openly argued that he was running the firm primarily to the end of something other than stockholder wealth, subordinating stockholders' financial well-being to his own unique social perspective. At Craigslist, according to this argument, the superior interest was the supposed community of users of its services, services the firm had been selling cheaply or giving away, when higher prices seemed to be readily attainable.[39]

But that core issue was not the subject of eBay's lawsuit, which instead focused on the measures Craigslist's founder took to ensure that he and his heirs would control Craigslist and to cement his vision that Craigslist be a community-oriented and community-driven corporation, not a cold-blooded profit machine. To that end,

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see also Sinclair Oil Corp. v. Levien, 280 A.2d 717, 720 (Del. 1971) ("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. A court under such circumstances will not substitute its own notions of what is or is not sound business judgment.").

36. *See, e.g.*, Kelli A. Alces, *Revisiting Berle and Rethinking the Corporate Structure*, 33 SEATTLE U. L. REV. 787, 792 (2010) ("[In Delaware, a] strong business judgment rule is coupled with strong, though rarely enforced, fiduciary rhetoric to try to keep managers faithful to shareholder wealth maximization . . . ."); Steven L. Schwarcz, *Fiduciaries With Conflicting Obligations*, 94 MINN. L. REV. 1867, 1909 (2010) ("In the corporate decisionmaking process, the business judgment rule encourages qualified directors to serve by limiting liability risk, [and] encourages inherently risky but value-maximizing transactions . . . ."); *see also Revlon*, 506 A.2d at 182 ("A board may have regard for various constituencies in discharging its responsibilities, *provided there are rationally related benefits accruing to the stockholders*." (emphasis added) (citing *Unocal*, 493 A.2d at 955)).

37. In reaching its conclusion, the Michigan Supreme Court observed the "attitude and . . . expressions of Mr. Henry Ford," quoting part of Ford's testimony: "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 in the business." *Dodge*, 170 N.W. at 683.

38. eBay Domestic Holdings, Inc. v. Newmark, 16 A.3d 1 (Del. Ch. 2010).

39. *Id.* at 8.

Craig Newmark (the Craigslist founder, controlling stockholder, and director) and Jim Buckmaster (the other controlling stockholder and director on Craigslist's three-member board) implemented actions aimed at stopping or slowing eBay's ability to acquire Craigslist, or otherwise disrupt what Craig and Jim called Craigslist's "corporate culture."[40]

The most important antitakeover measure was the adoption of a shareholder rights plan that would have diluted eBay's ownership of Craigslist upon even a minor increase in eBay's minority stockholding position. In defending their decision in court, Jim and Craig did not argue that they employed the poison pill to protect the economic interests of the company's stockholders. No, instead Jim and Craig argued that the pill was justified by their heartfelt desire to protect Craigslist's coveted social values and community-centered culture from the disruption an eBay acquisition might have on those values and culture.[41]

Echoing what I view as a standard notion behind the business judgment rule, Chancellor Chandler rejected Jim and Craig's argument. In so ruling, he stated, "Directors for a for-profit Delaware corporation cannot deploy a rights plan to defend a business strategy that openly eschews stockholder wealth maximization—at least not consistently with the directors' fiduciary duty under Delaware law."[42] This, to my view, rather expected statement, drew fire from both ends of our corporate law political spectrum, if there be such a thing.

A group promoting a new form of for-profit corporation, the charter of which indicates that other ends, such as philanthropic or community-aimed ends, can be put ahead of profit, reacted with hyperbole, urging corporations to leave Delaware.[43] If, they said, you remain incorporated in Delaware, your stockholders will be able to hold you accountable for putting their interests first.[44] You must

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40. *Id.* at 15–16.

41. *Id.* at 32.

42. *Id.* at 35.

43. *See* Jay Coen Gilbert, *What eBay's Court Fight With Craigslist Reveals*, FORBES (Sept. 21, 2010, 10:56 AM), http://www.forbes.com/sites/csr/2010/09/21/what-ebays-court-fight-with-craigslist-reveals/ ("If you want to maintain the social mission of your company, don't incorporate in Delaware.").

44. *Id.* Although he believes that "*in general,* a shareholder invests in a for-profit Corporation for the purpose of maximizing their returns," Maxwell S. Kennerly, a liberal commentator and lawyer, believes that that general principle must be "considered in light of *the specifics* of each company." Maxwell S. Kennerly, eBay v. Newmark*: Al Franken Was Right, Corporations Are Legally Required To Maximize Profits*, LITIG. & TRIAL (Sept. 13, 2010), http://www.litigationandtrial.com/2010/09/articles/the-law/for-lawyers/ebay-v-newmark-al-franken-was-right-corporations-are-legally-required-to-maximize-profits/. In that vein, Kennerly believes that because eBay bought its shares in Craigslist in an arms-length transaction and knew that Craigslist, for better or worse, had a "tangibly different idea of 'for-profit,'" eBay should not be able to

go elsewhere, to a fictional land where you can take other people's money, use it as you wish, and ignore the best interests of those with the only right to vote.[45] In this fictional land, I suppose a fictional accountability mechanism will exist whereby the fiduciaries, if they are a controlling interest, will be held accountable for responsibly balancing all these interests. Of course, a very distinguished mind of the political left, Adolph Berle, believed that when corporate fiduciaries were allowed to consider all interests without legally binding constraints, they were freed of accountability to any.[46] Equally unrealistic is the idea that

complain that Jim and Craig had no "sound business reasons for their decision to protect the highly successful, if idiosyncratic, corporate culture at craigslist, and that decision should be protected by the business judgment rule." *Id.* *See also* Joshua P. Fershee, *The Wake of the* eBay *Decision: Is Ben & Jerry's Next?*, BUS. L. PROF BLOG (Dec. 6, 2010), http://lawprofessors.typepad.com/business_law/2010/12/the-wake-of-the-ebay-decision-is-ben-jerrys-next-.html ("I still find myself troubled by the determination that, by embracing its 'community service mission,' craigslist was being run improperly as [a] corporate entity.").

45. The new B Corporation movement is an interesting attempt to address constituency concerns within corporate law. The idea is that the B Corporation would have a charter that would permit or even require the directors to consider interests, such as the public interest or more specific constituency concerns, and not just the interests of stockholders. *Legal Requirement*, CERTIFIED B CORP., http://www.bcorporation.net/become/legal (last visited Feb. 27, 2012). The problem with the B Corporation, though, is that the only stakeholders with a vote would continue to be the stockholders, who by electing a new board who supported a change, could presumably change the charter. *See, e.g.*, DEL. CODE ANN. tit. 8, § 242(a) (2010) (allowing corporation to amend its certificate of incorporation in any manner which would have been lawful in the first instance); *id.* § 242(b)(1) (setting forth procedural requirements for amending the certificate of incorporation and requiring, in addition to a stockholder vote, a resolution adopted by the board of directors setting forth the amendment and declaring its advisability). Moreover, it is not clear to what extent the B Corporation concept is designed to give standing to other constituencies to sue to enforce the directors' duty to them. The weight to be given to other constituencies would seem to be a matter entrusted to the judgment of the directors (albeit a calculus not so easily called a "business judgment") and would be difficult for courts to second guess. This reality, of course, is reflected in a long-standing concern that by permitting directors to justify their actions by reference to virtually everything, they will not be accountable to any constituency for anything. Adolf A. Berle, Jr., *For Whom Corporate Managers Are Trustees: A Note*, 45 HARV. L. REV. 1365, 1367 (1932).

46. *See* Berle, *supra* note 45, at 1367 ("When the fiduciary obligation of the corporate management and 'control' to stockholders is weakened or eliminated, the management and 'control' become for all practical purposes absolute."). Berle was not entirely against a corporate governance regime in which corporate managers could consider the interests of a larger polity outside the stockholders, but was steadfast in arguing that until a sensible system emerges—one that prudently monitors and constrains managers, even while they balance a wider host of interests—we must not deviate lightly from the status quo. *See id.* at 1372 ("Unchecked by present legal balances, a social-economic absolutism of corporate administrators, even if benevolent, might be unsafe; and in any case it hardly affords the soundest base on which to

corporations authorized to consider other interests will be able to do so at the expense of stockholder profits if voting control of the corporation remains in the stock market.[47] Just how long will hedge funds and mutual funds subordinate their desire for returns to the desire of a founder to do good?

From a different political perspective come those who seem to take umbrage at plain statements like the Chancellor's for unmasking the face of capitalism. These commentators seem dismayed when anyone starkly recognizes that as a matter of corporate law, the object of the corporation is to produce profits for the stockholders and that the social beliefs of the managers, no more than their own financial interests, cannot be their end in managing the corporation. Maxwell Kennerly, in his review of the *eBay* decision, noted what he perceived to be a triad of conservative academic commentators who were unhappy with Senator Al Franken's statement that "it is literally malfeasance for a corporation not to do everything it legally can to maximize its profits"—a statement, that in Kennerly's view, encapsulates a material portion of the holding in the *eBay* opinion.[48]

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construct the economic commonwealth which industrialism seems to require. *Meanwhile, as lawyers, we had best be protecting the interests we know, being no less swift to provide for the new interests as they successively appear*." (emphasis added)).

