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2018 Leet Symposium Introduction

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2018 Leet Symposium: Fiduciary Duty, Corporate Goals, and Shareholder Activism Introduction

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The debate over the proper purposes of the public corporation extends back to the very dawn of modern corporate law. Way back in 1932,[1] Columbia Law Professor Adolf Berle and Harvard Law Professor E. Merrick Dodd, Jr. engaged in a famous debate in the pages of the Harvard Law Review over what has come to be called corporate social responsibility. The prior year, Berle had published a now-classic article analogizing corporate managers to trustees, bound by fiduciary obligation to use their powers to benefit the shareholders.[2] To put it in modern terms, Berle argued that the sole governing norm of corporate decision-making is, and ought to be, shareholder wealth maximization.[3]

In response, Dodd penned an article arguing for a broader conception of the duties of corporate managers—what would now be called a stakeholder model of corporate governance.[4] Dodd suggested that the law permitted—and ought to encourage—corporate managers, as holders of a public charter endowed with great power, to take into account the interests of "employees, consumers, and the general public, as well as of the stockholders."[5] He further argued—or perhaps threatened—that the failure of corporations voluntarily to act in a

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1. The year 1932 has as good a claim as any to being the birthdate of modern American corporate law, as it was the year Adolf Berle, Jr. and Gardiner Means published their foundational text, Adolf Berle, Jr. & Gardiner Means, The Modern Corporation and Private Property (1932).

2. A. A. Berle, Jr., *Corporate Powers as Powers in Trust*, 44 Harv. L. Rev. 1049 (1931).

3. *See id.* at 1049 ("It is the thesis of this essay that all powers granted to a corporation or to the management of a corporation . . . are necessarily and at all times exercisable only for the ratable benefit of all the shareholders as their interest appears."). An early version of this view was famously advanced in *Dodge v. Ford Motor Company*, 170 N.W. 668 (Mich. 1919).

4. E. Merrick Dodd, Jr., *For Whom are Corporate Managers Trustees?*, 45 Harv. L. Rev. 1145, 1156 (1932).

5. *Id.*

public-spirited fashion would inevitably lead public opinion to demand coercive government intervention.[6]

Berle's response was caustic.[7] Berle expressed his sympathy with the "dream of a time when corporate administration will be held to a high degree of required responsibility."[8] Nonetheless, he argued that granting corporate managers discretion to serve the interests of non-shareholder constituencies would, in practice, simply be giving them license to favor one constituency above all others: themselves.[9] It was, Berle suggested, naïve in the extreme to expect that weakening the norm of stockholder wealth maximization would lead to social responsibility, rather than a managerial kleptocracy.[10]

The Berle-Dodd debate presaged many—if not most—of the issues that have constituted the corporate responsibility debate over the ensuing decades. Does relaxing the norm of shareholder wealth maximization free corporate managers to take other interests into account—such as employees, consumers, and the environment? Or does it merely give managers cover to serve their own self-interest? To what extent do "social responsibility" and shareholder wealth maximization really conflict?[11] Where they do conflict, is any goal other than

6. *See id.* at 1151 (suggesting that "the day may not be far distant when public opinion will demand a much greater degree of protection to the worker"); *id.* at 1153 (forecasting "legal compulsion . . . to keep those who failed to catch the new spirit up to the standards which their more enlightened competitors would desire to adopt voluntarily"); *id.* at 1158–59 (noting that public benefits not provided by private enterprise instead "might be undertaken as a public enterprise supported by taxation").

7. A. A. Berle, Jr., *For Whom Corporate Managers Are Trustees: A Note*, 45 Harv. L. Rev. 1365 (1932).

8. *Id.* at 1372.

9. *See id.* 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. The claims upon the assembled industrial wealth . . . which managements are likely to enforce (they have no need to urge) are their own.").

10. *See id.* ("Now I submit that you cannot abandon emphasis on 'the view that business corporations exist for the sole purpose of making profits for their stockholders' until such time as you are prepared to offer a clear and reasonably enforceable scheme of responsibilities to someone else.").

11. Dodd suggested that "social responsibility" included much that was compatible with shareholder wealth maximization, but also went beyond it:

> If the social responsibility of business means merely a more enlightened view as to the ultimate advantage of the stockholder-owners, then obviously corporate managers may accept such social responsibility without any departure from the traditional view that their function is to seek to obtain the maximum amount of profits for their shareholders.

shareholder wealth maximization compatible with the fact that shareholders alone elect the board of directors?[12] As is shown by the Articles in this issue, these questions are still with us eighty-seven years later.

