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Is There a Cure for Corporate "Psychopathy"?

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I. Introduction

Has corporate law created a monster? This article explores three recent indictments of corporate law that suggest that the constitutive law of corporations is responsible for a monstrous flaw in the institutional character of the Anglo-American public corporation—specifically, its exclusive focus on profits. Constitutional lawyer Joel Bakan has argued, in *The Corporation: The Pathological Pursuit of Profit and Power*,[1] that the law constitutes the corporation as a dangerous psychopath. Bakan follows in the footsteps of Lawrence Mitchell, a corporate law scholar, who a few years ago compared the corporation to "a golem that can never be called back" in *Corporate Irresponsibility: America's Newest Export*.[2] In a relatively unknown work, *Reinventing Aristocracy: The Constitutional Reformation of Corporate Governance*,[3] constitutional theorist Andrew Fraser characterized the corporation, less colorfully but no less disparagingly, as an uncivilized power.[4]

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[121]Sagusa, Inc. v. Magellan, Petroleum Corp., No. 12, 977, 1993 WL 512487 (Del. Ch. 1993) 19 Del. J. Corp. L. 1119, 1304 (1994).

[1]Joel Bakan, The Corporation: The Pathological Pursuit of Profit and Power (Simon & Schuster 2004).

[2]Lawrence E. Mitchell, Corporate Irresponsibility: America's Newest Export 47 (2001).

[3]Andrew W. Fraser, Reinventing Aristocracy: The Constitutional Reformation of Corporate Governance (1998).

[4]*See id.* at 2.

Arguments such as these, while far from new,[5] challenge the announcement of the "end of history for corporate law,"[6] the claimed consensus around the notion that the internal law of the corporation should require its management to be guided solely[7] by the aim of maximizing the stockholders' profits.[8] Indeed, if the success of the cinematic

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[5]They are, in particular, reminiscent of the positions defended by Maurice Wormser in his 1931 book, *Frankenstein, Incorporated*, and by Merrick Dodd in his 1932 debate with A. A. Berle in the pages of the Harvard Law Review. *See* ISAAC MAURICE WORMSER, FRANKENSTEIN, INCORPORATED (1931); E. Merrick Dodd Jr., *For Whom are Corporate Managers Trustees?*, 45 HARV. L. REV. 1145 (1932); A. A. Berle Jr., *For Whom Corporate Managers are Trustees: A Note*, 45 HARV. L. REV. 1365 (1932).

[6]Henry Hansmann & Reinier Kraakman, *The End of History for Corporate Law*, 89 GEO. L.J. 439 (2001). Even many critics of the underlying normative position acknowledge that there is a consensus around the position they oppose; *see, e.g.*, Paddy Ireland, *Shareholder Primacy and the Distribution of Wealth*, 68 MODERN L. REV. 49, 49 (2005) (acknowledging that there is a "growing consensus in favour of the shareholder-oriented corporation").

[7]Some use the word "primarily." Although this formulation might suggest a multiplicity of possible objectives ordered by weight and traded off against one another in a balancing exercise, the more usual understanding among defenders of corporate profit-maximization is that all nonprofit objectives are "secondary" in the sense that the corporation is to pursue them only to the extent consistent with the maximization of profits. *See, e.g.*, Stephen M. Bainbridge, *In Defense of the Shareholder Wealth Maximization Norm: A Reply to Professor Green*, 50 WASH. & LEE L. REV. 1423, 1435–37 (1993) (rejecting the view that, in the event of conflict, shareholders and nonshareholders' interests should be balanced against one another, and arguing that the shareholders' interests should be preferred).

[8]For a representative sample of the extensive literature on this issue, see William T. Allen, *Our Schizophrenic Conception of the Corporation*, 14 CARDOZO L. REV. 261 (1992) (describing the tension within corporate law between shareholder-centrism and a broader conception of corporate goals); Bainbridge, *supra* note 7 (defending stockholder wealth maximization); Margaret Blair & Lynn A. Stout, *A Team Production Theory of Corporate Law*, 85 VA. L. REV. 247 (1999) (taking issue with shareholder wealth maximization and arguing that the directors should instead be seen as "mediating hierarchs" responsible for allocating impartially the rents produced by the "team production" efforts of all participants in the venture); Douglas M. Branson, *Corporate Social Responsibility Redux*, 76 TUL. L. REV. 1207 (2002) (discussing the evolution, since the 1960s, of the movement for greater "corporate social responsibility"); Thomas Dunfee, *Corporate Governance in a Market with Morality*, 62 L. & CONTEMP. PROB. 129 (1999) (advocating an approach to corporate decision making that would permit departures from shareholder wealth maximization on certain types of moral grounds discussed by the author); 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 (1998) (discussing qualifications to the principle that corporate decisions should be guided by the maximization of "shareholder gain"); Ronald M. Green, *Shareholders as Stakeholders: Changing Metaphors of Corporate Governance*, 50 WASH. & LEE L. REV. 1409 (1993) (discussing the metaphor of stockholder "ownership" of the corporation and its relationship to the profit-maximization debate); Jonathon R.

version of *The Corporation* is any indication,[9] Bakan's misgivings about the legitimacy of the corporate constitution resonate with a segment of the lay public, even if the critical literature has had relatively little traction in the corporate law academy.

In Part II of this article, I analyze and evaluate the arguments advanced respectively by Bakan, Mitchell, and Fraser. There are difficulties with all three arguments. Bakan's conceptualization of the corporation in monstrous or pathological terms tends to mask a more insidious problem: the banality of evil.[10] Mitchell, while adopting a more sophisticated explanation of corporate irresponsibility, proposes a solution that demands a heroic assumption about the incorruptibility of corporate managers. Fraser's position is more complex and carefully argued, but, as Fraser himself recognizes, corporations are unlikely to implement his revolutionary proposal, which includes per-capita voting, anytime soon.

Nonetheless, as I argue in Part III, there is within the three authors' arguments a common challenge to the respective roles of markets and politics in social decision making; this challenge cannot so easily be dismissed. In particular, Mitchell's and Fraser's implicit argument that there should be a space for public-spirited deliberation within the corporation, although heretical to most corporate law academics, is not without merit. In Part IV, I conclude by suggesting that our corporate law already accommodates public-spirited deliberation within the corporation.

Macey & Geoffrey P. Miller, *Corporate Stakeholders: A Contractual Perspective*, 43 U. TORONTO L.J. 401 (1993) (arguing that corporations owe fiduciary duties exclusively to shareholders); Mark J. Roe, *The Shareholder Wealth Maximization Norm and Industrial Organization*, 149 U. PA. L. REV. 2063 (2001) (discussing the implications of competition in national product markets for the social desirability of the shareholder wealth-maximization norm); M. Friedman, *The Social Responsibility of Business Is to Increase Its Profits*, N.Y. TIMES MAGAZINE 6 (Sept. 13, 1970) (arguing that corporate managers wrong the shareholders if they sacrifice profits in the name of social responsibility).

[9]THE CORPORATION (Big Picture Media Corporation 2003). The film won audience awards at the Toronto, Vancouver, Philadelphia, Thessaloniki, Brasilian, and Sydney film festivals.

