2

Background

The corporate duties discussed in this book are best understood against the background of the long-standing relationship between corporations and the public. In this chapter, we unpack that relationship, first, by looking at historical aspects of the societal role of corporations, moving from the origins of business entities to recent developments. This is followed by a more nuanced examination of four specific reasons that justify the imposition of public duties – or the strengthening of such duties – on corporations.

2.1 BRIEF HISTORY OF THE CORPORATION AND ITS RELATIONSHIP WITH THE PUBLIC

In this section, we take a historical look at the relationship between corporations and the public. Our discussion begins with medieval guilds, moves to trading companies and vehicles requiring charters, and ultimately concludes with the corporate entities we are most familiar with today. The section highlights the origins of corporations as public or quasi-public institutions and the subsequent transformation to the focus on private profit generation. It ends with a look at contemporary developments that re-emphasize the connection between corporations and the public.

2.1.1 *Public Functions of Early Corporations and Precursors*

During early medieval times, the first prominent corporate bodies emerged. These bodies had distinctly public functions. They were institutions founded to support religion and learning – for example, the Roman Catholic Church and European universities – as well as towns and guilds of merchants and tradesmen.[1] Medieval guilds, with their principles of exclusion and hierarchy can already be seen as

[1] See M. Aoki, *Corporations in Evolving Diversity: Cognition, Governance and Institutions* (Oxford: Oxford University Press, 2010), pp. 3–7.

https://doi.org/10.1017/9781108377072.002 Published online by Cambridge University Press

precursors of contemporary forms of *business* corporations.[2] In addition to the core function of organizing and advancing the interests of their members, guilds assumed useful public roles and made financial contributions to the sovereign, which were seen to justify the special privileges they were given by the state.[3] For instance, various guilds in London helped maintain public order and played a role in governing the city.[4] It was also guilds in England, and later Britain (and other European monarchies), that led to the formation of trading companies – royally chartered associations of merchants who were granted monopolies of trade with specific foreign markets – that rose to prominence particularly in the sixteenth to eighteenth centuries.[5] Similar to the guilds, these bodies were given special privileges based on their valuable contributions to the state, including in the form of substantial financial assistance, governmental administration, and military protection of overseas territories. In many ways trading companies constituted a symbiosis of state and private interests, representing an extension of governmental power bolstered through the means of private capital and initiative.[6]

A key difference between guilds and trading companies was that the latter engaged in the pooling of capital in order to finance bigger, more costly ventures that had the potential to boost financial benefits to investors.[7] The reliance on pooled capital evolved from funding that was raised from fewer investors and used for specific overseas voyages (these less sophisticated precursors of the full-fledged trading company can be referred to as 'regulated companies')[8] to the issuance of permanent stock to investors.[9] This method of financing, which became the norm by 1650, meant that the stockholders benefitted from profits, but, given the absence of limited liability at this time, were normally also fully exposed to their companies' liabilities. Although trading companies pursued private aims – returning profits to their investors – they also had features that implied public functions, including armies, police forces, a system for conducting criminal trials, and jails.[10] The British

[2] The concept of public or municipal corporations also developed from these early precursors but their treatment is beyond the scope of this book. On guilds, see T. