Corporate Directors as Purpose Fiduciaries:

Reclaiming the Corporate Law We Need

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Abstract

Much of the debate over corporate governance centers on whether directors have fiduciary duties to stockholders alone, or to stakeholders more broadly. I argue instead that, certainly historically and arguably still today, directors have a fiduciary duty not to specific persons, but to the corporate entity and its authorized purposes. Drawing on the distinction advanced by Miller and Gold between "service fiduciaries" (i.e. personal fiduciaries) and "governance fiduciaries" (i.e. purpose fiduciaries), the first section makes a series of analytical arguments in defense of the position that corporate directors are purpose fiduciaries, based on the legal structure of corporations. The second section backs this up with historical argumentation. The corporate bodies of the medieval Catholic Church were clear purpose fiduciaries, and monasteries in particular were the laboratory for charters with purpose clauses. These practices passed over to civil corporations, including merchant guilds. Drawing on the previously unutilized evidence offered by corporate oaths of office, I show that the corporate boards of merchant guilds also began as clear purpose fiduciaries. However, circumstances surrounding the emergence of the business corporation in England, from out of the merchant guild, resulted in this new type of corporation being described in the vocabulary of the joint stock company (a variety of partnership), or alternatively, in the vocabulary of the English trust. Each suggested that stockholders were the "owners" and legal beneficiaries of the corporation, and that the board's fiduciary duty was to them rather than to purposes. Transformations in corporate enterprise at the end of the 19th century finally made these legal conceits untenable, and recognition of the underlying purpose fiduciarity of directors began to emerge in progressive era legal thought. However, beginning in the 1970s, Chicago neoliberals successfully reasserted the partnership conceit with its implication of "shareholder primacy." This has caused much intellectual confusion and policy mischief, as it has shaped the norms and laws under which business corporations are governed, with the consequence that corporate managers have turned their firms away from corporate mission and long-term growth and towards the short-term stockholder's interest in high dividends and stock price, with all of the dysfunctions this entails. But the core of corporate law continues to reveal directors to be purpose fiduciaries, and the courts, while significantly swayed by Chicago conceits, have not fully abandoned a purpose interpretation, although they have narrowed and misconstrued it. The paper concludes with recommendations for strengthening the purpose fiduciarity of directors, with the potential to significantly improve the performance of corporate firms.

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Introduction

In ancient Rome, the corporation borrowed its legal form from the state. In the words of Justinian's *Digest*, the corporation exists "on the model of the state" (*ad exemplum rei publicae*). Specifically, like the state, it has a "treasury" with property wholly distinct from the property of natural persons. And it has "an attorney or syndic through whom, as in a state, what should be transacted and done in common is transacted and done"—which is to say that neither state nor corporation can itself act, but must act through representatives, that is, through fiduciaries.[1]

A millennium later, in medieval Europe, the state returned the compliment and borrowed its legal form from the corporation. Indeed, both the corporation of Roman law and (derived from it) the corporation of canon law, with their legally-defined governance structures and procedures, became important constitutional models for government in general, with constitutionally organized collectivities at all levels styled as corporations.[2] The Church was a corporation;[3] the empire was a corporation;[4] the kingdom was a corporation;[5] the republic was a corporation;[6] and the chartered town was (most usually) a corporation.[7] Parliament was a corporation, with the king as its head.[8] And the king himself was a "corporation sole."[9] The main significance of this is that, in contrast to the

[1] Dig. 3.4.1. (Gaius, Provincial Edict 3).
[2] F.W. MAITLAND, STATE, TRUST AND CORPORATION 34 (noting that in medieval thought, "[w]hat we should regard as the contrast between State and Corporation was hardly visible. The 'commune of the realm' differed rather in size and power than in essence from the commune of a country or the commune or a borough. And as the *comitatus* or county took visible form in the *comitatus* or county court, so the realm took visible form in a parliament.") [year?]
[3] BRIAN TIERNEY, FOUNDATIONS OF CONCILIAR THEORY: THE CONTRIBUTION OF THE MEDIEVAL CANONISTS FROM GRATIAN TO THE GREAT SCHISM 132-3 (1955).
[4] OTTO VON GIERKE, POLITICAL THEORIES OF THE MIDDLE AGE 39-40 (1900).
[5] BRIAN TIERNEY,
[6] J.P. Canning, *The Corporation in the Thought of the Italian Jurists*, 1 HIST. OF POL. THOUGHT 9-32 (1980).
[7] REYNOLDS, SUSAN, AN INTRODUCTION TO THE HISTORY OF ENGLISH MEDIEVAL TOWNS 113-4 (1977).
[8] MAITLAND, *supra* note 2, at 34; ERNST KANTOROWICZ, THE KING'S TWO BODIES 228 (1957).
[9] MAITLAND, *supra* note 2, at 36.

patriarchal metaphor so pervasive in agrarian civilizations, in which the ruler is the *paterfamilias* and *dominus* of the nation, the corporate metaphor, as rival to the patriarchal, distinguishes ownership (*dominium*), which lies with the corporate whole, from control (*jurisdictio* and *administratio*), which lies with the ruler. This effectively turns rulers into office holders, whose authority derives from the corporate body, at least by consent if not always by election,[10] and it helped underwrite the spread of councils, parlements, and other representative bodies throughout medieval Europe.[11]

Nor did the borrowing end with the Middle Ages. The earliest American colonies—Virginia and Massachusetts Bay—were literal corporations of the Crown, with governments established by and limited by their charters. In 1787, their governance practices passed to the United States as a whole. The United States Constitution, and all constitutions modeled thereon, has the form and function, not of a "social contract," but of a corporate charter—a written instrument that authorizes and limits a government and establishes its offices and procedures. The great Federalist innovation was to have this charter promulgated not by a sovereign king, but by a sovereign people. Otherwise, all of the things that we think of as American constitutional innovations—written constitutions (charters), ratifying conventions, judicial review, and charter amendment—simply transfer the governance technology of the corporation to the state.[12] The constitutional state and the corporation are twinned institutions, and one cannot tell the history of the one without the other.

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[10] Cite Otto von Gierke, on this eliminating any deep-seated distinction between kings and republican magistrates. Also ANTONY BLACK, GUILDS AND CIVIL SOCIETY IN EUROPEAN POLITICAL THOUGHT FROM THE TWELFTH CENTURY TO THE PRESENT 149-52 (1984).
[11] Maitland supra; Tierney, supra.
[12] David Ciepley, *Is the U.S. Government a Corporation? The Corporate Genesis of Modern Constitutionalism*, 111 AM. POL. SCI. REV. 418 (2017).

It should not be surprising that after two millennia of such reciprocal modeling between state and corporation, the fiduciary governance of the one replicates that of the other, and in particular that the fiduciary duties of corporate directors are, properly reconstructed, of the same nature as the fiduciary duties of government officials. Namely, they have duties not to specific persons, such as the stockholders, but to the corporation and its purposes—that is, to the good government of the corporation in pursuit of the corporation's authorized purposes—which purposes historically were specified in the corporate charter (just as American constitutional officials have a duty to the good government of the state in pursuit of the state's authorized purposes, as specified in the Preamble to the Constitution). That, at least, is what I will argue, based on history and on close analysis of the rules of corporate law regarding relations between directors and stockholders.

It is an argument that has become important to make. Not only does it cut against the grain of current Delaware opinion about the duty of directors. It has implications for the ends that business corporations ought to serve, steering us away from what has turned out to be a damaging notion that the board's fiduciary duty is to its stockholders and stockholders alone.[13] The corporation (both non-profit and for-profit) was developed in order to dedicate property to long-term, cooperative purposes.[14] Its governance structure was designed to implement such long-term purposes, which was done by putting purpose fiduciarity at its core. It therefore stands to reason that, if one substitutes for this a fiduciary duty to specific *persons*—especially when the interest of these persons is short-term and pecuniary—one will deform the institution, transforming it from a device for property

[13] Infra pp.**
[14] Lynn Stout, Corporation as Time Machine.

accumulation and specialization into a device for property liquidation and extraction. This is exactly what the doctrine of shareholder primacy has done to the corporation, and it is what this article sets itself against.

Existing arguments against shareholder primacy are indirect, attacking the conceits that commentators have used to defend the primacy of shareholders, through a process of elimination. This has meant attacking such notions as that stockholders "own" the corporation, or are its "residual claimants," or its "members," or attacking the Efficient Market Hypothesis, or the notion that directors need a unitary constituency.[15] Such arguments are welcome and even necessary. But the argument presented here does not rest on the debunking of any particular corporate theory or market theory. It is direct. To qualify as a legal beneficiary, certain attributes must obtain, and if under fiduciary protection, certain rights will follow. Using these tests, it can be shown that stockholders are not situated as proper fiduciary objects of the board, nor for that matter are any other natural persons. All signs point to directors being purpose fiduciaries, in line with government officials more generally.

"Purpose" is a hot topic in management circles today—the subject matter of business conferences and worker recruitment literature. It has even spawned a small industry of "purpose consultants."[16] The question has been raised, however, whether this is really more than the latest corporate public relations gambit or employee recruitment tool[17]—what one might call "purpose washing," the successor to "green washing." This article explores when corporate purpose was not aspirational, voluntaristic, or

[15] Cite Stout; Ciepley; Stout and Belafanti; et al.
[16] Cite Andrew at University of Colorado Law School.
[17] Maria Hengeveld, *Big Business Has a New Scam: The 'Purpose Paradigm,'* THE NATION (2019).

propagandistic, but at the heart of the director's duties. And it considers to what extent it can be reclaimed.

To be clear at the outset, my view is that directors are the legal agents of, and owe fiduciary duties to, the corporation, not the stockholders. So stated, this view is utterly conventional. It is both the historical norm and, today, the international norm. Delaware, in extending this directorial duty to the stockholders, i~~a~~s an outlier. But to the conventional view I add that, historically, corporations were authorized for specific purposes, and could only act as a corporation when pursuing those purposes, so that the director's duty extended to the faithful pursuit of the corporation's authorized purpose. Furthermore, the office of director was designed for this kind of fiduciarity and makes most sense, and arguably works best, when ~~tethered~~ connected to it. It is therefore worth reclaiming this fuller conception of the director's duty, to the extent possible. Finally, I do not think the corporation itself has fiduciary duties to the stockholders, anymore than the directors do ~~either~~. It has its own purposes which it is to pursue, authorized by the state; it would be self-defeating for it to have a duty of loyalty to others. However, the corporation must act equitably towards its stockholders, and it is fitting that stockholders have equitable remedies against it. Indeed, the equitable relation between the stockholders and the corporation is embedded in our corporate language—shareholders purchase "equity" in a corporation, or an "equity stake," when they purchase a share.[18]

Part I introduces the distinction between fiduciarity to persons and to purposes and notes the nearly unanimous opinion today that corporate directors are fiduciaries to persons, with serious debate only over whether the relevant persons are the stockholders

[18] Asaf Raz, Share Law: Toward a New Understanding of Corporate Law. Universi~~is~~ty of Penn. J. of International Law 255, ** (2018).

only, or stakeholders more broadly. Part II provides the analytical argument that corporate directors are not personal fiduciaries to the stockholders, but are in the structural and legal position of purpose fiduciaries. Part III, in three sections, traces the development of purpose fiduciarity within Church corporations, its transfer to civil corporations, and its transfer again to the business corporation specifically.

Part IV describes the origins of the modern business corporation—first the Dutch East India Company (VOC) and then the English East India Company (EIC), which, abandoning its original form, copied the Dutch form beginning in 1657. Its major point is that, in copying the Dutch, the English retained their existing vocabulary for describing the unincorporated joint stock company, thus significantly mischaracterizing the new form of business. Most distorting of all, they retained the notion, not shared by the Dutch, that stockholders "own" the corporation.

Part V describes the intellectual conundrums and legal problems raised by th~~3~~e business corporation that could not be adequately addressed by received corporate law, which was geared toward a very different kind of corporation—the "member corporation" rather than this new "property corporation." It then described how English and American jurists creatively, if sometimes problematically, addressed these problems by applying the legal rules of partnerships and trusts, justified on the grounds that stockholders are "owners." It describes in particular how the trust metaphor switched the perceived purpose of the corporation, from the *chartered* purpose to the *stockholder* purpose of making money. This birthed the notion that directors owe fiduciary duties to the stockholders—the doctrine of shareholder primacy.

Part VI describes how the development of liquid stock markets and corporate concentration exploded the conceits of the corporation as a partnership or trust. This revived the entity conception of the corporation and redirected director duties to this entity, although now shorn of any specific purpose.

Part VII described the neoliberal (Chicago School) revival of the partnership conceit in order to square the corporation with free market principles of private property and contract. It looks at the institutionalization of Chicago theory and reviews some of the deleterious consequences, especially in the area of corporate short-termism and exploding inequality.

Part VIII describes the Delaware Court's shift, from imposing directorial fiduciarity to the corporation, then to the corporation and its stockholders, and then, effectively, to its stockholders alone. The~~y~~ rules of fiduciarity that the Court is now applying can best be analogized to those of a public trust, but now with a purpose of private profit. The rules are not like those of a private trust. Even if the stockholders unanimously wished to pursue a public purpose other than stockholder profit maximization (short term or long term), the court ~~regards this~~holds it an "illegitimate *corporate* purpose" for a Delaware corporation, in a complete reversal of the historical norm. This Part also critiques a new argument from Chief Justice Leo Strine in support of shareholder primacy—the argument from stockholder~~constituent~~ power.

Part IX concludes with a number of steps that could be taken to return a degree of purpose fiduciarity to the corporation.

I. Duties to Persons versus Duties to Purposes

It is accepted that corporate directors have fiduciary duties. Least controversially, they have duties of care and loyalty. The debated question is, to whom or what are these duties owed?

Law-and-economics scholars and Chicago finance scholars answer that directorial duties are to stockholders—currently-existing stockholders. What is more, they hold that directorial duties of care and loyalty are just the proscriptive side of a more general, affirmative directorial duty to stockholders (or "shareholders"[19]), which is to maximize "shareholder value," meaning in effect, to maximize their dividends and stock price. In the corporate firm, stockholders are the principals and directors are their agents.[20] Over the past two generations, this view has become the reigning wisdom.

The main rival to this view is that the directors have a fiduciary duty not just to stockholders, but to *stakeholders* more generally—including workers and perhaps suppliers and customers and community members. This was the reigning wisdom coming out of World War Two,[21] and in recent years it has been staging something of a comeback, at least

[19] I prefer the traditional term "stockholder" to "shareholder," which gained favor in the 1970s (likely as part of the law-and-economics movement), because "stockholder" makes more clear that stockholders own a share of stock (a financial instrument) and not a "share" of the company's assets, as was true in unincorporated joint-stock companies, from which much of our corporate vocabulary misleadingly descends. It is an elementary point of corporate law that the assets of the corporation are owned by the legal entity that is the corporation in law, not by stockholders or any other natural persons, who have no legal claim on the firm's assets or profits while a going concern. *See* Jean-Phillipe Robé, *The Legal Structure of the Firm*, 1(1) ACCOUNTING, ECONOMICS, AND LAW 1 (2011); David Ciepley, *Beyond Public and Private: Toward a Political Theory of the Corporation*, 107(1) AM. POL. SCI. REV 139 (2013).

[20] Michael Jensen & William Meckling, *Theory of the Firm: Managerial Behavior, Agency Costs and Ownership Structure*, 3 J. FIN. ECON. 305, 309 (1976) ("the relationship between the stockholders and manager of a corporation fit [*sic*] the definition of a pure agency relationship.").

[21] Dahlia Tsuk Mitchell. Lord Wedderburn of Charlton, *The Legal Development of Corporate Responsibility: For Whom Will Corporate Managers Be Trustees?, in* CORPORATE GOVERNANCE AND DIRECTORS' LIABILITIES 1, 3-5 (Klaus J. Hopt and Gunther Teubner eds., 1985).

among theorists, as part of a reaction against the consequences of implementing "shareholder primacy."[22]

What both views have in common is the notion that directors have a fiduciary duty to specific natural persons—whether to stockholders or to corporate "constituents" more broadly. Another formula, advanced in recent decades in Delaware, is that directors have a duty to "the corporation and its shareholders." This view is less distinct than it sounds, however, because Delaware judges construe the interest of "the corporation" to be the long-run interest of the shareholders as a class.[23] I will argue instead that, certainly historically and arguably still today, directors have a fiduciary duty, not to specific persons, but to the corporate entity and its authorized purposes.