47. The "practical consequence" of an adherence to the so-called "property model" of the corporation is that the board of directors will, when faced with a conflict among the corporation's stockholders and other corporate constituencies, almost always favor the stockholders' interests because "in the intra-corporate republic, only capital has the right to vote!" Leo E. Strine, Jr., *The Social Responsibility of Boards of Directors and Stockholders in Charge of Control Transactions: Is There Any "There" There?*, 75 S. CAL. L. REV. 1169, 1186–87 (2002).

48. Kennerly, *supra* note 44. As recounted by Kennerly, Professor Todd Henderson argued that although "the duty to maximize shareholder value may be a useful shorthand for a corporate manager to think about how to act on a day-to-day basis, this is not legally required or enforceable." *Id.* (quoting Todd Henderson, *The Shareholder Wealth Maximization Myth*, TRUTH ON THE MARKET (July 27, 2010), http://truthonthemarket.com/2010/07/27/the-shareholder-wealth-maximization-myth/). Professor Stephen Bainbridge agreed, positing that "[t]he fact that corporate law does not intend to promote corporate social responsibility, but merely allows it to exist behind the shield of the business judgment rule, becomes rather significant in—and is confirmed by—cases where the business judgment rule does not apply." Stephen Bainbridge, *Al Franken, Shareholder Wealth Maximization, and the Business Judgment Rule*, PROFESSORBAINBRIDGE.COM (July 27, 2010), http://www.professorbainbridge.com/professorbainbridgecom/2010/07/shareholder-wealth-maximization-and-the-business-judgment-rule.html#tp. Finally, Professor Larry Ribstein was also quick to contest Franken's comment: "The Franken misconception is widely espoused by those in the radical anti-corporate camp. . . . This is why the corporate social responsibility debate is largely empty. While many corporate social responsibility proponents argue for giving managers more legal freedom to serve society's needs, managers already have

One suspects that this vein of commentary does not fear the unmasking because these commentators believe that courts would actually prevent corporations from pursuing profit in an enlightened manner.[49] To the contrary, one senses that they may be uncomfortable with a plain acknowledgment that corporate managers' primary duty is to seek as much profit as can be achieved within the limits of the law, precisely because to do so emphasizes the importance of the law in channeling corporate behavior. Preferable is suggesting that corporate managers themselves while seeking to maximize corporate profits will take care of the public interest, and that government should leave it to corporate managers.[50]

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that freedom." Larry Ribstein, *The Shareholder Maximization Canard*, TRUTH ON THE MARKET (July 28, 2010), http://truthonthemarket.com/2010/07/28/the-shareholder-maximization-canard/. Kennerly attributed this dismissal of Franken's views to an underappreciation of what he describes as a legal requirement that corporations, even if allowed to engage in certain philanthropic efforts, undertake to maximize profits. *See* Kennerly, *supra* note 44 ("[T]he duty to maximize profits isn't, as Henderson said, a 'canard.' It's an enforceable . . . legal doctrine, and it was just enforced against craigslist.").

49. This sense comes from the conservative response discussed *supra* in note 48, in which the commentators appear to argue that corporations already enjoy the prerogative to pursue philanthropic ends to the extent that those who would argue, as Al Franken does, that corporations are legally required to maximize profits, underemphasize the wide latitude managers already enjoy under the business judgment rule.

50. To this extent, this position echoes the "just trust the business leaders" approach of Merrick Dodd, in his debate with Adolph Berle. E. Merrick Dodd, Jr., *For Whom Are Corporate Managers Trustees?*, 45 HARV. L. REV. 1145, 1153 (1932) ("If, however, as much recent writing suggests, we are undergoing a substantial change in our public opinion with regard to the obligations of business to the community, it is natural to expect that this change of opinion will have some effect upon the attitude of those who manage business. If, therefore, the managers of modern businesses were also its owners, the development of a public opinion to the effect that business has responsibilities to its employees and its customers would, quite apart from any legal compulsion, tend to affect the conduct of the better type of business man. The principal object of legal compulsion might then be to keep those who failed to catch the new spirit up to the standards which their more enlightened competitors would desire to adopt voluntarily. Business might then become a profession of public service, not primarily because the law had made it such but because a public opinion shared in by business men themselves had brought about a professional attitude."). By contrast, Berle believed that corporate managers needed to be subject to regulation in the public interest. *See, e.g.*, Berle, *supra* note 45, at 1368 ("Either you have a system based on individual ownership of property or you do not. If not—and there are at the moment plenty of reasons why capitalism does not seem ideal—it becomes necessary to present a system (none has been presented) of law or government, or both, by which responsibility for control of national wealth and income is so apportioned and enforced that the community as a whole, or at least the great bulk of it, is properly taken care of. Otherwise the economic power now mobilized and massed under the corporate form, in the hands of a few thousand directors, and the few hundred individuals holding 'control,' is simply handed over, weakly, to

The consternation at Chancellor Chandler's *eBay* decision is surprising for another related reason. The whole design of corporate law in the United States is built around the relationship between corporate managers and stockholders, not relationships with other constituencies. In the corporate republic, only stockholders get to vote and only stockholders get to sue to enforce directors' fiduciary duties.[51] The natural focus of the managers in such a system is therefore supposed to be on advancing the best interests of the stockholders, subject to the legal constraints within which the firm operates.[52] Precisely because it is ultimately the equity market that is the primary accountability system for public firms, efforts to tinker around with the margins of corporate law through initiatives like constituency statutes, the so-called Corporate Social Responsibility movement, and antitakeover provisions have been of very little utility in insulating corporate boards from stockholder and stock market pressures.[53]

The *eBay* case also points out again the idiosyncratic nature of a reliance on special founders. The founder of Craigslist apparently cares about users of online classifieds, but who knows about his

the present administrators with a pious wish that something nice will come out of it all." (internal citations omitted)).

51. *See* Strine, *supra* note 47, at 1187 (observing that in the "intra-corporate republic," only stockholders have the right to vote); *see also* FRANKLIN BALOTTI & JESSE A. FINKELSTEIN, DELAWARE LAW OF CORPORATIONS & BUSINESS ORGANIZATIONS § 13.11 (3d ed. 2009) ("Thus, a plaintiff who is not a stockholder, or who ceases to be a stockholder during the pendency of his [derivative] suit, loses standing to maintain a derivative action."); 5 WILLIAM MEAD FLETCHER ET AL., FLETCHER CYCLOPEDIA OF THE LAW OF CORPORATIONS § 2025 (perm. ed., rev. vol. 2009) ("Generally, the right to vote is a right that is inherent in and incidental to the ownership of corporate stock . . . ."); *cf.* J. Travis Laster, *Goodbye to the Contemporary Ownership Requirement*, 33 DEL. J. CORP. L. 673, 681 (2008) ("[B]ecause the selling stockholder no longer has stockholder status, the right to sue [derivatively] with respect to those shares is extinguished by the sale.").

52. *See, e.g.*, Strine, *supra* note 47, at 1187 n.35 ("'I'm gonna take two weeks, gonna have a fine vacation/I'm gonna take my problem to the United Nations/Well I called my congressman and he said, quote/'I'd love to help you, son, but you're too young to vote.'" (quoting EDDIE COCHRAN, SUMMERTIME BLUES (Liberty Records 1958))).

53. *See, e.g.*, Marcel Kahan & Edward B. Rock, *How I Learned To Stop Worrying and Love the Pill: Adaptive Responses to Takeover Law*, 69 U. CHI. L. REV. 871, 909 (2002) (citing statistics which show takeover activity in the United States has actually increased over time); Robert E. Spatt, *The Four Ring Circus–Round Twelve: A Further Updated View of the Mating Dance Among Announced Merger Partners and an Unsolicited Second or Third Bidder*, SIMPSON THACHER & BARTLETT LLP 1 (Mar. 24, 2008), http://www.simpsonthacher.com/content/publications/pub698.pdf (cataloging numerous instances of "deal jumping" in which additional bids are made for a target by third parties after the signing of a merger agreement, and noting that such instances have "become a standard execution risk of getting a deal done, and tend[] to reflect the ebb and flow of hostile acquisition activity").

other views. Henry Ford said he cared about labor, but was responsible for one of the most violent crack-downs on labor in American history during the "Battle of the Overpass" at Ford's River Rouge plant in Dearborn, Michigan in 1937. Other entrepreneurs have unique religious or social views, which they seek to spread to their workers and customers.[54] As many have noted, the legitimacy of such managers to use others' money to advance their own view of the good is suspect.[55] And over time, as transitions in industries like the newspapers show, the ability of a founder to sustain a vision after having taken investors' money is extremely limited. The point here is not that views on these matters are not contestable, but that the idea of a public corporation with outside investors pursuing a controversial political or moral agenda is intrinsically problematic

54. Take Chick-fil-A, for example. Its founder, Truett Cathy, has closed all of its restaurants on Sundays since he opened the first restaurant in 1946 to enable its employees to attend church. Melissa Lee, *Chick-fil-A Does Business with Religious Conviction*, CNBC (Dec. 6, 2007), http://www.cnbc.com/id/22114420/Chick_Fil_A_Does_Business_With_Religious_Conviction. Recently, there has been concern about the company's subsidy of groups that believe that homosexuality is immoral. Alex Pareene, *Koch Brothers, Christian Chicken-Sellers Besieged by Thuggish Liberal Criticism*, SALON (Feb. 3, 2011), http://www.salon.com/news/first_amendment/?story=/politics/war_room/2011/02/03/koch_chick_fil_a_liberals.