And yet, as Professor Lipton notes in her contribution to this volume, "the theoretical question of the nature of directors' duties continues to fascinate."[13] In part, this is due to the rich ironies that abound in the debate. On the one hand, advocates of corporate social responsibility—often otherwise suspicious of the motives of big business—would, in practice, entrust the handling of important social problems to the tender mercies of the managers of big businesses. On the other hand, libertarian Milton Friedman famously argued that businesses should focus exclusively on maximizing profits while operating within the law, while reserving entirely to the government—an entity he did not generally hold in high esteem—the role of crafting rules to promote social welfare.[14]

In part, the continuing fascination may stem from the recurring idea that changing circumstances are making a robust notion of corporate social responsibility more practical than it once may have been. Perhaps a consumer base increasingly attuned to environmental and social issues has narrowed the gap between "responsibility" and shareholder wealth maximization. Perhaps shareholders themselves are more willing than previously to leave money on the table to pursue other social ends, provided corporations disclose the information

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> And yet one need not be unduly credulous to feel that there is more to this talk of social responsibility on the part of corporation managers than merely a more intelligent appreciation of what tends to the ultimate benefit of their stockholders.

Dodd, *supra* note 4, at 1156–57.

12. *See, e.g.*, 3 Henry G. Manne, *First Lecture*, *in* The Collected Works of Henry G. Manne: Liberty and Freedom in the Economic Ordering of Society, 15–16 (Fred S. McChesney & Jonathan R. Macey eds., 2009) (arguing that "socially responsible" actions that reduce shareholder wealth will be constrained by shareholder voting and the market for corporate control).

13. Ann M. Lipton, *What We Talk About When We Talk About Shareholder Primacy*, 69 Case W. Res. L. Rev. 863 (2019).

14. *See* Milton Friedman, *The Social Responsibility of Business is to Increase its Profits*, N.Y. Times Mag. (Sept. 13, 1970). In fairness to Friedman, he rejects the intrusion of "social responsibility" into the corporate boardroom—in favor of relegating it to the government—on the grounds that doing otherwise would inevitably lead to political intrusion into private enterprise. *See id.* at 3 (arguing that "the doctrine of 'social responsibility' involves the acceptance of the socialist view that political mechanisms, not market mechanisms, are the appropriate way to determine the allocation of scarce resources to alternative uses").

necessary for them to do so effectively. Perhaps shareholders are simply better able to express and enforce their desire for socially responsible governance via activist funds or the managers of the large index funds that increasingly dominate markets.[15] Perhaps fiduciary duty law has developed to the point where it can protect shareholders from self-interested behavior by corporate managers while still allowing those managers discretion to achieve social goals not obviously linked to shareholder wealth maximization.

In part, though, the enduring fascination with corporate social responsibility may simply reflect the profound fundamental issues at stake. None is more fundamental than that no economic system can long survive in a free society unless that system benefits—and is *understood* to benefit—the bulk of the populace. Writing in the first half of the twentieth century, both Dodd and Berle had this reality front of mind.[16] We may have occasion to be reminded of it in the first half of the twenty-first century.

On November 1, 2018, the *Case Western Reserve University Law Review* held the 2018 Leet Symposium, bringing together a group of nationally respected corporate law scholars to explore the current state of play between traditional shareholder wealth maximization and modern shareholder environmental and social activism. The Symposium

15. Larry Fink, the head of BlackRock, the world's largest asset manager, has been clearest in positioning his fund to appeal to such investors. In his January 2018 annual letter to companies in which BlackRock invests, he emphasized that "[t]o prosper over time, every company must not only deliver financial performance, but also show how it makes a positive contribution to society. Companies must benefit all of their stakeholders, including shareholders, employees, customers, and the communities in which they operate." Annual Letter from Larry Fink, Chairman & Chief Exec. Officer, BlackRock, Inc., to Chief Exec. Officers (Jan. 2018), https://www.blackrock.com/corporate/investor-relations/2018-larry-fink-ceo-letter [perma.cc/ZKG7-7XDB]; *see also* Leslie P. Norton, *Blackrock's Larry Fink: The New Conscience of Wall Street?*, Barron's (June 23, 2018), https://www.barrons.com/articles/in-defense-of-social-purpose-1529716548 [http://perma.cc/3ZF3-3BM3].

16. *See, e.g.*, Dodd, *supra* note 4, at 1151–52 (noting that belief in the inevitability of government control of the economy "is no longer confined to radical opponents of the capitalistic system; it has come to be shared by many conservatives who believe that capitalism is worth saving but that it can not permanently survive under modern conditions unless it treats the economic security of the worker as one of its obligations and is intelligently directed so as to attain that object"); Berle, *supra* note 7, 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 . . . 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.").

also included a panel on the difficult role of in-house corporate counsel in a world where serving as a zealous advocate for the corporation may conflict with in-house counsel's compliance function. This issue contains Articles that were presented on the occasion, together with the prepared remarks of the keynote speaker, SEC Commissioner Hester Peirce.