In an important 2015 article, Miller and Gold distinguish two basic types of fiduciary duty. The first is the more familiar and, in fact, is commonly taken to be the *only* kind of fiduciary duty—what Miller and Gold call "service fiduciarity", and which I will call "personal fiduciarity." It is fiduciary duty to a specific person or persons.[24] This is the duty of a lawyer to her client, a trustee to a designated beneficiary, a doctor to a patient, and, if law-and-economics scholars are correct, the duty of a director to the company's stockholders.

But there is another kind of fiduciary duty—what the authors call "governance fiduciarity," and which I will call "purpose fiduciarity"—which involves a mandate to advance a stipulated purpose or purposes rather than to advance the interests of a specific person or persons.[25] It is fiduciary duty to a purpose.[26] This is the duty of the trustees of a

[22] [cite]
[23] *See infra* pp. **
[24] Paul B. Miller & Andrew S. Gold, *Fiduciary Governance*, 57 WM. & MARY L. REV. 513, 519-20 (2015).
[25] *Id*. at 524.
[26] A very clear example is provided by the German *Zweckvermogen*, a personified purpose to which officers have a fiduciary duty.

charitable foundation to the charitable purpose (hunger alleviation, art appreciation, etc.) and the duty of a president or member of congress to the public welfare. While a paradigmatic form of *personal* fiduciarity is the "private trust," with its "defined beneficiaries," the paradigmatic form of *purpose* fiduciarity is the "public trust," "indefinite beneficiaries (the trust for charitable or religious purposes). The benefit almost always ends up going to natural persons, and designedly so.[27] But the benefit redounds to these persons as a consequence of the pursuit of the abstract purpose, whether this be public safety, meals to the hungry, or arts education. The beneficiaries may well be an identifiable group at any point in time—the citizenry, the hungry, the art lovers—but typically the members of the group keep changing, and in any case, the duty is not to the interests of any specific individual or individuals, but to the mission, or purpose, from which individuals benefit if they have an interest in that purpose. In a word, while a personal fiduciary acts as a *substitute* for her authorizer, the purpose fiduciary acts for purposes *stipulated* by her authorizer.[28]

Having drawn this distinction, the authors, with intentional agnosticism, suggest that business corporations might be placed in either category, depending upon one's theory of the corporation.[29] If one follows the law-and-economics view, the fiduciary duty of the directors is to specific persons, namely, the stockholders.[30] The other theory they explore—the "team production" theory of the corporation put forward by Margaret Blair and Lynn Stout—is said

[27] Miller, *supra* note 13 at 569.
[28] *Id.* at 544. The distinction Miller and Gold draw has attracted some criticism for being overdrawn. For example, all fiduciaries, including personal fiduciaries, must exercise their discretion in a manner consistent with the norms of the legal relationship involved, which Miller & Gold describe as a characteristic feature of governance fiduciarity. What presents itself as a more fundamental objection is that all fiduciary duties, including those to specific persons, can be recast as duties to a purpose. This is true, but recasting them in this way continues to leave us with a relatively clear distinction between cases in which the purpose is to advance (usually a subset of) the interests of specific individuals and cases in which the purpose is to advance a purpose. *See* EVAN FOX-DECENT, SOVEREIGNTY'S PROMISE: THE STATE AS FIDUCIARY 96-100 (2012).
[29] Miller, *supra* note 13 at 536.
[30] *Id.* at 536-7.

to imply a "governance" conception of directors' duty. In fact, however, the object of Blair and Stout's 1999 essay is not to sever the board's tie to specific beneficiaries, but to lengthen the list of beneficiaries to whom it owes duties, expanding from the stockholders alone, to all those who make "firm-specific investments" beyond what has been specified contractually (i.e. "stakeholders" more broadly).[31] Directors remain personal fiduciaries.

At the end of their paper, Miller and Gold discuss the new "benefit corporation," which they describe as a hybrid, with fiduciary duties both to stockholders and to the beneficial purpose specified in the charter. But as they note, there are designedly no legal consequences when a benefit corporation fails to pursue its declared beneficial purpose. It is easy to conclude from these examples that, in the usual case, corporate directors have duties only to natural persons (although with continuing disagreement over exactly who these persons are) and, in the exceptional case, may have a permissive right, but not an enforceable duty, to pursue a beneficial purpose.[32]

Drawing on their own criteria for classification, I will argue a stronger position—that the duty of the director falls squarely into the second category, of purpose fiduciarity.

[31] As glossed by Miller and Gold, "the team production theory suggests ... that directors are granted governance-type mandates to act for purposes that encompass but transcend the interest of various constituencies. It consequently becomes impossible to specify particular beneficiaries of the exercise of power by boards." *Id* at 538. But this is at odds with the argument of Blair and Stout, whom they quote in the next sentence: "directors are allowed free rein to consider and make trade-offs between the conflicting interests of different corporate constituencies," and are thus charged with maximizing "a joint welfare function of *all* the individuals" participating in the firm. *Id.* (quoting Margaret M. Blair & Lynn A. Stout, *A Team Production Theory of Corporate Law*, 85 VA. L. REV. 247, 288, 291 (1999). In other words, the interest of the corporation is, for Blair and Stout (at least circa 1999), reducible to the interests of specific beneficiaries; indeed, one cannot calculate a joint welfare function without reference to specific individuals with determinate preferences. Their interests are not "transcended" to encompass more abstract purposes. The fiduciary duty of directors thus remains of the "personal" type, on their account.

[32] The authors also take up the notion that the "business judgment rule" creates "agency slack" that allows managers in practice to pursue purposes other than maximizing shareholder value, without legal repercussion. It is suggested that this, too, might make the business corporation a hybrid. Miller, *supra* note 13 at 580-2. But being able to "get away with" something seems categorically different from having a duty to do that something, so this line of interpretation doesn't really lead away from the "personal" conception.

Classically, this was a duty to the corporation and its authorized purpose, although as we will see, this has become muddied in recent history by the hollowing out of corporate purpose clauses. Nonetheless, the rules of corporate law still show that the corporation is not akin to a private trust, with a duty to persons, and that the fiduciary duty of directors is thus not to current stockholders nor to *any* natural persons. Below I first make an analytical case for this, showing that the fiduciary duty of directors displays none of the three major marks of personal fiduciarity, but fits squarely in the category of purpose fiduciarity. I then support this with historical argumentation.

II. Analytical argument

1. *Unspecified Beneficiaries*. A defining feature of a private trust or other "service" relationship, is that the duty of the fiduciary is to the interests of a beneficiary, taken in her specificity. A private trust is invalid if it lacks a *specific*, *ascertainable* beneficiary (or beneficiaries).[33] In the words of the United States Uniform Trust Code, "A private trust must have one or more ascertainable beneficiaries to whom the trustee owes fiduciary duties and who can call the trustee to account. This rule … follows from the more fundamental principle that a private trust must be for the benefit of beneficiaries".[34] In line with this, should the designated beneficiary die or, say, achieve the age of majority, or otherwise refuse to take the beneficial interest of the trust, the trust is dissolved.[35] At the same time, a trust beneficiary cannot transfer or sell her standing to another.[36] Personal fiduciarity is always of finite duration.

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[33] Miller, *supra* note 13, at 522.
[34] UNIF. TRUST CODE § 402(a)(3) (UNIF. L. COMM'N 2010).
[35] Miller, *supra* note 13, at 522.
[36] cite

In contrast, purpose fiduciaries have no specific beneficiaries, but are dedicated to abstract, often trans-generational purposes (although again, advancing these purposes is generally expected to benefit individuals).[37] As Miller and Gold observe of purpose, or governance, mandates, "their independence from … beneficiaries, is found in their persistence over time despite changes in the membership of collectivities with which they are associated".[38] Indeed, purpose fiduciarity—characteristic of government bodies and charitable foundations, for example—typically (although not universally) has no natural expiration date, but continues in perpetuity. And because the fiduciary mandate is enduring, it is usual for an institutional structure to be built out from it for the sake of better attaining the purpose both now and well into the future. Therefore, while personal fiduciarity is interpersonal (between two or more specific persons), purpose fiduciarity is, as Gold and Miller put it elsewhere, "institutional," obtaining "between fiduciaries and an institution or organization"[39] —or, I would further suggest, obtaining between fiduciaries and a "juridical person" (legal entity) authorized to pursue a specified purpose, with the institution as an instrument with which the fiduciary helps realize this purpose. The duty of the director is to provide good government of the institution in pursuit of the corporation's authorized purpose.[40]

[37] As Miller and Gold note, all fiduciary mandates can be seen as creating duties to purposes; but personal, or service, mandates are tied to specific beneficiaries, whereas what I am calling purpose mandates oblige *only* to purposes, not to specific persons. Miller, *supra* note 13, at 549.
[38] Miller, *supra* note 13, at 522.
[39] Paul B. Miller & Andrew S. Gold, *Fiduciary Duties in Social Enterprise*, *in* THE CAMBRIDGE HANDBOOK OF SOCIAL ENTERPRISE LAW, 5 (J. Yocket & B. Means eds., forthcoming).
[40] The salience of governance in this mode of fiduciarity presumably accounts for Miller and Gold's language of "governance fiduciarity." But even the faithful discharge of the office of trustee of a private trust may entail a governance dimension, so I find it preferable to emphasize the focus of this fiduciarity on a *purpose*, which differentiates it from the private trust, which focuses on a person.

In light of the above, the first ground for holding that directors of business corporations are not personal fiduciaries, is that they do not have specific and ascertainable beneficiaries. Against this, it will immediately be contended that the current stockholders are the specific and ascertainable beneficiaries of the corporation—or even more strongly, are the principals of the corporation—and that directors have a fiduciary duty to them. This has indeed become the received view, pushed with especial success by law-and-economics scholars and echoed in some courtrooms. But as an interpretation of the underlying corporate law, it does not survive sustained analysis.

One difficulty for this view is that, in today's typical publicly traded firm, with many thousands of rapidly churning stockholders, management is unlikely to know who most of the stockholders are, which raises serious doubts about the extent to which stockholders meaningfully meet the specificity requirement for beneficiaries. But the view has deeper problems than this.

One such problem is that a corporation is formed, and directors installed, before shares of stock are even issued and thus before stockholders even exist—a state of affairs that may last for some time.[41] Nonetheless, during this period, directors may not act in a self-serving manner. They are still under fiduciary strictures.[42] These strictures cannot possibly derive from a fiduciary duty to specific stockholders, since there are no stockholders. Evidently, the director's fiduciary duty is not strictly personal.

It might be replied, that the duty of the directors during this period is not to existing, but to future stockholders. However, this does not eliminate the problem that these future stockholders are unknown and unascertainable. And to this is added the difficulty that what

[41] Corp law I cite to Asaf
[42] cite

law-and-economics scholars standardly regard as the interest of the stockholding class—generous dividends and increasing stock price—can hardly be pursued before shares have even been issued.

That the board should have fiduciary duties before there is seemingly anyone for it to have fiduciary duties *to*, and specifically before there are stockholders, is an unexplained anomaly for those who conceive of the business corporation as a personal fiduciary, and especially anomalous to those who see it as a personal fiduciary to the stockholders. But this is the normal state of affairs for a charitable corporation or indeed any other kind of corporation—a university, town, church, monastery, cathedral chapter, or whatnot. These are all purpose fiduciaries without stockholders or other specific beneficiaries (in the legal sense). This is our first hint that, properly interpreted, the board of a business corporation has a fiduciary mandate of the same type as corporate boards in general. This is a mandate not to stockholders, but to "the corporation" and its purposes—that is, to the legal entity that owns all firm property, is party to all contracts and appears in court in its own name, and to the state-authorized purposes of this entity (its "interests").

Perhaps it will be thought that the argument so far places undue emphasis on the duties of the board in what might be seen as an anomalous period after a business corporation is first formed, and that the received view can be applied without problem thereafter. But the difficulties do not end for this view once stock has been issued and shareholders created. Stockholders have perpetual succession, one succeeding the other through sale or gift of stock, without any interruption or diminution of stockholder rights and legal standing. Were stockholders legal beneficiaries, this succession would blatantly violate the rule against designated beneficiaries transferring or selling their legal standing to others. So either this is an enormous and previously unnoticed exception to the general rule, or existing stockholders do not have the legal standing of true beneficiaries. Perpetual succession is, however, consonant with what we expect to see when boards have governance, or purpose, mandates, which "persist over time, despite changes in the membership." This is our second hint that the fiduciary duties of directors are of the same sort as those of members of all other types of corporate boards.

One possible way to sidestep this "objection from perpetual succession" would be to say, that directors owe fiduciary duties not to specific stockholders (whose rights as designated beneficiaries otherwise seem to pass illegitimately from one pair of hands to the next), but to stockholders as a *class*. This is in fact what, at least on the level of metadiscourse, the Delaware Supreme Court currently says of the board's duty, as we will see.[43] But for those who would impose a model of personal fiduciarity upon the corporate board, saying so dodges the bullet only to lose the battle, for it amounts to conceding that directors are purpose fiduciaries rather than personal fiduciaries. In particular, it eliminates the specificity of beneficiaries; and it eliminates their ascertainability, since fiduciary duty to stockholders as a *class* means a duty not only to current but also to future stockholders. (The objection from perpetual succession is not dodged if this is not entailed.) It thus leaves the board once again without fully specified or ascertainable beneficiaries, which means that the board could not be a personal fiduciary. It becomes a purpose fiduciary to a class.

Below I will consider further whether this particularly narrow definition of the board's purpose fiduciarity—a duty to the (presumptively pecuniary) interests of the stockholders as a class—is analytically, historically, or normatively more accurate or better

[43] See pp,?????

than the alternative hinted at above, that the board's duty is to the corporation and its purposes. All that is being established at present is the more general point that corporate boards are purpose fiduciaries rather than personal fiduciaries. So far, the argument rests on two legal facts: that boards, at birth, operate under fiduciary strictures despite the absence of stockholders or other plausible beneficiaries; and that even after stockholders have been brought into being, they are implausibly cast as legal beneficiaries, either on account of their being possessed of legal capacities that exceed what is allowed to true beneficiaries (such as the right to sell their legal standing), or on account of being unspecified and unascertainable as a class. But this is not the end of the difficulties for the notion that stockholders are legal beneficiaries of the board.

2. *Absence of Rights Claims*. Where there is a fiduciary duty to a person (a beneficiary), correlative rights are created and the beneficiary gains an enforceable right claim for the fiduciary's loyalty and care.[44] In contrast, those who may hope to benefit from a charitable trust or other purpose-type fiduciary have no private right of action against the fiduciary.[45] Stockholders traditionally have fallen in the latter camp. They had no legal standing to sue directors.

The derivate suit was developed in the 19th century precisely because of this. It is a workaround that allows wayward directors to be brought to heel through private action, while still upholding the corporate rules on legal standing. In a derivative suit, stockholders sue the corporate entity for its failure to sue the directors for their failure of duty to *it*. (This is our second hint that, on the traditional understanding, the designated legal beneficiary of the directors is not the stockholders, but the corporate entity.) Today, in some jurisdictions,

[44] Miller, *supra* note 13, at 544-47.
[45] Ibid., 529

including Delaware, subsets of stockholders are allowed to sue directors directly for certain kinds of harms (roughly, direct harms to the stockholder, as opposed to harms to the corporation that redound to the stockholders as a whole, in which instance the derivative suit must still be used).[46] In other jurisdictions, however, including New York, Pennsylvania, Maryland, North Carolina, and many others, the traditional rule holds—stockholders have no private right of action against directors, but must use the derivative suit.[47] This strongly suggests the board does not have personal fiduciary duties to stockholders, but is instead a purpose fiduciary.