[10]The expression "banality of evil" is from HANNAH ARENDT, EICHMANN IN JERUSALEM: A REPORT ON THE BANALITY OF EVIL (1963). Arendt famously argued against the common assumption that only extraordinarily evil people, or "monsters," can commit monstrous crimes (such as during the Holocaust). This article argues, among other things, that Bakan's portrayal of the corporation as a monster obscures the role played by ordinary people, especially shareholders, in corporate irresponsibility.

II. Three Diagnoses; Three Prescriptions

A. Bakan's *The Corporation*

The thesis of *The Corporation* is that corporate law constitutes the public corporation as a psychopath.[11]According to Bakan, "[t]he corporation's legally defined mandate is to pursue, relentlessly and without exception, its own self-interest, regardless of the often harmful consequences it might cause to others."[12] As Bakan makes clear at various points in the book, not least in its secondary title, the corporation's "self-interest" is equated with its profitability,[13] and hence the stockholders' profits.

Bakan cites two cases in support of the proposition that, as a matter of corporate law, "corporations exist only to maximize returns to their shareholders."[14] The first case is the inevitable *Dodge v. Ford Motor Co.*,[15] in which Bakan says, "Henry Ford learned this legal lesson the hard way."[16] Mr. Ford had decided that the Ford Motor Company should drastically reduce its dividend payout to shareholders and instead invest in an expansion plan that would reduce car prices for consumers and create employment. As Bakan reminds us, the court criticized Ford "for forgetting that, 'a business corporation is organized and carried on primarily for the profit of the stockholders.'"[17] Bakan also refers to *Hutton v. West Cork Railway Co.*,[18] familiar to law students in many Commonwealth nations for Lord Bowen's statement that "the law does not say that there are to be no cakes and ale, but there are to be no cakes and ale except such as are required for the benefit of the company."[19]

These cases lead Bakan to conclude that corporate social responsibility is "illegal, at least when it is genuine" and not driven by the ulterior

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[11]*See* Bakan, *supra* note 1.

[12]*Id.* at 1–2.

[13]*See id.* at 45 (noting that the corporation must choose the course of action that is "most beneficial—i.e., profitable" for itself).

[14]*Id.* at 39 (quoting Marjorie Kelly).

[15]170 N.W. 668 (Mich. 1919), *discussed in* Bakan, *supra* note 1, at 36.

[16]Bakan, *supra* note 1, at 35.

[17]*Id.* at 36 (quoting from *Dodge*, 170 N.W. at 684).

[18]23 Ch. D. 654 (1883), *discussed in* Bakan, *supra* note 1, at 38.

[19]*Id.* at 673.

motive of generating profits,[20] and that corporate law obligates managers to pursue the stockholders' interests to the exclusion of all other considerations.[21] It is on this legal foundation that Bakan builds much of his analysis of corporate behavior.

For instance, Bakan argues that the legal mandate to maximize profits drives corporate managers to foist the costs of corporate activity on third parties, to externalize their costs.[22] Bakan provides several examples of "externalities," including two—the two to which he gives the most prominence—that are staples of the corporate social responsibility literature. The first of these is General Motors' decision in the early 1970s not to alter the design of its Chevrolet Malibu to reduce the risk that the fuel tank would explode in a collision, on the basis of an estimate that General Motors' legal liability from fatalities would represent an average of $2.40 per vehicle whereas eliminating the defect would cost $8.59 per vehicle.[23] Bakan's second example concerns the exploitation of manufacturing in the third world, specifically the plight of teenage girls employed under subcontracts from well-known clothing labels.[24] The young people Bakan describes are paid very low wages and work long hours under miserable conditions that include "humiliation and physical beatings" by company guards until companies fire them at the age of 25 "because they're used up."[25]

The profit-maximizing logic allegedly imposed on corporations by their constitutive law also drives them to disregard regulatory law unless compliance is cost-justified,[26] and to engage in political activity directed at the removal of regulatory obstacles to profit making[27] and the privatization

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[20]BAKAN, *supra* note 1, at 37.

[21]*Id.* at 35 (corporate law "compels executives to prioritize the interests of their companies and shareholders above all others").

[22]*Id.* ch. 3 (chapter entitled "The Externalizing Machine").

[23]*See id.* at 61–65.

[24]*See id.* at 65–70.

[25]*Id.* at 65–70.

[26]*Id.* at 80 ("[T]he corporation's mandate to pursue its own self-interest, itself a product of the law, actually propels corporations to break the law.").

[27]*See* BAKAN, *supra* note 3, ch. 4.

of a public sector which they regard as "a collection of unwarranted exclusions from vast profit-making opportunities."[28]

There is no easy remedy to the problem described in *The Corporation*. Bakan appears to wish for a wholesale reformation of economic relations in society,[29] but as a near-term proposition he does not suggest attempting to correct the corporation's flawed nature by reforming its constitutive law.[30] Rather, his strategy operates outside the domain of corporate law. Bakan notes that some commentators would rely on conscientious action on the part of stock market investors or consumers to pressure corporations to act responsibly,[31] but Bakan prefers to place his confidence in the democratic state.[32] His strategy is both defensive—protect the public sphere from being swallowed up by the corporate sector[33]—and offensive—toughen the system of external regulation of corporations.[34] Bakan's message is that of a monster movie: corporations are not redeemable, but, if we work together, perhaps they can be kept at bay.

One may be tempted to forgive the analytical shortcomings of *The Corporation* in light of its intended audience[35] and its cinematic alter ego. But one should resist this temptation. *The Corporation* is presented as the work of a legal scholar and it is intended as a serious contribution to the debate about corporate responsibility. As such, it is disappointing to find in the book that the risks faced by Malibu owners and the suffering of sweatshop laborers are presented as "externalities," when in fact neither is a

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[28]*Id.* at 113.

[29]*See id.* at 160–61 (describing his proposals as "what we can do tomorrow, next week and next year . . . even while we hope and strive in the longer term for a more fully human and democratic economic order").

[30]*See id.* at 159 ("tinkering with corporate governance is not enough"); *see also id.* at 161 ("realism dictates presuming that the corporation's constitution will remain much as it is: self-interested to the point of psychopathy").

[31]*See id.* at 144–45.

[32]*See* Bakan, *supra* note 3, at 151–52.

[33]*See id.* at 163 (advocating a "robust public sphere").

[34]*See id.* at 161–62 (recommending "improve[ment of] the regulatory system" by, among other things, increasing enforcement and enhancing penalties).

[35]*See id.* at 3 (describing his objective of making the book "accessible to the lay reader and the professional").

good example of an externality because both car buyers and sweatshop workers are in a contractual relationship with those responsible for putting them at risk.[36] Bakan's loose invocation of what he terms the "coolly technical jargon of economics"[37] obscures the more pertinent and complex issues raised by those cases, especially informational asymmetry, commodification, and distributive injustice.[38]

In addition, Bakan's recommendations are formulated in unspecific terms that belie their billing as a "realistic" program for "tomorrow, next week and next year."[39] For instance, Bakan recommends, without elaboration, that "the roles of trade unions and other workers' associations in monitoring and regulating the behavior of corporations be protected and enhanced,"[40] and that "nations should work together to shift the ideologies and practices of international institutions, such as the WTO, IMF and World Bank, away from market fundamentalism. . . ."[41] Worse still, Bakan does not offer any analysis of the impact of his proposals. A glaring example is Bakan's call for the robust enforcement of regulatory law against corporations, as part of which Bakan argues for the use of fines and charter

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[36]Externalities are costs imposed by an activity on strangers to the activity. By contrast, the costs imposed on contracting parties by the activity to which the contract relates are part of the bargain itself. In the conventional law-and-economics wisdom, the parties consent to these costs by virtue of their assent to the contract. *See* Richard A. Posner, *The Rights of Creditors of Affiliated Corporations*, 43 U. Chi. L. Rev. 499 (1976) (arguing that there is no externalization of risks onto "voluntary creditors," meaning persons in a contractual relationship with the corporation); Frank H. Easterbrook & Daniel R. Fischel, The Economic Structure of Corporate Law 50, 58 (1991) (same). The risks faced by nonowners of Malibus are a better example of an externality, but Bakan does not make this distinction.

[37]Bakan, *supra* note 1, at 60.

[38]For example, we might be concerned about the quality of the Malibu owners' consent to the risks of ownership if the sellers of Malibus withheld information about those risks (asymmetric information), about the devaluation of human dignity if sweatshop workers trade their physical integrity away in exchange for employment (commodification), or about the inequality of resources underlying the terms of trade between workers in developing countries and consumers in the developed world (distributive injustice). For a theoretical exploration, see Michael Trebilcock, The Limits of Freedom of Contract 23–57 (discussing commodification), 102–26 (discussing asymmetry of information), 20–21 and 252–53 (discussing distributive justice).

[39]*Id.* at 161.

[40]*Id.* at 162.

[41]*Id.* at 164.

suspension.[42] Bakan does not pause to acknowledge, let alone analyze the implications of, the negative consequences that those sanctions would have for the people behind the corporate veil, namely the corporation's shareholders and workers.[43]

But there is a more basic flaw in Bakan's argument. The legal foundation of Bakan's argument about corporate psychopathy is the proposition that corporate law obligates management to pursue corporate self-interest, conceived as the maximization of stockholder profits or of the stock price, to the exclusion of all other considerations.[44] It is a shaky foundation.

In fact, on this point, corporate law is persistently ambiguous. Two reasons well known to corporate lawyers explain this ambiguity. The first reason is that there is almost always a plausible profit-oriented rationalization for an act of corporate social responsibility. The second reason is that courts are loath to second-guess, in hindsight, management's business judgments.[45] Together these facts make it virtually impossible for a dissenting shareholder to challenge an act of corporate social responsibility in court. It is sometimes forgotten that in the *Dodge v. Ford Motor Co*. case itself, the court ultimately refused to interfere with management's plan to expand production and reduce prices because the judges were not certain that the plan would not ultimately result in greater profits.[46]

Moreover, courts almost always frame their opinions in terms that preserve the ambiguity of the legal standard. Take, for example, the well-known case of *Theodora Holding Corp. v. Henderson*,[47] in which the Delaware

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[42]*See id.* at 157–58, 161.

[43]*See* John C. Coffee Jr., *"No Soul to Damn: No Body to Kick": An Unscandalized Inquiry into the Problem of Corporate Punishment*, 79 MICH. L. REV. 386 (1981) (discussing these issues). That is not to say that there is no case to be made for corporate penalties, only that Bakan's proposal does not reveal any awareness of the social costs of imposing a large fine on a corporation or putting it out of business by revoking its charter.

[44]*See* text accompanying notes 14–21.

[45]*See, e.g.*, Aronson v. Lewis, 473 A.2d 805, 812 (Del. 1984) (describing the business judgment rule).

[46]170 N.W. 668, 684 (Mich. 1919) (The "judges are not business experts."). The court ordered the Ford Motor Company to pay a dividend to the extent that the company's cash resources exceeded what was necessary for the expansion plan, but it refused to interfere with the expansion plan itself. *See id.*

[47]257 A.2d 398 (Del. Ch. 1969).

Court of Chancery held that corporate management is allowed to make reasonable charitable donations.[48] The court's opinion states both that it is per se appropriate for corporations to make contributions to public causes[49] and that the shareholders benefited from the contributions in the long run.[50] One cannot tell from reading the opinion whether the benefit to the shareholders was a necessary condition of the donation's legality or whether it was merely interesting.

For decades, with every opportunity to resolve the ambiguity, the courts have instead chosen to preserve it.[51] As former Delaware Chancellor William Allen put it, the law is "schizophrenic."[52]

I want to make clear the significance of this legal ambiguity. My point is not that Bakan's interpretation is arguable, if uncompelling, as I might have said if Bakan were a litigator advocating the same interpretation on behalf of a stockholder client. Rather, the ambiguity of the legal standard is an enduring feature of corporate law, one that determines the conclusions Bakan can reasonably draw as an analyst about the impact of the law on behavior. The persistent ambiguity of corporate law means that one cannot say, if corporate executives pursue profits overzealously, that it is because the law instructs them to do so. The letter of the law does not give a clear instruction, and in practice the courts will rarely interfere. If corporations act irresponsibly, another culprit must be found.

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[48]*See id.*

[49]*See id.* at 404 ("The recognized obligation of corporations towards philanthropic, educational and artistic causes is reflected in the statutory law of all of the states, other than the states of Arizona and Idaho.").

[50]*See id.* at 405 ("[T]he relatively small loss of immediate income otherwise payable to [the shareholders because of the donation] is far out-weighed by the overall benefits flowing from [the donation, which in providing] justification for large private holdings, thereby [benefits the shareholders] in the long run.").

[51]The law clearly opts for the maximization of shareholder value only in circumstances where management has decided to "abandon its long-term strategy" or to pursue a sale of the business. *See* Paramount Comms. Inc. v. QVC Network, Inc., 637 A.2d 828 (Del. 1993).

[52]Allen, *supra* note 8, at 280 (describing the ambiguity in corporate law as to whether only the stockholders' interests must guide managers or whether they should also consider the general welfare).

B. Mitchell's *Corporate Irresponsibility*

The Corporation is, in many ways, reminiscent of Lawrence Mitchell's book, *Corporate Irresponsibility*. Both authors write in an accessible style, using anecdotes to illustrate their claim that corporations pursue stockholder profits regardless of the cost for others, and both of them ultimately blame corporate law for constituting the corporation as a pathological profit-maximizer.

That said, Mitchell's analysis of the relationship between corporate law and corporate irresponsibility is more sophisticated than Bakan's. The thesis of *Corporate Irresponsibility* is that corporate law creates a structural imperative of stock price maximization.[53] Mitchell does not argue, as Bakan does, that corporate law obligates management to maximize the stock price or the stockholders' profits. However, in Mitchell's view, three "structural traps"[54] within corporate law combine to achieve the same result: shareholders' exclusive right to elect or remove directors, their exclusive standing to initiate derivative litigation, and their ability to sell control of the corporation to the highest bidder.[55] These rights, unique privileges of stockholders as a matter of corporate law, give directors "every incentive for a focus on stockholder wealth and very little reason to care about anything else."[56]

Although Mitchell initially describes three structural traps, he undermines two of them, curiously, in a later chapter when he asserts that the procedural obstacles to derivative litigation are all but insurmountable[57] and that voting—aside from its role in transfers of control—is an ineffectual means for stockholders to advance their interests.[58] Of the three

[53] *See* MITCHELL, *supra* note 2, at 99 (arguing that the "legal structure and rules of corporate law" create an "imperative to maximize stockholder profit").