Professor Ann Lipton, a corporate law scholar at Tulane Law School, asks the fundamental question of whether corporate purpose is determined by the shareholders themselves, or imposed by the law. If it is the former, she argues, there is reason to believe that shareholders would not uniformly choose a corporate purpose of maximizing long-term shareholder wealth, even at the expense of other social goals. If the latter—and she catalogues several features of positive law that at the very least *presume* a purpose of shareholder wealth maximization—the role of shareholders in corporate governance becomes decidedly murky. She concludes by suggesting that increasing shareholder assertiveness may heighten the tension between actual, expressed shareholder preferences and what the law has long presumed those preferences to be.[17]

Professor Claire Hill, a corporate law scholar at the University of Minnesota Law School, argues that we may be seeing a convergence between the goals of corporate social responsibility and profit maximization. She argues that reputational concerns in product, labor, and financial markets, together with the potential for legal liability for bad behavior, render the tension between responsible corporate behavior and profit maximization less acute than it may seem. Professor Hill uses the example of the #MeToo movement and corporate efforts to prevent and respond to sexual misconduct to demonstrate that the line between social responsibility and wealth maximization is often unclear.[18]

Andy Green, managing director of economic policy at the Center for American Progress, also argues that the perceived trade-off between wealth maximization and social responsibility is overstated. In his Article, he suggests that environmental, social, and governance issues often go to the heart of the systemic risks firms face, and that long-term investors would benefit from expanded SEC-mandated disclosure of information pertinent to such issues.[19]

In her prepared remarks, SEC Commissioner Hester Peirce—our keynote speaker—argued against an extension of mandatory disclosure to matters not directly relevant to financial performance. She pointed

17. Lipton, *supra* note 13.

18. Claire A. Hill, *#MeToo and the Convergence of CSR and Profit Maximization*, 69 CASE W. RES. L. REV. 895 (2019).

19. Andy Green, *Making Capital Market Work for Workers, Investors, and the Public: ESG Disclosure and Corporate Long-Termism*, 69 CASE W. RES. L. REV. 909 (2019).

out the difficulty surrounding the definition of "material" information even in the narrow context of financial information, and the compounding of that difficulty if disclosure were extended to broader classes of information. She also emphasized the costs associated with broader disclosure and the possibility that expanded non-financial disclosure would interfere with one of the primary purposes of our capital markets—the efficient allocation of capital to productive endeavors.[20]

Professor Sean Griffith, a corporate law scholar at Fordham University School of Law, comes at the Symposium topic from a different angle, examining shareholder suits challenging merger transactions. In particular, Professor Griffith examines how plaintiffs' lawyers have innovated in the face of case law developments that have made it more difficult to bring and settle disclosure-based lawsuits in Delaware, the leading corporate law jurisdiction.[21]

Finally, this issue contains two Articles on the role of in-house counsel. In the first, Professors Sally and Hugh Gunz explain the difficult position of the in-house counsel—a professional bound by professional rules of ethical conduct, but operating under the authority of non-professional business managers not similarly bound. They then explore the interaction between how in-house counsel perceive themselves and how they ultimately conduct themselves in terms of ethical decision-making.[22] In the second paper, Professor Paula Schaefer of the University of Tennessee College of Law explores what behavioral science can tell us about the pressures and biases that may lead in-house counsel to behave in ways that violate their ethical obligations, and that may ultimately harm their employers.[23]

This Symposium would not have been possible without the hard work and dedication of the editors of the *Case Western Reserve Law Review*. Special thanks are due to Editor in Chief Rachel Ippolito and Executive Symposium Editor Emily Cunningham for their work in making the Symposium a success. Thank you also to Professors Jonathan Adler and Cassandra Burke Robertson for their assistance in organizing this event.

20. Hester M. Peirce, Comm'r, Sec. & Exch. Comm'n, *Pondering Financial Reporting: Remarks Before the 2018 Leet Business Law Symposium* (Nov. 2, 2018), *in* 69 Case W. Res. L. Rev. 849 (2019).

21. Sean J. Griffith, *Innovation in Disclosure-Based Shareholder Suits*, 69 Case W. Res. L. Rev. 927 (2019).

22. Hugh Gunz & Sally Gunz, *Ethical Challenges in the Role of In-House Counsel*, 69 Case W. Res. L. Rev. 953 (2019).

23. Paula Schaefer, *Behavioral Legal Ethics Lesson for Corporate Counsel*, 69 Case W. Res. L. Rev. 975 (2019).