This raises a question. Who enforces the fiduciary duty of a purpose fiduciary given that the fiduciary lacks specific human beneficiaries (who could enforce it through legal suit)? As Miller and Gold answer, "[f]iduciary accountability under governance-type mandates ... is served by standalone duties that may be enforced by any of a number of persons or entities occupying a monitoring and enforcement role in respect of the mandate".[48] The authors have in mind the oversight that the General Accounting Office has over public bodies, or donors have over charitable foundations. But corporations too have always, at least formally, been overseen to ensure the faithful pursuit of their authorized purposes. This is the function of the "visitor." As far back as the 6th century, monasteries, operating as

[46] "Suits based on breaches of the directors' fiduciary duties of care and loyalty under state law, such as suits based on grossly negligent mismanagement, waste of corporate assets, excessive compensation, usurpation of corporate opportunity, and on general self-dealing, are actionable only as derivate suits. On the other hand, suits for the deprivation of shareholders' voting rights, preemptive rights, or rights to inspect the corporation's books and records, suits to compel the declaration of dividends, and suits alleging that the directors/officers fraudulently induced the shareholder to sell stock, are generally treated as direct actions." Timothy Oliver Brandi, *The Strike Suit: A Common Problem of the Derivative Suit and the Shareholder Class Action*, 98 DICK. L. REV. 355, 360 (1994) (internal citations omitted). That said, skillful plaintiffs can in certain circumstances turn a duty of loyalty violation into a direct action, for example recasting it as an infringement of stockholder voting rights or as a violation of securities law. *Id.* at 360-7.

[47] MICHAEL SMITH & BETHANY REZEK, DIRECTOR FIDUCIARY DUTIES: OWED TO THE CORPORATION OR TO THE SHAREHOLDERS? (King & Spalding Directors Governance Center, Jan. 22, 2014), https://www.kslaw.com/blog-posts/director-fiduciary-duties-owed-corporation-shareholdersmj.

[48] Miller, *supra* note 13, at 554.

proto-corporations, were subject to visitation by their ordinaries (usually the local bishop) to ensure they were fulfilling their purpose of intercessory prayer.[49] By the early modern period, visitation of civil corporations and business corporations was done by the king, which in practice meant figurative visitation by the court of King's Bench during legal suit.[50] And still today, the state attorney general and the courts under him or her (to speak of the American arrangement) have inherited the role of visitor of business corporations.[51] Besides the visitor, stockholders in a derivative suit and in *ultra vires* suits are also authorized by the state to help serve as enforcers of the director's fiduciary duty to the corporation and its authorized purposes. But they never gain any personal restitution from these suits, because they don't have a private right claim. The corporation gains. All of this strongly marks the corporate board as under purpose fiduciarity, not personal fiduciarity.

3. *State Authorization*. In a personal fiduciary relationship, the fiduciary is typically authorized by the beneficiary, although sometimes, where the beneficiary lacks legal capacity (because a minor, for example), the fiduciary may be authorized by a benefactor (including the state). A purpose fiduciary, on the other hand, is never authorized by beneficiaries (since, in the legal sense, it has none), but either by a benefactor (such as the founding donor of a charitable trust) or again by the state (for example, instituting governmental offices and agencies).

This strikes me as the most likely point leading commentators astray, for it has become conventional to view the authority of corporate directors as derived from the stockholders. They are elected by the stockholders, after all. This makes it appear very much

[49] BARBARA ROSENWEIN, NEGOTIATING SPACE: POWER, RESTRAINT, AND PRIVILEGES OF IMMUNITY IN EARLY MEDIEVAL EUROPE 33-36 (1999).

[50] 1 WILLIAM BLACKSTONE, COMMENTARIES ON THE LAWS OF ENGLAND IN FOUR BOOKS 481 (1893).

[51] Roscoe Pound, *Visitatorial Jurisdiction over Corporations in Equity*, 49 HARV. L. REV. 369, 380-88 (1936).

like a principal-agent or private trust relationship, with the stockholders as beneficiaries authorizing the board as agent or trustee to pursue their interests.

While superficially plausible, this is a false account of how directors get their authority. I observe again, that a board is constituted, and directors begin directing, before shares of stock are ever issued. The authority of the board therefore cannot possibly come from the stockholders. Nor do stockholders, once constituted, have the authority to manage the firm directly; and if they do not have this authority, they cannot be said to have delegated it to others. *Nemo dat quod non habet* ("no one can give what he does not have"). The authority to manage the firm is original with the board.[52]

The seeming contradiction between original board authority and stockholder voting rights is dispelled once it is noted that a corporate directorship is an *office* with powers vested therein. In Anglo-American jurisdictions (and in many others), the holders of common stock select those who *occupy* the office of director (after the expiration of the terms of the initial directors). But they do not create the office itself or its powers, nor can they alter its central features. These are created and vested by the state, through means of the corporate charter, and are assumed and exercised before the stockholders even exist.[53] In other words, the authority of the board to control the property of the firm, hire its personnel, declare their duties, and generally manage the affairs of the business, is an authority bestowed upon the board by the state, expressly granted in the text of every corporate charter or general law of incorporation.[54] Among the powers vested in the board by the state is the power of issuing

[52] Cite Delaware corporate law.
[53] *Bank of the United States v. Dandridge*, 25 U.S. (12 Wheat.) 64 (1827), at 113 ("The stockholders impart no authority to [the members of the board] except by electing them as directors…. [T]he authority is given in the charter.")
[54] *See, e.g.*, MODEL BUSINESS CORPORATION ACT §8.01, §3.02. (AM. BAR ASS'N, CORPORATE LAWS COMMITTEE 2005).

shares of stock, up to an authorized amount.[55] This is the clinching point. Directors create the stockholders; stockholders do not create the directors. Most stockholders are legally capable individuals and, if the board were really their agent or trustee, would not need the state as benefactor to intercede and establish the board for them. That directors are nonetheless empowered by the state rather than by supposed stockholder-beneficiaries thus further marks the board as a purpose fiduciary rather than a personal fiduciary.

In other words, what Miller and Gold say of the "public purpose corporation" (such as Amtrak or the United States Post Office, which have no stockholders), I believe to be true of all corporations, including those with stockholders: "…directors of public purpose corporations receive their mandate from the state … through legislative or executive acts whereby the state establishes (a) the corporation; (b) its purposes; (c) the offices through which the corporation will be administered; (d) the powers attached to the corporation and its offices; and (e) other details in respect of corporate governance, reporting, and accountability."[56] A so-called "private" corporation (whether for-profit or non-profit) differs from this only in that the mandate from the state is solicited by private parties (who also propose the corporate purpose), rather than initiated by the state itself.

This reality of the business corporation, which is the reality of all corporations, has been obscured by the labors of corporate attorneys and classical liberal and neoliberal scholars to square the corporation with the principles of free market economics by reducing it to the categories of private property and contract. Specifically, by characterizing the corporation as a form of *partnership* or *trust*, the conceit can be maintained that stockholders "own" the assets of the corporate firm (if not as literal legal

[55] *Id.* § 6.01.
[56] Miller, *supra* note 13, at 550-1.

owners, then at least as "beneficial owners"); that the corporation is, or at least could be, constituted through private contract; that the authority of the board is delegated to it by the stockholders; and that the board is thus the agent or trustee of the stockholders, with fiduciary duties to their persons. So characterized, the corporation appears as a fully private entity, the natural result of entrepreneurs pursuing efficient productive scale in an expansive free market economy.

Unfortunately, every timber of this structure is wormwood. The stockholders do not own the assets of the firm; the legal entity does (stockholders owning rather a financial instrument, namely, stock). The corporation cannot be constituted through private contract, because there is no way contractually to create the separate legal entity, or "person," at its heart[57] (which is why every business corporation ever has needed a charter or its equivalent, which creates this entity and vouchsafes it will be recognized in court). The board, as we will see,[58] gets its authority from the state, not from the stockholders. And, as I argue below, the board is neither the agent nor trustee of the stockholders, but the agent of the corporation itself and fiduciary to it and its purposes. Corporations hail from an age of economic promotionalism, not an age of free markets. They are constituted by the state as special-purpose governments—with mandatory offices, legal personhood, and jurisdictional authority,[59] just like a government—and are then placed in private hands ("franchised"), to be privately financed, staffed, and operated. They are "franchise governments."[60] They are therefore not simply private,

[57] Hansmann, Kraakman and Squire.
[58] Infra pp**.
[59] In the case of corporations, the authority to make by-laws, instituted by vote, not by contract.
[60] David Ciepley, *Beyond Public and Private: Toward a Political Theory of the Corporation*, 107 AM. POL. SCI. REV 139, 151-52; Ciepley, *supra* note 8, at 420-21.

and certainly not "natural" to the marketplace. They are a public-private hybrid, what Lord Hardwicke called a "mixed form," with a "public office" but private financiers.[61] That the position of corporate director is a publicly-constituted office is the key to why directors have the fiduciary duty of government officials. That they are privately financed is the key to why we so readily analogize them with, and confound them with, more fully private associations like partnership and trusts, whose directors exercise personal fiduciarity.

III. Origins and Spread of Purpose Fiduciarity among Early Corporations

The present Part backs up the above analytical arguments with history. It documents that the corporate board, in its origins, was a clear purpose fiduciary. As the above analysis shows, it remains legally situated as such to this day even in for-profit business corporations, and certainly in non-profit corporations. However, circumstances surrounding the emergence of the business corporation in England resulted in there being overlaid upon it a legal "metadiscourse" that for long classed business corporations as a species of joint stock company, or partnership, in which fiduciary duties are to person rather than to purposes. Stockholders were discussed in terms similar to that of partners, as if they were the owners and beneficiaries of the corporation, and the board was discussed as having fiduciary duties to them, as if their legal agents. In a later development, the private trust also became a common metaphor for the relationship of the directors to the stockholders. These analogies never squared with the foundational features of the corporation, which courts continued to enforce—for example, that boards have original jurisdiction and are not simply the legal

[61] The Charitable Corp. V. Sutton (1742), 26 Eng. Rep. 642; 2 Atk 404 (Ch. 1742).

agents of the stockholders, that stockholders can't sue them for failing to enact their will or failing to maximize their benefits as "beneficiaries," and so forth. In practice, boards maintained all the legal features of purpose fiduciaries. But in the reigning theory, they were talked about as personal fiduciaries.

Transformations in business enterprise at the end of the 19th century finally made these legal conceits untenable, and recognition of the underlying governance fiduciarity of corporations began to emerge in progressive era legal thought. However, law-and-economics scholars, concerned about the statist implications of the progressive view, reasserted the partnership conceit after WWII, and it went mainstream in the 1980s. This has caused much intellectual confusion and policy mischief, as it has shaped the norms by which business corporations are governed and even reshaped the penumbra of corporate law, with the consequence that corporate managers have turned their firms away from long-term growth and towards short-term stock price. But the core of corporate law continues to reveal corporations to be purpose fiduciaries, as shown above, and the courts, while significantly swayed by law-and-economics conceits, have not fully abandoned a purpose interpretation, although they have narrowed and misconstrued it.

Christianity, Church property, and fiduciary duty to a purpose

In Europe, it was the Church that first put the corporate form to widespread use, as a way of legally rationalizing its many semi-subordinate, semi-independent bodies.[62] It was a natural fit. The separation between ownership (*dominium*) and control (*iursidictio* and *administratio*) that is at the heart of any corporation, was also at the heart of the Church.

[62] Tierney, *supra* note 3; 3 W. HOLDSWORTH, A HISTORY OF ENGLISH LAW 471 (1923).

Indeed, it was built into the ground floor of Christian (and Jewish) civilization. God created the world and it belonged to Him; Adam was its steward.[63] The early Church institutionalized this archetype by adapting and deploying trust-like legal concepts from Rome (which, as a slave society, and as a patriarchal society with ownership centered in the *paterfamilias*, also pervasively separated ownership and control). Christ, it was said, owned the Church, as *dominus*; but until Christ's return, the pope (or other cleric) was its steward (*dispensator*) and custodian (*custos*).[64]

Beyond its cultural resonance, the denial of clerical ownership served two practical purposes, each essential to the development of the institutional church. It allowed a cleric (and later, a monk) to serve within the increasingly well-endowed Church without feeling himself in violation of Christ's injunction to "sell all that thou hast … and follow me".[65] And it blocked a cleric's heirs (for clerical marriage was not prohibited until the Gregorian Reform in the late 11th century) from appropriating Church property.[66]

With the Edict of Milan in 313, Emperor Constantine not only decriminalized the Church, but gave the Church's figurative separation of ownership and control a proper legal basis, granting the Church a special corporate form, the *Corpus Christianorum*.[67] From a theological vantage point, the Church was still owned by Christ. But from a legal vantage point, Church property could now be owned by a corporate body, or bodies, each conceptualized as a mystical union of local Christians. The sum of the property in these

[63] In line with this, Jewish law expressed the notion that the land ultimately belonged only to God; the holy land was on rent to the Jewish people as stewards. Jewish conceptions of land ownership seem to have provided a model for early Christian conceptions. Shael Herman, *Utilitas Ecclesiae: The Canonical Conception of the Trust*, 70 TUL. L. REV. 2239, 2246 n.16 (1996).

[64] *Id*. at 2244-45.

[65] Matthew 19:21; Mark 10:21.

[66] Herman, *supra* note 42, at 2247 n.16, 2247, 2251-52.

[67] *See id*. at 2256.

bodies was the patrimony of the Church as a whole, with the Church also conceptualized, in the quasi-corporate terms of St. Paul, as the "body of Christ," the mystical union of all Christians, with Christ as its head.

The recovery of the Roman law of corporations in the 11th century revitalized the Church's use of the corporate form, which, after adaptation by canon lawyers, was deployed to reform, and create, a host of corporate bodies—monasteries, nunneries, cathedral chapters, bishoprics, confraternities, universities, and so on—which mushroomed across Europe. As corporations, these artificial bodies could act in law, but only through a legal representative. This gave rise to another legal metaphor describing the relationship of the clergy to the Church. In language that would be applied to medieval corporations in general, the Church, as a (legally incapable) corporate person, was described as being in the legal position of a "perpetual minor," or perpetual ward, never dying yet never coming of age, with the pope as its legally capable guardian and representative (*custos* and *procurator*).[68]

Although the language of guardian and ward suggests personal fiduciarity, the "person" in question was not "natural" but "artificial," with members changing over time. Accordingly, the fiduciarity assumed by the clergy over the Church was not in fact fiduciarity to specific persons, but to purposes. Church property was not to be used for the personal benefit of the cleric, nor for the worldly interests of the laity as legal beneficiaries, but for spiritual ends.[69] In the most common formulation, it was to be managed *ad utilitatem ecclesiae*, "for the advantage of the Church," understood as the

[68] *Id.*; KANTOROWICZ, *supra* note 6, at 374-78.
[69] "[T]he church's spiritual mission imposed upon early churchmen duties that made them trustees centuries before medieval church courts refined the concept of the trust." Herman, *supra* note 42, at 2241.

eternal Church, the trans-temporal community of all believers with Christ as its head.[70] Under this general rubric, property was dedicated to more specific purposes, but always of a spiritual, soteriological nature. Chantries and monasteries, for example, were foundations dedicated to the pious purpose of intercessory prayer. Of course, by intent, natural persons in the "class" of Christians benefited from the soteriological purposes to which the property was put; but they were not the corporation's literal legal beneficiaries. Indeed, as Harold Berman notes, the property of ecclesiastical corporations of all stripes—from monasteries and cathedral chapters, to confraternities and universities—"was always committed to the purposes of the corporation," not to persons.[71]

These purposes were to be pursued until the end of time; and in the corporate form, Church leaders found a vehicle that "never dies" that could carry these purposes, and the property dedicated to these purposes, all the way through that indefinite future. Fiduciarity to purposes was the warp, and corporate devices the woof, from which the institutional church was built. By way of contrast, feudalism and early medieval lordship were built up from personal fiduciarity—homage and fealty—not from purpose fiduciarity.[72]

It is within the Church and its corporate bodies that Europe's understandings and practices of purpose fiduciarity were developed, subsequently spreading to other institutions such as civil corporations and the state. Indeed, the history of the West can be told in terms of the gradual displacement of personal fiduciarity by purpose

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[70] *Id.* at 2247, 2252, 2255. Other identified beneficiaries were "Christ, the meek and poor, the community of faithful" as well as "the eternal church." *Id.*

[71] HAROLD BERMAN, LAW AND REVOLUTION: THE FORMATION OF THE WESTERN LEGAL TRADITION 239 (1983).