[54] *Id*. at 99.

[55] *See id*. at 99–108.

[56] *Id*. at 107 (referring to derivative litigation; parallel claims are also made in respect of stockholder voting and the transferability of control).

[57] *See id*. at 204 (describing the procedural obstacles to derivative litigation and concluding that it "doesn't happen a whole lot" that "a stockholder is going to have a chance even to bring a lawsuit to enforce the rather insipid fiduciary duties to which directors are subject" and that "[w]e might as well not have fiduciary duty at all").

[58] *Id*. at 125 (stating that "stockholder voting is not very effective").

structural traps that he initially describes, the only one left standing by the end of the book is the transferability of corporate control.

The market for corporate control is sufficient, however, to support Mitchell's overall point that management's fate is tied to the stockholders' pleasure. In fact, Mitchell's assessment of the significance of the market for corporate control would attract agreement even from his ideological adversaries.[59] The basic argument originates with Henry Manne, who is no friend of corporate social responsibility.[60] Manne introduced the notion that poor management—by which we were to understand the failure to realize as great a return as possible for the stockholders—would result in a decline in the stock price and create the possibility for a third party to profit from a transaction in which he or she would acquire control from the existing shareholders and replace the incumbent management.[61] Writing four decades before Mitchell, Manne argued that this mechanism "affords strong protection to the interests of vast numbers of small, non-controlling shareholders. Compared to this mechanism, the efforts of the SEC and the courts to protect shareholders through the development of a fiduciary duty concept and the shareholder's derivative suit seem small indeed."[62]

The difference between Bakan's and Mitchell's accounts may appear to be one of nuance, but in fact it has great significance. In Bakan's account, the law is a convenient external scapegoat: the rapacious corporate sector is the product of corporate law.[63] The truth is more complicated, and in some ways, more awkward. The duties imposed on managers

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[59]*See* Frank H. Easterbrook & Daniel R. Fischel, *The Proper Role of a Target's Management in Responding to a Tender Offer*, 94 HARV. L. REV. 1161, 1169 (1981) (noting the role played by hostile takeover in "monitoring the performance of corporate managers"); Henry G. Manne, *Mergers and the Market for Corporate Control*, 73 J. POL. ECON. 110 (1965); Roberta Romano, *Public Pension Fund Activism in Corporate Governance Reconsidered*, 93 COLUM. L. REV. 795, 852 (1993) (arguing that pension fund activism is a poor substitute for an "active market in corporate control" and describing the latter as the most potent disciplining force for aligning managers' incentives with shareholders' interests).

[60]For an example of Manne's disparagement of corporate social responsibility, see Henry G. Manne, *Shareholder Social Proposals Viewed by an Opponent*, 24 STAN. L. REV. 481 (1971) (criticizing shareholder proposals on social responsibility issues).

[61]*See* Manne, *supra* note 59.

[62]*Id.* at 113.

[63] *See supra* note 12.

by corporate law do not, in practice, prevent them from acting responsibly. As Mitchell observes, corporate law does, indirectly, ensure that management is responsive to the desires of stockholders, to the extent that shares are marketable and that a majority of the shares confers the right to replace the directors. But what this means is that if the critics are right that management pursues stockholder profits to the exclusion of all considerations of ethics, decency, and social responsibility, it is not so much because corporate law requires it as because it suits the stockholders.

This conclusion is awkward because it deprives us of the easy answer —the problem is with the law—and forces us to confront the fact that if there is a problem of corporate irresponsibility, we, in our capacity as shareholders, are part of it. I say "we," of course, because the paradigmatic stockholder is not a super-rich individual, but a working person saving for his or her retirement or a retired person receiving pension benefits.[64] In the real world, ordinary people are not the uncomplicated action-movie heroes Bakan makes us out to be, but the more flawed protagonists of a darker narrative.

What I have said so far may give the impression that Mitchell is more of a realist about human nature than Bakan is, but that is not so. Mitchell's principal proposed solution to the problem of corporate irresponsibility is to liberate management from the market for corporate control by abolishing stockholder voting for the board of directors, and making the board self-perpetuating.[65] This solution rests on an assumption about human nature which is, to state the obvious, optimistic: Mitchell believes that managers are, at heart, "decent people;"[66] if left alone, they will use their powers responsibly.

One would like to believe, as Mitchell does, that managers are fundamentally decent, but what reassurance can Mitchell provide to those of us who do not share his confidence in their incorruptibility? Mitchell essentially responds in two ways. First, he argues that trust is inevitable. In an

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[64]In 2002, 49.5% of all U.S. households owned stock directly or indirectly. Ireland, *supra* note 6, at 55; *see* MITCHELL, *supra* note 2, at 147. For a reminder that there remains considerable inequality of stock ownership, just as there are significant disparities of wealth, see Ireland, *supra* note 6.

[65]As a second-best alternative, Mitchell would lengthen directors' terms to five years while extending voting rights to workers and creditors. MITCHELL, *supra* note 2, at 129–31.

[66]*Id*. at 13.

interesting twist on contractarian logic,[67] he argues that if investors buy shares despite the largely ineffectual legal duties owed by managers, it must be because they also assume that "most people, most of the time, act in good faith."[68] The laxity of the rules also suggests that "we don't really care that much about self-dealing. We permit it, and we set up rules to show managers how to do it. Once we've gone this far, to say that boards need to be elected by stockholders in order to ensure they're monitored and controlled is silly."[69] I, for one, am not persuaded that the laxity of management's legal duties is a good reason to assume that shareholders do not require the protection of the market for corporate control.[70] It is as if an engineer coming across a house erected on two pillars, upon discovering one of them to be hollow and not bearing any weight, ordered the other pillar demolished on the grounds that it, too, must be superfluous.

Mitchell's second line of defense is that, despite the abolition of stockholder voting, some constraints would remain: "[T]he corporation would have to be profitable to survive . . . [and] would also have to do well enough to attract investors."[71] This is another twist on familiar contractarian arguments, but contractarians normally use their version of these arguments to justify an unregulated status quo (e.g., "if it were bad for investors, why do so many of them invest?") rather than as a safety valve for a proposed new regulation. As Mitchell uses them, the arguments do not work. "Survival" does not guarantee any return for the stockholders; it just means that the corporation remains solvent. Moreover, "attracting investors" is about making commitments on which potential capital-providers can base a decision whether and at what price to invest. It is far from

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[67]For the best-known exposition of the contractarian approach to corporate law, see EASTERBROOK & FISCHEL, *supra* note 36. The "nexus of contracts" conception of the corporation, which underlies the contractarian approach to corporate law, characterizes the relationship among participants in the corporation as a set of voluntary quid pro quo arrangements, or "contracts." *See id.*

[68]*Id.* at 125.

[69]*Id.* at 128.

