IN SEARCH OF A PARADIGM OF CORPORATE SOCIAL RESPONSIBILITY

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Businessmen, scholars, jurists, employees, consumer advocates, environmentalists, and many others affected by the enormous power wielded by large corporations (that means most of us) continue to debate the range and limits of corporate social responsibility. Despite an overabundance of time and ink expended analyzing the proper range and limits of corporate social responsibility no consensus view dominates the controversy. This controversy arises because advocates of the various explanatory models disagree on basic assumptions regarding the ethical implications of the corporate form. These corporate philosophers often recommend that existing statutory and common law rules governing corporate responsibility be changed whenever the extent law deviates from the recommendations of their proposed paradigms. A general acceptance of the appropriate underlying principles and particular applications seems impossible to obtain. Instead epithets fly in place of rational discourse. Perhaps the central role played by corporations in the American economy justifies an on-going debate; certainly the stakes at issue demand a coherency that this author finds lacking. This article outlines the contours of the most popular models of corporate social responsibility, their sociological derivation, and their correspondence with existing law; all in search of a more acceptable descriptive and prescriptive paradigm. It is the thesis of this article that statutory and common law trends reflect a proper adoption of a rights model of the corporation that has not yet been adequately articulated.

I. PROPOSED MODELS OF CORPORATE GOVERNANCE AND THE DEMAND FOR INCREASED CLARITY

For several reasons, Professor Eisenberg's recent TePoel Lecture offers a starting point for a moral and legal analysis of corporate social responsibility. First, the method of analysis he selects, working from an explanatory model to particular application, al-

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allows for rational evaluation and parallels the methodology used throughout this article. Second, he paints with broad strikes what he describes as the two "major relevant" models of corporate governance, the economic model and the political model, exploring in detail their respective merits and limitations. Third, as a Reporter for the American Law Institute's Tentative Draft No. 1 on the Principles of Corporate Governance and Structure, he uses the Lecture as an opportunity to introduce and defend the proposed restatement. Finally, the Lecture demonstrates the difficulty of matching conceptual models with practical applications. A brief critique of Professor Eisenberg's Lecture follows.

A. METHODOLOGY (PARADIGMS—THE NEXUS BETWEEN THEORY AND PRACTICAL APPLICATION)

Professor Eisenberg first outlines conceptual paradigms that explain the normative implications of competing theories of corporate responsibility and then tests those models against the cogency of particular applications. This methodology allows for rational discussions at both the conceptual and applied levels. At the conceptual level, if the proposed model does not explain an acceptable ethical theory it loses persuasiveness against morally preferred paradigms. At the applied level, any model which can justify particular cases that appear intuitively correct increases its credibility against conflicting models. Working back and forth from explanatory principle to particular application thereby contributes to the rationality of the discussion and makes analytical progress possible.

Professor Eisenberg in other contexts explains the search for an explanatory paradigm as a methodology made famous by Thomas Kuhn's *The Structure of Scientific Revolutions.* Kuhn explains that paradigms are models or principles that explain most phenomena within their scope. Their value lies in accounting for phenomena that would otherwise appear random or inexplicable. If unaccounted phenomena predominate then there exists good reason to abandon the model for a more comprehensive alternative. Paraphrasing Kuhn, Professor Eisenberg explains "as the paradigm is applied and extended in this manner, it typically happens that anomalies—phenomena the paradigm does not account

2. The proposed restatement has received some criticism. The ABA's Litigation Section, for example, "takes issue with the need for the publication, its approach, its interpretation of law and the rules it suggests." See discussion of the criticisms in *Litigation News,* Vol. 8, No. 3 at 1, 17-18 (1983).

for—are uncovered. These anomalies may eventually lead to the formation of an entirely new paradigm."\textsuperscript{4}

John Rawls employs a similar methodology in \textit{A Theory of Justice}, but introduces innovations worth noting.\textsuperscript{5} Rawls's rational investigation aims toward "reflective equilibrium";\textsuperscript{6} the state of affairs reached by the mutual adjustments of principles (or paradigms in Kuhn's terminology) and considered judgments. Considered judgments represent our intuitive convictions about certain social issues; they are provisional fixed points which we presume (hope) our explanatory principles will justify if put to the test. Rawls describes the process as one of duly pruning and adjusting principles and judgments:

This state of affairs I refer to as reflective equilibrium. (citation omitted) It is an equilibrium because at last our principles and judgments coincide; and it is reflective since we know to what principles our judgments conform and the premises of their derivation. At that moment everything is in order.\textsuperscript{7}

Applying the methodology to the issue of corporate social responsibility, the object is to select a paradigm capable of reconciling normative implication with acceptable legal results. The paradigm must be capable of carrying the weight of difficult cases; anomalies which surface must be persuasively evaluated as either insignificant deviations or mistakes. A contrary result would require the reformulation of the explanatory model in search of reflective equilibrium.

B. A \textbf{FIRST LOOK AT THE POLITICAL AND ECONOMIC MODELS OF CORPORATE GOVERNANCE}

Professor Eisenberg describes economic and political models of corporate governance as reflecting the major relevant currents of thought.\textsuperscript{8} In considering the respective merits of each model, Professor Eisenberg prefers an economic view based on normative and practical grounds; his Lecture explicates his preference. Although further elaboration of each of these models will be undertaken later, a brief outline of them is necessary here for an understanding of Professor Eisenberg's arguments.

Professor Eisenberg views Robert Dahl as the champion of the

\begin{itemize}
\item \textsuperscript{4} \textit{Id.} at 751, \textit{citing} T. Kuhn, \textit{The Structure of Scientific Revolutions} 6, 7, 27, 29, 52-65 & passim (2d ed. 1970).
\item \textsuperscript{5} J. RAWLS, \textit{A Theory of Justice} 20, 49-51, 120, 432, 434, 579 (1972).
\item \textsuperscript{6} \textit{Id.} at 20.
\item \textsuperscript{7} \textit{Id.}
\item \textsuperscript{8} Eisenberg, \textit{supra} note 1, at 1 n.1.
\end{itemize}
political model. The model largely rests on Dahl's normative claim that in a rational society every institution ought to be controlled by those constituencies affected by it. Consumers, employees, shareholders, and the general public are each affected by corporate power; accordingly, each ought to have a voice in its governance.\textsuperscript{9} The corporation, in effect, is morally responsible in some complicated sense to these various constituents. Since the law has not internalized these expanded responsibilities it ought to be reformed. Organizationally the board ought to be comprised of representatives from each group, and ought to owe fiduciary duties to all affected constituencies. Dahl's recommended model thereby repudiates the traditional corporate model, where the board is elected by the shareholders and owes its fiduciary duties only to them, in favor of a reformed model evidencing increased political responsibility.

Professor Eisenberg defends the traditional corporate model (from an economic angle of view) against Robert Dahl's normative criticisms. The corporate institution derives its moral legitimacy as an empirical matter from widespread popular acceptance of the desirable economic outcomes it produces.\textsuperscript{10} Normative legitimacy flows primarily from the efficient utilization of economic resources, and secondarily from ethical notions regarding the sanctity of private property. Further, Dahl's political model appears unworkable in this country where a diffusion of management responsibility would result in the disappearance of investment capital and the dilution of any meaningful accountability on the part of management.\textsuperscript{11}

C. The Proposed Restatement

At the applied level of his argument, Professor Eisenberg claims that the economic model (and its limits) are reflected in section 2.01 of the Tentative Draft No. 1 of the American Law Institute's Principles of Corporate Governance and Structure. The relevant provisions of the proposed restatement provides:

\begin{quote}
[T]he objective of the business corporation is to conduct business activities with a view to corporate profit and shareholder gain, except that, even if corporate profit and
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\textsuperscript{9} Id. at 2 n.2, quoting R. D. A., AFTERTHE REVOLUTION? 7 (1970).
\textsuperscript{10} Eisenberg, supra note 1, at 2.
\textsuperscript{11} Id. at 16-17. The feasibility of the political model has been enhanced somewhat recently in the automobile industry. The United Auto Workers were allowed to install their president, Douglas A. Fraser, on Chrysler Corp.'s Board in 1979 in return for wage and benefit concessions.
shareholder gain are not thereby enhanced, the corporation, in the conduct of its business

(a) is obliged to the same extent as a natural person, to act within the boundaries set by law,

(b) may properly take into account ethical principles that are generally recognized as relevant to the conduct of business, and

(c) may devote resources, within reasonable limits, to public welfare, humanitarian, educational, and philanthropic purposes.\textsuperscript{12}

The economic objective, of course, is plainly exhibited in the first part of the section. Professor Eisenberg stresses the importance of the fact that the economic rather than the political view informs the model; the proposed restatement inclines the law toward efficiency and away from an all-encompassing obligation to every constituency remotely affected by corporate power. However, subparagraphs (a), (b) and (c) of section 2.01 represent serious anomalies for devotees of the economic model of corporate governance. These exceptions raise troublesome issues in the search for reflective equilibrium.

D. ANOMALIES, REFLECTIVE EQUILIBRIUM AND MEANINGFUL DICHOTOMIES

Professor Eisenberg makes some effort, typical of the economic tradition from which he speaks, to squeeze socially responsible objectives under the umbrella of the economic principle. He argues that in the "vast bulk of cases" economic objectives (long-run profitability) mandate social responsibility on the part of the corporation.\textsuperscript{13} On the other hand he frankly admits that under the proposed restatement "there will be instances when adherence to social goals or imperatives are neither designed nor likely to enhance corporate profit and shareholder gain."\textsuperscript{14} Corporations, obligated to abide the law,\textsuperscript{15} may act in accordance with "ethical principles" that are relevant to the conduct of the business,\textsuperscript{16} and may reasonably devote resources in the public interest.\textsuperscript{17} Concessions on each of these points obviously vitiate the pristene quality of the economic model; suddenly a difference of great significance

\textsuperscript{12} American Law Institute, Principles of Corporate Governance and Structure: Restatement and Recommendations § 2.01, at 17 (Tent. Draft No. 1, 1982).

\textsuperscript{13} Eisenberg, supra note 1, at 8.

\textsuperscript{14} Id. at 6.

\textsuperscript{15} Id. at 7-10.

\textsuperscript{16} Id. at 10-12.

\textsuperscript{17} Id. at 12-13.
in theory appears muted in practice. Ethical business conduct may encompass such concerns as employee relations, consumer safety, or environmental protectionism; humanitarian contributions may be targeted for special interests affected by the corporation. The real distinction between the models, therefore, rests upon Professor Eisenberg's recommendation that various constituent groups not be actually represented on the board, although (or because) virtual representation is already insured by law, ethical, principles, and humanitarian impulses. In brief, Professor Eisenberg does not advocate the adoption of a true economic model that would prohibit legal, ethical and humanitarian conduct unrelated to corporate profit and shareholder gain. Instead he offers a revised "restatement" complete with anomalies and unexplained limitations. It is doubtful that the serious student of corporate affairs is any better off understanding Professor Eisenberg's "major relevant currents of thought" on corporate models where the intuitive legitimacy of specific applications override the authority of the conceptual paradigms. The paradigms are supposed to decide difficult cases, not give way in difficult areas. It is suggested that the proposed restatement offers valid considered judgments or fixed provisional points that can be explained by the reformulation of a rights paradigm. The development of that model, however, requires a broader investigation of conceptual alternatives and their sociological underpinnings.

II. MODELS OF CORPORATE GOVERNANCE

The political and economic models of corporate governance identified by Professor Eisenberg do not exhaust the range of possible explanatory paradigms. Since conceptual models have a way of affecting our perception of reality, as well as our reform efforts, we should strive to be sure that the received model makes better sense than available alternatives. By identifying the political model as the only major alternative to his preferred economic model, Professor Eisenberg stacks the deck in his favor. The political model is not descriptive of existing law; its strength lies in a controversial normative assertion that all institutions ought to be organized along democratic lines. But what about other models which make descriptive as well as ethical claims of authenticity?

At least five distinct paradigms of corporate governance offer differing answers to the issue of corporate social responsibility: (1) the contract model; (2) the public-interest model; (3) the political model; (4) the economic model; and (5) the rights model. Understanding the ethical, descriptive and sociological underpinnings
of each of these models enhances our ability to rationally choose between them. Accordingly, each of these models will be described from the perspective of the sociological milieu out of which they arose. After describing each paradigm the common and statutory law will be examined with the various models in mind. The search among these models is aimed at establishing reflective equilibrium, i.e., the reconciliation of our considered judgment (or intuition) concerning allowable corporate activities with those activities actually allowed by either our model or the law. If anomalies exist adjustments must be made to our intuition, our model, or the existing law.