[72] The fiduciary ties created by homage and fealty were intensely personal—so much so that if either party to the "contract" died, the heir would need to go through the ceremony again for the relationship to continue. CARL STEPHENSON, MEDIEVAL FEUDALISM 17-19, 24 (1942).

fiduciarity. Feudalism, with its system of personal services, gave way, first, to land leases and basic merchandizing (the "individualist" world of property and contract, although not without its early corporate bodies)[73], and thereafter, to the administrative state, civil society, and the corporate economy (the world of corporately organized institutions).[74] This was a movement not merely "from status to contract" (Maine), but from status, to contract, to organization—which is to say, a movement from personal fiduciarity to purpose fiduciarity. Americans especially tend to think of their society as built on private property. But ours is a society in which the property that matters most—the property of private enterprise, of civil society organizations, and of governments—is overwhelmingly owned, not by natural persons, but by abstract legal entities—corporations and states. These are forms of socialized property, dedicated to a purpose, with fiduciarity to purpose central to their proper functioning.

The following three sections trace the development of purpose fiduciarity within Church corporations, its transfer to civil corporations, and its transfer again to the business corporation specifically. Subsequent sections trace the declension of purpose fiduciarity as an interpretive touchstone of the corporation, the consequences of its considerable if not total displacement by personal fiduciarity to stockholders, and the prospects for reviving purpose fiduciarity within the corporation.

[73] Brenner, MERCHANTS AND REVOLUTION ** (1993).
[74] Tierney 1982; Black, Guilds and Civil Society.

Monastic charters and the purpose clause

Among Church institutions in Europe, the monastery is especially significant as a cradle for corporate fiduciary practices. Monasteries were quasi-corporations even before the 11th century revival of Roman law introduced (or reintroduced) the corporate concept to Europe. A principle of non-alienation of lands was imposed upon them by Church councils already in the 5th century, preventing personal expropriation;[75] and by the 10th century, monastic charters, including that of Cluny, were declaring monastery property to be owned by "St Peter and St. Paul."[76] This clearly separated the property of the monastery from that of natural persons, in what amounted to quasi juridical personhood. Early medieval monasteries also already enjoyed a form of jurisdictional authority, imposing one or another version of the "rule of St. Benedict" upon their members, for example.

The corporate fiduciary practice with which we are presently concerned, to which the monastery made significant contributions, is the corporate charter. Monasteries stood out as unprotected concentrations of wealth dotting the medieval landscape. They relied on others for protection, and to this end secured charters, and endlessly renewed charters, from bishops, popes, and kings, for privileges but also as vouchsafes of their protected status (including against the king himself).[77] Monasteries were thus a leading site for the development of both episcopal and royal charters.

One of the oldest authentic European charters that has come down to us is that of the monastery of Rebais, from the year 625. Of its many noteworthy features, what concerns us here is that already at this early date it contains the kernel of a purpose clause. That purpose,

[75] Rosenwein, *supra* note 33, at 33.
[76] Rosenwein, *supra* note 33, at 157, 166.
[77] [add citation]

seen as of the highest import for the community as a whole and assigned to all monasteries of the era, was to perform intercessory prayer. "[T]he monks ... should enjoy perfect quietness to rejoice guided by God forever, and living under the holy rule and sharing the life of the blessed fathers, should pray more fully to God for the state of the church and the well-being of the King and the fatherland."[78] As this suggests, monks typically had some duties to specific persons, such as to the king (were he understood as a specific person rather than as the occupant of an office). But the overarching duty of the monks was not to specific persons, but to a purpose—to pray for Church and kingdom. The monasteries were manufactories of merits for the Church and the kingdom. Visitation by the diocesan bishop—or, in the "free" monasteries, by the abbot and pope to the exclusion of the bishop—was established to verify that the purpose was being fulfilled.[79]

Although the precise filiations remain to be worked out, it seems very likely that the monastic charters issued by the king were a significant model for the civil charters subsequent issued by the king for civil purposes, and that fiduciary duty to a purpose as expressed in the charter was part of this legacy.[80]

The oldest charter of which the UK government has record (although some few older are known to have been issued) is that of the University of Cambridge, issued by Henry III in 1231 and confirmed by the pope in 1233?…. That university charters were issued by popes as well as by emperors and kings, and sometimes by both, likely facilitated the transfer of the fiduciary practices of ecclesiastical charters to civil charters.

[78] 2 J.M. PARDESSUS, DIPLOMATA, CHARTAE, EPISTOLAE, LEGES 39-41, no. 275 (1849). I thank Albrecht Diem for sharing a copy, with his English translation.
[79] Rosenwein, *supra* note 33, at 33-36.
[80] While Roman law suggested that Roman corporations had received charters, there were no extant Roman examples to look to as models, but plenty of examples from the on-going chartering of monasteries.

[brief excerpt from Cambridge charter here. Still working on the translation from Latin—I'm slow at this!]

At the time of the American founding, the notion of a duty to charter purposes was still alive and well. For example, James Wilson, a leading framer of the American Constitution and a future Supreme Court justice who aspired to be the American Blackstone, noted in his famed *Law Lectures* that every corporation, having been established for specific purposes, has a duty to "fulfil the purposes for which it was formed."[81] This was no mere ethical counsel. If the corporation failed to fulfill this purpose, it was dissolved by the state in a *quo warranto* proceeding. "[I]t is now well settled," wrote Joseph Angell and Samuel Ames in the first American treatise on corporate law, "that it is a tacit condition of a grant of incorporation that the grantees shall act up to the end or design for which they were incorporation … and hence through neglect or abuse of its franchises a corporation may forfeit its charter, as for condition broke, or a breach of trust."[82] What is more, the corporation could not go outside of this purpose. Actions unrelated to this purpose (or outside of any other bounds set in the charter) they were subject to being struck down by the courts as *ultra vires*, "beyond powers" of the corporation.[83] The corporation was to pursue its authorized purpose, and that purpose alone.

[81] Supra, 2 JAMES WILSON, COLLECTED WORKS OF JAMES WILSON 1037 (2007); *see also* BLACKSTONE, *supra* note 34, at I.303.
[82] JOSEPH K. ANGELL & SAMUEL AMES, A TREATISE ON THE LAW OF PRIVATE CORPORATIONS AGGREGATE 510 (1832).
[83] HERBERT HOVENKAMP, ENTERPRISE AND AMERICAN LAW, 1836-1937, at 56-61 (1991).

Origins and duties of the corporate director

Historically, a corporation was constituted for some specific purpose. But being a "juridical person" rather than a natural person, a corporation—whether we conceptualize it as a mystical unity of members or as a purely abstract legal posit—cannot itself act in law, but must act through a legal representative. In the modern corporation, the ultimate legal representative, with plenipotentiary power to act in the corporation's name, is generally a board—a board of trustees or board of directors. Accordingly, it becomes the board's duty—as representative, or guardian, of the corporate ward—to advance the corporation's purposes on its behalf. While ecclesiastical corporations are the place to look for the elaboration in medieval Europe of purpose fiduciarity and corporate purpose clauses, the board structure of the modern business corporation has roots elsewhere, in the medieval civil corporations. To these we now turn to trace the development of directorial duty to the corporation and its purposes.

Before there was the business corporation, there was the merchant guild.[84] This too was a corporation, but of a very different kind. The merchant guild was not a unified business enterprise. The individual merchants traded on their own capital. The merchant guild, rather, was the governing body of the industry as a whole. Its main purposes were, first, to regulate the industry—imposing standards and also protecting the monopoly—and second, to adjudicate disputes among merchants.[85] It was in effect the regulatory agency for the industry and its court system, rolled into one. At a time when the king did not have the

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[84] 1 CHARLES GROSS, THE GILD MERCHANT: A CONTRIBUTION TO BRITISH MUNICIPAL HISTORY 127-9 (1890).
[85] Gross, 32-33 [check].

capacity for such a granular level of governance, he delegated this authority to the merchants themselves by way of a corporate franchise.[86]

Like most medieval and early modern civil corporations, the early merchant guilds were what I call "member corporations." Following the Roman law of corporations, they operated as little republics, at least as a norm. All authority lay with the members, operating by majority vote in assembly. The members controlled the membership, admitting new members or excluding current ones, by vote. The members also typically elected a head—a "governor," "alderman," or "mayor" (from *maior*, meaning "greater")—who undertook quotidian tasks and might represent the corporation in legal suit (although a separate procurator might also be appointed by the members for this).[87]

Evidently for practical reasons of increased size, later guilds established councils. This could well have been in imitation of the medieval free towns and boroughs, which underwent the same development, but earlier, because they reached large size earlier.[88] These were the first corporate boards, and they were granted some of the powers of the general assembly of members.[89] Since the members as a whole still controlled the membership and elected the governor and council (or "assistants"), their primary task

[86] The sovereign's delegation of jurisdictional authority to an incorporated group is comparable to the medieval king's delegation of lordship over a fief to a vassal. In the case of a corporation, jurisdictional authority is delegated to an *artificial* person, and to the members or officers who act in its name, rather than to a natural person. Ciepley, *supra* note 11, at **

[87] Gross, 32-33, 28. This principle of member authority was partly Germanic custom and partly the Roman law of corporations. ANTONY BLACK, GUILDS AND CIVIL SOCIETY IN EUROPEAN POLITICAL THOUGHT FROM THE TWELFTH CENTURY TO THE PRESENT 53-65 (1984).

[88] For details, see Franklin Gevutz, *The Historical and Political Origins of the Corporate Board of Directors*, 33 HOFSTRA L. REV. 89 (2004).

[89] Gewurtz.

appears to have been rule-setting and enforcement, and especially, adjudication of disputes among members.[90]

As a governing body—a legislature, executive, and court—the board naturally had the role of a purpose fiduciary, not a personal fiduciary. The fiduciary duties of officers of these medieval and early modern corporations are not to be discovered in case law or in statute, but in the oaths that all officers swore. Oaths were the fiduciary glue of organizational life and governance throughout the medieval and early modern period. Taking an oath was *de rigeur* before entering upon a corporate ~~n~~ office, or even before becoming a member, with the oath often specified in the charter—as the oath of office of the U.S. president is specified in the U.S. constitutional charter—or at least referenced therein. ~~Shockingly, no scholar writing in the English language over the past century appears to have authored a book-length monograph or even a scholarly article~~ e Scholarship on oaths is scarce, which is indicative of the neglect under which the concept (but not necessarily the practice) of purpose fiduciarity suffers, and I have found no sustained discussion of corporate oaths, despite their obvious relevance to the history of directorial fiduciary duty. ~~outside~~ of the ancient world, ~~which is indicative of the neglect under which the concept (but not necessarily the practice) of purpose fiduciarity suffers.~~ One must go to the primary sources.

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One illustrative example—far from the earliest, but recorded in decipherable English—comes from ~~the records of~~ the transactions of the merchant guild of Dublin (the Guild of the Holy Trinity of the City of Dublin), which record "the forme of the othe [i.e. oath]" as administered to guild officers in 1480:

"Yee shall bee trewe Mastirs vnto the yelde [guild] of the holy trinte of the Cyty of Deweling [Dublin], and ye shall see that all the due rewerence and worship be done to the

[90] Gross, 28; Gewurtz. For a detailed example, *see* ALFRED C. WOOD, HISTORY OF THE LEVANT COMPANY, at 205-228, especially 209 (1964).

Trynnyte …. Allsoo ye shall be goode and trewe mastirs vnto all the brethren that bene [are] marchaunts of the sayd yelde [said guild] and them ye shall mayntayne by yowr powere in all ryghte. Allsoo yow shall duly & trewly mantayne all rulys and ordinauncis, statuttis & lawis thereof and due execucion, and ye shall doo according to the sayde rulis agayns ewerye man according to his offense…. Allsoo all due sembles [assembies] ye shall holden … as nedithe [needed] to the goode rulle and gowernaunt of the sayde yelde … so god yow help and holydome [so god you help at the holy doom]."[91]

The singular emphasis upon good and just government is clear—to be "goode and trewe (or as we would say. caring and loyal) mastirs," first of the corporation (the guild), and also of the individual merchant members, maintaining them in their rights and privileges, and faithfully executing the laws, judging disputes, and convening other organs of government. Duty to augment or maximize the pecuniary gain of the merchants is nowhere mentioned, although of course this was a principal motive of organizing as a guild and something that could be expected to follow from its good governance.

IV. From member corporation to property corporation: rise of the business corp

Important changes would come to the corporate board when Dutch and English merchants set their sights on the lucrative East Indian spice trade. The Dutch were the more successful institutional innovators. Within a span of two decades, the Dutch East India Company (VOC) was transformed into a new kind of corporation with a new kind of board.

The English East India Company (EIC) was an innovation also. But its fusion of the merchant guild with the joint stock company proved an organizational dead end. Consistently outcompeted, the EIC finally copied the VOC model (although with one important change), in a process that began with a new charter in 1657. Yet the English persisted in describing this new type of corporation in the legal vocabulary proper to the

[91] Charles Gross, Gild Merchant ii, 70-1.

merchant guild and joint stock company. This introduced basic confusions into the English language discussion of business corporations, including the proclivity to speak of the stockholders as the "members," owners, and legal beneficiaries of the corporation. These conceits in turn underwrite the doctrine of shareholder primacy. In this place, I can only telegraph the organizational innovations and legal mischaracterizations involved.[92] But even this brief relation will help us understand what is otherwise a great mystery—how the English could have mischaracterized their business corporations from the very outset.

The Dutch East India Company

The VOC, as founded in 1602, was not any kind of corporation, but a kind of legalized cartel among six so-called "pre-companies"—that is, the six merchant partnerships that had begun successfully trading to the Indies at the close of the 16th century. They were "united" at the instigation of the Dutch Estates General, so as to create a coordinated force that, in addition to pursuing profit, could attack Spanish and Portuguese interests in Asia, relieving Spanish and Portuguese pressure on the Dutch homeland. A central board—the Heren XVII—was instituted to set general policy for the six merchant groups (now denominated "chambers" of the company) and to set the sale price of goods upon return.[93] But the VOC lacked separate "juridical personhood." The leading merchants of each of the chambers remained personally responsible for equipping their chamber's fleet and fully liable for all

[92] For a bit more detail, see David Ciepley, *Member Corporations, Property Corporations, and Constitutional Rights*, 11 L. ETHICS HUM. RTS. 31 (2017).

[93] F.S. Gaastra, *The Organization of the VOC, in* THE ARCHIVES OF THE DUTCH EAST INDIA COMPANY (VOC) AND THE LOCAL INSTITUTIONS IN BATAVIA (JAKARTA) 19-20 (G.L. Balk, F. van Dijk & D.J. Kortlang eds., 2007).

debts contracted (with the exception only of the sailors' wages, which were to come out of profits or not at all).[94]

Outside investors could put money into one or another of these individual chambers, on terms that involved two innovations. First, their investment would be locked into the chamber for a period of ten years (rather than only until the return of the fleet), returned to them only upon the company's first scheduled liquidation in 1612.[95] Second, as compensation for this long lock-up period, investors were allowed to sell their shares to any willing buyer, returning liquidity to them. This created the first corporate stock market.[96] However, the investors had no role in selecting the members of the board. This was done by the Dutch Estates General (or by the burgomeisters of the Dutch cities, on permission of the Estates General) from among candidates nominated by the individual chambers.[97]

Over the first two decades of the VOC's operation, a number of changes occurred that had the effect of transforming the VOC into a fully-fledged business corporation. Here I mention only the two most important.