55. *See, e.g.*, William T. Allen, *Our Schizophrenic Conception of the Business Corporation*, 14 CARDOZO L. REV. 261, 275 (1992) ("[M]any people would find . . . disturbing [the proposition] that directors know what is better for shareholder[s] than they themselves do. . . . May [directors] act to protect others (and themselves) from claims of shareholder exploitation?"); Stephen M. Bainbridge, *In Defense of the Shareholder Wealth Maximization Norm: A Reply to Professor Green*, 50 WASH. & LEE L. REV. 1423, 1445 (1993) (arguing against displacing the shareholder wealth maximization model with a model that allows corporate managers to consider various nonshareholder interests in line with their own ethical preferences because of the "very real risk that some corporate directors and officers will use nonshareholder interests as a cloak for actions taken to advance their own interests"); Milton Friedman, *The Social Responsibility of Business is to Increase Its Profits*, N.Y. TIMES MAG., Sept. 13, 1970, at 33 (arguing that the notion that corporations have a "social responsibility" impermissibly displaces the democratic political process with a doctrine that permits minorities to effect extra-political changes that may or may not be the best policies); Mark E. Van Der Weide, *Against Fiduciary Duties to Corporate Stakeholders*, 21 DEL. J. CORP. L. 27, 54–55, 69–70 (1996) (arguing against displacing the shareholder wealth maximization norm with one that allows more leeway to corporate directors, whose ability to redistribute wealth between different social groups is "doubtful," and that the ability to consider and balance a host of nonstockholder constituencies and personal views of the good would, among other undesired results, create a system where protection from managerial self-interest would "dissolve" because managers could in effect "reallocate the costs of the duty of loyalty among stakeholders groups"); *cf.* City Capital Assocs. Ltd. P'ship v. Interco Inc., 551 A.2d 787, 796 (Del. Ch. 1988) ("[H]uman nature may incline *even one acting in subjective good faith* to rationalize as right that which is merely personally beneficial.").

because that is not why investors invest nor is that the basis on which boards are elected.

The public interest, in the end, depends on protection by the public's elected representatives in the form of law. The well-intentioned efforts of many entrepreneurs and company managers, who have a duty to their investors to deliver a profit, to be responsible employers and corporate citizens is undoubtedly socially valuable. But it is no adequate substitute for a sound legally determined baseline.

By so stating, I do not mean to imply that the corporate law requires directors to maximize short-term profits for stockholders. Rather, I simply indicate that the corporate law requires directors, as a matter of their duty of loyalty, to pursue a good faith strategy to maximize profits for the stockholders. The directors, of course, retain substantial discretion, outside the context of a change of control, to decide how best to achieve that goal and the appropriate time frame for delivering those returns.[56] But, as I have noted in other writings, the market pressures on corporate boards are making it more difficult for boards to resist the pressure to emphasize the delivery of immediate profits over the implementation of longer-term strategies that might yield more durable and more substantial benefits to stockholders, as well as society in general.[57] In these other writings, I have suggested some modest initiatives to better align the corporate governance system so that the shared interests of the end-user providers of capital and the interests of talented managers and societies in sound, long-term wealth creation are given greater weight.[58]

III. NATIONAL INTERESTS IN COMMUNITY ICONS: SOME INSTRUCTIVE LESSONS FROM ABROAD

The power of stockholders' ardor for profits shows up especially in corporate takeovers, where the benefits to stockholders are on full

56. Paramount Commc'ns, Inc. v. Time Inc., 571 A.2d 1140, 1154 (Del. Ch. 1989) ("Delaware law confers the management of the corporate enterprise to the stockholders' duly elected board representatives. The fiduciary duty to manage a corporate enterprise includes the selection of a time frame for achievement of corporate goals. . . . Directors are not obliged to abandon a deliberately conceived corporate plan for a short-term shareholder profit unless there is clearly no basis to sustain the corporate strategy." (internal citations omitted)).

57. *See* Strine, *supra* note 26, at 16–17 (citing various sources); Leo E. Strine, Jr., *Toward Common Sense and Common Ground? Reflections on the Shared Interests of Managers and Labor in a More Rational System of Corporate Governance*, 33 J. CORP. L. 1, 15 (2007) [hereinafter Strine, *Toward Common Sense*]; Leo E. Strine, Jr., *Why Excessive Risk-Taking is Not Unexpected*, N.Y. TIMES DEALBOOK (Oct. 5, 2009), http://dealbook.nytimes.com/2009/10/05/dealbook-dialogue-leo-strine/ [hereinafter Strine, *Risk-Taking*].

58. *See, e.g.*, Strine, *Toward Common Sense*, *supra* note 57, at 15; Strine, *supra* note 26, at 18–19; Strine, *Risk-Taking*, *supra* note 57.

display and the costs to other corporate constituencies can be stark. The tension revealed in a takeover is highlighted when the corporation is an icon with a long history of presence and responsibility in a community. How does corporate and takeover law choose? Two interesting answers come from outside the United States. In Kraft's takeover of the iconic Cadbury, long-standing U.K. law tilted decidedly in favor of stockholder interests, but U.K. politicans found the logical consequences of their own settled law dismaying. By contrast, when the Australian mining firm BHP Billiton sought to acquire the Potash Corporation of Saskatchewan, the Canadian government had the legal authority to express its objection in full conformity with the law, and did so. It turns out that even in capitalist societies whose economies are premised on profit-seeking, the full implications of giving stockholders the power to make societally-important decisions remains controversial.

A. Frustrations of Nonfrustration: Lessons from the Odd Case of Cadbury

Perhaps the most surprising manifestation of political naïveté about the nature of the corporation comes from England and the controversy over Kraft's acquisition of Cadbury, the maker of very sweet, nearly chocolate products.[59] The idea that the maker of Dairy Milk would be acquired by a maker of boxed macaroni and cheese was seen as a threat to a British icon, and to British jobs, rather than as a natural alliance of culinary co-travelers. Despite the fact that Kraft was already an employer of many in England[60] and had a good reputation as a quality employer responsive to environmental and free trade concerns,[61] opposition to a Kraft takeover was widespread in the United Kingdom.

59. Cadbury's signature product, Dairy Milk, is made from 26% cocoa solids, which qualifies it to be called "Milk Chocolate" in the European Union, but not "Chocolate." *See Products*, CADBURY, http://www.cadbury.com.au/Products/Blocks-of-Chocolate/Dairy-Milk-Block/Dairy-Milk-Ingredients.aspx (last visited Feb. 27, 2012); Council Directive 2000/36, Annex I, 2000 O.J. (L 197) 19, 22 (requiring that "Milk Chocolate" contain at least 25% cocoa solids and "Chocolate" contain at least 35% of the same). But, the name "Dairy Milk" long pre-dates the European Union's naming convention, having been used since the bars were introduced in 1905 as a testament to the fact that there has "always [been] a glass and a half of fresh, natural milk in each half pound of chocolate." *Cadbury Dairy Brands*, KRAFT FOODS, http://www.kraftfoodscompany.com/brands/featured-brands/dairy_milk.aspx (last visited Feb. 27, 2012).

60. *See* Amy Wilson & James Quinn, *Kraft Moves Fast to Silence the Doubters*, THE TELEGRAPH, Jan. 23, 2010, at 8 (reporting that even before the purchase of Cadbury, Kraft employed about 1500 workers in the United Kingdom).

61. *See, e.g.*, Press Release, Kraft Foods, Kraft Foods Makes Dow Jones Sustainability Index Sixth Year in a Row (Sept. 9, 2010), *available at* http://phx.corporate-ir.net/phoenix.zhtml?c=129070&p=irol-

A wide range of commentators, the British public, and Members of Parliament from not just the Labour party, but also the Tory and Liberal Democrat parties, voiced objection to the idea that an English icon would be owned by an American company. Even though the current British ownership was already well on its way to shutting down some of the company's most historic operations and shipping production to lower wage Poland,[62] U.S. ownership was thought to make the prospect of even more moves of this kind possible. Despite the fact that Cadbury was itself a company that had prospered by buying up other nation's icons—remember A&W Root Beer,[63] or Dr. Pepper, or Canada Dry Ginger Ale[64]—its Chairman, Sir Roger Carr, was aghast that so-called short-term stockholders had taken shares from the company's long-term investors when Kraft made its bid public.[65] How could these long-

newsArticle&ID=1469308&highlight= (noting that Kraft Foods was named to the Dow Jones Sustainability Index for the sixth year in a row, received the food industry's leading scores in operational eco-efficiency for the third year in a row, and received leading scores in corporate citizenship/philanthropy).