A. The Contract Model

The contractual model posits that the rights and responsibilities of the various corporate actors is a matter of contract. From an ethical perspective notions of property and contract rights supply moral justification for this received paradigm. The shareholders collectively are the owners of the corporation as a species of private property. They exercise their ownership interest by contracting with the corporate entity; shareholders agree to limit their immediate control of their property (the investment capital) in return for their right to elect democratically the board, make extraordinary business decisions, and receive dividends. The board in return, as the principle policy maker of the corporation, agrees to pursue the legitimate business expectations of the investors: maximum return on the investment. Corporate democracy, property and contract rights are the key concepts that inform this model.

The contract model had its heyday around the turn of the twentieth century with the elevation of contract reasoning to the level of constitutional doctrine. During this period economic rights to property and contract became synonymous with liberty. From a jurisprudential perspective the dissents of Justices Bradley and Field in the Slaughter House Cases\(^1\) began a campaign for the preservation of inalienable property and contracts rights against interference by the state.\(^2\)

The most important judicial decision on the issue of corporate responsibility decided during this period is *Dodge v. Ford*. The case, which will be discussed in greater detail later in connection

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\(^{18}\) 83 U.S. (13 Wall) 36 (1872).

\(^{19}\) For the most comprehensive explanation of the importance of rights in preserving liberty and free government written during this period see T. Cooley, *Treatise on the Constitutional Limitations* (7th ed. 1903).
with the development of the common law, fits well with the intellectual milieu of this the Lochner era. The controversy pitted the majority shareholder, Henry Ford, against minority owners, the Dodge brothers, in a contest over the proper limits of corporate responsibility. Henry Ford believed that Ford Motor Company had more than satisfied its financial obligations to its original investors, and sought to extend corporate benefits to other corporate constituents (namely employees and consumers) by way of expanded work opportunities, higher wages and lower purchase prices. The Dodge brothers argued that only the shareholders were entitled to the benefits of the corporation, and that Henry Ford's altruistic actions were therefore ultra vires. The Michigan Supreme Court agreed:

A business corporation is organized and carried on primarily for the profit of the stockholders. The powers of the directors are to be employed for that end. The discretion of directors is to be exercised in the choice of means to attain that end, and does not extend to a change in the end itself, to the reduction of profits, or to the nondistribution of profits among stockholders in order to devote them to other purposes.20

The notion that owner-shareholders are entitled to the fruits of contractual labors as a matter of right and as part of their natural liberty pervades the opinion. The argument is normative rather than historical: the corporation is assumed to be strictly a form of private property and contract as a matter of ethical if not descriptive reality.

Critics of this contract model challenge its historical, as well as its ethical, validity. They view the corporation as a public, rather than a private, institution. In support of this public conception of the corporation they trace the historical pedigree of the business corporation to its "public" lineage in medieval corporations. The key attribute investigated in this critical historical analysis is the necessity of having the sovereign authorize the incorporation. Incorporation by royal prerogative historically meant that corporations had a public (usually royal) caste: corporations were simply not another form of private property organized solely for private gain. According to these critics of the contract model of the corporation, early incorporation in this country similarly required legislative approval and entailed public responsibilities. That is, incorporation by special legislative grant usually meant that quasi-public corporations enjoyed certain privileges, such as exclusive

utility or transportation rights, in exchange for certain public responsibilities. The argument concludes that since corporations historically existed as a matter of public concession with public responsibilities, they continue to owe the public recognizable duties. Accordingly, the contract model of the corporation as an amalgam of private property and contract lacks historical validity.

Contemporary devotees of the contract model have recently supplied arguments detailing the historical continuity of the business corporation as a contractual entity in refutation of these critics. Hessen, for example, traces the business corporation's antecedents to the joint-stock companies of sixteenth-century England. These business forms operated without sovereign grant strictly as a matter of contract. The transition away from incorporation by special legislation to general incorporation statutes, during the Jacksonian period, confirmed the trend toward a contractual view of corporations in this country. The modern business corporation, Hessen concludes, is essentially contractual rather than concessionary in nature; its duties, correspondingly, would be to the shareholders rather than the general public.\(^{21}\)

The normative implications of the contract model also have received recent attention in libertarian writings. Roger Pilon, for example, expresses sympathy for Hessen's historical contract model; ultimately, however, Pilon concludes that the model can best be justified by ethical rather than historical reasoning. Thus he concerns himself less with "the 'crazy-quilt' that is corporation law—that is any law for that matter—as with the larger normative or jurisprudential theory that stands behind or might stand behind the law."\(^{22}\) Pilon nostagically harkens back to the theoretical underpinnings of *Dodge*; the natural law or higher law tradition "when freedom of contract was rather more highly regarded."\(^{23}\) From a normative perspective the corporation is justified under a Nozickian variant of this tradition because it "might arise by a process that violates no one's rights . . . ."\(^{24}\) If the extant law varies from the normative implications, which Pilon believes it does in

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such areas as limited liability in tort, then this provides an ethical justification for changing the law. Pilon argues, therefore, that the rightness of the explanatory principles underlying the contractual model ought to justify reforming the mistaken law in accordance with identified principles. Here Pilon is in accord with Hessen, who contends that present corporate relationships predicated on a contractual model ought to be respected because they rest "on the principles of choice, consent, and contractual authorization."

Scholars and jurists, therefore, have offered historical and normative arguments supporting a Dodge-like contract model of corporate responsibility: the corporation is responsible to maximize profits for the benefit of its shareholders as a matter of property and contract rights, because the corporation strictly arises (could arise) in consequence of voluntary arrangements between its contractual participants. Although this model is related to Eisenberg's economic model, it is distinct in its property and contract rights (rather than public interest) orientation. Eisenberg, in fact, alludes to the model as a secondary reason for adopting his economic model. It seems more plausible to view the contract model as a separate paradigm with distinct ethical premises.

The contract model makes descriptive as well as prescriptive claims: the law recognizes the right of shareholders to demand management be strictly constrained by profit motivation; private property and contract rights ought to be respected even where they run counter to the public interest. The first claim is historical and can be tested by a closer examination of the common and statutory law impinging on corporate responsibility. The second contention is ethical, and requires an acceptance of entitlement over utilitarian moral theories. If one rejects the moral assertion that individuals are entitled to respect as free and equal moral persons, then the force of the law predicated on that assumption loses its normative basis. Revised theories of corporate governance which give priority to the public interest over the rights of the corporate participants reflect this reorientation of ethical reasoning.

B. THE PUBLIC INTEREST MODEL

Devastating criticisms launched in the 1920's and 30's against democratic theory, formalism in the law, and the priority of prop-

25. Id.
27. Eisenberg, supra note 1, at 5.
roperty and contract rights prompted, among other things, a reorientation of reasoning concerning corporate decision-making. If democratic processes could not be justified at the political level they were certainly ill-suited at the economic level; if formalism in the law was an illusion then doctrinal consistency in contract theory could not be offered in substitute of desired social results; if property and contract rights were merely high-sounding abstractions that obscured the need for social reform they would have to be disregarded. These intellectual tendencies contributed to a revised public interest model of corporate responsibility.

The criticism of democracy as a viable system came from social scientists and psychologists during the early decades of the twentieth century. These academics persistently argued that the underlying premises of democratic theory are descriptively unrealistic and therefore ethically unsound. Lauding the insights of Freudian psychology, for example, Walter Lippman denied that people are rational either in a normative or a practical sense in pursuing their interests in politics. Similarly, Harold Lasswell suggested "that the individual is a poor judge of his own interest." Social scientists recommended the adoption of government by administrative elite. Their empiricist orientation led to the rejection of ethical ideas in favor of pragmatic results. Lippman wrote:

The old effort was to harness mankind to abstract principles—liberty, justice or equality—and to deduce institutions from these high-sounding words. It did not succeed because human nature was contrary and restive. The new effort proposes to fit creeds and institutions to the wants of men, to satisfy their impulses as fully and beneficially as possible.

Idealized notions of democracy, property, and contract rights received continuous haranguing by these political scientists who insisted that society ought to focus on the public interest rather than legal abstractions. Legal realists during this same period found

28. For a general discussion of this issue see E. Purcell, Jr., The Crisis of Democratic Theory 95-113 (1973).
32. W. Lippman, supra note 29, at 67-68.
33. John Dewey, for example, commented that Lippman's Public Opinion was "the most effective indictment of democracy as currently conceived ever penned." Dewey, Public Opinion—A Review of Walter Lippman's Book, 30 New Republic 288.
little solace in the rule of law upon which the contract model rests. They argued that "mechanical" jurists offered the image of legal formalism as a substitute for the public interest. Following Holmes's lead\(^\text{34}\) sociological jurisprudences and the legal realists in the 1920's and 30's condemned efforts to maintain the myth of doctrinal consistency used in substitution of a policy-oriented approach to legal decision-making. The freedom of contract doctrine became a favorite target of critics of legal formalism. Pound, condemning mechanical jurisprudence, contended that law

must be judged by the results it achieves, not by the niceties of its internal structure; it must be valued by the extent to which it meets its end, not by the beauty of its logical processes or the strictness with which its rules proceed from the dogmas it takes for its foundation.\(^\text{35}\)

Pound noted that "[m]anifestations of mechanical jurisprudence are conspicuous in the decisions as to liberty of contract."\(^\text{36}\) Although the focus of Pound's criticism is the so-called right a person has to sell his labor unfettered by paternalistic legislation limiting hours or working conditions, the implication is broader: excessive judicial preoccupation with doctrinal consistency in lieu of public policy considerations leads to unacceptable results in modern society. Legal realists in the 20's and 30's increasingly denied the authority of legal rules in resolving important social issues.\(^\text{37}\)

This is not to say that these intellectual movements in political science and jurisprudence operated as determinative historical forces in the area of corporate law. Nonetheless, they undoubtedly influenced the persuasiveness of the contract paradigm; especially to the extent the model relied on theories of corporate democracy, property and contract rights.

The initial crack in the corporate dike appeared when Adoph A. Berle, Jr. and Gardiner C. Means published in 1932 what has

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\(^{34}\) Oliver W. Holmes's The Common Law, first published in 1881, first announced the realist view that the "felt necessities of the time" are more critical in legal development than syllogistic reasoning. O. Holmes, The Common Law 1 (1881).

\(^{35}\) Pound, Mechanical Jurisprudence, 8 COLUM. L. REV. 605, 605 (1908).


\(^{37}\) For a discussion of realism generally, see Llewellyn, Some Realism About Realism—Responding to Dean Pound, 44 HARV. L. REV. 1222 (1931). Llewellyn identifies a group of twenty-one legal scholars who had been "more or less interstimulated." Id. Although Llewellyn is responding to Pound's criticism of the realist's skepticism, the similarities between Pound's sociological jurisprudence and Llewellyn's realism, at least in regard to the criticism of formalistic reasoning, are striking.
been described as the most seminal work on corporations ever written, *The Modern Corporation and Private Property*. The empirical findings of their study of the corporation paralleled the findings of the Lippmans and Lasswells in the area of political science: the expansion in numbers of shareholder had resulted in a corresponding diminution of their control over corporate policy. Corporate management consequently had gained unfettered discretion over giant corporations. Corporate democracy in reality worked little better than political democracy: administrative elites controlled economic power in corporate America just as they controlled politics in democratic America. Theory and reality diverged on the same points in economics and politics.

This empirical realization launched a debate between E. Merrick Dodd, Jr. and Adolf Berle over the proper model which should inform corporate law. Berle wanted to patch up the dike by retaining the contract model of the corporation with a revised view of how it works. While individual shareholders could exert little or no influence over management through corporate democratic processes, management nonetheless was obligated to serve the shareholder's investment interests: "all powers granted to a corporation or to the management of a corporation, or to any group within the corporation, whether derived from statute or charter or both, are necessarily and at all times exercisable only for the ratable benefit of all the shareholders as their interest appears." Professor Dodd, in contrast, advocated the replacement of the old dike with a radically different explanatory structure. According to Dodd the publicly-held corporation existed as an entity separate from its shareholders, with social responsibilities of its own. Private property reasoning simply made no sense in the context of giant corporations. Thus corporate management "should concern themselves with the interests of employees, consumers, and the general public, as well as of the stockholders . . . ."