First, the board, with the support of the Dutch States-General, reneged on the planned 1612 liquidation out of fears (surely accurate) that doing so would deprive the company of its hard won (indeed, violently won) positions and fortifications in Asia.[98] The investors' money was locked in indefinitely, creating "permanent capital" for the company. This was an expropriation pure and simple, and the investors howled in protest. They were under no

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[94] Oscar Gelderblom, Abe De Jong, & Joost Jonker, *The Formative Years of the Modern Corporation: The Dutch East India Company VOC, 1602-1623*, 73 J. ECON. HIS. 1055, 1069 (2013).
[95] Neils Steensgaard, *The Dutch East India Company as an Institutional Innovation*, *in* DUTCH CAPITALISM AND WORLD CAPITALISM 246-47 (Maurice Aymard ed., 1982).
[96] NEILS STEENSGAARD, THE ASIAN TRADE REVOLUTION OF THE SEVENTEENTH CENTURY: EAST INDIA COMPANIES AND THE DECLINE OF THE CARAVAN TRADE 128 (1975).
[97] Gaastra, *supra* note 66, at 18.
[98] Gelderblom, *supra* note 67, at 1060-61.

illusions that they remained part "owners" of the company. Their stock certificate was now just a financial instrument, like a bond but with no fixed yield. Their mollification was secured, however, with a massive 162.5% dividend (representing the return of their initial investment (100%) plus ten years of interest at 6.25%, the going rate in Amsterdam).[99]

Second, it turned out that the scale necessary for efficient operation in Asia as a bellicose trader could not be achieved through share subscriptions or retained earnings alone (which were meager until such a scale could be reached). On top of these, it would take massive borrowing—which the chamber directors were unwilling to do while on the hook for the liability. In 1623, the Dutch courts provided the solution by allowing the VOC to issue bonds in its name alone, giving it the status of a separate property-owning and contracting entity—a "juridical person."[100] This was a momentous development for the company, which thereupon rapidly took on debt, increased scale, and achieved a supremacy in the Asia trade never eclipsed until its dissolution in 1800.

This was also a momentous development for the legal form of business. The VOC had, through these improvised institutional innovations, acquired all of the attributes singled out by present-day legal scholars as defining of the modern business corporation: a permanent capital, legal personhood, separation of stockholder and management, limited liability for stockholders and directors, and tradable shares.[101] It was, one could say, the first modern business corporation (although it continued to possess any number of early modern features as well). And it was a business corporation whose stockholders understood they

[99] Steensgaard, 1982, *supra* note 68, at 246, 248.
[100] Gelderblom, *supra* note 67. at 1069-71.
[101] REINER KRAAKMAN, PAUL DAVIES, HENRY HANSMANN, GERARD HERTIG, KLAUS J. HOPT, HIDEKI KANDA & EDWARD B. ROCK, THE ANATOMY OF CORPORATE LAW: A COMPARATIVE AND FUNCTIONAL APPROACH 5-12 (2004).

were neither "members" nor "owners" of the corporation, but simply outside investors. This new form of corporation was not an incorporation of persons (*universitas personarum*), or what I call a "member corporation," but an incorporation of things (*universitas rerum*), what I call a "property corporation."[102]

The English East India Company

The EIC travelled down a very different path, until it abandoned that path and copied the Dutch. Unlike the VOC, the EIC *did* begin as a corporation, but not as a unified business corporation. It was chartered as what was then called a "regulated company"—a merchant guild whose members enjoyed a monopoly on some branch of overseas trade. The members collectively set the rules for use of this monopoly, for the most part through an elected board. But in principle, each merchant traded on his own capital.[103] In this, it was a typical member corporation, with the members establishing a government over themselves as individuals.

However, the costs involved in trade to the Indies were so great that, from the very first[104], members of the guild (not all, and not always the same ones) organized a succession of joint stock companies—a form of partnership—to undertake trading expeditions, selling all assets at the end of each trip and dividing the proceeds, as was customary with merchant partnerships.[105]

[102] Ciepley 2017, *Member Corporations*, *supra* note **. Member corporations, too, incorporated some property, but the focus was on the membership and its privileges.
[103] Charter Granted by Queen Elizabeth to the Governor and Company of Merchants of London, Trading into the East-Indies, *in* CHARTERS RELATING TO THE EAST INDIA COMPANY, 1600-1761 (J. Shaw ed., 1887) [hereinafter Charter].
[104] CALENDAR OF STATE PAPERS, COLONIAL SERIES, EAST INDIES, CHINA AND JAPAN, 1513-1616 (W. Noel Sainsbury ed., 1862), at 102.
[105] K.N. CHAUDHURI, ENGLISH EAST INDIA COMPANY: STUDY OF THE EARLY JOINT-STOCK COMPANY 1600-1640, at 25-57 (1965).

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The results of this arrangement, however, were not happy, with the separate joint stock enterprises undercutting one another in Asia, and with merchants quarreling over the pre-sale valuations and fair divisions of the return goods.[106] The superiority of the revamped VOC was not hard to see, with its cash dividends, accumulating permanent capital, permanent bases, and seemingly permanent dominance over the diminutive English joint stocks.

A new charter in 1657 began the process in which the EIC was enabled to compete with the Dutch company by adopting the form of the Dutch company.[107] The EIC already enjoyed juridical personhood as a regulated company. Now it received it as a permanent unitary enterprise. Capital that previously had been temporarily invested in individual joint stock ventures was now locked in the company permanently, owned by the corporate entity. The employees of individual merchants became the employees of the company. The erstwhile corporate members who, as joint stock partners, had been co-owners of the individual expeditions, became outside investors who owned shares of stock alone. Directors were exempted from liability for company debts, as were stockholders.[108] And shares were made freely tradeable.[109] The EIC was thus transformed from a regulated company with members, to a property corporation with external stockholders. Just like the VOC. Or almost so. The erstwhile members of the guild, who had elected the board, continued to elect the

[106] 2 WILLIAM SCOTT, THE CONSTITUTION AND FINANCE OF ENGLISH, SCOTTISH AND IRISH JOINT-STOCK COMPANIES TO 1720, at 109-10 (1910).
[107] Unfortunately, all copies of the 1657 charter, issued by Cromwell, appear to have been destroyed with the Restoration. But we can infer the changes from subsequent royal charters and from changes in company practice.
[108] The archaic concept that stockholders have "limited" liability is a misnomer once shares of stock are fully paid up at the time of purchase. They are in fact exempted from liability.
[109] Gelderblom, *supra* note 67, at 1051.

new board in their role as stockholders. This made the EIC, unlike the VOC, a stockholder-controlled enterprise. And this would become the Anglo-American norm.

The English Misdescription of the Business Corporation

At this point, several observations are in order. First, the formation and evolution of the EIC involved a radical change in the function of the corporate board. Its function was still that of governance, the authority for which it still received from the state. But the nature of the governance was changed, from a legislative and judicial function to a managerial function.[110] The board still legislated, in the form of by-laws. But its primary task was now to manage the affairs of the business—something it was not originally designed to do and arguably has never done especially well. This transformation to a permanent enterprise, it should be noted, did not significantly change the chartered purpose of the EIC, which was still to trade to Asia and Africa for the increase of the navigation, wealth, and honor of England.[111] But it changed the role of the corporate board in advancing this purpose.

Second, judging from the oath of office, the change in board function was not thought to require reorienting the board's fiduciary duty. The charter of 1600 did not spell out the directors' oath, but what is said about it is enough to make clear that the focus was on the duty to the office rather than to specific persons. Those nominated were to "take a Corporal Oath" (an oath on the Bible) "that they and every one of them shall well and faithfully [yet another formulation of "care and loyalty"] perform their said office … in all things

[110] The change was bigger than for the board of the VOC, since control of company operations was delegated and divided among six semi-autonomous chambers.
[111] Charter, *supra* note 76, at 5.

concerning the same."[112] The oath accompanying the 1661 charter was not spelled out either. But it described the oath in exactly the same words.[113]

A third point to observe, which is of the greatest import, is that the English did not change their legal terminology to reflect the change in corporate form, but retained their existing terminology, however inapt, of "joint stock companies" (although the capital was no longer joint, but unified) and stockholder "proprietors." Why?

Likely, this was facilitated by the gradualism in the transition between forms. The stockholders of the EIC never experienced an overnight expropriation as did the stockholders of the VOC. 1657 is conventionally cited as the birthyear of the EIC remodeled with a permanent joint stock. Yet it was not until September 1661 that the board, in declaring the first dividend, announced the policy that dividends would come only out of profits earned and not in the form of "divisions" of the value of both assets and profits, as had been the practice of terminable joint-stock companies.[114] Only such a change in policy could make the company a permanent joint stock in practice, and its belated announcement shows that the change in mentality from the old to the new form of the company was coming only gradually.

Why didn't the EIC stockholders see this as an expropriation? Perhaps because the charter of 1657 mandated a valuation of the company after seven years, and every three years thereafter, at which time any stockholder could demand the ratable value of his or her portion of the stock subscription, provided that a replacement stockholder could be

[112] *Id*., at 10. It might be wondered if the "office" entailed a duty to maximize shareholder returns. The remainder of the charter discusses many activities that will occupy directors, but nowhere does it mention stockholder returns. These were expected, but were not confused with fiduciary duty.
[113] Citation to 1661 charter, p. 4.
[114] SCOTT, *supra*, note **, at 131-2.

found.[115] In other words, stockholders were entitled to receive, as an alternative to the going market price for their stock (or in the absence of a ready market in the stock), a price based on the book valuation of all assets minus liabilities. This would have helped carry forward the notion that the stockholders were the owners of a portion of the company's assets, even if their claim on these assets no longer derived from legal title, but was episodic and conditional, resting on a charter provision.

When the first valuation came, in 1664, few exercised their right to exit. Annual dividends of 20% were being distributed, a ready market for EIC stock appears to have been on foot, and the stock was trading at or near par value.[116] Under these conditions, there was little reason to avail oneself of the charter provision, and it disappeared from subsequent charters. But the notion of stockholders as the "owners" remained.

V. Conundrums and Confusions

[These first paragraphs just roughed in. They explain the basic problematic that this new form of corporation posed for the court.

On the one hand, the business corporation, in its early history, was a shotgun wedding of two parties with different interests. The state sees something it wants done but doesn't have the capacity or will to do, so it agrees to create a privileged business vehicle—a corporation—dedicated to this purpose, to entice private parties to dedicate their own resources and administrative capacity to the purpose, although with usually with the ultimate motive of gain. So unlike traditional member corporations, in which the purposes of the corporation were also the purposes of the members, in the business corporation, there

[115] *Id*. at 129.
[116] *Id*., at 132.

are cross purposes—the public purpose (originally) and the private purpose. Which would be prioritized?

Secondly, the business corporation generated social relations without precedent. The stockholder was the main puzzle. Received corporate law had been developed over the centuries to handle disputes arising from member corporations, not property corporations. For example, in a university, guild, or other member corporation, "minority oppression" was not an issue that needed to come before the court. When electing a head, or voting on corporate legislation, the majority carried the day, and that was that. If unhappy with the results, one could leave the university or guild. No one was out any money, just out of certain legal privileges. This didn't fit for stockholders

What would the stockholder's rights and duties be with respect to the corporation? With respect to the board? With respect to creditors? With respect to third parties? With respect to each other? Received corporate law provided no answers. So other bodies of law—the private law of partnerships and trusts—was marshalled to fill the breach—sometimes with problematic results.

By and large, the partnership analogy implies stronger participation rights, but weaker fiduciary protections, while the trust analogy implies stronger fiduciary protection, but weaker participation rights.

The Business Corporation as Partnership

The initial tendency was to think of the business corporation as a form of partnership—specifically, a joint stock company, the immediate precursor in England to the full business corporation. The English now distinguished between the "incorporated" joint stock company, and the "unincorporated" joint stock company. But the incorporated version was nonetheless fleshed out with rules of partnership law. The strength of the partnership metaphor in England is borne out by the fact that well into the 19th century, business corporations were generally discussed in textbooks on partnerships, as in the 1860 volume by the English jurist Nathaniel Lindley, *A Treatise on the Law of Partnerships, including its Application to Joint Stock and other Companies*.[117]

English approaches naturally echoed in the United States. But American experience with the chartering of corporations in its first decades was chartering towns, universities, and other non-profits which lacked shareholders. These, not the joint stock company, were the forebears of the American business corporation, which thus was viewed through a more thoroughly corporate lens. It wasn't until after the American Civil War, when classical free market economics enjoyed its heyday, that the partnership conceit became prevalent,[118] partly as part of a generational reaction against "metaphysical" notions such as invisible "bodies politic," and partly as a way to square the corporation with individualist, market concepts of private property and contract. Corporations, wrote the prominent corporate lawyer Victor Morawetz, in his popular corporate law treatise, "are formed by the voluntary association of their members…. Although a corporation is frequently spoken of as a person or unit…the existence of a corporation as an entity, independently of its members, is a fiction; …the rights and duties of an incorporated association are in reality the rights and duties of the persons who compose it, and not of an imaginary being" (Morawetz 1882, 2).

The partnership conception impacted late 19th century corporate law in a number of ways. Corporations were allowed to go outside of their charters with unanimous stockholder

[117] See also examples cited in Ireland.
[118] 2 Morton Horwitz, The Transformation of American Law 90-3 (1992).

asset, as if the charter were just a stockholder contract.[119] Stockholders were given strong rights to examine corporate books, on grounds that these were really *their* books.[120] It also led some to challenge the principle of limited liability for stockholders, on grounds that the same liability rules should apply as for partnership.[121] In many cases, the result was to strengthen stockholder participation rights. But if anything, it led to a weakening of the standards for directorial loyalty and care that protected them. On the assumption that stockholders were active principals, the courts reasoned that they should simply be more careful in selecting their agents.[122]

The Business Corporation as Trust

The private law lens that really shaped directorial fiduciary duty was not that of the partnership, but of the trust. The trust conceit was strong in the 19th century U.S. especially, lasting into WWII—after which it abruptly disappeared.[123]

The trust conceit, too, could be squared with the notion of stockholder proprietorship. In the conceptualization that emerged in the 18th century, legal title to the company's property was vested in the corporation, which held it in trust for the individual stockholders, who held an "equitable interest" in the property. In the language of the English and also the early American courts, "the corporation was the trustee, the shareholders the *cestuis que trust*," or beneficiaries.[124] In the vernacular of English trusts, this made the corporation the legal

[119] Cite.
[120] Jennifer Hill, Visions and Revisions of the Shareholder, 48 Am. J. Comp. L. 39, 44 (2000).
[121] Horwitz supra, at **.
[122] Hill supra, at 43.
[123] Gordon Smith, *The Shareholder Primacy Norm*, 23 J. CORP. L. 277 (1996).
[124] Ireland 1996, 49-50. See also examples in Smith 1998, 301-4.

owner, but the stockholders, as natural persons, could be considered the "beneficial owners" or "equitable owners."

American courts especially[125] turned to the trust metaphor in order to justify drawing on the well-accepted rules of the English trust to resolve the new questions about stockholder-director relations being raised by the corporate form of business.

The conceit that directors are trustees for *corporation* goes back to an English case of 174.[126] But it wasn't until the 1830s that American courts of equity first began entertaining stockholder suits on grounds that directors had violated their fiduciary duties as trustees.[127] This was the beginning of the derivative suit, and its purpose was to enable stockholders to correct director misconduct through the courts when unable to do so through the stockholders' meeting. In essence, it reflected a realization by the courts that the corporate principle of majority rule—now become rule by majority stock owners—needed to be tempered by the trust principle of fair treatment to all, especially as more and more stockholders became corporate outsiders.[128] The utility of the trust analogy was that it imposed justiciable fiduciary duties upon the board, and this allowed the courts to address a range of issues that today would be addressed through more specialized statutory rules—issues such as minority shareholder oppression (treated as a violation of purpose), director

[125] Bert Prunty, Jr., *The Shareholders' Derivative Suit: Notes on its Derivation*, 32 NYU L. REV. 980, 985 (1957).

[126] See the opinion of English Chancellor, Lord Hardwicke, in The Charitable Corp., *supra* note **. Especially important to future American courts for its dictum on this point is the 1817 opinion of Chancellor Kent in *Attorney General v. Utica Ins. Co*. ("the persons who … exercise the corporate power, may, in their character of trustees, be accountable to this court for a fraudulent breach of trust"). Attorney Gen. v. Utica Ins. Co., 2 Johns. Ch. 371, 389 (N.Y. 1817).

[127] Prunty, *supra* note 86; Smith, *supra* note 85 at 307-09. England's Chancery court arguably heard its first stockholder case in 1810, and certainly heard one in 1828, although conventional histories date the practice to *Foss v. Harbottle* (1843). *See* Prunty, *supra* note 86, at 980-82.