[70]In fairness, I should note that Mitchell may believe that hostile takeovers could still occur. In a cryptic passage, he writes that "takeover law . . . does not create a serious impediment to the kind of board independence I am advocating." *Id.* at 207. However, Mitchell does not provide further elaboration on the grounds that "the technicalities and details of takeover law could fill an entire book." *Id.*

[71]*Id.* at 129.

apparent how the kind of firm that Mitchell envisages—one that can neither make a strong contractual commitment to maximize the stockholders' profits nor empower the latter to replace the managers if profits are unsatisfactory—could make any commitment capable of attracting capital, other than the promise of a fixed return akin to that made to creditors.[72]

C. Fraser's *Reinventing Aristocracy*

Like Mitchell, Fraser seeks to reform corporate law rather than work around it. However, unlike Mitchell's account of what is wrong with the corporation, Fraser's argument sounds in political theory. His conceptual vocabulary is that of Hannah Arendt,[73] not Henry Manne. The argument is framed in terms of power. Fraser argues that corporations exercise power indistinguishable in its impact from the power of the state.[74] This power, no less than that of the state, must be "constitutionalised,"[75] thereby making the relevance of corporate governance to political theory and not to economic analysis alone. A self-described civic republican, Fraser imagines a future in which shareholders who act not as "bourgeois" economic automatons, but as public-spirited "citizens"[76] oversee corporations.

For Fraser, a crucial obstacle to this future is the rule of one share, one vote, which he denounces as plutocratic and inconsistent with political equality.[77] In a system where "only money talks . . . the sheer dumb weight of proprietary interest" rather than "reasoned speech" determines important corporate decisions, shareholders understandably do not conduct themselves as citizens.[78] By way of a remedy, Fraser proposes requiring the

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[72]One possible structure would involve the managers' committing to maintain a sizeable investment of their own resources in the corporation's equity. This arrangement would provide some assurance to outside equity investors that management's interests will remain aligned with those of the outside stockholders. If Mitchell has this kind of structure in mind—a reunification of ownership and control—he does not say so.

[73]The book draws in particular on Arendt's conceptual opposition of the public-spirited, politically active "citizen" and the self-interested, politically passive "bourgeois." *See* H. ARENDT, THE HUMAN CONDITION (1958).

[74]*See* FRASER, *supra* note 3, at 20.

[75]*Id.*

[76]*Id.* at 21–22.

[77]*See id.* at 15.

[78]*Id.* at 17.

use of dual-class common stock.[79] Corporations would reserve voting stock for natural persons with a significant economic stake in the corporation and voting would be on a per-capita rather than a per-share basis.[80] Corporations would limit other shareholders to nonvoting common stock.[81]

Fraser's proposal, like Mitchell's, would make hostile takeovers virtually impossible.[82] An acquirer could not hope to wind up with more than a single vote, no matter how many shares it purchased, short of all of them. Unlike Mitchell, however, Fraser does not ask us simply to trust managers. He argues that the monitoring activities of a small group of committed voting stockholders would be an adequate substitute for the market for corporate control.[83] Reviewers of *Reinventing Aristocracy* have not been convinced by this argument: blind faith in voting stockholders seems no better than blind faith in managers.[84]

Fraser's argument is not quite as vulnerable as his critics suggest. The existence of dual-class structures in the real world indicates that there is a market for equity having inferior voting rights but otherwise equal to the class of stock held by a small group of committed investors.[85] It is critical to the viability of the dual-class structure that the holders of superior stock have a substantial economic investment—the larger, the better. The small number of superior stockholders and their substantial economic stake are

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[79]*See id.* at 44–46.

[80]*See id.* at 47. As a second-best alternative, "in particular circumstances," Fraser suggests a cap on voting entitlements. *Id.* A version of this alternative proposal exists in some jurisdictions. In France, for example, the charters of some public corporations impose a cap on voting rights, but it is typical to find that the cap ceases to operate once a stockholder acquires an overwhelming (e.g., 2/3) economic interest.

[81]*See id.*

[82]Fraser appears to see this as an advantage. *See id.* at 48 (referring to the "deleterious consequences" of hostile takeovers).

[83]*See id.* at 48.

[84]*See* Stephen Bottomley, Book Review, (reviewing ANDREW FRASER, REINVENTING ARISTOCRACY: THE CONSTITUTIONAL REFORMATION OF CORPORATE GOVERNANCE (1998)) 11 AUST. J. CORP. L. 1, 7 (1999) ("[W]hat will prevent the [cadre of voting stockholders] from pursuing its own interests rather than those of the corporation?"); Joellen Riley, Book Review, (reviewing ANDREW FRASER, REINVENTING ARISTOCRACY: THE CONSTITUTIONAL REFORMATION OF CORPORATE GOVERNANCE (1998)) 21 SYDNEY L. REV. 328, 331 (1999) (expressing "skepticism" at Fraser's "faith in the selflessness of a noble elite").

[85]Well-known examples include Google, Inc.; Berkshire Hathaway Inc.; Steinway Musical Instruments, Inc.; and The New York Times Company.

the inferior stockholders' assurance that active monitoring will occur, while the fact that the superior stock ranks no higher than the inferior stock in terms of access to cash flow (dividends and liquidation proceeds) protects the inferior stockholders against a divergence in interests between the two classes. The alignment of interests is not, of course, perfect.[86] In particular, there is the potential for self-dealing on the part of the superior stockholders. But because the market for corporate control is also imperfect, we should not be surprised that under some circumstances passive investors are willing to give up the protection of the market for corporate control in order to ride on the coattails of a group of committed, active shareholders.[87]

Although dual-class capitalization is far from radical, two aspects of Fraser's proposal make it revolutionary. The first is that dual-class capitalization would be mandatory. Fraser would stage the implementation of mandatory dual-class capitalization, beginning "on an experimental basis" with corporations in the media and communications sectors, in light of what he says is an important public interest aspect of their business.[88] However, in the chosen industry sectors, it would not be left to shareholders and managers to decide whether to implement a dual-class structure, because what is at stake is not solely those parties' economic interest, but the constitutionalization of corporate power.

Because investments in nonvoting shares would be made only if long-term investors with a commitment to at least active supervision held the voting stock in large quantities, a mandatory dual-class structure would, in effect, eliminate as a possible form of private economic organization the

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[86]Agency costs are positive as long as the controlling stockholders are entitled to less than 100% of the cash flow from the venture. For an analysis of the problem of agency costs in closely held corporations, see Frank H. Easterbrook & Daniel R. Fischel, *Close Corporations and Agency Costs*, 38 STAN. L. REV. 271 (1986).

[87]In many cases, the identity of the active shareholder group will be important to passive investors, for example, where the active shareholders have a reputation for effective monitoring (or management) and for not engaging in self-dealing. If this is the case, one might expect to find provisions to protect the nonvoting stockholders from a sale of the superior voting stock to investors less willing or able to monitor the corporation. For example, the dual-class arrangement may provide that the superior voting stock loses its voting proponderance in the event that it is transferred outside the existing group. This is the case with Steinway Musical Instruments, Inc.