This expanded view of corporate responsibility fit the intellectual milieu of the New Deal era. For Dodd, corporate management ought to act "in a manner appropriate to a person practicing a profession and imbued with a sense of social responsibility without


thereby being guilty of a breach of trust." The public interest model of the corporation had come of age. Two decades later this radical view had obtained consensus status. Berle then conceded, at least for the time being, that Dodd's view had prevailed:

Twenty years ago, the writer had a controversy with the late Professor E. Merrick Dodd, of Harvard Law school, the writer holding that corporate powers were powers in trust for shareholders while Professor Dodd argued that these powers were held in trust for the entire community. The argument has been settled (at least for the time being) squarely in favor of Professor Dodd's contention.

The public interest angle of view has continued to change the way many writers presently look at the corporation. The corporation, once a bastion of private property, has become a public institution with public responsibilities. John Kenneth Galbraith, for example, argues that management's profit obligation requires only a fair and normal return on investment capital. For Galbraith the public interest demands more emphasis on economic growth than shareholder profit. More recently Ralph Nader and company insist that the privileged status of the corporation as a chartered entity justifies increased attention to public-interest obligations. Nader explains "[t]he law creates and protects that bundle of rights called property or the corporation, and this same law can rearrange that bundle of rights if it is in the public interest." The publicly-inspired legal arrangement Nader has in mind is the federal chartering of giant corporations and their close regulation in view of the existing interests of consumers, employees, environmentalists and others.

The public interest model, therefore, abandons the traditional view of the corporation as a species of private property owned by its shareholders to whom it owes strict duties, in favor of a description of the giant corporation as a public institution with broad social responsibilities.

Legal trends since the 1930's support an expanded view of corporate responsibility. Common law opinions and state statutes increasingly recognize corporate purposes broader than profit

42. Id. at 1161.
46. Id. at 258. See also R. Nader & M. Green, Corporate Power in America 81 (1973).
maximization. Accordingly the public interest model explains noticeable changes in corporate law that appear arbitrary or random to a contract analysis. Moreover utilitarians stress the preferred ethical status of a public interest over an entitlement approach to corporate governance.

Serious questions, however, remain. What are we to do about the fact that the law makes corporate management fiduciaries to the shareholders? If the proper constituencies include consumers, employees, and other interested groups affected by corporate power, can each of these interests file derivative suits to protect their respective interests? How do we reconcile conflicting claims? How does management identify the affected interests and properly weigh their claims? These and related questions raise practical problems for a public interest approach to corporate governance. The political and economic models of corporate governance attempt to answer some of these questions, but neither is persuasive.

C. The Political Model

A variant of the public interest model that has gained much attention since the 1950's is the political model criticized by Professor Eisenberg in his Tepoel Lecture. In brief the paradigm combines the broad constituency premise of the public-interest model with an expanded theory of corporate democracy. Corporate constituencies, rather than administrative elites, ought to have a democratically enforced say in corporate policy decisions. In determining the constituencies entitled to a voice in corporate decisionmaking processes, one must look beyond property relations to interest groups affected by corporate power.

This resurgence of faith in democratic processes requires some sociological explanation considering the “impossible ideal” appellation given democracy by the political scientists of the 1920's and 1930's. By the 1950's the skepticism of the political scientists had given way to newly found optimism for a variety of reasons. First, the ad hoc administrative elite approach identified with New Deal progressives had not proven totally satisfactory. Second, the events of fascism and totalitarianism had demonstrated the undesirability of unfettered discretion in politics. Third, modern studies in interest-group pluralism indicated that members of society could influence policy decisions. Fourth, democratic processes were thought ethically preferrable to administrative elitism because the results would more likely accord with majoritarian preferences; moreover the participants enhanced their sense of well
being through active involvement in the decisional processes. Implicit in much of the writings of these political scientists of the 1950's and 1960's was faith in the practical possibility of democracy working effectively. In this regard Louis Hartz wrote:

We have made the Enlightenment work in spite of itself, and surely it is time we ceased to be frightened of the mechanisms we have devised to do so. We have implemented popular government, democratic judgment and the equal state on a scale that is remarkable by any earthly standard.47

Berelsen, Lazarsfield and McPhie explained the practical workings of the democratic processes through an empirical study of interest-group pluralism and voting patterns. Despite all the conceptual problems, democratic processes seem to work surprisingly well:

If the democratic system depended solely on the qualifications of the individual voter, then it seems remarkable that democracies have survived through the centuries. After examining the detailed data on how individuals misperceive political reality or respond to irrelevant social influences, one wonders how a democracy ever solves its political problems. But when one considers the data in a broader perspective—how huge segments of the society adapt to political conditions affecting them or how the political system adjusts itself to changing conditions over long periods of time—he cannot fail to be impressed with the total result. Where the rational citizen seems to abdicate, nevertheless angels seem to tread.48

Similarly, Latham relied on empirical studies to demonstrate “the significance of the group in the enactment of legislation, in the conduct of party activity, in the formulation and execution of public policy, in the process of public administration, and in the protection of civil liberties.”49

With the rekindled faith in liberal democracy in hand, political scientists advocated the proliferation (rather than the obliteration) of democratic processes throughout the community. David Truman suggested that “the participation of interest groups in the formation of policy” avoids “morbific politics,” or the exclusion or blocking of organized interests.50 Democratic processes, according

to these writers, lend respectability to any significant social organization. Truman suggested:

The attitudes themselves are vague, but they usually involve approval of such devices as periodic elections of key officials, broad participation by the membership in the group's policy making, either directly or through a system of elected representatives, written constitutions, and the like. These, in fact, become elements without which an organization cannot achieve 'respectability' and 'legitimacy' in the community. No matter how solidly the rank and file of a labor union may stand behind their leaders, if the latter do not submit to regular elections at periodic 'legislative' conventions, they invite censure from other groups and guilt feelings among the membership that may destroy their cohesion.\(^{51}\)

Robert Dahl expresses this same faith in the effectiveness and normative significance of democratic processes. Dahl and Lindblom explained that the democratic goal "consists of a condition to be attained," political equality, and a "principle guiding the procedure for attaining it," majority rule.\(^{52}\) Political equality is normatively justified in that first, the lack of equal opportunity to have one's preferences considered produces anxiety and distress; second, there exists no rational basis for weighing the preferences of some over those of others; third, there can be no confidence that an elite group's preferences will be respected over time.\(^{53}\)

As a practical matter these theorists realize that there never exists a perfect fit between the theory of popular rule and the actual results. Nonetheless equal participation in the process provides an element of fairness and increases the likelihood that political decisions will actually reflect broad preferences: the ultimate justification for policy decisions. As a result "[s]pecific policies will rarely violate highly ranked, intense, stable, and relatively broad preferences of the greater number for a longer period than about the interval between elections."\(^{54}\) More importantly for our purposes, the condition of political equality and the principle of majority rule, normatively required for any social organization, is realized only through interest-group politics.

As Professor Eisenberg indicated, Dahl projected the political model into the debate over models of corporate governance. For

\(^{51}\) Id. at 129.

\(^{52}\) R. DAHL & C. LINDHOLM, POLITICS ECONOMICS AND WELFARE 41 (1953); see also R. DAHL, POLYARCHY 1-2 (1971); R. DAHL, A PREFACE TO DEMOCRATIC THEORY 63-81 (1956).

\(^{53}\) R. DAHL & C. LINDHOLM, supra note 52, at 42-43.

\(^{54}\) Id. at 314.
Dahl, the corporation's legitimacy as a public institution that yields enormous social power depends on the democratic participation of those affected by it: "[i]n a rational society . . . [people] would see an economic enterprise as a kind of association of all those who are affected by its activities. . . . [W]hy should people who own shares be given the privilege of citizenship in the government of the firm when citizenship is denied to . . . employees and customers . . . and the general public . . .?"^{55}

The political model, therefore, presents yet another distinct view of corporate governance. The model's preoccupation with interest-group participation in corporate decision-making processes distinguishes it from the closely-related public interest perspective: the emphasis is on process rather than results. Allowing the affected interest groups to participate at the policy-making level of the corporation avoids "morbific politics"^{56} and serves the public interest more effectively than any other decisional process.

The political model answers some of the questions posed by a public interest approach, but leaves others open. The issue of how one mediates among conflicting claims is settled by the institutional processes of democracy. But the question arises: which interest groups should be represented on the board, and in what proportion to other competing interests?^{57} How do we enforce (should we enforce) strict constituency loyalty in corporate decision-making? How do we balance the economic viability of the entity against the respective claims of the affected constituents? An alternative approach is to locate the public interest in economic efficiency; if this can be persuasively accomplished then the traditional model of corporate governance suddenly takes on a public interest caste: the public is benefitted by an efficient corporate structure.

D. THE ECONOMIC MODEL

The economic model Professor Eisenberg offers as the pre-

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^{55} Eisenberg, supra note 1, at 2 (quoting R. DAHL, AFTER THE REVOLUTION? 116-23 (1970)).

^{56} See note 49 and accompanying text supra.

^{57} Ralph Nader proposes that consumer, employee, environmental and community representatives each be afforded a seat on the board "so that each important public concern would be guaranteed at least one informed representative on the board." R. NADER, M. GREEN & J. SELIGMAN, supra note 45, at 125. Professor A. Conard criticizes the practicality of these proposals in Conard, Reflections on Public Interest Directors, 75 MICH. L. REV. 941 (1977).

ferred alternative to the political model is in reality one more variant of the public interest paradigm. From a sociological perspective the economic angle of view has its antecedents in the legal realist movement and the functional or policy-oriented approach to law. The legal realists demanded that legal scholars abandon preoccupation with logical consistency and turn to a study of the social functions served by the law. Law must serve the public interest through increased attention to the social effects of legal decisions. Their methodological appeal to an increased reliance on social sciences in the study of law several decades later struck a responsive chord in the law and economics movement.

Coase launched the movement with his famous essay on law and social costs.\(^{58}\) Coase’s theorem in that article posits that if transaction costs are zero then the law will not affect the actual distribution of goods: the parties will make market transactions to effect an efficient allocation of resources regardless of the law’s initial allocation of rights and responsibilities. Since in reality transaction costs are not zero the law does have an important affect on the efficient allocation of resources in society. The common law follows a rational pattern to the extent it favors the efficient allocation of liability by anticipating how the market would react if transaction costs were zero, and assigning rights and responsibilities in accordance with the efficiency principle.

The rationality the law and economics advocates have in mind is a calculated maximizing of one’s self interest.\(^{59}\) Although this psychological assessment of individual motivation is meant to be scientific or descriptive in nature, the theory necessarily takes on normative implications. In its wealth maximization version the legal system is morally acceptable to the extent wealth is maximized. Posner explains: “‘[n]ormative economics holds that a policy, law, etc. is to be judged by its effect in promoting ‘welfare,’ and this term is often defined so broadly as to be practically synonymous with the utilitarian concept of happiness . . . .’”\(^{60}\) Eisenberg reduces the normative claim of the wealth-maximization

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60. Posner, Utilitarianism, Economics, and Legal Theory, 8 J. LEGAL STUD. 103, 104-05 (1979). Although Posner argues that economic theory, especially wealth maximization, “provides a firmer basis for a normative theory of law than does utilitarianism,” id. at 103, he ultimately fails to make a meaningful distinction between the two traditions. For a more persuasive argument that utilitarianism is the inspiration of the economic analysis of the law, see Hart, American Jurisprudence Through English Eyes: the Nightmare and the Noble Dream, 11 GA. L. REV. 969, 987-88 (1977).
angle of view to an empirical assessment of its “popular accept-
ance” in producing “desirable outcomes.”

Applied to the issue of corporate responsibility the corporation
ought to act to maximize profits because such “rational” conduct
serves to maximize wealth; a profit orientation thereby satisfies
the normative demand required by the economic analysis form of
utilitarianism. The invisible hand of the market in essence fur-
thers the social interest. Rostow suggests as an advocate of this
tradition that society reasonably relies on the economic characteri-
ization of the modern business corporation: “the basic service for
which society looks to business and labor is the production of
goods and services at the lowest possible costs, and at prices which
measure the comparative pressure of consumer’s choices.”