[128] Prunty, *supra* note 86, at 986; Smith, *supra* note 85, at 310.

self-interested action (treated as a violation of the duty of loyalty), and director negligence (treated as a violation of the duty of care).

The trust analogy, in other words, was a judicial way station on the road to statutory regulation of this new breed of corporation. No rule of corporate law today relies upon the trust analogy, which is perhaps why it has disappeared from legal discussion. Once either independent common law rules or express statutes against minority oppression, self-interested director action, and director negligence were in force, there was no reason for a court to press the trust metaphor, and good reason not to. Nonetheless, lingering at this particular way station had long term consequences for our understanding of corporations. Specifically, although the trust analogy was embraced by the courts as a means to regulate directors and majority stockholders, the analogy brought in its train a very strong norm of shareholder primacy, because it concomitantly placed the stockholders in the position of legal beneficiaries. Indeed, Gordon Smith argues that it is precisely in these cases that shareholder primacy received its first legal expression.[129]

Minority stockholder oppression cases appear to have led the way. The typical mid-19th century case was a close corporation in which the majority stockholders had elected themselves directors and steered the company's benefits to themselves, with minority stockholders powerless to stop it (and often unable even to exit). This was a clear injustice. Absent statutory law, courts protected minority stockholders from this by invoking a trustee's equal duty to all similarly situated beneficiaries. However, arguing that corporate benefits should be provided to stockholders, and to *all* the stockholders, was most compellingly done

[129] Smith, *supra* note 85, at 306-09.

by pressing the trust metaphor all the way to the floor and declaring the corporation to be *for* the stockholders.

> The corporation itself holds its property as a trust fund for the stockholders who have a joint interest in all its property and effects, and the relation between it and its several members is, for all practical purposes, that of trustee and *cestui que trust* [*i.e.* beneficiary]…. Persons occupying this [community of interest] are under an obligation to make the property or fund productive of the most that can be obtained from it for all who are interested in it; and those who seek to make a profit out of it at the expense of those whose rights in it are the same as their own are unfaithful to the relation they have assumed….[130]

Michigan's court was even more literal about the trust analogy in *Miner v. Belle Isle Ice Co.*, a case in which the majority stockholder appointed himself the company manager, with princely pay. "It is the essence of the trust that it shall be so managed as to produce for each stockholder the best possible returns for his investment. The trustee has so far absorbed all returns."[131]

One important point to be learned from these cases is that the shareholder primacy doctrine began not as a rule prescribing the priority to be accorded different corporate constituencies, as it is construed today (for example, privileging stockholders over workers or consumers), but as a rule coincident to enforcing equal treatment within one constituency, the stockholders.[132] Beyond this, shareholder primacy functioned as ethical counsel, not binding law. Its otherwise revolutionary implications—that stockholders, as trust beneficiaries, might second-guess the business decisions of management in court and sue for damages—was cabined by the courts from the very beginning with the business judgment rule.[133] Nevertheless, norms matter. Just as today, so through most of the 19th century, the

[130] Smith, *supra* note 85, at 313 (quoting Ervin v. Oregon R. & Nav. Co., 27 F. 625, 631-32 (S.D.N.Y. 1886)).
[131] Miner v. Belle Isle Ice Co., 53 N.W. 218 (Mich. 1892).
[132] Smith, *supra* note 85, at 310-20.
[133] *Id.* at 309-10.

strong norm of shareholder primacy went hand-in-hand with an actual business practice of passing along the lion's share of corporate profits to the stockholders.[134]

In addition to midwifing the shareholder primacy doctrine, the trust metaphor flipped the traditional understanding of corporate purpose, from the charter purpose to the investor "purpose." This was possible because the business corporation has an unusual duality. In medieval corporations such as towns, universities, and even guilds, the public purpose ascribed to the corporation roughly corresponded with the purposes and interests of the individual members.[135] In contrast, the business corporation, besides being chartered for a public purpose, is also an investment vehicle, and this can create cross purposes, with the stockholder "members" caring not at all about the corporate purpose, but only about the dividend. In other words, the business corporation is a shotgun wedding between two purposes—the purpose of the state that grants the charter (to advance the public interest) and the purpose of the stockholder who invests (for pecuniary gain).[136] This is in fact the genius of the institution. As Henry Carter Adams summarized in his 1896 President's Address to the American Economic Association, "A corporation … may be defined in the light of history as a body created by law for the purpose of attaining public ends through an appeal to private interests."[137] The corporation, historically, served as an indirect arm of public policy. The trust metaphor, however, contributed to the eclipse of the public purpose—the charter purpose—in favor of the private, pecuniary purpose, when identifying the "purpose" of the corporation.

[134] *Id.* at 298-99.
[135] For example, a primary public purpose of the guild was to uphold product standards, which was also the collective interest of all guild members, to prevent "lemons" from sinking the entire market.
[136] Preferably for ethical pecuniary gain. As Lynn Stout emphasizes, stockholders care about more than just money and overwhelmingly would like their broader ethical values shared by the companies they invest in. LYNN STOUT, THE SHAREHOLDER VALUE MYTH 95-101 (2012).
[137] Henry Carter Adams, *Economics and Jurisprudence*, 2 ECON. STUD. 7, 16 (1897).

A good illustration of this comes from *Miner v. Belle Isle Ice Co.*, quoted above. Acceding to the request of the stockholders, the court put the corporation into receivership. The court begins a summary of its reasoning by enunciating a familiar rule: "[W]hen it turns out that the purposes for which a corporation was formed cannot be attained, it is the duty of the company to wind up its affairs." As previously observed, this rule followed naturally from the directors' duty to the corporation's chartered purpose. The end of the purpose triggers the end of the corporation. But with the corporation construed as a stockholder trust fund, a very different purpose is now in view of the court. In the next sentence of its summary, the court gives no attention to the corporation's chartered purpose—providing ice to the public—but shifts our attention to the purpose of the stockholders in investing in it. "[T]he ultimate object of every ordinary trading corporation is the pecuniary gain of its stockholders; that it is for this purpose, and no other, that the capital has been advanced; and if circumstances have rendered it impossible to continue to carry out the purpose for which it was formed with profit to its stockholders, it is the duty of its managing agents to wind up its affairs." The summary then returns incongruously to the traditional line of reasoning for dissolving a corporation, that the corporation was operating *ultra vires*, "beyond powers" authorized by its charter, as if the chartered purpose had been stockholder profit. "To continue the business of the company under such circumstances would involve both an unauthorized exercise of the corporate franchises and a breach of the charter contract."[138]

At about this same time, purpose clauses were evolving in a direction that would undermine the very idea that corporations are dedicated to public purposes, or even to any concrete purpose at all. Several developments stood behind this. On the one hand, there was

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[138] *Miner*, 53 N.W. at 223.

a conceptual privatization of the corporation over the course of the 19th century, in which the partnership and trust metaphors doubtless played some part and the advent of general incorporation laws an even greater part.[139] Corporations were allowed into an ever-widening circle of activities with ever more tenuous public benefits.[140] This relaxed attitude, when combined with interstate competition for incorporation fees, led to lenient charters with lenient purpose clauses. Increasingly, the chartered "purpose" of a corporation was a long list of allowable lines of business it was authorized to pursue. This transformed the purpose clause from a statement of affirmative duty, to a zone of liberty. And this made it all the more likely that the purpose of the corporation would be associated with stockholder interests rather than with its motley list of allowable activities.

VI. The Business Corporation as Separate Legal Entity

A corporation is clearly neither a partnership nor a trust. A stockholder, for example, is much less than a partner, lacking enforceable rights of ownership over corporate assets as well as lacking rights of direct control, which belong to the board. A stockholder's "control" is indirect at best, in that she gets a vote on the composition of management (the board) and a vote of concurrence on the most major of decisions (such as a merger), whereas in all of these areas a partner receives a veto (since general partnerships operate on the principle of unanimity). And she has no right to corporate profits. Meanwhile, directors are both less and more than trustees. Directors (unlike trustees) lack legal title to the assets they control; but (unlike trustees) they are able to bind contractually their beneficiary, the corporate entity;

[139] Compared to securing a charter by legislative bill, filing papers with a secretary of state's office made incorporation look like a private act of registration, although in reality it was still an act of state creation.
[140] Handlin and Handlin; Seavoy.

and they exercise jurisdictional authority, because unlike a classic trust, a corporation is a government and is used not just for passive property preservation, but active property transformation and expansion.

We've traced the origins of these conceits to the EIC's transition from a series of terminable joint stocks to a unified business corporation, which left the stockholder feeling himself an owner. But we have yet to mention the underlying precondition for these conceits to grab hold and, for so long, hold on. Until there were liquid stock markets—and not just for the shares of a few massive monopolies, but for a broad spectrum of firms—the ownership of shares tended to be long-term and stable. Furthermore, the day-to-day price of these shares was not so clear. Under these conditions, it was possible to imagine that the physical assets of a corporation were tied to specific, identifiable stockholders, and that stock prices reflected the valuation of the firm's assets.[141] To own a share still felt like owning a piece of the company. This made it possible to maintain the partnership and trust conceits.

But once liquid stock markets developed—in England, in the mid-19th century; in the U.S., at century's end—the conceits began to collapse. As Paddy Ireland argues, the fluctuations in stock price were proof that the value of a share was not tied to the value of some underlying set of assets, but was a form of property distinct therefrom, with a price perhaps related to the present value of the company as a "going concern," but in any case not a price representing a "piece" of the firm's assets.[142] The share came to be recognized as a form of property in its own right—a negotiable asset so liquid that it was almost like money—separate from the industrial property of the firm, now recognized as

[141] Ireland 1997, 67.
[142] *Id*., 68-9.

belonging to the corporation itself, not the stockholders. In the U.S., this was largely accomplished by the time of the First World War. "It cannot be too strongly emphasized," wrote one textbook writer in 1919, "that stockholders today are primarily investors and not proprietors."[143]

The same corporate concentration that, in the final years of the 19th century, injected liquidity into the stock market, also sharply centralized corporate management. Prior to this, the nascent corporate economy of the U.S. was, outside of the railroad sector, dominated by small, closely held firms whose stockholders were often also founders, board members, and managers—active participants in the enterprise. This was the backdrop for inroads of the partnership analogy. But the rise of the new industrial Behemoths led courts and state legislatures to clarify that all authority to manage the corporate firm was original with the board. The board did not act as an agent of the stockholders, and it was free to delegate operational authority and legal agency to hired executives. This put a nail in the coffin of the partnership conceit, or so it seemed. Eye-witness to the early stages of this process, Ernst Freund noted in 1897 that "[W]here the whole sum of corporate powers is vested by law directly in a board of directors … such an organization … allows us to see in a large railroad, banking or insurance corporation rather an aggregation of capital than an association of persons."[144] At the dawn of the progressive era, developments in the corporate economy had finally rendered untenable the longstanding fiction that stockholders are the "owners" and "members" of the corporation. The business corporation at last appeared to the Anglophone world as the

143 Quoted in Horwitz, 93.
144 Quoted in Horwitz 1992, 100.

Dutch had created it in the beginning—an incorporation of property alone, a "property corporation," with the property held by an abstract legal entity.[145]

Fiduciary Duty to the Corporation

The rise of a separate entity conception of the corporation significantly impacted the courts' conception of the fiduciary duty of directors. They did not so much change its content, as change its object. The fiduciary duty to the stockholders (understood as trust beneficiaries) reverted to being a fiduciary duty to the corporation itself. In 1932, Berle and Means summarized the reigning law:

> The three main rules of conduct [for a director] which the law has developed are: (1) a decent amount of attention to [the] business; (2) fidelity to the interests of the corporation; (3) at least reasonable business prudence.
>
> In applying these rules a distinction must be taken … between loyalty to the "corporation" and loyalty to the stockholders or security holders…. [T]he corporation is a distinct legal identity, separate and apart from stockholders.
>
> [A]t present, any fair statement of the law would have to be based on the theory that the fiduciary duties of the director were limited to the corporation.[146]

It will be noted that prohibiting director self-interested action and negligence does not require reference to stockholders or any other natural persons.

It will also be noted that, although Progressive Era courts had moved away from extend directorial duties to stockholders, they had not returned to the more rigorous notion of directorial fiduciarity to the corporation *and its chartered purpose*. Because of the

[145] The ground was also well-prepared for that other separate entity conception derived from Otto von Gierke—the corporation understood not as an abstract legal posit, but as a "real entity," a living willing emanation from the associates of the corporation. Set against at the time as near opposites, they were, in broader view, siblings.

[146] ADOLF A. BERLE & GARDINER MEANS, THE MODERN CORPORATION AND PRIVATE PROPERTY 197, 201 (1932).

expansion of corporate purpose clauses noted above, the idea of fiduciary duty to the chartered purpose of the corporation was by this point more or less out of the picture. Nonetheless, what the courts had gravitated to was a far cry from the personal fiduciarity of a trustee to a stockholder-beneficiary. It was fiduciarity to a perpetual legal entity and to the honest and diligent management of its estate so that it might prosper and continue to prosper. It was thus a form of governance fiduciarity, or purpose fiduciarity, although with a very general purpose of building a business rather than a charter purpose of providing a specific kind of service to the public. It carried no implication of stockholders as the legal beneficiaries of corporation, and no implication of stockholder primacy—although again, stockholders could expect to benefit from the directors' duty to the corporation, especially over the long term.

Fiduciary Duty to the Public

It is a misfortune that Berle and Means continued to speak of the stockholders as the "owners" of the corporation despite this being inconsistent with their recognition that the corporation is a separate legal entity. It helped carry the myth of stockholder ownership into the postwar era. Nonetheless, their point of emphasis was that, with the multiplication and geographic dispersion of the stockholders of publicly traded firms, "ownership" had become separated from "control."[147] In other words, just when responsible control of corporations was most needed, as they ballooned into semi-sovereign entities with power comparable to that of nation states, stockholders had become passive—mere rentiers, free from liability and

[147] Berle, *supra* note 109, at 84. This is a case of arriving at the correct conclusion from the wrong premise. The separation of ownership and control is inherent to all corporations because a legal entity owns but relies on natural persons for control. This separation does not wait upon the dispersion of the stockholders. What Berle and Means actually document is the separation of *stockholder* and control.

exercising no responsibility. "By surrendering control and responsibility over the active property," Berle and Means argued, the stockholders had released the community from its obligation to honor their full property rights and had placed "the community in a position to demand that the modern corporation serve not [only] the owners or the control [group] but all society".[148] By the 1930s, the dominant view in legal circles was that directors were trustees for the corporation, but also for the community at large.[149]

VII. Neoliberalism and the Return of the Partnership Conception

This view of the corporation as "quasi-public"[150] was a central target of postwar Chicago neoliberals, who saw in it a stalking horse for increased state intervention in the economy, which they in turn saw as a slippery slope to totalitarianism.[151] Free market economics once again required that the corporation be reduced to market principles. In the University of Chicago economics department, business school, and law school, a contractualist, partnership conception of the corporation was reasserted.

Like Chicago neoliberalism more broadly, the neoliberal view of the corporation began to get traction in the 1970s as stagflation shook confidence in Keynesianism.[152] It was aided by the perduring myth that stockholders "own" the corporation. "In a free-enterprise, private-property system," Milton Friedman averred in a famous *New York Times Magazine*

[148] *Id*. at 312.
[149] Dalia Tsuk Mitchell, Status Bound: The Twentieth Century Evolution of Directors' Liability, 5 NYU J. L. & BUS. 63, 87-88 (2009).
[150] Berle, *supra* note 109, at 305.
[151] Rob Van Horn, *Reinventing monopoly and the Role of Corporations: The Roots of Chicago Law and Economics*, *in* THE ROAD FROM MONT PELERIN: THE MAKING OF THE NEOLIBERAL THOUGHT COLLECTIVE (Philip Mirowski & Dieter Plehwe eds., 2009); David Ciepley, *The Neoliberal Corporation*, *in* OXFORD HANDBOOK OF THE CORPORATION (Forthcoming).
[152] DANIEL RODGERS, THE AGE OF FRACTURE 41-76 (2012).

essay with the combative title "The Social Responsibility of Business is to Increase its Profits,"

> a corporate executive is an employee of the owners of the business. He has direct responsibility to his employers. That responsibility is to conduct the business in accordance with their desires, which generally will be to make as much money as possible….[153]

This put the stockholder back in charge. Which is to say, it reasserted the interests of the rentier class against the Progressive and New Deal emphasis on public responsibilities.