[88]Interestingly, several media corporations are among those that already have dual-class structures. Examples in addition to The New York Times Company include The Washington Post Company and Dow Jones & Company, Inc. (publishers of the Wall Street Journal).

corporation under dispersed ownership. Critics of the status quo might well view this as a positive development. The public corporation and its characteristic separation of risk bearing and management (or active supervision) may foster corporate irresponsibility by impairing the ability of the people for whose benefit corporate acts are undertaken to evaluate their consequences and, if warranted, influence them. However, the reform would come at an enormous cost. The separation of ownership and control facilitates economic growth by dramatically widening the group of potential suppliers of capital to include individuals who have money but no managerial skills as well as "small investors," individuals whose ability to supply capital is insignificant taken individually but significant in combination with many others similarly situated.

The second revolutionary aspect of Fraser's proposal concerns his argument that, for the sake of "political equality," voting within the clique of significant stockholders must be on a per-capita rather than a per-share basis. Among the many practical implications of such a change is the fact that it would entail limiting the franchise to natural persons, which would have two obvious and direct implications. First, it would essentially eliminate intercorporate equity investments, returning us to the prehistory of corporate law.[89] Second, it would consign some of today's largest investors, such as pension funds, to passive status. Again, Fraser may view these as positive developments, but they, too, would come at a substantial cost in terms of macroeconomic performance, which in concrete terms translates into employment and standard of living.

In short, one could perhaps remedy the problem of corporate irresponsibility by reverting to a more concentrated capitalism. However, one should not be under any illusion that the reform would be without sacrifice, for we would be eliminating a device described by some as "the greatest single discovery of modern times"[90] because of its contribution to our economic development.

More fundamentally, I have reservations about Fraser's argument that eliminating the one-share, one-vote rule is the key to constitutionalizing the

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[89]Early general incorporation laws prohibited corporations from owning shares in other corporations. In response to lobbying on behalf of industry, New Jersey abolished these restrictions in the late nineteenth century. Other states soon followed suit. *See* Morton J. Horwitz, *Santa Clara Revisited: The Development of Corporate Theory*, 88 W. VA. L. REV. 173, 182 (1985).

[90]NICHOLAS BUTLER, WHY SHOULD WE CHANGE OUR FORM OF GOVERNMENT? 82 (1912). Columbia University President Nicholas Butler was referring to the "limited liability corporation," which made possible the aggregation of the capital of innumerable passive investors. *Id.*

corporate body politic. I wonder, on the one hand, whether per-capita voting would be sufficient to transform shareholders into citizens. Perhaps the dumb weight of proprietary interest would simply be replaced by the dumb weight of numbers. On the other hand, I question whether a decision-making body governed by "reasoned speech" would necessarily be characterized by per-capita voting as Fraser claims. It seems to me that the role of reason in collective decision making depends ultimately on whether speakers invoke it and listeners heed it, and on the absence of practical obstacles to communication.[91] I am not persuaded that the decision rule, whether numerical majoritarianism, economic majoritarianism, or some other way of counting and weighting votes, is determinative.

III. Markets versus Politics

A. Corporate Law and the Hegemony of Markets

There are significant differences among Bakan's, Mitchell's, and Fraser's approaches to remedying or combating corporate irresponsibility. Bakan, a social democrat, reminds us that corporations are creatures of the state and exhorts us to be less timid in using the power of the state—regulation, punishment, and public management—to keep corporations in check. Mitchell appears to be a classic managerialist. Despite being a "left-of-center sort of guy,"[92] he does not endorse extensive regulation,[93] believing it to be unnecessary once managers have been liberated from the market and are free to follow their own best judgment. Fraser, as I have mentioned, describes his approach as civic republican; he focuses on the corporation's "citizens," its stockholders, as the locus of potentially legitimate authority within the corporation.[94]

I argue in this section that, these obvious differences aside, what the three projects have in common is a challenge to the hegemony of markets

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[91]Before recent reforms, the Securities and Exchange Commission's proxy solicitation rules applied to most communications among shareholders and would have been a serious obstacle to deliberative shareholder democracy quite apart from the rule of per-share voting. *See infra* note 118.

[92]Mitchell, *supra* note 2, at 112.

[93]*See, e.g., id.* at 278 (describing his proposal as a more attractive alternative to the "extensive regulation of business by government").

[94]*See* Fraser, *supra* note 3, at 77.

underwritten by corporate law at the expense of politics.[95] This theme is explicit in Fraser's argument that the citizen shareholder must replace the bourgeois. In Bakan's and Mitchell's arguments, it is implicit. Bakan, for example, never acknowledges the role of markets in creating the problems he describes, but in discussing the possible constraints on corporate psychopathic behavior, he indicates a clear preference for politics over markets.[96] He cites markets' inconsistency with the democratic principle of one person, one vote; consumers' and investors' practical reluctance to make marketplace decisions on the basis of social considerations; and the lack of adequate information in the hands of consumers and investors.[97] One of Bakan's proposals is to "strengthen political democracy," in particular by reducing the influence of corporations.[98] The same theme is present in Mitchell's argument. Even though Mitchell does not advocate greater external regulation, he describes the critical challenge as one of "curb[ing] the power of the market."[99] Mitchell's solution is no less political than Bakan's; the board of directors would join government as a deliberative arena.

There is more than a grain of truth to the description of corporate law as expanding the use of the market mechanism, instead of political deliberation, in social decision making. Laws often serve to delimit the boundary between markets and politics. For instance, when a regulatory law specifies employment standards, the idea is to remove matters such as termination notice and paid holidays from determination by the labor market and to substitute determinations arrived at through the political process.[100] Corporate law serves a similar boundary-setting function in relation to the governance of corporations. As things stand, corporate law

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[95] I hope that readers will recognize that when I refer to "markets," I mean a mechanism by which social decisions are made indirectly (as if guided by an invisible hand) through the aggregation of voluntary transactions among individuals, whereas "politics" refers to a collective deliberative process. For other discussions of the choice between markets and politics, see ALBERT O. HIRSCHMAN, EXIT, VOICE, AND LOYALTY: RESPONSES TO DECLINE IN FIRMS, ORGANIZATIONS, AND STATES (1970), and, in the context of environmental protection, DANIEL A. FARBER, ECO-PRAGMATISM: MAKING SENSIBLE ENVIRONMENTAL DECISIONS IN AN UNCERTAIN WORLD (1999).

[96] BAKAN, *supra* note 1, at 145–47.

[97] *See id*.

[98] *Id.* at 162.

[99] MITCHELL, *supra* note 2, at 277–78.

[100] Against the background of legislated terms, the market still operates. In particular, market conditions determine the overall balance of advantage in a contractual relationship, such as

leaves the determination of most significant matters of corporate governance to the participants in the corporation themselves,[101] rather than imposing terms arrived at through a legislative or bureaucratic process external to the corporation. In particular, corporate law does not obligate management to pursue stockholders' profits to the exclusion of all other considerations. As I have argued, market forces, more than obligations specified legislatively or bureaucratically, constrain management's freedom of action in this regard.

Beyond the absence of imposed *external* terms, the market mechanism equally dominates the *internal* life of corporations, at least in the dominant academic conceptualization of the corporation. In the "nexus of contracts" corporation,[102] the participants are modeled as interest-seeking participants in the market[103] rather than as citizens. The assumed method for the assertion of the participants' interests is the offering or withholding of their consent to transact, exit rather than voice. Academic corporate lawyers' frequent response to those features of corporate law that are suggestive of an internal political space—such as shareholder proposals and voting—is either to dismiss them as anachronistic[104] or to demote them conceptually to a role in support of a market mechanism.[105]

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employment, so that regulatory specification of individual terms is likely to result in compensating adjustments to other terms, such as wages.