62. *See* Roger Carr, Chairman, Cadbury, Distinguished Speaker Seminar at Said Business School at University of Oxford (Feb. 9, 2010) [hereinafter Carr Speech], *available at* http://mediastore1.sbs.ox.ac.uk/visiting_speakers/090210_1845_NMLT_Roger_Carr.mp3 (noting that some of Cadbury's "most recent and material manufacturing investments" in the years before the Kraft acquisition had been in Poland with an eye towards replacing U.K. production); *Cadbury Factory Closure by Kraft "Despicable"*, BBC (Feb. 10, 2010), http://news.bbc.co.uk/2/hi/8507780.stm ("Plans to close the Keynsham plant, at the cost of 400 jobs, were announced by Cadbury in 2007. Kraft said it had only become aware of how advanced plans for the new Poland factory were after the takeover deal had been agreed.").

63. A&W Root Beer was founded as an American company in 1919 by founder Roy Allen. *A&W History*, A&W ROOT BEER, http://www.rootbeer.com/history/ (last visited Feb. 27, 2012). The name A&W comes from Allen's business partner, Frank Wright, with whom Allen partnered in 1922. *Id.*

64. In 1986, Cadbury Schweppes, plc, purchased Canada Dry from RJR Nabisco, Inc. Richard Stevenson, *Cadbury Will Buy RJR Nabisco Units*, N.Y. TIMES, June 3, 1986, at D4, *available at* http://www.nytimes.com/1986/06/03/business/cadbury-will-buy-rjr-nabisco-units.html.

65. Carr Speech, *supra* note 62 ("In the final analysis, it was the shift in the register that lost the battle for Cadbury—the owners were progressively not long-term stewards of the business but financially motivated investors, judged solely on their own quarterly financial performance. At the end of the day, there were simply not enough shareholders prepared to take a long term view of Cadbury and prepared to forego short term gain for longer term prosperity. . . . At the end of the day, individuals controlling shares which they had held for only a few days or weeks determined the destiny of a company that had been built over almost 200 years."). Others in the U.K. political establishment in place at the time of the Kraft-Cadbury acquisition were also upset by short-termism's alleged evils. *See* Blanaid Clarke, *Directors' Duties during an Offer Period—Lessons from the Cadbury Plc Takeover* 5–6 (UCD Working Papers in Law, Criminology & Socio-Legal Studies, Research Paper No. 44/2011), *available at* http://ssrn.com/abstract=1759953 (quoting Lord Mandelson, Sec'y of State for Bus., Innovation and Skills, Speech at the Trade

term stockholders have abandoned the company, and why should these new short-termers decide the fate of a 200 year old British treasure?[66]

What surprised me about this was not that the English would wish Cadbury could remain independent. As an American, I get that. Our largest American beer company is now the Boston Beer Company, brewers of Samuel Adams,[67] a former upstart microbrewery founded only twenty-seven years ago![68] But what makes the Cadbury situation so odd is that the United Kingdom has long trumpeted its approach to corporate takeovers. The British have boasted that their legal regime—which prohibits corporate boards from taking any action to frustrate a fully financed, firm offer like Kraft's[69]—is the best model. The United Kingdom supported adoption of similar laws by the European Union[70] and has

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and Indus. Dinner, Guildhall, the Mansion House, London (Mar. 1, 2010)) ("Lord Mandelson, the Business Secretary at the time of the [Kraft] takeover complained that 'In the case of Cadbury and Kraft it is hard to ignore the fact that the fate of a company with a long history and many tens of thousands of employees was decided by people who had not owned the company a few weeks earlier, and probably had no intention of owning it a few weeks later.'"); *id.* at 6 ("Vince Cable[, the current Business Secretary,] subsequently referred to 'short term investors and financial gamblers [who] value a quick buck above all else.'" (quoting Press Release, Dep't of Bus., Innovation, and Skills (Sept. 22, 2010))).

66. *Our Story*, CADBURY, http://www.cadbury.co.uk/cadburyandchocolate/ourstory/Pages/ourstoryFlash.aspx (last visited Feb. 27, 2012).

67. After Anheuser-Busch was sold to Belgian-based InBev in 2008, Boston Beer Co., the makers of Sam Adams, became the largest, independent, publicly traded brewery in the United States. Beth Kowitt, *Meet the New King of Beers*, CNN MONEY (Aug. 8, 2008), http://money.cnn.com/2008/08/07/magazines/fortune/beer_koch.fortune/index.htm.

68. *In 1984, "Better Beer" Did Not Exist*, SAMUEL ADAMS, http://www.samueladams.com/discover-craft/history-sam-adams.aspx (last visited Feb. 27, 2012). Larger American beer companies, like Anheuser-Busch and Miller Brewing Company, are now owned by foreign companies. Clementine Fletcher, *SABMiller Spurning Femsa Means Higher Foster's Price: Real M&A*, BLOOMBERG (Feb. 24, 2011), http://www.bloomberg.com/news/2011-02-24/sabmiller-spurning-femsa-means-increased-price-for-foster-s-beer-real-m-a.html (noting that South African Breweries Plc, a South African company, purchased Miller Brewing Company in 2002); William Spain & Steve Goldstein, *Anheuser-Busch Accepts $52 Billion InBev Offer*, WALL ST. J. MARKETWATCH (July 14, 2008), http://www.marketwatch.com/story/anheuser-busch-accepts-52-billion.

69. CITY CODE ON TAKEOVERS AND MERGERS r. 21 (Panel on Takeovers & Mergers 2011) [hereinafter TAKEOVER CODE], *available at* http://www.thetakeoverpanel.org.uk/wp-content/uploads/2008/11/code.pdf.

70. *Cf.* PANEL ON TAKEOVERS & MERGERS, THE EUROPEAN DIRECTIVE ON TAKEOVER BIDS 2 (2005) (lamenting the fact that the United Kingdom was unable to secure passage of an EU directive that would have required EU member states to adopt a nonfrustration provision in their takeover codes like Rule 21 of the U.K.'s Takeover Code).

touted its model as being superior to that of the United States,[71] where boards are entitled to defend against bids they believe are inadequate.[72] The U.K. regime leaves no real room for a board to block a financed bid except by convincing its stockholders that the price is too low. If the stockholders believe the price is right, they get to accept the bid.

Given that reality, it was hardly surprising to see Kraft eventually succeed in its bid. After all, the whole focus of the U.K. approach is that if the stockholders like the price of a takeover bid, they get to take it.[73] And all market evidence has long made clear that, absent board or government interposition, stockholders will sell out into any bid offering a substantial premium.[74] What was

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71. *See, e.g.*, Paul Davies, Shareholder Value, Company Law and Securities Markets Law: A British View 22–24 (Oct. 2000) (unpublished manuscript), *available at* http://ssrn.com/abstract=250324 (observing that the U.S. takeover rules are "clearly less responsive to the conflicts of interest to which target boards are subject in hostile bids and more responsive to the argument that setting business strategy is the preserve of centralised management rather than of the shareholders" and questioning "whether the U.S. rules do more than permit the entrenchment of target management under the guise of protecting target shareholders against bidder opportunism or protecting the interests of non-shareholder groups"); *see also* John C. Coates, IV, *M&A Break Fees: US Litigation vs. UK Regulation* 30 (Harvard Law Sch. Public Law & Legal Theory Working Paper No. 09-57, 2009), *available at* http://ssrn.com/abstract=1475354 ("The UK's regulatory approach exhibits clear benefits. It generates little or no litigation, provides clear guidance for market participants, keeps fees low, and increases bid competition. . . . [I]t may make it harder for target fiduciaries to favor bidders for private benefits . . . ."). But others disagree. Lipton and Rowe point out that since 1985 and Delaware's embrace of the poison pill, the volume of merger activity in the United States has increased. Martin Lipton & Paul K. Rowe, *Pills, Polls, and Professors: A Reply to Professor Gilson*, 27 DEL. J. CORP. L. 1, 20–21 (2002). They also highlight two J.P. Morgan & Co. studies that show that "premiums paid to firms with pills were forty-two percent higher than the market price of the acquired firm's shares five days prior to the initial offer, while companies that did not adopt pills received an average premium of only thirty percent[,]" and they reject as lacking empirical support the proposition that hostile takeovers "either increase aggregate returns to shareholders or effectively 'discipline' corporate management[.]" *Id.*

72. *See, e.g.*, eBay Domestic Holdings, Inc. v. Newmark, 16 A.3d 1, 29 n.86 (Del. Ch. 2010) (citing Revlon Inc. v. MacAndrews & Forbes Holdings, Inc., 506 A.2d 173 (Del. 1986)) (noting that Delaware has recognized the propriety of a board's adoption of a rights plan in order to counter the threat posed by a hostile takeover at a price that the board reasonably concludes is below the corporation's intrinsic value).

73. John Armour & David A. Skeel, *Who Writes the Rules for Hostile Takeovers, and Why?*, 96 GEO. L.J. 1727, 1729 (noting that in the U.K., poison pills and other defensive measures that "will have the effect of impeding target shareholders' ability to decide on the merits of a takeover offer" are strictly forbidden).