This economic view denigrates altruistic corporate acts which
are not economically motivated. Such acts are not only inefficient,
and therefore adverse to the public interest, but they are also un-
democratic. Friedman explains that when management makes
corporate expenditures for non-economic purposes they are
“spending someone else’s money for a general social interest.”
Such “irresponsible” conduct is a disguised form of undemocratic
taxation:

The imposition of taxes and the expenditure of tax pro-
cceeds are governmental functions. We have established
elaborate constitutional, parliamentary and judicial provi-
sions to control these functions, to assure that taxes are
imposed so far as possible in accordance with the prefer-
ences and desires of the public.... if they are civil ser-
vants they ought to be selected through a political
process.

Thus Friedman objects to a broader sense of corporate social re-
sponsibility on the grounds that corporate managers would then
be “seeking to attain by undemocratic procedures what they can-

61. Eisenberg, supra note 1, at 4. Eisenberg ultimately discards a pure eco-
nomic model for certain social responsibility limitations. See id. at 7-8. For a criti-
cism of wealth maximization as the appropriate social value, see Dworkin, Why

62. Rostow, To Whom and for What Ends is Corporate Management Respon-
See also Demsetz, Social Responsibility in the Enterprise Economy, 10 Sw. U.L.

63. Friedman, The Social Responsibility of Business is to Increase its Profits,

64. Id. See also M. Friedman, Capitalism and Freedom 135 (1962); M. Fried-
man, An Economist’s Protest 177 (1972). For a criticism of Friedman’s “taxation”
argument, see Manne, The Limits and Rationale of Corporate Altruism: An Individ-
not attain by democratic procedures . . . ."65

A complication exists. Since "rational" conduct involves the calculating maximizing of one's self interest, it is unclear empirically whether an act which appears to be altruistic may be profit-motivated in reality. Samuelson, for example, advises that "[m]any acts of altruism and apparent generosity can be amply defended in terms of public relations and the maximization of long run profits."66 Eisenberg similarly notes that "activity that benefits the public may be based on the prospect of long-run gain to the corporation, and in such cases too the activity will fall within the economic objective."67 When the business judgment defense is added to the calculus the only altruistic acts caught by the economic model would be those acts undertaken with admitted non-economic motives, which in fact do not maximize profits. The proof problems dealing with long-term expectations of profits appear insurmountable.

The economic model, therefore, expresses an alternative paradigm for interpreting responsibility. The normative justification rests on a variant of public interest (wealth maximization) rather than individual entitlement; and the public interest is calculated scientifically by economic analysis rather than democratic processes or administrative elitism. In a way the model brings the issue of corporate responsibility full circle. The view legitimizes the traditional model of corporate governance where the shareholder-elected board decides corporate policy in an effort to maximize profits. The ethical justification for the model, however, has changed from an entitlement perspective to a utilitarian concern for maximizing the happiness of society. An efficient corporate structure simply is the most effective means we have available to serve the public interest.

The economic model does settle many of the practical problems facing a public interest approach to corporate decision-making. The traditional corporate form around which the law coalesces serves the public interest in an Adam Smith invisible-hand manner. The descriptive view of the corporation as a profit maximizer thereby receives normative justification. Nothing needs to be revised other than the normative paradigm explaining the corporate processes: the shareholder-entitlement theory merely is shuffled to the background, and the public interest in wealth maximization is brought front and center. Indeed the Friedman per-

65. Friedman, supra note 63, § 6, at 33.
67. Eisenberg, supra note 1, at 7.
pective denounces as "pure and unadulterated socialism" the corporate doing anything but profit maximization.

The economic model has more likelihood of succeeding at the applied level than any other public interest paradigm, but it too has flaws worth noting. From an ethical perspective its utilitarian orientation requires some justification. Eisenberg uses so-called empirical reality that the model is widely received as the preferred paradigm because of the efficient results it achieves. If we examine public opinion, however, we find an increasing cry from President Reagan and others encouraging corporations to increase their charitable contributions and good works as part of their social responsibility. Few are willing to allow corporations to stick to profit maximization: so much for empirical reality as a basis for normative justification. More importantly from an ethical perspective the economic theory avoids reliance on entitlement theory as a basis of legitimacy. Eisenberg slides over the issue by suggesting that a rights view and an economic view would concur on the appropriateness of profit maximization. While the contract model and the economic model both embrace profit maximization other rights paradigms do not. What if the shareholders want to set aside profit maximization for humanitarian gestures? What if they want to donate to Creighton University despite the fact that a cost-benefit analysis turns up negative?

Another problem for the economic model is that the law permits corporations to act socially responsible even if national wealth suffers as a result. Rather than recommending that the law be reformed in accordance with economic principles Professor Eisenberg would accept these "humanitarian" limitations to his model. Other adherents of the economic paradigm, such as Friedman, would change the law to make it more efficient. Is efficiency the overriding principle of rational conduct to which the corporation ought to pay homage, or are other social values worth considering? The viability of the economic model largely rests on a satisfactory answer to this question.

68. M. FRIEDMAN, AN ECONOMISTS' PROTEST 147 (1972).
69. The Reagan administration has pursued substantial cuts in arts and humanities grants reasoning that the private sector, especially corporations, ought to be the financial patrons of artistic and literary pursuits. See Wall St. J., Feb. 26, 1981, at 25, col. 4.
70. See Note, Corporate Altruism: A National Approach, 59 GEO. L.J. 117 (1970), where the author notes that "there is growing recognition that the quality of life in our industrialized society cannot be improved by governmental initiatives alone." Id. at 117 (citing Berger, Goldston & Rothrauff, Slum Area Rehabilitation by Private Enterprise, 69 COLUM. L. REV. 739, 740, 788-89 (1969); Stone, Tax Incentives as a Solution to Urban Problems, 10 Wm. & Mary L. Rev. 647, 648 (1969)).
E. THE RIGHTS MODEL

With the exception of the contract model discussed initially, each of the paradigms of corporate governance discussed herein exhibit utilitarian tendencies. Their objective is to devise a pragmatic means of securing the public interest; personal and property rights, if relevant, are secondary. Entitlement perspectives are rejected as inimical to the well being of society. This expressed bias against a rights orientation, however, disregards the most coherent explanation of the common law as it has developed in the area of corporate social responsibility; it also denigrates a persuasive ethical theory underlying the law. It is suggested that this final model of corporate governance to be discussed is descriptively and ethically preferred to the other models previously presented.

The rights paradigm begins with the assumption that individuals have rights that even the public interest cannot override. It is distinctly liberal in orientation positing that individuals are entitled to equal respect as a matter of their rationality and individuality. Individuals ought to be allowed to choose freely their sense of the good so long as they do not violate the equal rights of others to do the same. This deontological perspective offers an alternative view of corporate responsibility.

The rights perspective had its debut in legal history during the Lochner era. The ensuing onslaught against rights and legal formalism initiated by progressivism, legal realism and New Deal reasoning, forced entitlement theory to regroup and re-evaluate. Legal theorists began in the '50s to articulate a new legal theory, I will describe as legal principlism, which is essentially a rights-oriented theory. Legal principlism provides a theoretical matrix around which an entitlement theory of corporate governance can be organized. Several observations link these theorists. First, they express faith in the rule of law over unfettered judicial discretion. With the erosion of formal contract reasoning the courts felt more comfortable deciding corporate governance issues in an ad hoc manner. Principlism would reinstate the rule of law, a necessary correlative to entitlement theory. Perhaps their earliest advocate, Lon Fuller, suggested that "even the most arbitrary rule of law ... has that minimum of reason back of it that justifies a respect for established and authoritative sources of law." Similarly Hart and Sacks indicated that institutional procedures associated with the rule of law are "more fundamental than the substantive arrangements in the structure of a society ... since they are at once the

71. Fuller, Reason and Fiat in Case Law, 59 Harv. L. Rev. 376, 387 (1945).
source of the substantive arrangements and the indispensable means of making them work effectively."\textsuperscript{72} These writers turned the focus away from discretionary elitism in adjudication toward doctrinal consistency.

Second, legal principles assert that common law or adjudicative reasoning is and ought to be analytically distinct from political reasoning. Fuller repeatedly asserted "that adjudication is institutionally committed to a 'reasoned' decision, to a decision based on 'principle.'"\textsuperscript{73} Hart and Sacks followed Fuller in contending that adjudicative reasoning offers a special type of rational discourse:

The process of elaboration, or one form of it, has been referred to repeatedly as the process of \textit{reasoned} elaboration. It has been fashionable to deprecate the claims of law to rationality, and to emphasize the element of \textit{fiat} . . . . What has just been said about the process of elaboration, however, points to two factors which necessarily introduce a rational element also into legal arrangements, and which compel some semblance of rational method in their development and application.

The first of the two proposed tests of a satisfactory elaboration was that of consistency with other established applications of it.

. . . .

The second of the proposed tests of a satisfactory elaboration reflects a distinct factor making for rationality in the development of legal arrangements . . . . Underlying every rule and standard . . . is at the least a policy and in most cases a principle. This principle or policy is always available to guide judgment in resolving uncertainties about the arrangement's meaning.\textsuperscript{74} (emphasis original)

Herbert Wechsler similarly deduced: "I put it to you that the main constituent of the judicial process is precisely that it must be genuinely principled resting with respect to every step that is involved in reaching judgment on analysis and reasons quite transcending the immediate result that is achieved."\textsuperscript{75} Ronald Dworkin, in this same tradition, argues that legal reasoning is principled reasoning.\textsuperscript{76}


\textsuperscript{73} Fuller, \textit{The Forms and Limits of Adjudication}, 92 Harv. L. Rev. 353, 372 (1978).

\textsuperscript{74} H. Hart, Jr. & A. Sacks, \textit{supra} note 72, at 165-67.


\textsuperscript{76} R. Dworkin, \textit{Taking Rights Seriously} 84-87 (1977).
Third, these writers locate the analytical distinctiveness of adjudicative reasoning in the rights tradition. The theory suggests that while social policies are hammered out and decided at the legislative level of institutional processes, adjudicative decision-making is a rights-oriented process. In this regard Hart and Sacks adopt Fuller's rights formulation of the adjudicative process:

Adjudication works best when a claimant asserts a right to a remedy within the power of the tribunal to grant and the focal question for decision is whether the claimant is or is not entitled to any such remedy. . . . For, as Professor Fuller says . . . 'any claim of right necessarily implies a principle or rule' by which the validity of the claim can be judged, and this is a matter which can be reasoned about.77

Dworkin similarly contends that unlike other institutions "judicial decisions enforce existing political rights . . . ."78 Dworkin notes that if a judge decides on any other basis "then he decides on the basis of his own convictions and preferences, which seems unfair, contrary to democracy, and offensive to the rule of law."79

Fourth, these writers ground their arguments concerning "claims of right" on the tradition of philosophical liberalism: the Kantian notion that each individual is entitled to equal respect in society pervades much of their normative reasoning. What is problematic for these and other writers in the liberal tradition is the range and limits of individual rights. While personal rights of free conscience, free speech, equal protection, etc., are uniformly embraced by liberals, property rights present real difficulties for many. Libertarians make no distinction between personal and property rights and therefore, harken to the restoration of Lochner reasoning where contract ruled supreme. Other liberal theorists characterize property rights as conventional. Their typical solution is to assign allocational decisions for economic resources to the legislatures (who after all are institutionally competent to decide policy issues) and then to insist that the courts follow "pure procedural justice"80 in deciding economic matters.81

77. H. Hart, Jr. & A. Sacks, supra note 72, at 668.
78. R. Dworkin, supra note 76, at 87.
79. Id. at 123.
80. The term "pure procedural justice" is borrowed from J. Rawls, Theory of Justice 86 (1971). Rawls believes property distributional issues are properly a legislative decision, and that if certain background conditions are met, the issues ought to be decided at the adjudicative level according to the pure procedural justice associated with the rule of law. Id. at 86-87.
81. Fuller, supra note 71, at 400. Fuller uses the term "polycentricty" to refer to many centered problems that are resolved on an ad hoc discretionary basis as required by the parties involved. The reluctance to decide distributional policy is-
An application of this form of deontological reasoning to the issue of corporate responsibility would entail the following. First, policy decisions regarding the proper allocation of property in society, if proper at all, would be characterized as legislative issues. Thus the state may tax corporations, impose environmental constraints, regulate labor relations, etc. all in a non-discriminatory manner. Second, subject to legislative constraints affecting corporations, the shareholder-investors are entitled to contract regarding the proper use of their property. Third, the corporation may seek to maximize profits, or it may expand its objectives to include other humanistic concerns. One of the most controversial issues in liberal theory is the scope of our affirmative duties to provide mutual aid. While liberal theorists vary in their assessment of the extent to which individuals can be compelled to aid others, they uniformly agree that we each can voluntarily choose to be altruistic. Thus an individual may sacrifice for his family or a friend even though the law would permit a more self-interested attitude. The question remains whether an individual combining with another abandons his right to act in a supererogatory manner. Reasonably the issue should be decided by the contractual relation between the parties. The parties could agree to restrict the use of their

82. Again libertarians deny that the state has any right to interfere with property and contract rights, even at the legislative level. See R. Nozick, Anarchy, State, and Utopia 167-173 (1974).