[101]*See* EASTERBROOK & FISCHEL, *supra* note 36, at 2 (describing corporations statutes as "enabling," meaning that it permits "managers and investors . . . to establish systems of governance without substantive scrutiny from a regulator").

[102]*See* William T. Allen, *Contracts and Communities in Corporation Law*, 50 WASH. & LEE L. REV. 1395, 1400 (describing the "nexus of contracts" as the "dominant legal academic view").

[103]*See* Ian B. Lee, *Corporate Law, Profit Maximization and the 'Responsible' Shareholder,* 10 STAN. J. L. BUS. & FIN. 31 (2005) (discussing the assumption that investors are ruthlessly self-interested).

[104]Stephen Bainbridge, for example, describes as a "historical anachronism" the shareholders' right to initiate bylaw amendments by way of shareholder proposal. *See* Stephen Bainbridge, *Can Shareholders Use the Bylaws to Limit Director Compensation?*, ProfessorBainbridge, *at* http://www.professorbainbridge.com/2004/05/can_shareholder.html (May 13, 2004).

[105]Thus, for example, such lawyers conceptualize shareholder voting not as an opportunity for shareholders to participate in deliberative governance, but as an element of the "market for corporate control." *See* John C. Coates IV, *Measuring the Domain of Mediating Hierarchy: How Contestable Are U.S. Public Corporations?*, 24 J. CORP. L. 837, 850–51 (1999) (arguing that although stockholder voice is "radically limited," voting is nonetheless important because of its role in the market for corporate control); *see also* Stephen M. Bainbridge, *Director Primacy:*

B. Should There Be a Greater Role for Political Deliberation?

I take it that a view fairly attributable to all three authors is that social choices must not be made solely through the market mechanism. Bakan and Fraser, in particular, make explicit their concern that we rely on markets, rather than politics, for too many of our social choices. While it is not my intention to make a call on what the right ratio of markets to politics is, I have little difficulty agreeing that we would not want to rely exclusively on the market mechanism.

One of the most appealing characteristics of the market mechanism is the Pareto-improving character of the decisions it produces.[106] Because all moves are universally consensual, the market outcome leaves everyone better off, in his or her own eyes, after the transaction compared to before —at least if there are no externalities.[107] Moreover, as a means of reconciling competing individual preferences in the face of scarcity, the market mechanism might achieve better results than a political decision. Through the market mechanism, the priorities revealed by individuals in voluntary transactions are aggregated into social trade-offs that more faithfully reflect individuals' priorities than if one relied on a bureaucrat to judge the value of the interests at stake from a perspective external to that of the affected individuals. Few critics of the market (Bakan, Mitchell, and Fraser are no exceptions) acknowledge explicitly the market's virtues.[108]

The Means and Ends of Corporate Governance, 97 NW. U. L. REV. 547, 568–70 (2003) (arguing that stockholder voting rights do not provide stockholders with any decision-making power within the corporation or control over the board of directors; they support the takeover market, a mechanism of "market-based accountability"); Lee, *supra* note 103 (discussing academic disparagement of the shareholder proposal mechanism).

[106]*See* MILTON FRIEDMAN, CAPITALISM AND FREEDOM 13 (1962) (noting that "both parties to an economic transaction benefit from it, provided the transaction is voluntary and informed"); TREBILCOCK, *supra* note 38, at 7 (describing the Pareto-improving quality of voluntary transactions in the market).

[107]Preference shifts (regret) may also qualify the proposition that both parties are necessarily better off following a voluntary transaction. *See* Daniel A. Farber, *Economic Efficiency and the Ex Ante Perspective*, *in* THE JURISPRUDENTIAL FOUNDATIONS OF CORPORATE AND COMMERCIAL LAW 54, 71 (Jody S. Kraus & Steven D. Walt eds., 2000); Guido Calabresi, *The Pointlessness of Pareto: Carrying Coase Further*, 100 YALE L.J. 1211, 1226 (1991) (noting that the problem of regret "casts doubt on the desirability of those changes upon which people truly agree unanimously and that occur without the need for compulsion or complex analysis").

[108]Bakan, for example, does not pause to consider the question arising from his third-world sweatshop narrative as to whether the garment workers of the third world are better off than

However, it is not always the case that the resulting allocation will be the best achievable allocation, on a plausible understanding of "best." This is particularly clear when initial endowments are very unequal. As a clearinghouse for the interests of different individuals, the market measures any given interest of an individual in terms of what the individual is willing and able to give up in order to protect or advance it. This characteristic of the market mechanism results in the weighting of the interests of different individuals according to their respective economic resources. So it is, for instance, that greater resources are allocated to the development of medicines that fight baldness than to drugs against tuberculosis.[109]

More generally, markets lack the argumentative element that is a characteristic of politics. The social function of the market mechanism is to reconcile interests, taken as a given, in the face of scarce resources, not to structure public-spirited or ethical deliberation.

One must be careful, of course, not to idealize politics. Regrettably, Bakan, Mitchell, and Fraser do not pay much attention to politics' shortcomings.[110] Political outcomes may be determined not only by the merits of the arguments but also by the relative power of the arguments' proponents. The arguments themselves, while likely formulated in terms of the public-spirited concerns of citizens, may in fact mask the bourgeois vested interest of their proponents. Indeed, economic analysts of politics remind us that, if one understands political actors as pursuing their self-interest, then the political mechanism is a forum in which small homogeneous groups will be able to obtain the satisfaction of their own preferences at the expense of larger groups, with no necessary benefit in terms of social welfare.[111] Far better, the argument continues to rely on the market

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they would be if the clothes were instead manufactured in North America or Europe. *See* Peter Shawn Taylor, *Whose Rules?*, NAT'L POST BUS., Aug. 2004, at 24 (describing Placer Dome Inc.'s investment in a gold mining project in Papua New Guinea and implying that the local people consider that the project improves their situation despite outsiders' criticism of the project for not meeting certain environmental standards).

[109]BAKAN, *supra* note 1, at 49.

[110]Bakan spends one paragraph discussing regulatory capture. *See* BAKAN, *supra* note 1, at 152.

[111]*See* J. M. BUCHANAN & G. TULLOCK, THE CALCULUS OF CONSENT ch. 19 (1962) (describing the activities of pressure groups as "profit-seeking" and socially costly); G. STIGLER, THE CITIZEN AND THE STATE: ESSAYS ON REGULATION ch. 9 (1975) (articulating a rent-seeking theory of regulation).

mechanism so that trade-offs depend on the choices of the affected individuals rather than on their ability to lobby a decision maker.

It is not the case, however, that we are faced with an all-or-nothing choice between the political and market mechanisms. The market mechanism affords greater protection to those who would be dissenters in a political system, but the political system provides a more adequate framework for public-spirited or ethical deliberation and may, as a result, be more protective of those without economic power. One cannot deny that political acts may *sometimes* mask the advancement of the actor's self-interest. However, unless one believes that this is *always* the case, and consequently that there is no such thing as ethical deliberation, the argument for an exclusive reliance on markets is not made out. My point is not, of course, that politics is always preferable to the market but, less controversially I hope, that there is a role for both modalities of decision making.