74. *Cf.* Stephen M. Bainbridge, Unocal *at 20: Director Primacy in Corporate Takeovers*, 31 DEL. J. CORP. L. 769, 816 (2006) (rejecting the proposition that directors should be precluded from interfering with a stockholder's desire to tender his stock because it would allow the bidder, instead of bargaining hard

more surprising was to see politicians of all the major parties in the United Kingdom bemoan the foreordained result that followed from the United Kingdom's long-standing approach,[75] especially given that Cadbury could have had a lot of suitors less savory than Kraft.[76]

The world's most venerable parliamentary assembly even issued a hand-wringing report deploring the situation[77] but failed to identify any tangible policy proposal to address future situations like it, which are inevitable under the long-standing nonfrustration rule. The new Tory-Liberal coalition government then commissioned an inquiry to explore certain proposals made by Roger Carr,[78] including requiring that a supermajority of stockholders decide whether to accept a takeover bid and disenfranchising short-term holders. But the key regulatory body—the Takeover Panel—has already looked at and rejected those proposals,[79] and its

with the target board for a merger, to acquire stock at a "low-ball tender offer" at a premium to market price); Henry G. Manne, *Mergers and the Market for Corporate Control*, 73 J. POL. ECON. 110, 118 (1965) ("The shareholders should ordinarily be willing to accept any offer of a tax-free exchange of new marketable shares worth more than their old shares."); Guhan Subramanian, *Bargaining in the Shadow of Takeover Defenses*, 113 YALE L.J. 621, 643 (2003) (noting that in the absence of takeover defenses, stockholders will accept a bid at a premium to market price).

75. *See, e.g.*, *Clegg Attacks Brown over RBS Funding for Cadbury Bid*, BBC (Jan. 20, 2010), http://news.bbc.co.uk/2/hi/8470776.stm (noting that British politicians from the Labour Party and the Liberal Democrat Party expressed anger over Kraft's acquisition of Cadbury and reporting former Business Secretary Lord Peter Mandelson's declaration that the British government would mount a "huge opposition" to Kraft's takeover of Cadbury); Sarah O'Grady, *Famous Chocolate Factory Cadbury's Gets Chop*, EXPRESS (Jan. 15, 2011), http://www.express.co.uk/posts/view/223231/Famous-chocolate-factory-Cadbury-s-gets-chop (noting Conservative Party member Jacob Rees-Mogg's anger at the Kraft takeover and Kraft's decision, despite its promises, to close a Cadbury production plant in Somerdale).

76. *See supra* notes 60–61 and accompanying text.

77. *See* BUSINESS, INNOVATION, AND SKILLS COMMITTEE, MERGERS, ACQUISITIONS, AND TAKEOVERS: THE TAKEOVER OF CADBURY BY KRAFT, 2009–10, H.C. 234.

78. Robert Hutton, *Cable Slams Finance Industry, Pledges Takeover Probe*, BLOOMBERG BUSINESSWEEK (Sept. 22, 2010), http://www.globe-expert.eu/quixplorer/filestorage/Interfocus/3-Economie/31-Europe/31-SRCNL-BusinessWeek_com_--_Europe/201009/Cable_to_Continue_Finance_Attack_With_UK_Takeover_Pay_Probe.html (reporting that U.K. Business Secretary Vince Cable, a Liberal Democrat member of the governing coalition, announced an "inquiry into corporate-governance rules, with takeovers and pay both in the spotlight," and denied that his outspoken stance against the finance industry had created a rift with his Tory colleagues in the coalition government).

79. Roger Carr, the chairman of the Cadbury board of directors and one of the leading figures in the British corporate arena, made three key proposals in the wake of Kraft's acquisition of Cadbury, all of which were rejected by the U.K. Takeover Panel, whose Code Committee conducted a review of certain provisions of the Takeover Code in late 2010. First, Carr proposed that the

response to the Cadbury takeover actually seems likely to make it even more difficult for targets to resist a hostile bid.[80] The Cadbury takeover confirms how deeply rooted the power of the stockholder profit motive is in the for-profit corporation.

It is revealing to consider the aftermath of the Cadbury takeover. After the Code of the Takeover Panel rejected all three of Carr's proposals, it instead offered its own proposals as to how the Takeover Code might be amended to prevent future Cadbury-like hostile takeovers. I offer a couple of the most material proposals as examples. First, the Code Committee recommended that the formal offer period—the period in which an interested acquirer may make an offer or bid for the target—be shortened by requiring a potential offeror to make a bid within twenty-eight days of announcing its interest to make a bid.[81] Second, the Code Committee proposed a

threshold stock ownership that triggers a stockholder's disclosure obligation under Rule 8.3 of the Takeover Code be reduced from 1% to 0.5%. Carr Speech, *supra* note 62. Rule 8.3(a) currently requires a stockholder owning 1% of the target company's stock to publicly disclose such holdings following the commencement of the offer period (which begins after a "proposed or possible" offer is made by the hopeful acquirer). TAKEOVER CODE, *supra* note 69, at r. 8.3(a). Rule 8.3(b), in turn, requires a stockholder who owns, or comes to own during the offer period, 1% of the target company's stock to disclose the details of any transaction involving the target company's stock. *Id.* r. 8.3(b). Carr also proposed what even he called "a more radical move," which was to raise the acceptance threshold from 50.1%, as currently required under Rule 9.2 of the Code, to 60% of the target corporation's voting stock voting in favor of the proposed acquisition. Carr Speech, *supra* note 62. Finally, Carr suggested "an even more radical move": disenfranchising stockholders who acquire their shares during the formal offer period in order to, in Carr's words, "ensure short term money does not determine long term futures." *Id.*

80. After receiving an "unprecedented number of responses" to its Consultation Paper (an official public request for commentary on suggested proposals), on October 21, 2010, the U.K. Takeover Panel Code Committee published its statement of the proposed changes to the Takeover Code it recommended. CODE COMMITTEE, PANEL ON TAKEOVERS & MERGERS, REVIEW OF CERTAIN ASPECTS OF THE REGULATION OF TAKEOVER BIDS (Oct. 21, 2010) [hereinafter COMMITTEE REPORT], *available at* http://www.thetakeoverpanel.org.uk/wp-content/uploads/2009/12/2010-221.pdf.

81. Under the Takeover Code as it is now written, if a potential bidder announces an interest in making a bid to purchase the target company, but does not commit to doing so, the target company may go to the Takeover Panel and request that the Panel impose a deadline on the potential bidder, the so-called "put-up or shut-up" date. TAKEOVER CODE, *supra* note 69, at r. 2.4(b). When the "put-up or shut-up" deadline arrives, the potential bidder either has to "put-up" a bid or "shut-up" and is forbidden to make any further bid for the target for a period of six months as a sanction. *Id.* r. 2.8. The amount of time given to the potential acquirer varies case by case, but is typically six to eight weeks. COMMITTEE REPORT, *supra* note 80, at 4. Although the purpose of the put-up or shut-up mechanism was to protect the target from being under "protracted siege," in practice there were many instances where the target board would decline to ask the Panel to impose a put-up or shut-up deadline when approached by a potential acquirer because of pressure exerted by

prohibition of certain deal protection devices currently legal under the Code—very limited termination fees and matching rights.[82]

Upon a preliminary inspection of the Code Committee's proposals, however, it appears that were the Takeover Code modified as proposed, it might actually make hostile takeovers more, not less, likely, at least insofar as the proposed changes would make it more difficult for U.K. target companies to negotiate and secure a friendly acquisition over a hostile one. That is, for those in England who decried the result in the Cadbury/Kraft saga as the tragic end of British Dairy Milk at the sword of a cheesy American JELL-O-molded company, and who would presumably have been less outraged by an acquisition of Cadbury by British Hob Nobs,[83] the proposed changes to the Takeover Code seem likely to make it even easier for future hostile foreign takeovers of U.K. corporations.

For instance, take the proposal that would truncate the put-up or shut-up time period and require that target companies make public the identity of any potential offeror that has expressed an interest in making a bid. Although the purpose of this change is to dissuade the practice of making so-called "virtual bids"—ones where a would-be hostile acquirer announces that it is interested in making a bid well before that potential acquirer has any intention of doing so in order to: (i) alter the stockholder makeup of the target company by attracting hedge funds and other short-term investors (recall Carr's lament about the rapid influx of short-term stockholders in Cadbury after Kraft made its bid public); and (ii) put pressure on the target management—the Committee's proposal to make mandatory the reporting and public disclosure of the interested bidder's identity might have the unintended consequence of dissuading overtures from would-be friendly acquirers, particularly friendly strategic acquirers, who would rather remain anonymous and maintain the confidentiality of merger negotiations with the target until a binding contract is inked.[84]

stockholders eager to allow the potential acquirer to have all the time it desired to formulate an offer. *Id.* at 6–7. Thus, in practice, the put-up or shut-up deadline was much less potent than what was originally contemplated. *Id.* Under the Code Committee's proposal, however, it will no longer be up to the target company whether or not to approach the Panel and seek the initiation of the put-up or shut-up clock. Rather, under the Code Committee's proposal, as soon as the potential offeror is identified—and under the proposal the potential offeror *must* be made known, even if it wishes to remain anonymous in a friendly deal—the put-up or shut-up clock begins to tick and the potential offeror has 28 days to either make a bid, announce a firm intention to make a bid, or announce its intention not to make a bid and subject itself to the restrictions in Rule 2.8 of the Code. *Id.* at 11.