83. See C. Fried, Right and Wrong 168-69 (1978).

84. This is not to assume that the corporation is strictly a contractual entity. The notion is that the state may regulate by legislation the business entity as required by the public interest. Once the corporation satisfies the legislative constraints it is free to act according to the interests of its contracting parties. This contract view of corporate personality is not a recent invention. Chief Justice Marshall, in Trustees of Dartmouth College v. Woodward, 17 U.S. (4 Wheat.) 518, 636 (1819), explained: “It [the corporation] is no more a state instrument, than a natural person exercising the same powers would be.” Similarly, V. Morawetz, A Treatise on the Law of Private Corporations § 1, at 2 (1886) offered that “[t]he existence of a corporation independently of its shareholders 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.” For a discussion of how the various views of the corporate person affect substantive outcomes see Note, Constitutional Rights of the Corporate Person, 91 Yale L.J. 1641 (1982); O’Kelley, the Constitutional rights of Corporations Revisited: Social and Political
property for self-interested purposes, or they could agree that other purposes may be pursued subject to some institutional constraints on the decisional processes. In the corporate context a charter provision could put shareholders on notice that their combined property will be used solely to maximize return; or conversely the lack of a restriction would permit the corporation to use its property in any way an individual could use his or her property. If the corporation, for example, wanted to make charitable contributions to the Sierra Club it could freely do so, so long as it acted in accordance with corporate decisional processes. Likewise if it decided instead to pay a dividend in the amount it would have otherwise allocated to the Sierra Club, then again the conduct would be permissible. In either case a dissatisfied shareholder could voice his or her opinion at shareholder meetings, seek to install different board members who would effect different policy decisions, seek to amend the articles to permit or prohibit the preferred conduct, or sell his or her shares to avoid further disappointment. Property rights are thereby maintained within the auspices of corporate decision-making processes. Finally, if the corporate actors fail to take voluntarily the public interest into account the relevant legislatures could intervene by tax or regulation to heighten corporate responsibility to the public.

It will be noticed that this rights model can be contrasted with the economic model in its tracing out of non-economic rights.85 In-

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Individuals are not required to act "rationally" in their economic self interest. Such a requirement would constitute a utilitarian imposition on the exercise of property rights. Rather, liberal rationality includes an enriched sense of the individual having both economic and humanistic impulses. At bottom these different approaches entail varying views of human psychology and potentiality.

Whether the liberal view is more descriptive of reality than the utilitarian perspective may be beyond our abilities to assess. When we examine the underlying implications of the law in any area we are, in part, making descriptive claims in this regard. For a utilitarian, humanistic conduct that is not self-interest motivated is random or irrational; for liberals such conduct affirms individual choice. In discussing the descriptive accuracy of utilitarian and entitlement models, Frank Michelman suggests that "which is the 'systematic' component and which the 'random' is very much in the eye of the beholder."\textsuperscript{86} Michelman further observes "[t]he critical point is to avoid mistaking an organizing construct for a structural reality that, by defining the possible, limits vision and deadens will."\textsuperscript{87}

If we examine corporate altruism with the rights model in mind, we find that humanistic acts, which are limitations on any economic model, are fully explainable. The corporation may act, as the collective representative of its owners, in either a strictly self-interested manner (within legal constraints) or as a moral entity with mixed self interested and altruistic objectives. The model is distinguishable from the "public interest" and "political" alternatives in that corporate acts exhibiting social responsibility beyond that required by law are permissive rather than mandatory. Corporations may choose between maximizing profits and otherwise serving private or public interests; the relevant constituent for deciding between these purposes is the shareholders and their elected representatives. The corporation acting on behalf of the shareholders may choose to assist its employees or other affected interest groups. In doing so it is serving the rational interests of its shareholders, who recognize that by providing mutual aid for worthy causes the corporate participants enhance their self respect and the bonds of social cooperation. This rights model, therefore, offers a coherent alternative to other theories of corporate governance.

One problem with the rights model is that it gives management the right to act socially responsible apart from economic con-

\textsuperscript{86} Michelman, \textit{supra} note 85, at 201.
\textsuperscript{87} \textit{Id.}
siderations and perhaps contrary to the preferences of shareholders. To the extent the Bearle and Means thesis is correct it allows management unfettered discretion with someone else’s property. Fiduciary duties, of course, would catch any self-interested management decision. Common law fraud would catch other inappropriate conduct. We would be left, however, with corporate do-gooders. Our business history, however, suggests that we have little to fear from corporate Robin Hoods. Eisenberg and Cary have noted that despite the fact that shareholders do not control giant corporations, several factors weigh in favor of shareholders having a say in corporate affairs; first, a large percentage of most corporation’s stock is held by relatively few shareholders; second, financial institutions control a substantial percentage of the stock now owned by wealthy individuals; and third, the very real threat of corporate takeovers alerts management to the importance of maintaining a strong share price. Further, recent history has demonstrated that many shareholders are sensitive to social issues impacting on their corporations regardless of profitability. All these factors temper any concern caused by legitimizing in theory the giving of corporate management a certain amount of discretion in social responsibility matters, especially since the law in fact has long recognized the legitimacy of such an arrangement.

III. THE PARADIGMS APPLIED: COMMON LAW AND STATUTORY DEVELOPMENT OF CORPORATE SOCIAL RESPONSIBILITY

With these variant models of corporate governance in mind, we can examine applicable common and statutory law. The question is whether our ethical models accurately reflect existing law; if not the moral claim must bear the entire burden of reform.

Advocates of the respective models of corporate governance for good reason often conjoin ethical and descriptive claims of authenticity. Professor Eisenberg, for example, contends that the economic model both describes existing law (with some limitations) and entails normative validity predicated on wealth maximization. The political model he opposes, in comparison, is

89. Henry Manne in The Limits and Rationale of Corporate Altruism: An Individualistic Model, 59 VA. L. REV. 708 (1973) agrees with this position: “Arguably, the most appropriate approach for courts is to prohibit fraud and self-dealing by corporate managers but not to second guess their non-fraudulent activities. Market displacement mechanisms will generally take care of efficiency problems, including non-profitable charitable activities.” Id. at 714.
largely reformatory in nature. Part of the cogency of Professor Eisenberg's criticism of the political model rests on the impracticality of the proposed revisions. While impracticality may not override ethical considerations, there is something to be said for locating the burden of persuasion with those recommending reform. This is merely to affirm that the rule of law or formal justice is an aspect of justice which respects legitimate expectations. As Rawls suggests "[o]ne kind of injustice is the failure of judges and others in authority to adhere to the appropriate rules or interpretations thereof in deciding claims." Consequently where reform is necessary in the law for normative purposes special attention must be paid to the justificatory reasons for the departure.

Accordingly, there is some ethical significance in matching our proposed models with an adequate description of existing law. Cases and statutes that do not fit have to be explained. Some anomalies may be disregarded as mistakes: the courts and legislatures involved simply do not always understand the legitimate premises of corporate law. Other exceptions and limitations are more problematic. Certain "mistake" cases may match our intuitive judgment about how the particular case ought to be decided; in this sense, they may recommend further revision of the model. Other exceptions by their number or force may challenge the model's accuracy. An investigation of common law decisions and legislative provisions, therefore, provides a necessary testing ground for evaluating the cogency of the alternative models of corporate governance. Again, the object of our inquiry is the attaining of a reflective equilibrium between our preferred model and the law.

A. Common Law Development of Corporate Responsibility

1. Dodge v. Ford

The landmark common law case on the subject of corporate social responsibility remains *Dodge v. Ford*, discussed previously in connection with the contract model. Its holding that management is strictly liable to maximize profits for the benefit of shareholders heavily influences common law reasoning to the present, warranting a closer examination of the case.

The original investors incorporated Ford Motor Company in 1903, paying in $100,000 in cash and other property for the stock originally subscribed. As a result of the immediate and complete

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90. J. RAWLS, supra note 80, at 59.
success of the business the corporation was able to later distribute to the original investors an additional $1,900,000 in capital stock in lieu of cash dividends. Henry Ford owned fifty-eight percent of the capital stock; the Dodge brothers owned ten percent.92

For a number of years the corporation paid regular quarterly dividends equal to five percent monthly on capital stock. In addition the corporation paid $41,000,000 through October of 1915 in special dividends. During this amazingly prosperous period the Company reduced the selling price of its touring car from an original $900 to $440 and accumulated $111,960,908 in capital surplus.93

The Dodge brothers, who were financing a competitive manufacturing corporation with the dividends they were receiving from the Ford Motor Company, became discontented in 1916 when Henry Ford declared the corporation’s future policy to discontinue paying special dividends. The Company was to limit future dividends to the 60% regular annual dividends paid on the $2,000,000 authorized capital stock of the corporation. Explaining his change of policy, Ford published in the public press the following declaration:

‘My ambition’ declared Mr. Ford, ‘is to employ still more men; to spread the benefits of this industrial system to the greatest possible number, to help them build up their lives and their homes. To do this, we are putting the greatest share of our profits back into the business.’94

Specifically the plaintiffs condemned as ultra vires several of the board’s decisions which adversely effected their receiving the maximum dividends possible. First, the board’s decision on August 1, 1916 reducing the selling price from $440 to $360 would cost the corporation $40,000,000 in profits for the year ending July 31, 1917. The plainiffs alleged this decision “was adopted only for the purpose of enabling him [Henry Ford] to continue to carry out the policy he had decided upon”95 of extending the benefits to additional workers and the consuming public. Second, the board’s decision to establish a smelting plant was made in furtherance of the expansion policy and “for the purpose of absorbing profits which ought to be distributed to shareholders”96. Lastly, the board’s refusal to pay any special dividends over and above the sixty percent on the capital stock was made because Henry Ford believed the shareholders had made too much money; Ford preferred sharing

92. Id. at 462-67, 170 N.W. at 669-71.
93. Id. at 464-65, 170 N.W. at 669-70.
94. Id. at 468, 170 N.W. at 671.
95. Id. at 472, 170 N.W. at 672.
96. Id. at 497, 170 N.W. at 681.
the benefits with the public through expansion of business and reduction of selling price.

Ford Motor Company defended on the ground that the proposed expansions of the business were necessary to secure the continued success of the company. The Company further denied that its policy of reducing the sales price from $900 to $360 for an improved touring car "was adopted for any reason except the permanent good of the company." Finally, the Company defended their vast accumulation of surplus on the ground that should there be a collapse of business the company would need resources to avoid the necessity of discharging a large number of employees, which policy would "ultimately redound to the best financial interests of the company and its stockholders."

The trial court on December 5, 1917 enjoined the board-recommended smelting expansion, as well as the accumulation of vast capital surplus, and directed the corporation to declare a special dividend of $19,275,385.96.

Ford Motor Company argued on appeal that motives of a humanitarian character would not invalidate the good-faith business decisions of the board of directors, if believed to be in the permanent interest of the corporation. The Dodge brothers, in response, asserted that the board's duty to maximize profits precluded their deciding corporate policy on the basis of philanthropic or altruistic motives. The court on appeal refused to enjoin the smelting expansion or Ford's price reduction policy, as matters within the sound business discretion of the board, but affirmed the trial court's order requiring the corporation to pay $19,275,385.96 in dividends from the accumulated capital surplus.