Taking Friedman's broadside as their starting point,[154] Michael Jensen and William Meckling elaborated on this partnership conception in what is easily the most cited and influential article on the corporation since WWII. Although their theory of the corporate firm is generally referred to as the "nexus of contracts" theory, because of their opening statements to this effect, the organizing principle of their theory is the partnership principle that "[T]he relationship between the stockholders and manager of a corporation fit [*sic*] the definition of a pure agency relationship."[155] Of course, as a statement of law, this is wildly inaccurate. As a normative statement, it is highly contestable. Nonetheless, the bulk of their analysis is about the "agency costs" that self-interested (i.e. faithless) managers impose upon stockholders, the rightful beneficiaries of the firm.

[Add Jensen and Murphy on shifting CEO pay to stock]

[remainder of this section just roughed in]

Earlier I noted that the partnership analogy generally implies strong participation rights, but weaker fiduciary protections, while the trust analogy implies strong fiduciary

[153] Milton Friedman, *The Social Responsibility of Business Is to Increase Its Profits*, N.Y. TIMES MAGAZINE, Sept. 13, 1970, at 32.

[154] Fourcade

[155] Jensen, *supra* note 10, at 309.

protection, but weaker participation rights. It is therefore striking to see that, in recent decades, the position of stockholders has been strengthened in *both* participation rights and fiduciary protection, by virtue of a favorable distribution of the partnership and trust analogies across business and judicial opinion. In the arena of business opinion, which impacts board practices and government legislation, the partnership analogy of the Chicago School has held sway, leading to a strengthening of the stockholder's hand in the boardroom. Meanwhile, on the court, which imparts fiduciary protections, the view of the board as a special form of stockholder trustee holds sway, and the stockholder's fiduciary protection has been strengthened. What the two distinct figurations share is support for shareholder primacy.

Inroads in business practice

Under its ideology of shareholder primacy, reforms have been put in place that:

* expand the number and influence of independent directors
* separate chairman and CEO positions
* facilitate a market for corporate control
* pay executives in stock and stock options

Substituting personal fiduciarity for purpose fiduciarity, in an organizational architecture designed around purpose, expectedly sends it into dysfunction. The main point of the corporate form is to dedicate property to a purpose for the long term. Becomes impossible under neoliberal governance.

The result is a focus on short-term stockholder interests that is much sharper than anything the Delaware court mandates. And it has brought with it all the familiar dysfunctions of short-termism. Instead of investing profits in plant expansion, or research and development, or worker training, or increased wages, investments are cut, jobs are deskilled and exported, so that profits can be "disgorged" to stockholders in the form of dividends and stock buybacks (which boost the stock price).[156] Buybacks now consume on average over 50% of the profits of S&P 500 firms. In any given year, the buybacks of some companies top 100%.[157] In other words, the companies spend more on repurchasing their stock than they earn for the year, with the difference made up by cutting into reserves, taking on debt, or selling off assets. This is "vampire management," in which current, accumulated, and future value is sucked out of firm for the benefit of current stockholders.[158] Of course, top executives are among the major stockholders, with over 80% of the pay of Fortune 500 CEOs now coming from stock and stock options.[159] This buys their commitment to raising the stock price in the near-term regardless of its damage to the long-term. The change in the distribution of corporate revenue effected by shareholder primacy, from workers to stockholders, is one of the major sources of the dramatic increase in economic inequality in the United States in recent decades.

[Will add a paragraph on inequality and a paragraph on workers.]

[156] William Lazonick, *Profits Without Prosperity*, 92 HARV. BUS. REV. 46 (2014).
[157] *Id.*
[158] David Ciepley, *The Corporate Contradictions of Neoliberalism*, 1 AM. AFFAIRS 34 (2017).
[159] Lazonick, *supra* note 127.

VIII. The Delaware Court Responds

The members of the court, and its Chief Justice Strine preeminently,[160] are aware of the pathologies of corporate short-termism. And they have resisted much of the Chicago reinterpretation of the corporation. For example, the court certainly has not begun treating the Board as the literal legal agent of the stockholders, at all times dismissible and barred from subdelegation. Nonetheless, the Delaware Supreme Court has not been immune to the general tide and has drifted in a more stockholder-centric direction. The noteworthy shift has been, not in the area of agency law, but in the understanding of the board's fiduciary duty.

One thing the court has not done and hardly could do is refocus attention on the charter purposes of corporations. As discussed above, on the traditional understanding, directors have a duty to realize the purpose of the corporation—its declared activity as expressed in its charter. But after WWII, state legislatures finished the process of emptying out the corporate purpose clause. General incorporation statutes were revised to allow incorporators to fill out the purpose clause in their certificate of incorporation with "any lawful purpose."[161] Of course, having a duty to pursue "anything lawful" makes little sense. The notion that directors have a fiduciary duty to specific chartered purposes was lost.

The obvious intent of this liberalization of the purpose clause was to free management to shift into whatever line of business would be best for the future of the company as a going concern. This was entirely consistent with the reigning notion that the duty of the directors

[160] Leo E. Strine, *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(2010).
[161] Michael Schaeftler, *The Purpose Clause in the Certificate of Incorporation: A Clause in Search of a Purpose*, 58 ST. JOHN'S L. REV. 476, 482-83 (1984).

is to "the corporation." Under the influence of Chicago theory, however, the Delaware court began to expand the scope of directorial duty to "the corporation and its shareholders."

This, it is worth noting, is an anomalous formula. The United States is exceptional in extending directorial duty to stockholders,[162] and even in the U.S. the practice is far from universal, with many state jurisdictions, including New York, Pennsylvania, North Carolina, and Maryland, persisting in holding that directors have duties to the corporation alone and not to stockholders.[163]

There is good reason for this rarity. While it is possible to balance the interests of multiple parties[164]—and this is surely what corporate management must do to run a company successfully, and thus may be thought of as part of their fiduciary duty to the corporation—it is not possible, in the view of most commentators, to have a *fiduciary duty* to multiple parties. Unlike its parent principle, equity, fiduciary duty includes a duty of loyalty. And it is a dictum of ancient pedigree and common reason that one cannot be loyal to two masters, at least if there is any possibility of a divergence between their interests, as loyalty to one is then disloyalty to the other.[165] And certainly the interests of stockholders (who typically push for such things as high dividends and stock repurchases—the latter even, or especially, during moments of peak stock price, when it is most damaging to the balance sheet of the corporate firm, though most likely to push the stock price to new heights[166]) can conflict with the interests of the corporation (chartered as a perpetually-lived entity with, therefore, at minimum, an interest in sound finances and avoidance of bankruptcy).[167]

[162] Asaf Raz, 290.
[163] Smith, *supra* note 31.
[164] Stout and Belafonti
[165] Asaf Raz.
[166] Lazonick.
[167] Cite University of Colorado guy.

Harming the long term prosperity of a corporate firm for the pecuniary benefit of current stockholders ought to be viewed as a breach of the directors' fiduciary duty to the corporation (even though there would be no one to enforce it other than the visitor—the state attorney general and the courts—which means that, given the business judgement rule, it would only be prosecuted in extreme cases). Unfortunately, the Delaware court has been resolving the tension between the interests of the corporation and its stockholders in the other direction, eliding the interest of the corporation with the interest of the stockholders, until the interest of the stockholders stands alone as the object to which the board has fiduciary duties. In this way, the court has come around to shareholder primacy, but not on the ground that directors are agents of the stockholders (the partnership analogy of the Chicago School) but on the ground that they are their fiduciaries (the trust analogy).

The prestidigitation that reduces the corporation's interest to that of its stockholders is well illustrated by William Allen, who, as Chancellor of Delaware's Court of Chancery, summarized the Court's position after its landmark decision in *Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc*. (1986).[168] Allen begins with what he describes as the non-controversial position that directors have a dual fiduciary duty to "the corporation and to the shareholders" (although as we have seen, it is anything but non-controversial outside of the Delaware courts). But within the space of a single paragraph, Allen shifts the referent of "corporation" until it is conflated with the shareholders, leaving only a duty to them:

> I take it as non-controversial that, under established and conventional conceptions, directors owe duties of loyalty to the corporation and to the shareholders; that this conjunctive expression is not usually problematic because the interests of the shareholders as a class are seen as congruent with those of the corporation in the long run; that directors, in managing the business and affairs of the corporation, may find it prudent (and are authorized) to make decisions that are expected to promote corporate (and shareholder) long run interests, even if short run share value can be expected to be

[168] Revlon, Inc. v. Macandrews & Forbes Holdings, Inc., 506 A.2d 173 (Del. 1986).

> negatively affected, and thus directors in pursuit of long run corporate (and shareholder) value may be sensitive to the claims of other "corporate constituencies." Thus, broadly, directors may be said to owe a duty to shareholders as a class to manage the corporation within the law, with due care and in a way intended to maximize the long run interests of shareholders.[169]

The former Chancellor and current Chief Justice of the Delaware Supreme Court, Leo Strine, Jr., cites this passage approvingly as perfectly capturing the court's reigning understanding.[170] It is worth underscoring that this is not a doctrine of *personal* fiduciarity to stockholders. Rather, the current court attributes to the board a form of narrow purpose fiduciarity, to the long-run pecuniary interests of the stockholders as a class. This subtly sets off the court's use of the trust analogy from its 19th-century use. The corporation is like a so-called "public trust" with indefinite beneficiaries (the ever-changing members of a defined class) rather than like a private trust with specific beneficiaries. Yet this "public trust" has the purpose, not of charity, but of private profit!

The sharpest recent statement of this new fiduciary form of shareholder primacy comes from *eBay v. Newmark*,[171] which among other things voided a "poison pill" provision that Newmark and Buckmaster, the defendant directors of Craigslist, implemented to preserve (they argued) Craigslist's culture of providing a public service rather than maximizing profit, against the monetizing agenda of eBay, a minority stockholder. The court disallowed the provision because its aim was not a "proper *corporate* purpose."[172] Not everything pursued by a corporation need have an immediate payoff to stockholders, the Court reiterated, and the business judgment rule leaves

[169] TW Services Inc. v. SWT Acquisition Corp., 14 DEL. J. CORP. L. 1169 (Del. Ch. 1989).
[170] Leo E. Strine, *The Dangers of Denial: The Need for a Clear-Eyed Understanding of the Power and Accountability Structure Established by the Delaware General Corporation Law*, 50 WAKE FOREST L. REV. 761, 772 (2015).
[171] eBay Domestic Holdings, Inc. v. Newmark, 16 A.3d 1 (Del. Ch. 2010).
[172] *eBay, supra* note ??? at 34.

directors wide latitude in determining what eventually will.[173] But the business judgment rule does not protect policies that carry *no* intent of such a payoff. "I cannot accept as valid … a corporate policy that specifically, clearly, and admittedly seeks *not* to maximize the economic value of a for-profit Delaware corporation for the benefit of its stockholders…."[174] "Promoting, protecting, or pursuing non-stockholder considerations must lead at some point to value for stockholders."[175]

> Having chosen a for-profit corporate form, the craigslist directors are bound by the fiduciary duties and standards that accompany that form. Those standards include acting to promote the value of the corporation for the benefit of its stockholders. The "Inc." after the company name has to mean at least that.[176]

This carries us oceans away from the court's historical focus of keeping the corporation to its chartered purpose. It ostensibly shifts all consideration to stockholder purposes, as in *Verplanck*. But in actuality, it ignores even this. The commitment of a majority of stockholders—indeed, in principle, even the commitment of *all* of the stockholders—to purposes other than profit maximization, is of no matter to the court, which insists that the duty of all Delaware corporate directors is to run their companies so as to maximize stockholder profit.[177] This is the flipside of viewing directors as trustees for indefinite rather than definite beneficiaries. On the one side, this allows directors legally to ignore

[173] *Id.* at 33.
[174] *Id.* at 34.
[175] *Id.* at 33.
[176] *Id.* at 34.
[177] Although, as the court notes, if *all* stockholders are committed to ends other than profit maximization, "then there would be no one to object." *Id.*

the wish of current stockholders for immediate payouts. But on the obverse, it allows courts to ignore the wish of stockholders for anything *other* than payouts. This gives the lie to the notion that Delaware corporate law is, as far as practicable, an "enabling" law malleable to the wishes of company founders and participants. Advocates of such an approach, Frank Easterbook and Daniel Fishel, aptly respond that, if a corporation is founded with a mission of social benefit, "who cares?" So long as all investors are fully informed of the mission at the outset, "no one should be allowed to object."[178] This is also the response of those (such as the present author) who accept that corporate law should be more demanding than an enabling law, but who would ideally place a purpose, or "mission," at the center of directorial duty.

The new stockholder straightjacket that the court has placed upon Delaware corporations was a catalyst for the founding of B Lab and its crafting of a corporate vehicle—the benefit corporation, or B Corp—that protects the pursuit of socially beneficial purposes, even at the sacrifice of shareholder profit maximization.[179] In earlier times, this vehicle would have been, and still ought to be, redundant. But ironically, Chief Justice Strine now cites the advent of the Benefit Corporation as evidence that the conventional Delaware C Corporation is properly available for shareholder profit

[178] Frank H. Easterbrook and Daniel R. Fischel, THE ECONOMIC STRUCTURE OF CORPORATE LAW 1, 36 (1991). [quoted in Boatright infra, at 61.] It would of course be reasonable for the minority stockholders of a closely held corporation with restrictions on share transfer to receive equitable relief should the directors and majority stockholders unexpectedly *change* policy, from long-term profit maximization to, say, break-even operations in the pursuit of public benefits, as this change would violate reasonable expectations of the stockholders who had already purchased their shares. This might entail requiring the majority to buy out the dissenting minority before the policy change can be put into effect. However, it is neither necessary nor proper to start assigning a fiduciary to the stockholders when equity is sufficient to achieve this result. As for stockholders in publicly traded corporations undergoing such a policy shift, they should, if unhappy, sell their shares. For companies that make clear their priorities at the outset, say, in articles of incorporation or by-laws, there is no grounds for relief at all.

[179] Alyssa Harriman, THE MAKING OF A MOVEMENT: THE RISE OF THE B CORP ON THE GLOBAL STAGE at 18-19 (2015) http://academiab.org/wp-content/uploads/2015/10/Thesis-FINAL.pdf

maximization only.[180] This is an extraordinary restriction on the utility of the conventional corporation (which, in the 19th century especially, was once used for everything from consumer coops[181] to public goods provision,[182] often under profit *minimizing* policies). Indeed, it is an inversion of the original democratic rationale for corporations. The original policy reason for making the corporate form available to for-profit enterprises was to recruit private capital and organizational capacity for publicly beneficial purposes, and it was made available *only* for such purposes … which purposes are now declared by the Delaware Court to be *improper* for corporations.

Put another way, on the original understanding, the public benefit was the dog that wagged the stockholder tail. Stockholders bought shares if they thought that the incorporated pursuit of the public benefit would bring good profit (or, alternatively, because they felt it their responsibility to support it even if it *didn't* bring profit). On today's understanding, in contrast, only a happy coincidence of public benefits with profit maximization allows the conventional corporation legitimately to pursue public utility. Indeed, if duty really requires *maximizing* profits, then, whenever a publicly beneficial purposes is not the most profitable of available purposes, it is really only the latitude afforded by the business judgment rule that allows it to be pursued, and only by way of forcing the publicly-motivated entrepreneur to feign that their business activity is really all about maximizing value for stockholders, at least "in the long run." This is certainly an extraordinary fate for an institution authorized by the public authority of a democracy: that it should be bound by (judicially-imposed) duty to forgo the pursuit of benefits to the public except as these are coincident with maximizing

[180] Strine, supra note 168, at …
[181] Hansmann and Pargendler
[182] Roy, Socializing Capital.

pecuniary returns for its least knowledgeable, least responsible, least committed, least contributing participants, including even when this is against the wishes of these participants themselves.