82. COMMITTEE REPORT, *supra* note 80, at 15.

83. Hob Nobs are a popular "biscuit" or cookie in England manufactured by the U.K. multinational, McVitie's.

84. *See In re* Dollar Thrifty S'holder Litig., 14 A.3d 573, 603–04 (Del. Ch. 2010) ("It is no small thing for a strategic acquirer to come public about its

The Code Committee's second material proposed modification, the prohibition of termination fees and matching rights, poses a similar deterrent to would-be friendly acquirers that would—if the proposal is adopted—be unable to secure any, even trivial, deal protections to offset the risks posed to a friendly bidder who has made its intentions public and therefore has put itself in a compromised position as to its employees, suppliers and creditors, and as to hungry competitors eager to make a hostile bid for the now weakened friendly bidder.[85] Viewed differently, a friendly bidder is less likely to negotiate an acquisition with a target if it is unable to secure assurances from the target that the target is serious about doing a deal, and more crucially to the friendly bidder, serious about doing the deal proposed by the friendly bidder. Without the availability of modest deal protection devices, friendly acquisition partners may be even more reluctant to emerge than now, where the current regime already leaves strategic partners and private equity funds with very little compensation if they get topped.[86]

For an American, the Cadbury situation is, as our philosopher Yogi Berra put it, like déjà vu all over again. For over thirty years in the United States, a variety of palliatives, such as state constituency statutes allowing boards to block bids harmful to other constituencies,[87] and the infamous poison pill, have done little but

desire to buy another industry player. Although management-side doctrinal junkies will cry that a board's interest in buying another industry competitor does not mean that the company would be well served by a similar transaction in which it is the seller—i.e., that the company is 'in play'—the reality is that the announcement of interest in a strategic transaction does signal that some other business strategy rather than the status quo would, in the board's judgment, be optimal.").

85. *See* NACCO Indus. v. Applica Inc., 997 A.2d 1, 19 (Del. Ch. 2009) ("Bidders in particular secure rights under acquisition agreements to protect themselves against being used as a stalking horse and as consideration for making target-specific investments of time and resources in particular acquisitions.").

86. Others in the United Kingdom agree that the proposed changes are unlikely to have a meaningful effect in changing how takeover bids turn out in the United Kingdom. *See* Richard Lambert, *Takeover Code Tweaks Won't Affect Corporate Behaviour*, THE GUARDIAN (July 28, 2010), http://www.guardian.co.uk/commentisfree/2010/jul/28/takeover-panel-corporate-behaviour (arguing that "in the end, tweaking the [T]akeover [C]ode will not make any substantial difference to corporate behaviour in the UK," and that instead, the United Kingdom should focus on regulatory and tax changes that would encourage and make more permanent long-term investments by holders such as pension funds).

87. A majority of American states, but not Delaware, have such statutes. *See* William J. Carney & George B. Shepherd, *The Mystery of Delaware Law's Continuing Success*, 2009 U. ILL. L. REV. 1, 35–36 (2009) (noting that thirty states in the United States have adopted "other constituency statutes" that "effectively give directors *carte blanche* discretion by allowing them to consider other constituencies, which effectively makes them unaccountable to shareholders").

give target boards some room to get a better deal from a so-called white knight if a hostile bid loomed.[88] The pressures boards faced from their stockholders to accept lucrative bids made resistance in most cases futile.[89] As a result, U.S. communities have seen icon after icon fall into foreign hands, and our own major stock exchange may soon be a subsidiary of a merger vehicle formed by the owners of the German Boerse.[90]

But in our case, the United States, for all its capitalist leanings, never embraced takeovers with anything but deep ambivalence. Our British friends across the pond all the while trumpeted these contrary, nakedly pro-takeover policies. The acquisition of the beloved maker of Dairy Milk has, however, revealed that underneath the cold, simplistic, and single-minded, short-term focus of stockholders on stock price may result in outcomes that, from a broader societal perspective, are deeply uncomfortable.

B. Candid Canada: The Refreshing Honesty of the Potash Decision

By comparison, I come now to the Canadian government's decision to block the $40 billion bid of an Australian corporation, BHP Billiton, Ltd. ("BHP"), to acquire the Potash Corporation of Saskatchewan. As I have learned, potash is not an illicit admixture to add to brownies, but a valuable crop nutrient and with a capital letter, for our purposes, a company. And Saskatchewan is the Saudi Arabia of potash with a little "p" and the current home of Potash with a capital "P."[91] As I have further learned, the province has an

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88. *See supra* note 53 and accompanying text; *see also* John C. Coates, IV, *Takeover Defenses in the Shadow of the Pill: A Critique of the Scientific Evidence*, 79 TEX. L. REV. 271, 312 (2000) (stating that the "principal finding" of an early study about the poison pill's effectiveness has held up over time: "firms that have adopted pills before a bid or other acquisition receive higher premiums than firms that have not" (citing GEORGESON & CO. INC., POISON PILL IMPACT STUDY (Mar. 31, 1988))); Martin Lipton, *Pills, Polls, and Professors Redux*, 69 U. CHI. L. REV. 1037, 1054 (2002) ("The pill and the proxy contest have proved to yield the perfect balance. . . . A board cannot say 'never,' but it can say 'no' in order to obtain the best deal for its shareholders.").

89. *See, e.g.*, Marcel Kahan & Edward B. Rock, *supra* note 53, at 897–98 (noting the high level of M&A activity despite the various protections, including poison pills, that corporate law affords target boards and arguing that shareholders will apply pressure to boards that do not effectively use takeover defenses to enhance shareholder value rather than entrench management); Coates, *supra* note 71 (showing, on the basis of empirical data from the years 1990–2008, that there is a higher incidence of bids for control of U.S. companies than there is for U.K. companies).

90. Ken Sweet, *NYSE, Deutsche Boerse Agree to Merge*, CNNMONEY (Feb. 15, 2011), http://money.cnn.com/2011/02/15/markets/NYSE_exchange_merger/index.htm.

91. The Canadian Press, *Potash Corp. Making Good on Pledge Made to Saskatchewan in Bitter Takeover Battle*, THERECORD.COM (Feb. 14, 2011), http://catch21.ca/Wire/News_Wire/Agriculture/article/853033 (noting that

economic strategy to leverage its advantage in potash (and the resulting stream of governmental royalties) into a better overall economic position. Potash Corporation was already managed from the United States and BHP made certain assurances that it would protect provincial interests. But the provincial government was dubious that under BHP's ownership, Potash would maintain its commitment to the province's version of OPEC, Canpotex. Canpotex is an industry-wide marketing initiative fostered by the province.[92] Rather, the provincial government concluded that BHP's commercial interests as a profit-maximizing firm might lead it to cut prices, reduce royalties to the province, and otherwise be less likely to generate royalties and jobs for the province than if Potash remained independent.[93]

The Investment Canada Act was the tool used by the province to get its way. Under that statute, the Canadian government can block any transaction above C$312 million if the transaction does not promise "net benefits" to Canada.[94] After extensive advocacy by the Provincial government, Canadian Industry Minister Tony Clement blocked BHP's bid, finding that it would not produce a net benefit for Canada.[95] That this action was taken by a conservative government that generally advocates for a more open form of capitalism had special resonance.[96]

Saskatchewan is the world's leading producer of potash and accounts for approximately 25–30% of world production).

92. *See Canpotex Company Profile*, CANPOTEX, http://canpqlx.sasktelwebhosting.com/company_profile.pdf (last visited Feb. 27, 2012) ("[Canpotex's] sole marketing focus is overseas, and [Canpotex's] main objectives are to maximize exports and efficiently serve [Canpotex's] customers to the benefit of [Canpotex's member producers] and the Province of Saskatchewan.").

93. *E.g.*, Rob Gillies, *Canada Wary of Potential Foreign Takeover of Potash*, LAW.COM (Sept. 21, 2010), http://www.law.com/jsp/law/international/LawArticleFriendlyIntl.jsp?id=1202472308213 (noting that the premier of Saskatchewan, Brad Wall, expressed doubt as to whether the Saskatchewan people would be better off after a BHP acquisition); James Wood, *Say No BHP Takeover of PotashCorp, Saskatchewan Legislature Urges Federal Government*, LEADER-POST (Oct. 29, 2010), http://www.leaderpost.com/news/takeover+PotashCorp+Saskatchewan+legislature+urges+federal+government/3742049/story.html (reporting that the Saskatchewan provincial legislature unanimously passed a resolution calling on Ottawa to not approve the BHP bid for Potash Corporation).

94. Investment Canada Act, R.S.C. 1985, c. 28 § 16; *Thresholds*, INDUSTRY CANADA, http://www.ic.gc.ca/eic/site/ica-lic.nsf/eng/h_lk00050.html (last modified Dec. 21, 2011).

95. Ian Austen, *Canada Blocks BHP's Purchase of Potash*, N.Y. TIMES, Nov. 4, 2010, at B14; Alexander Deslongchamps & Greg Quinn, *BHP May Fail to Save Potash Bid in Politicized Rebuff*, BLOOMBERG (Nov. 5, 2010), http://www.bloomberg.com/news/2010-11-05/bhp-may-fail-to-save-potash-bid-after-canada-s-highly-politicized-rebuff.html.