In limiting the discretion of the board to the choice of means to maximize profits the court cited no applicable statutory or common law authority. Nonetheless the court made it clear on the
basis of contract-normative reasoning that humanitarian motives are inappropriate grounds for deciding corporate policy:

The record, and especially the testimony of Mr. Ford creates the impression that he thinks the Ford Motor Company has made too much money, has had too large profits, and that, although large profits might be still earned, a sharing of them with the public, by reducing the price of the output of the company, ought to be undertaken. We have no doubt that certain sentiments, philanthropic and altruistic, creditable to Mr. Ford, had large influence in determining the policy to be pursued by the Ford Motor Company. . . .102

The court distinguished a line of cases authorizing "incidental humanitarian expenditure of corporate funds for the benefit of the employees"103 from Ford's general purpose to benefit mankind at the expense of the shareholders:

There should be no confusion (of which there is evidence) of the duties which Mr. Ford conceives that he and the stockholders owe to the general public and the duties which in law he and his co-directors owe to protesting, minority stockholders. A business corporation is organized and carried on primarily for the profit of the stockholders. The powers of the directors are to be exercised in the choice of means to attain that end, and does not extend to a change in the end itself, and to the reduction of profits, or to the non-distribution of profits among shareholders in order to devote them to other purposes.104

This case represents the announcement of the contract model of corporate responsibility: the corporation is exclusively responsible to the investors who have property and contract rights to maximum profits. The decision reflects more of a normative commitment to contract principles than either historical authenticity or analytic allegiance to stare decisis. The opinion expressly rejects the public interest model's commitment to multiple corporate constituencies; it also repudiates the political model's deference to democratic processes. In addition the court's language is devoid of reference to the economic model's buzz words of efficiency and wealth maximization. Advocates of the economic analysis school, on the other hand, would certainly approve of Dodge as an exam-

shareholders have a right to expect the profits of their investment, 204 Mich. at 500-02, 170 N.W. at 682.

102. 204 Mich. at 505-06, 170 N.W. at 683-84.

103. Id. at 506, 170 N.W. at 684.

104. Id. at 507, 170 N.W. at 684.
ple of the invisible hand of the common law unconsciously tending toward efficiency and wealth maximization. However, there is some irony in the case. After the court held Ford’s altruistic motives improper, Ford bought out the Dodges, implemented his social policies and, as a result, made the corporation more profitable than it ever had been.\textsuperscript{105} The court’s economic decision, therefore, was inefficient. Finally the opinion disregards the right of the shareholders to choose objectives that might conflict with profit maximization in derogation of the entitlement theory. The majority shareholder, Henry Ford, was precluded from using his property for humanistic purposes: his non-economic interests were held hostage to the economic or limited profit-maximization interests of the minority.

If this case correctly states the law regarding the limits of corporate social responsibility then the public interest (other than economic) and rights (other than contractual) models would be relegated to the never-never land of advisory reforms: they simply would not be descriptive of existing law. In reality, the strict contract version articulated in \textit{Dodge} had little historical support then and has since been substantially revised by common law decisions and statutory reform.

A review of common law development on the issues of corporate social responsibility demonstrates the following: some courts revise the strictures of \textit{Dodge} by considering what appears to be altruistic corporate acts as compatible with the long-term economic interest of the corporation. These cases give descriptive credence to both the contract and economic models. At some point the liberality of the interpretation of economic interest transforms the profit-maximization constraint into a legal fiction which obscures the real justification for the decision. To the extent these cases use long-term economic interests as a screen to justify an intuitively acceptable result that is in reality not economically dependent, they call for a revised model of corporate results. Other courts openly disregard the economic constraint entirely in favor of an expanded view of corporate social responsibility. Professor Eisenberg describes these cases as limitations on the economic model. In fact these cases and statutes represent anomalies for the contract and economic models. Advocates of the public interest and rights models use these cases as examples of their descriptive authenticity; their intuitive validity is relied upon as a spring board to encourage further reform. Cases both before and after \textit{Dodge} evidence respect for a broader perspective of the proper

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limits of corporate responsibility. Models justifying their results, therefore, must be afforded increased respect.

2. Pre-Dodge Cases

The Court in Dodge distinguished a line of English and American cases validating “incidental humanitarian expenditures” which arguably were in the best interests of the corporation. These cases legitimized socially responsible decisions against ultra vires charges on both economic and humanitarian reasoning.

In Steinway v. Steinway & Sons, Henry Steinway, a seven percent owner of the corporation, filed a complaint against the corporation on the grounds that certain corporate expenditures were extravagant and unnecessary, having no basis in the business interest of the corporation. Specifically he challenged as ultra vires the company’s purchase of land for its employees and the subsequent “establishment of a church, a school, a free library, and a free bath . . . .” In denying the plaintiff’s petition for relief, the court held that the acts of the corporation “as they have [been] done, for the physical, intellectual, and spiritual wants of their employees, under the circumstances of the case, were not ultra vires.” The court explained that while corporate decisions must serve corporate ends, changing socio-economic circumstances often expand corporate ends: “As industrial condition change, business methods must change with them, and acts become permissible which at an earlier period would not have been considered to be within corporate power. This, I think, tends to explain the difference found in the reported cases.”

The court also noted that the corporation’s concern for the moral as well as material needs of its employees reduced strikes and agitations and increased their continued and faithful services. As a result the corporation actually benefitted both economically and socially from their humanistic activities. What is important for our discussion is that the court recognized a transition away from a strict economic constraint toward an image of the corporation as a socially responsible entity with moral sensitivities of its own.


107. 17 Misc. 43, 40 N.Y.S. 718 (1896).

108. Id. at —, 40 N.Y.S. at 719.

109. Id. at —, 40 N.Y.S. at 720.

110. Id.

111. Id. at —, 40 N.Y.S. at 721.
People v. Hotchkiss\textsuperscript{112} presents a similar fact situation. There the court permitted a life insurance company to purchase a hospital for the care and treatment of its employees afflicted with tuberculosis, despite shareholder complaints that their economic interests suffered as a result. The court permitted these socially responsible acts where they benefitted corporate employees:

The duties of the employer to the employé [sic] have been enlarged in recent years, and are not merely that of the purchaser of the employé's time and service for money. The enlightened spirit of the age, based upon the experience of the past, has thrown upon the employer other duties, which involve a proper regard for the comfort, health, safety and well-being of the employé. A corporation may not only pay to its employé the actual wage agreed upon, but may extend to him the same humane and rational treatment which individuals practice under like circumstances. . . . We see corporations . . . doing many humane and praiseworthy acts which formerly might have been questioned as not fairly within the powers or duties of the corporation . . . . [u]nless it is shown . . . unproductive of beneficial results, the practice may stand as well within the scope of its business. The reasonable care of its employés, according to the enlightened sentiment of the age and community, is a duty resting upon it, and the proper discharge of that duty is merely transacting the business of the corporation.\textsuperscript{113}

Again Hotchkiss represents a conscious enlargement of corporate powers beyond profit maximization. Moreover the acts are morally praiseworthy suggesting their supererogatory nature: the public interest does not require such caring conduct, but it is gratefully accepted as a good deed.

Hawes v. Oakland\textsuperscript{114} also permitted socially responsible acts even extending beyond the humane treatment of employees. The Court in Hawes validated the defendant corporation's voluntary furnishing the City of Oakland water free gratis, reasoning that since the city had conferred valuable rights on the company by special ordinance it might have been “of the highest wisdom”\textsuperscript{115} to be generous with the city. The opinion smacks of economic self interest, but also implies respect for socially responsible conduct that benefits the entire community.

The English line of cases the court distinguished in Dodge also

\textsuperscript{112} 136 A.D. 150, 120 N.Y.S. 649 (1909).
\textsuperscript{113} Id. at —, 120 N.Y.S. at 651.
\textsuperscript{114} 104 U.S. 450 (1881).
\textsuperscript{115} Id. at 462.
permitted socially responsible acts which had been challenged as ultra vires, where they were undertaken either to enhance employee\textsuperscript{116} or customer\textsuperscript{117} relations. The court in Taunton, for example, expressly recognized that customary or expected gratuities would normally not be ultra vires: “Let it be so called [a gratuity], it does not follow that it is beyond the power of the company if to give such gratuities be the generally received method of conducting such a business.”\textsuperscript{118}

If economic efficiency were the sole test then patterns of “inefficient” contributions could hardly justify their continuance. Dodge’s extreme limitation of managerial discretion in the area of corporate responsibility, therefore, can be viewed more as an aberration than the common law norm. The strict profit-maximization thesis it announced can be more persuasively supported by the contract reasoning that permeated legal thinking during that period rather than common law precedent. These cases might be reconciled to some extent with a long-term economic interest, consistent with the contract and economic models. The language of the opinions, however, implies social purposes beyond profit maximization. They are more understandable from a rights perspective: an “enlightened” sense of responsibility and the acceptability of moral choice seems to pervade each of these cases more than a calculating economic rationale. This is especially true since they effect an acceptable transition away from the stricter economic standard which had earlier controlled such cases.

3. Post-Dodge Cases

The line between justifying corporate expenditures because they benefit the corporation versus validating them on independent grounds of social responsibility is a difficult one to draw and apply. Nonetheless the broader ground of legitimation, embryonic in the pre-Dodge cases, has received substantial legislative and judicial support since Dodge. If taken seriously, as I argue they should be, then the economic and contract models of the corporation inspired by Dodge need reformation.

Perhaps the first post-Dodge case to articulate a broader justi-
fication for socially responsible corporate activities is *State ex rel. Sorenson v. Chicago, B. & O. R. Co.* 119 The plaintiff in *Sorenson* sought to enjoin “the defendant railroad companies from giving free passes or reduced transportation to ministers of the gospel and persons engaged in eleemosynary and charitable work.” 120 The complainant also sought to invalidate legislative approval of free passes or reduced transportation to the classes named in the act. 121 The issue arose because the Interstate Commerce Act of 1887 and the Nebraska Constitution prohibited “unjust discrimination” in the setting of railroad fares. 122 The court upheld the statutes and legitimated the “contributions” without making any complex profit-maximization argument: “We see no reason why a railroad corporation may not, to a reasonable extent, donate funds or services to aid in good works.” 123 The court could have avoided the “good works” argument by muttering the traditional incantation about long term corporate benefits. Instead, the court simply stopped at the plausible conclusion that corporations can reasonably participate in socially responsible activities, regardless of any economic benefit that may indirectly inure to the corporation as a result.