While Bakan's proposed response to the hegemony of markets is to increase the role of politics through an expanded regulatory and public management sphere, Mitchell's and Fraser's proposals are more ambitious. They argue, in essence, for a greater role for politics within the corporation. The notion of politics having a role in corporate governance is a subversive one for corporate contractarians, but, in my view, it cannot easily be dismissed. For one thing, as Hirschman famously pointed out, markets in the real world contain considerable "slack."[112] The implication of Hirschman's observation is that dysfunctionality within an organization is sometimes better corrected by recourse to political means (voice) than through the market mechanism (exit).[113] It is, in any event, inadvisable to rely solely on one of the two mechanisms.

What the opponents of corporate politics really object to, of course, is the idea that deliberation within the corporation might be public-spirited or ethical. While sometimes denying that they are against public-spirited deliberation or ethical argument, they may argue that the appropriate forum for such activities is within the political organs of the state.[114] The

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[112]HIRSCHMAN, *supra* note 95, at 5.

[113]*See id.; see also* John C. Coffee Jr., *Liquidity Versus Control: The Institutional Investor as Corporate Monitor*, 91 COLUM. L. REV. 1277 (1991) (describing by reference to voice versus exit the potential for active monitoring by institutional investors with a limited demand for liquidity).

[114]This is implicitly Hansmann and Kraakman's argument. *See* Hansmann & Kraakman, *supra* note 6, at 442 (advocating protection of nonshareholder interests through external regulation rather than corporate law). Bakan also appears to be resigned to this view. *See* BAKAN, *supra*

objection may be framed in terms of competence and the specialization of functions: let private sector managers and other corporate actors focus on the creation of private wealth while specialists in public policy, working in government, translate deliberations about the requirements of justice or the public interest into regulation or redistributive taxation.[115]

There is something to the argument that uncoordinated pursuit of the "public interest" by private actors might be ineffective and, perhaps, even counterproductive. However, if public policy is the domain of specialists, I am not persuaded that justice is as well. Sometimes, it is not difficult to tell that a decision raises an issue of justice; the decision on behalf of a manufacturer of data processing equipment to abstain from supplying equipment for use in a totalitarian government's slave labor program is within the abilities of nonspecialists in public policy.[116] Often, the matter will be less clear. The Malibu case is an example—is it a matter of justice or of policy whether 1/82,000 is an acceptable incremental fatality risk for an automobile design characteristic that reduces the price of the vehicle by one percent?[117] However, the fact that the line between justice and policy is often unclear is not a reason to assume that all considerations other than profit are policy matters best left to public-sector experts.

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note 1, at 161 ("Government regulation [is] the principal means for bringing corporations under democratic control and ensuring that they respect the interests of citizens, communities and the environment.").

[115]The argument may alternatively be framed in terms of illegitimate power. Even if corporate actors were competent policy analysts, it would be inappropriate for them to play this role when they have no democratic mandate. *See* Friedrich A. Hayek, *The Corporation in a Democratic Society: in Whose Interests Ought It and Will It Be Run?*, *in* MANAGEMENT AND CORPORATIONS 99, 116 (Melvin Anshen & George Leland Bach eds., 1960); *see also* Allen, *supra* note 52, at 269.

[116]For a concrete example of circumstances that appear to raise this type of issue, see E. BLACK, IBM AND THE HOLOCAUST (2001) (examining IBM's profitable business of selling machinery, design services, and supplies to the Third Reich).

[117]GM estimated that 500 fatalities per year would result from the fuel tank design, based on forty-one million vehicles. *See* BAKAN, *supra* note 1, at 63. This translates into one fatality per year for every 82,000 vehicles. By comparison, in 2001, traffic fatalities in the United States numbered approximately one per year for every 6,100 vehicles. The Bureau of Transportation Statistics reported 38,615 fatalities in 2001 for 235,331,381 motor vehicles. *See National Transportation Statistics 2003*, BUREAU OF TRANSPORTATION STATISTICS, *at* http://www.bts.gov/publications/national_transportation_statistics/2003/index.html (March 2004). The estimated cost to correct the design defect was $8.59 per vehicle. The plaintiff in the Malibu litigation paid $500 for the car. *See* Milo Geyelin, *Lasting Impact: How an Internal Memo Written 26 Years Ago Is Costing GM Dearly*, WALL ST. J., Sept. 29, 1999, at A1.

IV. Conclusion

I have criticized Bakan's argument for oversimplifying the relationship between corporate law and corporate irresponsibility and, as a result, neglecting the fact that it is the aggregated decisions of ordinary people—especially stockholders—that determine management's freedom to conduct corporate business responsibly. Mitchell does not commit the same error, but his call for the elimination of stockholder voting for the board of directors rests on a heroic assumption about the incorruptibility of corporate management. Even if I shared his confidence, I do not expect potential equity investors to do so. Finally, Fraser's proposal to make dual-class capitalization mandatory would entail the elimination of the separation of ownership and control and a return to a more concentrated capitalism; it is therefore so revolutionary as to disqualify it as part of a realistic reform agenda.

We may more readily accept, however, the authors' underlying concern that the expansion of the corporate sector has contributed to an increase in the role of market mechanism, at the expense of the political mechanism, in social decision making, and their implicit warning against coming to rely exclusively on only one of those two mechanisms. Moreover, I have argued that there is merit to the view, advanced implicitly by Mitchell and explicitly by Fraser, that there should be a space for politics, including ethical deliberation, internal to the corporation.

I want to conclude by pointing out that the structure of the corporation today does not, in fact, preclude deliberation, despite the contrary understanding of many contractarian corporate theorists. Restrictions on shareholder communications have been eased[118] and, through the shareholder proposal mechanism,[119] some communications are even subsidized. Boards of directors enjoy considerable legal freedom to act responsibly and to appeal to shareholders' ethical judgment when communicating with them if they believe the shareholders will be

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[118]Regulation of Communications Among Shareholders, Exchange Act Release No. 31,326, 57 Fed. Reg. 48,276, (Oct. 22, 1992) (to be codified at 17 C.F.R. pts. 240, 249). For a summary of the reforms, see Stephen Choi, *Proxy Issue Proposals: Impact of the 1992 SEC Proxy Reforms*, 16 J.L. Econ. & Org. 233, 235–37 (2000). Choi observed that, following the reforms, labor unions and religious organizations made greater use of the shareholder proposal mechanism, but that their proposals attracted little voting support. *See id.* at 257.

[119]*See* Shareholder Proposals, 17 C.F.R. §240.14a-8 (2005).

receptive. Corporate participants are even free to structure their ventures so that voting control resides with a small group of active stockholders.[120] Even per-capita voting is possible within a modern corporation.[121] If these opportunities are not taken up to the extent that they should be, the blame lies not principally with corporate law, but with the stockholders. The law leaves us the freedom to be irresponsible, but it does not make us irresponsible.

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[120] *See supra* note 85.

[121] Sagusa, Inc. v. Magellan, Petroleum Corp., No. 12, 977, 1993 WL 512487 (Del. Ch. 1993) 19 Del. J. Corp. L. 1119, 1304 (1994).