An odd new argument for shareholder primacy: the argument from shareholder power

Chief Justice Strine has recently waded into this dispute with a new argument in support of the primacy of stockholders in Delaware corporate law. Strine is well aware of the damage being caused by directorial fixation on the pecuniary interests of short-term stockholders, and he second's Allen's emphasis that boards are not obliged to maximize stockholder value in the short term.[183] But as for shareholder primacy itself, he accuses Lynn Stout and other critics of wishful thinking.

> [T]he contention that … directors are free to promote interests other than those of stockholders ignores the many ways in which the DGCL [Delaware General Corporation Law] focuses corporate managers on stockholder welfare by

[183] Strine *supra* note 168 at **, citing *Paramount Communications, Inc. v. Time Incorporated*, TW, 571 A.2d 1140, 1150 (Del.1989) ("[A]bsent a limited set of circumstances as defined under Revlon, a board of directors, while always required to act in an informed manner, is not under any per se duty to maximize shareholder value in the short term, even in the context of a takeover."); *Air Products and Chemicals, Inc. v. Airgas, Inc.*, 16 A.3d 48, 112 (Del. Ch. 2011) ("When a company is not in Revlon mode, a board of directors is not under any per se duty to maximize shareholder value in the short term. . . .") (internal quotation omitted).

> allocating power only to a single constituency, the stockholders.[184] (6).

> [O]nly stockholders can bring derivative actions. In addition, only stockholders have the right to vote for directors, to approve certificate amendments, to amend the bylaws, and to vote on important transactions such as mergers. In sum, under Delaware corporation law, no constituency other than stockholders is given any power.[185] (30).

Therefore, Strine infers, the legislature must have intended the corporation to cater solely to stockholder interests. And this must be the fiduciary duty of the board. It would be "an aggressive act of hubris" for the court to condone management pursuing any other end.[186] (30).

This inference is unfounded. There is no question that stockholders have a legitimate interest in the good government of the corporation, including its profitable government unless other priorities have been pre-advertised. This interest is primarily protected by the market in shares itself—stockholders are free to sell their shares, and this puts pressure on management to maintain a strong performance on profits and dividends. By the usual reasoning of market enthusiasts, this should be a sufficient discipline of management—market discipline. But even beyond this, Delaware protects the stockholder's interest by according stockholders certain statutory powers, as enumerated by Strine. And the law protects them indirectly in

[184] Strine *supra* note 168 at **
[185] Strine *supra* note 168 at **
[186] Strine *supra* note 168 at **

yet other ways, for example, with corporate auditing and disclosure requirements (which provide stockholders with reasonably reliable information on a company's financial condition), by prohibiting insider trading (which gives unfair advantage to corporate insiders), and by prohibiting director self-dealing (which generally raises corporate costs, to the likely ultimate detriment of the stockholders). Stockholders in the U.S. are a very well-protected constituency.

But it does not follow from all of these powers and protections that, on top of all this, directors have a fiduciary duty to them. Indeed, these powers and protections could as easily be treated as evidence *against* it—as being means by which stockholders are enabled to maintain their interest against boards that do *not* have a fiduciary duty to them (or interests wholly aligned with them). On this interpretation, directorial duty is instead aimed at the parties who are powerless—the corporation (the ward that cannot act on its own behalf) and its publicly-authorized purpose. These are otherwise unprotected. But placed within the director's fiduciary duty, they receive protection from the inherent strength of the duty itself, from the visitor (an institution Strine fails to mention, although he is part of it), and from the derivative suit. Protecting the powerless is, after all, the classic rationale for imposing fiduciary duties. Viewing the director's duty this way allows us to see corporate law as a balancing act. A fiduciary duty to the corporation and its purpose protects both the corporation and the public's interest in its work. If the corporation flourishes, stockholders will of course benefit also, especially in the long run (which is the perspective the corporation is chartered to take[187]). But on top of this, the

[187] Cite University of Colorado Law School guy.

stockholders are empowered—but not overly empowered (although perhaps too much empowered in recent years)—to make extra sure that a goodly portion of the revenue comes to them rather than all of it remain with the corporation or flow to management.

What is certain is that the line of reasoning Strine proposes cannot stand. The whole *point* of imposing fiduciary duties is to direct action toward ends other than where the power structure might take things if left to its own discretion. It is thus perverse to propose that we read off the duties of an office holder, including a director, from the structure of power. This is precisely what one should *not* do. Do judges have fiduciary duties to, and only to, the executive who appoints them? Or bishops to and only to the pope? Or kings to and only to their dead father, from whom all their powers derive?

Nor need one go outside the world of corporations to see the fallacy of this approach. Among non-profit corporations, many universities, charities, environmental organizations, and so forth, have co-optive boards. All power over the board members lies with the board members themselves. Does this mean the board has a duty only to the interests of its own members? This is of course absurd. Board members are precisely *not* supposed to pursue their own interests, even though, in such cases, they are the only ones "given any power." The board instead is supposed to pursue the corporate purpose. This, I contend, is also how we ought to understand the fiduciary duties of the for-profit corporate board.[188]

[188] Against my line of criticism, one might emphasize instead the continued weakness of the stockholders—that they are empowered, but insufficiently empowered, to achieve their objectives, so need fiduciary duties placed on directors to bolster their goal attainment. But this presupposes what needs to be proved—that the corporation is all about the stockholders, and that the fiduciary duty of

Following Strine's method of analysis, those in most need of fiduciary protection—the powerless—would be *excluded* from protection, precisely on grounds of their lack of power. Only those with at least *some* power would be marked as intended beneficiaries of the state or settlor. Children could not be the object of fiduciary duties, for lack of power. Purposes could not be the object of fiduciary duties, for lack of power. Applied in pure form, it would mean there could only be duties to the powerful, emptying fiduciarity of meaning.

Indeed, Strine's method of analysis would thwart the Delaware Court's effort to protect managements that focus on the long term. The Court holds that the fiduciary duty of the directors is "to maximize the long run interests of shareholders," not necessarily their short run interests. This is defended on grounds that the directors' duty is to "shareholders as a class," [189] rather than to current shareholders only. That is to say, the defense rests on including *future* stockholders within the directors' duty. But future stockholders obviously have no present power under Delaware corporate law. So if lack of power is grounds for exclusion from directorial duty, then Strine's method would have directors considering the interests of current stockholders alone, and the most powerful at that—the big institutional investors with their short term time horizons—with all of the pathologies that accompany this.

Earlier I noted that the partnership analogy generally implies strong participation rights, but weaker fiduciary protections, while the trust analogy implies strong fiduciary

directors is therefore to them. If this were Delaware's intent, it would be far more straightforward for the legislature to add additional power to the stockholders—for example, making the board their literal agent, or allowing stockholders to vote their own dividends—than leave it to the judiciary to create a fiduciary duty to them.

[189] TW Services Inc., *supra* note 148, at 1169.

protection, but weaker participation rights. It is therefore striking to see that, in recent decades, the position of stockholders has been strengthened in *both* participation rights and fiduciary protection, by virtue of a favorable distribution of the partnership and trust analogies across business and judicial opinion. In the arena of business opinion, which impacts board practices and government legislation, the partnership analogy of the Chicago School has held sway, leading to a strengthening of the stockholder's hand in the boardroom. Meanwhile, on the court, which imparts fiduciary protections, the view of the board as a special form of stockholder trustee holds sway, and the stockholder's fiduciary protection has been strengthened. What the two distinct figurations share is support for shareholder primacy.

Summary

The corporate board of directors was designed for purpose fiduciarity, with its officers operating under many of the same procedures and protections of the officers of constitutional republics (including operating under a written constitution and regular elections, while enjoying exemption from the second-guessing of courts and constituents, and exemption from liability for one's actions so long as legal). Originally designed as a legislative and judicial body for *member* corporations, it was repurposed in the era of the great trading companies as a managerial body for a new kind of *property* corporation, the for-profit enterprise.

Unfortunately, English corporate law got off on the wrong foot when it placed this Dutch innovation—the for-profit business corporation—under a more familiar pair of legal constructions that separately and in conjunction were inadequate to their object, and that were also mutually contradictory. That is, they described the business corporation as a joint stock company (a form of partnership), or as a trust.

Predictably, subjecting outside investors—the stockholders—to the inherited majoritarian rules of member corporations could lead to instances of minority oppression. Rather than looking to statutory investor protections, or making novel equity interventions, judges creatively addressed this injustice by superimposing the English trust upon the corporation for the sake of borrowing the trust's fiduciary rules.

A more proper legal construction for addressing minority stockholder oppression (if not willing to wait on statutory relief) would have been to continue treating the board as a guardian—and not a guardian for the stockholders, but for the corporation. This is more proper because guardians (like corporate directors but unlike trustees) do not hold legal title to the property they control. The legal title rests with the ward (in this case, the corporation), and this accurately captures corporate reality. This done, equity jurisdiction could have been used (after all, by invoking the trust conceit, it was already being used) to grant equitable relief either from the directors, or alternatively from the *corporation* (with directors seen as having acted on the corporation's behalf), or alternatively, to have appealed to the duties of equity that stockholders owe one another. Using the trust construction in lieu of these other options not only reinforced the notion of stockholder ownership, but introduced new perturbations into Anglo corporate law. Specifically, it recast the board from a purpose fiduciary to a personal fiduciary, and it birthed "shareholder primacy." (The guardianship construction avoids both of these, because the ward—the perpetual corporation—is not a natural person or set of specific natural persons. A guardian board remains a fiduciary to the corporate purpose.)

Judges then pushed the trust analogy deeper into the corporation by using it also to correct director self-interested action and negligence. But again, this was unnecessary. The protection against director self-interested action and negligence is just as strong if treated as a violation of directorial duty to the corporation, rather than to the stockholders, as it is in most other jurisdictions.

At the end of the 19th century, recognition of the share as an autonomous form of property, psychically connected to but legally separate from a corporation's assets, allowed Anglo legal thought really for the first time to see the property of the corporate firm as owned by an abstract legal entity, the corporation proper. But by the early 20th century, corporate purpose clauses were too far gone to recapture the notion of director fiduciarity to chartered purposes. Fiduciarity to "the corporation" was, however, a passable fallback position—a kind of purpose fiduciarity to the long-term flourishing of the enterprise, in whatever specific line of activity management sets. But Chicago neoliberalism was successful at reasserting a partnership conception of the firm, as well as shareholder primacy, while the Delaware court has embraced a conception of the corporation (in deed if not in word), as a privatized public trust, seconding the doctrine of shareholder primacy.

IX. Reclaiming the Corporate Law We Need

As shown in Part II, directors remain in the structural position of purpose fiduciaries, not personal fiduciaries. But the emptying of the purpose clause has attenuated its meaning, and free market ideology has obscured it further. Yet the personal fiduciarity that market defenders have asserted in its stead has only produced corporate dysfunction. Is there anything to be done to change the lens through which we view business corporations, to see them more clearly as purpose fiduciaries with purposes beyond stockholder interests, and to bring the norms governing boards into line with this? There are constructive roles to be played by academics, courts, corporate leaders, and legislatures.

The logical first step is already happening, in the work of legal scholars and others rebutting the most fundamental fallacy in this field, which is that stockholders "own" the corporation, or are their "residual claimants," and should therefore be run in their interests primarily or even alone.[190] This is the Chicago School view that has inspired most of the changes to executive pay, board rules, and tax law, that have encouraged management's reorientation to the short-term stockholder.[191] Clearing away this fallacy is the precondition for undoing this regime—and for imagining new ones.

A second step would be for the Delaware court to drop the directorial duty to stockholders that they have conjured up. Because of the business judgment rule, it is admittedly legally sterile in most circumstances (that is, outside the context of merger or sale of the company). Yet it is ideologically potent and counter-productive, suggesting that the only legitimate constituency of a corporation is its stockholders (not its customers, its workers, its business partners, or the broader public), and that the only ultimate end it may pursue is stockholder enrichment (and not building a world-class company, creating good jobs, or changing the world for the better). Court affirmation of the idea that directors have a duty to maximize shareholder wealth, while it is *permissive* of a long-run approach, is more likely to condone boards catering to the pecuniary interests of their most powerful stockholders (who are usually short-term focused), to the detriment of the firm, the long-term

[190] See preeminently Stout 2012.
[191] Other contributing factors have been structural, such as the rise of big institutional investors. These structural factors are outside the scope of the present paper.

stockholders, and all other constituencies. Stockholders are well-protected without it. They have the disciplining power of a thick stock market. They have electoral power. They have the protection of numerous statutes and agency regulations. And, most to the point, the rules against self-interested director action and director negligence are fully operative even when there is no directorial duty to stockholders. Rather than the court's mandate of stockholder wealth maximization providing extra protection, long-term stockholders and stakeholders would likely do better if the corporation were once again seen as providing benefits to natural persons incident to its pursuit of its corporate purpose, and then to make a judgment, before associating with a specific corporation, as to whether its faithful pursuit of its purpose, under its managerial regime, will provide them with the benefits they want.

Entrepreneurs and directors can help by publicly rededicating their firms to concrete purposes. Specifying a purpose in the charter's purpose clause would be the most helpful.[192] Putting it in the corporate by-laws would be second best. And putting it in a mission statement would be the third best. But better than nothing.

Naturally, the legislature could have the biggest impact. The reigning Anglo-American system of corporate governance was not designed with today's stockholders in mind—the most ignorant, least responsible, lease committed, least contributing of its constituencies. It is little wonder that a system of shareholder primacy struggles when these are one's shareholders.

One corrective proposed by Senator Warren is to put worker representatives on the board, with the thought of augmenting the slice of the pie received by workers and perhaps pushing the board to a longer-term perspective. Unfortunately, however, this would meet

[192] Which could of course be revised if need be.

with strenuous opposition from executives and large stockholders—among our most politically powerful groups.

A promising alternative that entrepreneurs would instead welcome, and that few would find reason to oppose, would be to repeal an obscure provision in the Tax Reform Act of 1969 that bars non-profit foundations from owning more than 20% of the shares of a for-profit corporation.[193] In Denmark today, 70% of the value of the Danish stock market is owned by non-profit foundations, or "industrial foundations," which, by owning all, or at least a majority, of a corporation's voting shares, control its board membership. Novo Nordisk and Carlsberg Group (the beer company) are just two examples of prominent companies so controlled, the latter since 1887. Such structures used to be common in the United States as well, before the 1969 law was passed (with foundation ownership of Hershey's surviving the law for idiosyncratic reasons and continuing to this day).[194]

In the typical case, a company founder who lacks interested or capable heirs establishes the foundation to continue the business, and the founder's vision for the business, after the founder is gone. To ensure this, a specific purpose is typically written into the foundation charter, indirectly placing the company back under the strictures of a purpose clause. Members of the foundation board, who are initially appointed, generally elect their own replacements, eliminating any pressure from outside stockholders (if there even are any), and, by law, they are compensated strictly in salary, which eliminates all personal interest in short-term stock-price improvements. The board is thus freed to fulfill its fiduciary duty to the foundation purpose without distraction, and to direct the

[193] [Add citation.]
[194] HENRY HANSMANN & STEEN THOMSEN, MANAGERIAL DISTANCE AND VIRTUAL OWNERSHIP: THE GOVERNANCE OF INDUSTRIAL FOUNDATIONS (Yale L. & Econ. Research Paper No. 467, 2013), https://ssrn.com/abstract=2246116 or http://dx.doi.org/10.2139/ssrn.2246116.

board of the operating company to make the investments in research, plant, and personnel that will advance the corporation's purpose for the long-term. The success of these companies strongly suggests this fiduciary duty is faithfully discharged. What is more, as revenues may not be disbursed to the board members in the form of dividends, all are either plowed back into the company (solving the problem of underinvestment), or, very often, the founder additionally designates a charity to which a portion of the earnings may go. This restores the public benefit function of the corporation, even in cases when the business purpose has no other strong association with public ends. Finally worth noting, foundation-controlled companies account for almost all the examples where progressive management practices—with respect to workers, the environment, and the community—have been preserved across generations.[195] This would not so much be reforming corporate governance, as building a better control structure on top of it.

[195] For more detail, see Colin Mayer, "Reinventing the Corporation," The Sir John Cass's Foundation Lecture delivered at the British Academy in London (2015); David Ciepley, "Can Corporations be Held to the Public Interest, or Even to the Law?" *Journal of Business Ethics*, online publication, May 2018, https://doi.org/10.1007/s10551-018-3894-2.