The implication in *Sorenson* of a broader purpose than the contract and economic models would substantiate is made explicit in *A.P. Smith Mfg. Co. v. Barlow*. 124 The defendant corporation, incorporated in 1896 for the purpose of manufacturing and selling fire hydrants and special equipment used in water and gas industries, had contributed regularly to local charitable institutions. 125 When shareholders questioned the board’s 1951 decision to appropriate $1,500 to Princeton University the corporation instituted a declaratory judgment action to determine whether it was within the board’s power to make such contributions. 126 When the chancery division held the donation intra vires the shareholders appealed. 127

The corporation argued several points to substantiate a “corporate benefit” claim. First, the corporation noted trial testimony given by Frank W. Abrams, chairman of the board of the Standard Oil Company, “that it was not ‘good business’ to disappoint ‘this

119. 112 Neb. 248, 199 N.W. 534 (1924).
120. *Id.* at 249, 199 N.W. at 535.
121. *Id.* at 249-50, 199 N.W. at 535.
122. *Id.* at 252-54, 199 N.W. at 535-36.
123. *Id.* at 256, 199 N.W. at 537.
125. *Id.* at —, 98 A.2d at 582.
126. *Id.*
127. *Id.*
reasonable and justified public expectation;" that corporations "acknowledge their public responsibilities" ... "nor was it good business for corporations 'to take substantial benefits from their membership in the economic community while avoiding the normally accepted obligations of citizenship in the social community.'"128 Second, the company stressed testimony given by Irving S. Olds, former chairman of the board of the United States Steel Corporation, and Harold W. Dodds, President of Princeton University, to the effect that private institutions of higher learning contributed significantly to our democratic society thereby furthering the "'long-range interest of its stockholders, its employees and its customers.'"129 Third, state legislation expressed "a strong public policy in favor of corporate contributions. . . ."130

Given the facts of the case the court could have validated the donation on the long-term economic benefit rule; instead the court justified the conduct as responsive to an increased sense of corporate social responsibility. The court explained that while business corporations in early history included "public" as well as "profit" objectives, social and economic developments led to the adoption of "profit" as the controlling objective. The court noted that "[d]uring the 19th Century when corporations were relatively few and small and did not dominate the country's wealth, the common law rule did not significantly interfere with the public interest. But the 20th Century has presented a different climate."131

The court explained that as social and economic conditions changed in this country, courts began modifying the strictures of the common law profit maximization rule by liberal findings of indirect benefit. Eventually the courts went even further in upholding socially responsible acts without any limitation based on economic benefits.132 It is in furtherance of this rule that the Barlow court upheld the donation: "It seems to us that just as the conditions prevailing when corporations were originally created required that they serve public as well as private interests, modern conditions require that corporations acknowledge and discharge social as well as private responsibilities as members of the communities within which they operate."133 The court recognized this approach to be broader than the Dodge economic benefit rule, but

128. Id. at —, 98 A.2d at 583.
129. Id.
130. Id.
131. Id. at —, 98 A.2d at 584.
132. Id. at —, 98 A.2d at 584-86.
133. Id. at —, 98 A.2d at 586.
stated in the *Steinway* tradition that the common law must evolve in tandem with social and economic changes:

The genius of our common law has been its capacity for growth and its adaptability to the needs of the times. Generally courts have accomplished the desired result indirectly through the molding of old forms. Occasionally they have done it directly through frank rejection of the old and recognition of the new. But whichever path the common law has taken it has not been found wanting as the proper tool for the advancement of the general good.\(^{134}\)

In legitimizing the grant under common law and statutory grounds the court concluded with a public-interest appeal for a modern vision of broadened corporate responsibilities:

Clearly then, the appellants, as individual stockholders whose private interests rest entirely upon the well-being of the plaintiff corporation, ought not be permitted to close their eyes to present-day realities and thwart the long-visioned corporate action in recognizing and voluntarily discharging its high obligations as a constituent of our modern social structure.\(^{135}\)

*Barlow* then represents a common law repudiation of both the contract and economic models. The court rejects the right of dissenting shareholders to demand a strict financial accounting of all corporate activities; it also denies that the public interest is most efficiently served by wealth maximization. Rather the court announced that the common law permits voluntary recognition by the business entity of moral duties to aid worthwhile causes.\(^{136}\) The focus on voluntariness implies an entitlement theory which fits the description of the rights model more accurately than any other explanation.

The social responsibility rule announced in *Sorenson* and explained in *Barlow* was cited in partial justification of the court’s decision in *Union Pacific R.R. Co. v. Trustees, Inc.*\(^{137}\) The corporate act complained of in *Union Pacific* was a $5,000 contribution made to a non-profit corporation organized by Union Pacific, which was dedicated to charitable, scientific, religious and educational purposes.\(^{138}\) Intermingling corporate benefit and social responsibility arguments, the court accepted Union Pacific’s explanation that a “new concept conceived in a shifting socio-economic atmosphere...

\(^{134}\) *Id.*

\(^{135}\) *Id.* at —, 98 A.2d at 590.

\(^{136}\) *Id.*


\(^{138}\) *Id.* at —, 329 P.2d at 399.
nurtured by legislative, corporate and judicial thinking" necessitated a "reasonable percentage of corporate income . . . [being] earmarked for worthy causes, as a necessary and proper item of business expenses, just as funds are tagged for advertising, public relations and the like." Thus the court held:

[w]e think that a power once denied today may be implied under changed conditions and philosophies, and that in the light of present day industrial and business exigencies, common sense dictates that included in the implied powers of a corporation, an authority should be numbered that allows contributions of reasonable amounts to selected charitable, scientific, religious or educational institutions, if they appear reasonably designed to assure a present or foreseeable future benefit to the corporation . . . .

Justice Worthen, in dissent, insisted that the quid pro quo explanation simply was not credible: "In my opinion the real purpose, of these public spirited directors, is their desire to aid worthwhile causes that need their assistance." For Justice Worthen that motivation was unjustified under economic-benefit principles.

The Worthen dissent honestly depicts the legal-fiction problem that has grown around the economic model. The courts increasingly have realized the appropriateness of corporations acting morally responsible; this intuitive conviction might be described as their considered judgment on the subject. The problem is that the received profit-maximization model does not allow non-economically motivated acts. Rather than having their considered judgment give way to the explanatory paradigm, they invent a legal fiction: the corporation will eventually benefit financially somehow if it adopts a socially responsible attitude. A more honest approach would be to reformulate the accepted paradigm (adopt a rights model) so that principle and intuition converge.

Shlensky v. Wrigley is another "corporate responsibility" case that seems to reduce the corporate-benefit rule to a legal fiction. The complaining shareholders in Wrigley sought to have the defendant corporation install lights in the Chicago Cub's baseball stadium for night baseball games. They argued that Philip Wrigley, the president and 80% owner of the corporation, "refused to install lights contrary to the economic interest of the corporation because of his personal belief that the installation of lights and

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139. Id. at —, 329 P.2d at 401.
140. Id. at —, 329 P.2d at 402.
141. Id. at —, 329 P.2d at 405 (Worthen, J., dissenting).
night baseball games will have a deteriorating effect upon the surrounding neighborhood.” The court in Wrigley noted that even though all of the other nineteen major league clubs had found it in their economic interest to play at night the court would not require conformity. Directors cannot be compelled to follow the lead of others; their good faith business decisions would be sustained absent the showing of fraud, illegality or conflict of interest.

Other cases have invoked a liberal interpretation of the business judgment rule to permit corporations to pursue activities aimed more in support of public than business interests. In Sylvia Martin Foundation, Inc. v. Swearingen, the court permitted Standard Oil of Indiana to float a bond issue abroad at a higher rate of interest than would have been required if they had been offered for sale in the United States where the interest rates were lower, solely to aid the United States balance of payments problem. Although the complaint was dismissed on jurisdictional grounds, the court in dictum indicated it would have allowed the decision in any event on the basis of the board’s discretion in making such business judgments. Similarly in Kelly v. Bell the corporation’s decision to honor a non-binding agreement to pay a voluntary tax on existing machinery, where the legislature relied on the agreement to repeal the tax so that machinery thereafter installed would not be taxed, was held to be a valid exercise of business judgment. The court had doubts about characterizing the payments as donations, as the Chancellor had in his opinion, but concluded that since the board had not been motivated by personal gain or bad faith the business judgment rule would validate their decision as reasonably in the best interest of the corporation.

Relying on the smoke screen of business judgment to justify acceptable corporate conduct that is not profit motivated seems improper from a jurisprudential perspective and totally unnecessary. If the common law rule ever was otherwise, the Steinway-Barlow-Union Pacific cases indicate in dicta that the common law was changed (can change) to permit a recognition of broader corporate purposes and powers.

143. Id. at —, 237 N.E.2d at 778.
144. Id. at —, 237 N.E.2d at 780.
146. Id. at 232.
147. Id. at 235.
149. 266 A.2d at 879.
The Supreme Court's decision in *First Nat'l Bank of Boston v. Bellotti*\textsuperscript{150} takes the analysis away from a business judgment defense and may impact significantly on the assessment of an adequate description of the corporate paradigm. *Bellotti* did not involve a derivative action predicated on ultra vires and breach of fiduciary duties. Accordingly its holding could be narrowly construed as inapplicable to the corporate power issue. Nonetheless the breadth of the opinion likely will influence the development of the corporate power doctrine, at least as applied to activities aimed at influencing public opinion. The issue, one of first impression, involved the constitutionality of a Massachusetts criminal statute which prohibited corporate expenditures on referendum issues.\textsuperscript{151} The referendum issue involved was a constitutional amendment permitting a graduated personal income tax; the tax did not materially affect the business property or assets of the corporation.\textsuperscript{152} The "materially affect" limitation would be consistent with the economic model. Although there otherwise may have been some leeway under a business judgment analysis as to what affected the business, the statute provided ""'[n]o question submitted to the voters solely concerning the taxation of the income, property or transactions of individuals shall be deemed materially to affect the property, business or assets of the corporation.'"\textsuperscript{153} The statute, therefore, took away management's opportunity to decide whether the corporation ought to engage in public debate on certain issues. The Court held the statute unconstitutionally infringed on the corporation's right of free speech.

What is important for this discussion is that the Court deprecated the state's alleged ""'overriding interest related to the prevention of corporate domination . . . assuring that shareholders are not compelled to support and financially further beliefs with which they disagree where, as is the case here, the issue involved does not materially affect the business, property, or other affairs of the corporation.'"\textsuperscript{154} The Court stated:

Ultimately shareholders may decide, through the procedures of corporate democracy, whether their corporation should engage in debate on public issues. Acting through their power to elect the board of directors or to insist upon protective provisions in the corporation's charter, shareholders normally are presumed competent to protect their

\textsuperscript{150.} 435 U.S. 765 (1978).
\textsuperscript{151.} *Id.* at 767.
\textsuperscript{152.} *Id.* at 769.
\textsuperscript{153.} *Id.* at 768.
\textsuperscript{154.} *Id.* at 812 (White, J., dissenting).
own interests.155

The Court also added that “minority shareholders generally have access to the judicial remedy of a derivative suit to challenge corporate disbursements alleged to have been made for improper corporate purposes or merely to further the personal interests of management.”156

Justice White in dissent made a Dodge-like argument that minority shareholders ought not to be saddled with the social preferences of the majority. The majority countered by arguing: first, that shareholders are bound by other “equally important and controversial corporate decisions...made by management or by a predetermined percentage of the shareholders”;157 second, “no shareholder has been ‘compelled’ to contribute anything...the shareholder invests in a corporation of his own volition and is free to withdraw his investment at any time for any reason”; and, third, a “hypothetical minority” ought not to be able to “completely silence the majority.”158

The Court also noted a practical problem with adopting a “materially affecting” (business judgment) test:

management never could be sure whether a court would disagree with its judgment as to the effect upon the corporation’s business of a particular referendum issue. In addition, the burden and expense of litigating the issue—especially when what must be established is a complex and amorphous economic relationship—would unduly impinge on the exercise of the constitutional right.159

The “rights” model explains the Court’s reasoning in Bellotti more adequately than any other model. The Court expressly rejects the economic constraint, as too restrictive of corporate freedom: the corporation may choose to participate in political campaigns regardless of any cost-benefit analysis. Similarly, the Dodge contract limitation on the majority is turned on its head: the Court prevents the minority from silencing the majority, a concern that the court in Dodge failed to appreciate. The “public interest” and “political” alternatives also cannot explain the Bellotti case: the political issue is whether a graduated income tax is in the public’s interest (corporate contributions may skew the process and work adversely to the public interest); and the shareholder-

155. Id. at 794-95.
156. Id. at 795.
157. Id. at 794 n.34.
158. Id.
159. Id. at 785 n.21.
ers are the only constituents the court recognizes as being entitled to protection.

If Bellotti is correct then the rights model expresses the most persuasive description of the parameters of corporate social responsibility. With the business judgment defense out of the way the proper focus on the rights of the shareholders to act collectively for purposes other than profit maximization is affirmed. It would seem inconsistent to suggest that corporations have a right to campaign for any social issue without also contending that they have a right to make direct contributions in support of non-economically motivated activities. Bellotti states a principle that brings the rights model into reflective equilibrium with our considered judgments.

In brief, the common law trend in corporate-social-responsibility cases follows a rights analysis more closely than any other explanatory paradigm. Gone are the Dodge days when management was required to act as a hired gun for profit maximization. Presently management can freely choose to act socially responsible, even if there exists no likelihood of resulting profits. At the same time the corporation may choose to be strictly profit oriented; the public interest models have not penetrated the common law to make socially responsible acts mandatory. Accordingly, the rights model carries descriptive as well as prescriptive authenticity. This analysis applied to the common law also cogently can be extended to statutory developments on the subject of corporate social responsibility.