96. *See, e.g.*, *Founding Principles*, CONSERVATIVE PARTY OF CAN., http://www.conservative.ca/party/founding_principles/ (last visited Feb. 27,

For present purposes, however, I wish to focus only on one refreshing aspect of the application of the Investment Canada Act to the Potash situation, which is its total lack of pretense or sham. The statute is a naked grant of power to the national government to block a takeover when it believes Canada will be better off without it. Obviously, there are legitimate questions to be asked about the overall utility of such a statute and I do not intend to comment one way or the other on the wisdom of the decision to use the statute to block the BHP bid. But I do think that the statute's candor deserves applause because it forces Canadian society to ask genuine questions about what is in the public interest. In other analogous situations, governments have twisted their antitrust rules, come up with situation-specific corporate law rules, or taken a strained view of what was a national security (i.e., military-terrorist) threat in order to find a basis to block transactions that were, in reality, feared to be economically injurious to the target company's nation.[97]

Although Australians may have been chagrined by the Canadian government's blockage of BHP's bid, Aussies could not claim shock because their nation has a similar statute.[98] Moreover, the reality that another possible bidder for Potash was a Chinese-government-owned firm highlights the difficult reality of the so-called global market.[99] Canada faced a situation in which a corporation that controlled an important national resource could pass into the hands of owners who either (in the case of BHP) were

2012) ("The Conservative Party will be guided in its constitutional framework and its policy basis by the following principles: . . . A belief that the greatest potential for achieving social and economic objectives is under a global trading regime that is free and fair.").

97. *See, e.g.*, I. Serdar Dinc & Isil Erel, Economic Nationalism in Mergers & Acquisitions (June 28, 2010) (working paper), *available at* http://web.mit.edu/dinc/www/research/assets/Dinc%20and%20Erel%20--%20Nationalism%20in%20Corporate%20Mergers.pdf (observing that "[g]overnment interventions are very effective in preventing foreign bidders from completing the merger and in helping domestic bidders succeed"); *id.* at 12 (describing a situation that took place in 2006 in Spain in which the Spanish government, in response to a German hostile bid for a Spanish energy company, "laid down onerous requirements for the [German company's] bid through its influence over the supposedly-independent Spanish energy regulator"); *see also* Bernard S. Black, *The First International Merger Wave (and the Fifth and Last U.S. Wave)*, 54 U. MIAMI L. REV. 799, 808 (2000) (observing that although it is an "exception[] to a more liberal general rule," national governments still block mergers when doing so would "stop a major company from falling into foreign hands"); *Will Germany Control Europe's Power Switch?*, THETRUMPET (Mar. 1, 2006), http://www.thetrumpet.com/?q=2179.975.0.0 (reporting that the Spanish government denounced the German hostile takeover bid of the Spanish energy company Endesa as a "national security threat").

98. *Foreign Acquisitions and Takeovers Act 1975* (Cth) (Austl.), *available at* http://www.austlii.edu.au/au/legis/cth/consol_act/faata1975355/.

99. Dinny McMahon et al., *Chinese Investors Mull Bid for Potash*, WALL ST. J., Aug. 24, 2010, at B1.

deemed more likely to be driven by market forces to reduce the benefits to Saskatchewan of the company's operations or (in the case of a potential Chinese-government-owned bidder) would have been free to take actions not directed primarily at producing benefits for stockholders, but rather for advancing the self-interest of another nation.

C. Globalized Capital and Product Markets Make Regulation in the Public Interest More, Not Less, Vital

The candor of the Canadian government's Potash decision highlights the most critical issue before us. We have globalized capital markets. These capital markets put more intense pressure than ever on corporations to deliver short-term profits. In almost all the Organization for Economic Cooperation and Development ("OECD") nations,[100] only capital has a vote on who comprises the board of directors. With increasing institutional ownership and greatly decreased holding periods, corporate electorates are more demanding than ever and unlikely to give serious thought to the long-term, given that few stockholders hold their shares for longer than a year at a time.

Although we have globalized capital markets and have opened our product markets to exports, we have done little to effectively globalize the regulatory structures that ensure that for-profit corporations do not generate unacceptable levels of harm to others in their pursuit of profit.[101] Although the World Trade Organization does in fact at times act as an effective club in keeping nations from preventing exports from entering their markets,[102] no similarly

100. I use the OECD label as a rough proxy for the United States, Canada, the EU nations, Australia, New Zealand, Japan, and South Korea. The United States, Canada, Australia, New Zealand, Japan, and South Korea are all currently members of OECD as are twenty-one of the twenty-seven member states of the European Union (Bulgaria, Cyprus, Latvia, Lithuania, Malta, and Romania are members of the European Union but not OECD). *List of OECD Member Countries*, OECD, http://www.oecd.org/document/58/0,2340,en_2649_201185_1889402_1_1_1_1,00.html (last visited Feb. 27, 2012).

101. For a succinct and provocative discussion of the perils of globalizing markets without globalizing effective and just regulatory institutions, see Dani Rodrik, *Hooray for Nation States*, THE NEW REPUBLIC, Feb. 17, 2011, at 12, 13.

102. Donald McRae, *Measuring the Effectiveness of the WTO Dispute Settlement System*, (Working Paper, 2008), *available at* http://ssrn.com/abstract=1140452 (citing William J. Davey, *The WTO Dispute Settlement System: The First Ten Years*, 8 J. INT'L ECON. L. 17, 50 (2005)) (hailing the WTO's success in channeling disputes into its highly regarded dispute resolution mechanism and noting that WTO-authorized sanctions are not compensatory, but instead retaliatory measures that can incentivize countries to comply with WTO Dispute Settlement Body reports); *see, e.g.*, Press Release, European Commission, European Union Welcomes Suspensions of US Sanctions Following Resolution of WTO Banana Dispute (July 2, 2001) (IP/01/930) (announcing that in consideration for the European Union's agreement to

powerful international body ensures that all corporations participating in international commerce must meet minimally decent standards of labor treatment or environmental safety and respect.[103] Likewise, although financial institutions can and do take actions that affect the stability of all nations, their safety and soundness is remitted to a patchwork of national regulation.[104]

We have opened up global capital and product markets and forced our corporations to compete in such markets, without

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loosen import restrictions on bananas coming from the United States, the United States had agreed to suspend the increased duties it was assessing on certain EU exports that had been authorized by the WTO as a sanction against the EU).

103. Kenneth W. Abbott & Duncan Snidal, *Strengthening International Regulation Through Transnational New Governance: Overcoming the Orchestration Deficit*, 42 VAND. J. TRANSNAT'L L. 501, 501 (2009) (noting the failure of traditional international law mechanisms such as treaties and intergovernmental organizations to adequately regulate international business and observing that "[n]ongovernmental organizations, business firms, and other actors, singly and in novel combinations, are creating innovative institutions to apply transnational norms to business"); Patrick Macklem, *Labour Law Beyond Borders*, J. INT'L ECON. L. 605, 605 (2002) (noting that despite the fact that international organizations, such as the International Labour Organization, have articulated core principles which firms ought to comply with as a matter of public international law, "these developments [still] primarily relate to international efforts to hold states accountable to public international labour standards when devising domestic labour market policy" and further that privately adopted "[c]orporate codes of conduct potentially enable transnational implementation of international labour standards in ways that do not rely on traditional modes of international legal authority"); Chantal Thomas, *Should the World Trade Organization Incorporate Labor and Environmental Standards?*, 61 WASH. & LEE L. REV. 347, 350–57 (characterizing both international labor law and international environmental law as severely lacking in their enforcement capabilities); Charles Sabel et al., *Ratcheting Labor Standards: Regulation for Continuous Improvement in the Global Workplace* (John F. Kennedy Sch. of Gov't Harvard Univ., Faculty Res. Working Paper No. RWP00-010, 2000) (noting that in the absence of an international organization charged with monitoring working conditions many have proposed the creation of such international organization responsible for promulgating universal minimum working standards, but that "the machinery to compel global producers to adopt those standards does not exist and will be quite difficult to build").

104. *See* Carl Felsenfeld & Genci Bilali, *The Role of the Bank for International Settlements in Shaping the World Financial System*, 25 U. PA. J. INT'L ECON. L. 945, 1017 (2004) (observing that although all major banks engage in international, cross border activity, "each bank has a strong domestic orientation" and is subject to each country's domestic regulation, which "do not match each other"); R. Michael Gadbaw, *Systemic Regulation of Global Trade and Finance: A Tale of Two Systems*, 13 J. INT'L ECON. L. 551, 563 (2010) ("The international financial regulatory system became a fragmented, complex, multi-tiered, multi-dimensional, resource-oriented system that accommodates the different domains and regulatory prerogatives of financial officials, central bankers, and bank regulators as well as the private financial community by creating a variety of different organizations . . . .").

simultaneously extending the regulatory protections that enabled the West to implement an enlightened form of capitalism that helped defeat communism and fascism. As a result, strong pressure has been exerted to diminish national protections in these areas. Nations fear that if they require fair treatment of workers, protection of the environment, the payment of taxes to support the nation's needs, and sound capital requirements for financial institutions, corporate activity will flee to other nations where there is little or no regulation.[105]

The examples I have discussed above are not designed to convince you that any particular level of regulation is optimal. But they are designed to point out this reality: if, as I do, you believe that the temptations of profit can lead to corporate behavior that can harm society, you should be skeptical about claims that corporations are better-positioned to regulate themselves now than they used to be.