B. STATUTORY PROVISIONS AND CORPORATE SOCIAL RESPONSIBILITY

While the special facts of any case may obscure the underlying rationale for any corporate responsibility decision, statutes often delineate their policy orientation. The early general corporation laws narrowly circumscribed corporate purposes and powers. Corporate statutes permitted business entities to organize for profit; the court as a result began circumscribing corporate powers with the profit objective in mind. Soon the courts began modifying the harshness of the profit constraint. The courts looked to the business judgment defense to justify what appeared to be socially acceptable conduct; suggesting at heart the decision was profit motivated. Later some courts openly acknowledged broader corporate powers predicated on an expanded view of the ethical duties of corporations. Recognizing the unsatisfactory implications of a strict profit constraint, state legislatures also gradually ex-
panded corporate powers to permit socially responsible acts that were beyond the profit-maximization requirement. Presently every jurisdiction in this country recognizes by statute specific corporate powers that are not economically inspired. The proposed Restatement defended by Professor Eisenberg is no different: certain socially responsible acts (those required by law, those recognized by ethical business conduct, and those devoted to limited humanitarian purposes) are authorized regardless of effect on corporate profit and shareholder gain. These statutes and proposal make it clear that an economic paradigm cannot adequately explain existing and recommended law covering social responsibility. An examination of these statutes further establishes the increased coherency of a rights model in interpreting the law of corporate social responsibility.

The earliest statutory expansion of general corporate powers which went beyond profit maximization is found in Texas's general corporation act of 1917. There the Texas legislature qualified the business-objective language by stating

nothing in this section shall be held to inhibit corporations from contributing to any bona fide association, incorporated or unincorporated, organized for and actively engaged for one year prior to such contribution in purely religious, charitable or eleemosynary activities, nor to local, district, or statewide commercial or industrial clubs, or associations, or other civic enterprises or organizations.

This statute established a policy-orientation that departed from profit maximization constraints. If the courts were inclined to interpret the common law as precluding charitable contributions, the legislature wanted to override that rule by providing some limitations.

Other states slowly followed Texas's lead. Six states enacted donative statutes between 1917 and 1937. Thirteen states adopted donative statutes in the 1940's. When the Model Business Corporation Act was first published in 1950, therefore, the trend already had been set. The Model Act closely followed the Illinois donative provisions. Section 4(m) empowered each cor-

160. See note 6 and accompanying text supra.
161. TEXAS CIVIL STATUTES tit. 25, art. 1164 (Vernon 1918).
162. New York (1918); Tennessee (1925); New Jersey (1930); Massachusetts (1933); Michigan (1935); and Missouri (1937).
163. Delaware (1941); Maryland, North Carolina, Pennsylvania and Virginia (1945); Colorado and Hawaii (1947); California, Illinois, Indiana, Minnesota, Oklahoma and West Virginia (1949).
164. ILL. ANN. STAT. ch. 32, § 157.5(m) (Smith-Hurd 1982).
poration "[t]o make donations for the public welfare or for charitable, scientific or educational purposes; and in time of war to make donations in aid of war activities."165 Section 4(n) further authorized each corporation "[i]n time of war to transact any lawful business in aid of the United States in the prosecution of the war."166 Twenty-three states, Puerto Rico, and the District of Columbia adopted comparable provisions in the 1950's.167 The "war provision" expanded socially acceptable acts beyond the donative category to include business activities made necessary by emergency circumstances. War became the touchstone that would allow economic considerations to be held in abeyance.

These early limitations on the profit constraint opened a Pandora's box that frustrates the economic model's ability to explain the existing law. While donative provisions could be treated as de minimus limitations and war provisions as extreme measures for extreme circumstances, further qualifications challenge the cogency of the economic model itself. Section 4(m) as amended in 1969 eliminated the language "and in time of war to make donations in aid of war activities."168 Section 4(n) broadened the power of the corporation in the public area by authorizing each corporation "[t]o transact any lawful business which the board of directors shall find will be in aid of governmental policy."169 Suddenly the emergency exception became the business-as-usual rule.

Presently the social responsibility provisions defy economic analysis. Nine states follow the Model Act's 1950 provisions.170 Delaware and Kansas have war donation provisions but have broadened their "n" provisions to allow activities "in aid of governmental authority."171 Ten states and the District of Columbia have amended their "m" donative provisions in accordance with the Model Act's 1969 amendments; but they still permit public activi-

165. MODEL BUSINESS CORP. ACT. § 4(m) (1966).
166. Id. at § 4(n).
167. Arkansas, Connecticut, Kansas, Maine, New Mexico, and Wisconsin (1951); Kentucky, Mississippi, and Rhode Island (1952); Georgia, Nebraska, Nevada, New Hampshire, Oregon, Vermont and Washington (1953); Louisiana and District of Columbia (1954); Florida and Utah (1955); Puerto Rico (1956); North Dakota, Alaska (1957); Alabama and Iowa (1959).
169. Id. at § 4(n).
ties furthering war efforts.\textsuperscript{172} Nine states have enacted the Model Act's amended versions of sections 4(m) and (n).\textsuperscript{173} Rhode Island adopted the language of (m), and has an "(n)" provision that is similar in substance.\textsuperscript{174} Four states enacted "m" donative provisions, but have nothing equivalent to "n".\textsuperscript{175} Five states subject their donative provisions to contrary restrictions in the articles.\textsuperscript{176} Virginia allows overriding instructions which would preclude corporate donations to be contained not only in the articles but also in shareholder resolutions.\textsuperscript{177} These states expressly recognize the right of shareholders to choose freely the extent to which profit maximization captures all of their interests and sense of responsibility. They are decidedly entitlement oriented. Maine authorizes activities in furtherance of war efforts regardless of the articles.\textsuperscript{178} For Maine property rights are, therefore, subject to public interest limitations at least in time of war. California, Maine and New Jersey, which have very broad altruistic provisions, expressly reject any requirement that corporate donations actually benefit the corporation in any economic sense.\textsuperscript{179} In this manner they repudiate the contract and economic models. Oklahoma allows donations to be in either the corporate or public interest.\textsuperscript{180}

Fourteen states have broader donative categories than the Model Act. These states specify charitable, humanitarian and social purposes for which corporate contributions can be made regardless of economic benefit; the broad donative purposes include

\begin{itemize}
\item \textsuperscript{172} ARK. STAT. ANN. § 64-104(6), (7) (1980); D.C. CODE ANN. § 29-304(13) (1983); GA. CODE ANN. § 22-202(13), (14) (1983); ILL. ANN. STAT. ch. 32, § 157.5(m) (Smith-Hurd 1982); IOWA CODE ANN. § 496A.4(13), (14) (West 1983); LA. REV. STAT. ANN. § 12:41(12), (13) (West 1983); MICH. COMP. LAWS ANN. § 450.1261(K) (West 1983-1984); MISS. CODE ANN. § 79-3-7(m), (n) (1982); PA. STAT. ANN. tit. 15, §§ 1302(16), 1314 (Purdon 1983-84); UTAH CODE ANN. § 16-10-4(m), (n) (1953); WIS. STAT. ANN. § 180.04(12), (13) (West 1982-83).
\item \textsuperscript{173} ALA. CODE § 10-2A-20(13) (1983); COLO. REV. STAT. § 7-3-101(m) (1983); FLA. STAT. ANN. § 607.011(k), (n) (West 1983); IDAHO CODE § 30-1-4(m), (n) (1983); KY. REV. STAT. ANN. § 271A.020(13), (14) (Baldwin 1983); N.M. STAT. ANN. § 53-11-4(m), (n) (1982); OR. REV. STAT. § 57.030(13), (14) (1981); TEX. BUS. CORP. ACT ANN. art. 2.02(14), (15) (Vernon 1982-83); W. VA. CODE § 31-1-8(m), (n) (1983).
\item \textsuperscript{174} R.I. GEN. LAWS § 7-1.1-4(m), (n) (1982).
\item \textsuperscript{176} ARK. STAT. ANN. § 64-104(6) (1981); CONN. GEN. STAT. ANN. § 33-291(d)(2) (West 1982); IND. CODE ANN. § 23-1-2-17 (Burns 1982); N.J. STAT. ANN. § 14A:3-4 (West 1983-1984); OHIO REV. CODE ANN. § 1701.13(D) (Baldwin 1979).
\item \textsuperscript{177} VA. CODE § 13.1-2.1(m) (1983).
\item \textsuperscript{180} OKLA. STAT. ANN. tit. 18, § 1.19(11) (West 1982).
variously the following list of eligible beneficiaries: community
chests or funds, religious, literary, prevention of cruelty to children
or animals, hospital, civic, contributions for political candidates,
and issues, to the extent permitted by law, the preservation
and betterment of social and economic conditions in any commu-
nity in which such corporation is doing business, philanthropic, be-
nevolent, veteran rehabilitation service, artistic, patriotic
purposes, cultural purposes, or of boards of trade, chambers of
commerce, commercial clubs, employee credit unions, company
pension, annuity and bonus plans.

Some states limit the amounts that can be contributed for hu-
manistic purposes. In effect they are making policy choices re-
garding the reasonable limits of the moral duty of mutual aid.
Three base their limitations on amounts that will qualify for tax
deductions. North Carolina has a contribution limitation that
"no part of the net earnings . . . inures to the benefit of any private
stockholder or individual . . . ." New Jersey precludes dona-
tions "if at the time of the contribution or immediately thereafter
the donee institution shall own more than 10% of the voting stock
of the donor corporation or one of its subsidiaries." These provi-
sions protect the corporation from acting disingenuously to benefit
management rather than worthy causes. Tainted business contri-
butions would already be protected by fiduciary duties of loyalty
placed on management, but these provisions provide further pro-
tection. Tennessee provides that the donations shall be charged to
operating expense, and can be made only from earned surplus.
Maryland authorizes "reasonable gifts . . . out of profits." Indiana
requires that contributions must come from "gross income."
These last provisions are designed to protect innocent third parties
(especially creditors) from corporate humanitarianism.

The pattern set by these statutes is clear: the states have each

181. ARK. STAT. ANN. § 64-104(6) (1981); CAL. CORP. CODE § 207(e) (West 1983);
1983); MD. CORPS. & ASS'NS CODE ANN. § 2-103(13)(ii) (1982); MASS. ANN. LAWS ch.
155, § 12A (Michie Law. Co-op. 1983-1984); MICH. COMP. LAWS ANN. § 450.1261(k)
(West 1983-1984); MINN. STAT. ANN. § 300.66 (West 1983); MO. ANN. STAT.
§ 351.385(15) (Vernon 1983); NEB. REV. STAT. § 21-2004(13) (1982); N.J. STAT. ANN.
§ 14A:3-4 (West 1983); N.Y. BUS. CORP. LAw § 202(a) (12) (McKinney 1983); N.C. GEN.
182. IND. CODE ANN. § 23-1-2-17 (Burns 1982); S.C. CODE ANN. § 33-3-20(a)(7)
187. IND. CODE ANN. § 23-1-2-17 (Burns 1982).
empowered corporations to act beyond what a cost-benefit analysis would require. While the parameters of the non-economic rights possessed by corporations may be appropriate for discussion, the viability of limitations is not. No state restricts corporate power in accordance with the economic principle; corporations generally are entitled to act in accordance with mixed profit and humanitarian purposes.

Corporate management under these permissive statutes and the liberal common law can voluntarily expand their sense of purpose. Rather than acting as cold-calculating business school graduates with an accounting sheet forever in their minds, they can internalize the moral responsibility of individuals generally and apply them to corporate circumstances. The statutes, of course, are specific in many respects and may not cover certain socially motivated acts. The common law supplies an additional safety net, but the security it provides largely depends on the paradigm used to evaluate the conduct. For my part the gravitational pull, the weight of the cases, the trend in the law bespeaks of a rights-oriented paradigm of corporate responsibility.

IV. CONCLUSION

The rights paradigm of corporate social responsibility both adequately describes existing law and comports with an ethical theory predicated on a view of the individual as a moral being capable of moral conduct and entitled to mutual respect. The individual acting either as a shareholder or as a member of management is entitled (obligated) to act rationally in his or her own self-interest and in the interest of those in society he freely chooses to aid. Corporations under this view potentially become caring, responsible reflections of those who own its property and wield its enormous power. This rights-oriented view of the corporation not only matches our intuitive judgment about how corporations ought to behave, it also explains cases and statutes that are characterized as limitations to other models. This convergence of intuition, normative theory, and law brings us into reflective equilibrium: corporations can act (ought to be able to act) socially responsible, regardless of the economic consequences of their acts.