In many ways, the opposite is in fact true. Corporations increasingly have no genuine connection to any particular community or even nation. A huge disconnect has arisen between the wealth, lifestyle, daily experiences, and interests of the top corporate managers and that of most of the employees in the various nations in which their corporations have operations.[106] Corporate

105. *E.g.*, Alvin K. Klevorick, *Reflections on the Race to the Bottom*, *in* 1 FAIR TRADE AND HARMONIZATION 459, 459–60 (Jagdish N. Bhagwati & Robert E. Hudec eds., 1996) ("[G]overnments will choose policies—for example, environmental standards, occupational health and safety standards, competition policy—that entail suboptimal requirements, which afford their citizens too little protection—whether from environmental hazards, unsafe or unhealthy working conditions, or cartel behavior. The idea is that to make its country a hospitable location in which to do business, a government would establish lax standards to be imposed upon those it wishes to draw."); Chris Brummer, *Post-American Securities Regulation*, 98 CAL. L. REV. 327, 333 (2010) (observing that securities regulators and lawmakers compete globally by fashioning regulatory regimes to attract capital).

106. *E.g.*, Chrystia Freeland, *The Rise of the New Global Elite*, THE ATLANTIC, Jan.–Feb. 2011, at 44, 44 ("Our light-speed, globally connected economy has led to the rise of a new super-elite that consists, to a notable degree, of first- and second-generation wealth. Its members are hardworking, highly educated, jet-setting meritocrats who feel they are deserving winners of a tough, worldwide economic competition—and many of them, as a result, have an ambivalent attitude toward those of us who didn't succeed so spectacularly. *Perhaps most noteworthy, they are becoming a transglobal community of peers who have more in common with one another than with their countrymen back home. Whether they maintain primary residences in New York or Hong Kong, Moscow or Mumbai, today's super-rich are increasingly a nation unto themselves*." (emphasis added)); Randall S. Thomas & Harwell Wells, *Executive Compensation in the Courts: Board Capture, Optimal Contracting, and Officers' Fiduciary Duties*, 95 MINN. L. REV. 846, 862 (2011) (reporting that in 2007 the average U.S. CEO of a major company earned 275 times more than a typical worker (citing LAWRENCE MISHEL ET AL., THE STATE OF WORKING AMERICA 2008/2009, at 220 (2009))). Current CEO pay and the gap between that pay and

managers are increasingly subject to removal at the instance of highly aggressive institutional investors who do not hold shares or think long-term.[107] The actual long-term providers of capital are more and more divorced from the ownership of the shares of particular companies, and have largely yielded their votes to money managers compensated largely on short-term metrics. Providers of debt are also less well positioned to act as monitors, as corporate debt is syndicated and trades largely like equity capital, leading to far less stable lender-borrower relationships and less intensive, long-term monitoring of corporate risk-taking.[108]

To deliver profits, corporations must endure competition from competitors willing to locate jobs in nations without labor or environmental protection. That creates incentives to reduce wage rolls and pay, particularly in the European Union or in nations like Canada and the United States that have responsible regulatory standards, and to take fewer product safety and environmental precautions. When their competitors seem to be making large, short-term profits by suspect means that have substantial long-term risk—see the subprime debacle discussed above—corporate managers face strong pressure from the capital markets to get in the game, regardless of whether they personally believe the game to be just another form of gambling.

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the salary of ordinary workers is much larger today than it has been in the past. *See, e.g.*, Shanon Lynn, *CEO Salaries: What is the Average Salary of a CEO?*, PAYSCALE (July 31, 2008), http://blogs.payscale.com/content/2008/07/ceo-salaries—1.html (reporting that in 1970, the average CEO salary was around $700,000 and that that number represented a salary 25 times the salary of an average production worker).

107. Marcel Kahan & Edward Rock, *Embattled CEOs*, 88 TEX. L. REV. 987, 1007, 1031 (2010) (observing that the rise in institutional shareholder activism has led to decreased CEO power and a correspondent tendency, on the part of boards of directors, to be increasingly willing to remove CEOs even in mere anticipation of poor future performance); Murali Jagannathan & A.C. Pritchard, *Does Delaware Entrench Management?* 23 (Univ. of Mich. Law and Econ., Olin Working Paper No. 08-024, 2011), *available at* http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1313274 (arguing that Delaware CEOs experience greater turnover in part because large institutional investors exert pressure on board members to be active monitors of management performance).

108. *Cf.* Lawrence E. Mitchell, *Financialism: A Lecture Delivered at Creighton University School of Law*, 43 CREIGHTON L. REV. 323, 332 (2010) ("Traditional small lending institutions thus became further removed from their clients, and banks sought greater profits in the process of securitization, which brought higher profits than mere lending and allowed banks to evade capital restrictions. Securitization . . . [also] allowed loan officers to pay less attention to the safety of their loans, since they were promptly to be sold off and removed from banks' balance sheets (although not entirely from the risk assumed by the banks).").

CONCLUDING THOUGHTS: RULES FOR THE GLOBAL GAME

Milton Friedman is a person who has written a lot of things I don't necessarily agree with. But he wrote a famous article in which he said that "there is one and only one social responsibility of business—to use its resources and engage in activities designed to increase its profits so long as it stays within the rules of the game . . . ."[109] When the pressure to deliver profits becomes, as it has, more intense, the rules of the game become even more important. Human nature, the founders of my nation teach,[110] should be taken into account in designing those rules, and we should not assume that men and women of commerce are somehow better than average.

To ensure that for-profit corporations do not generate excessive externalities, strong boundaries remain critical. To address externality risk and fundamental concerns about appropriate protection of workers and the environment in globalized capital and product markets, the rules of the game must ultimately become global, too.[111] But in the meantime, enlightened societies must

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109. Milton Friedman, *The Social Responsibility of Business is to Increase its Profits*, N.Y. TIMES MAG., Sept. 13, 1970 (quoting MILTON FRIEDMAN, CAPITALISM AND FREEDOM 134 (University of Chicago Press 2002) (1962)). Others in the academy have harbored similar misgivings toward the notion that corporations, nonhumans, can have a "social responsibility." *See, e.g.*, Michael Jensen & William Meckling, *Theory of the Firm: Managerial Behavior, Agency Costs, and Ownership Structure*, *in* THE ECONOMIC NATURE OF THE FIRM 209, 215–16 (Louis Putterman ed., 1996) ("Viewing the firm as the nexus of a set of contracting relationships among individuals also serves to make it clear that the personalization of the firm implied by asking questions such as 'what should be the objective function of the firm', or 'does the firm have a social responsibility' is seriously misleading. *The firm is not an individual.* It is a legal fiction which serves as a focus for a complex process in which the conflicting objectives of individuals (some of whom may 'represent' other organizations) are brought into equilibrium within a framework of contractual relations. In this sense the 'behavior' of the firm is like the behavior of a market; i.e., the outcome of a complex equilibrium process. We seldom fall into the trap of characterizing the wheat or stock market as an individual, but we often make this error by thinking about organizations as if they were persons with motivations and intentions.").

110. *See* THE FEDERALIST NO. 51 (James Madison) ("If men were angels, no government would be necessary. If angels were to govern men, neither external nor internal controls on government would be necessary. In framing a government which is to be administered by men over men, the great difficulty lies in this: You must first enable the government to control the governed; and in the next place, oblige it to control itself. A dependence on the people is no doubt the primary control on the government; but experience has taught mankind the necessity of auxiliary precautions.").

111. Leo E. Strine, Jr., *Human Freedom and Two Friedmen: Musings on the Implications of Globalization for the Effective Regulation of Corporate Behaviour*, 58 U. TORONTO L.J. 241, 272–73 (2008) (arguing that the globalization of capital in recent decades counsels strongly in favor of

resist the temptation to roll back the societal protections that spread the blessings of capitalism more broadly, ended child labor, gave workers safe places to work, protected consumers from harmful products, provided decent wages and humane working hours, and ensured that the pursuit of profit would not pollute the world in which we live. After all, it was speedy national, not international, action that kept the financial crisis from being even worse.[112] We cannot dispense with the protections provided by the nation-state until we come up with an effective replacement.

The coalition- and consensus-building required to develop an effective global (or at the least, OECD-wide) scheme of externality regulation will require enormous leadership and dedication. But it cannot even begin if we delude ourselves into believing that corporations will effectively regulate themselves. That is not what they are built to do and enormous harm will result if we pretend otherwise. All you have to do is look at the unemployment rate or the Louisiana marshlands to know that that is true.

establishing a globalized regulatory system capable of monitoring responsible corporate behavior that "advances social welfare").

112. Dani Rodrik, *Hooray for Nation States*, THE NEW REPUBLIC, Feb. 17, 2011, at 12.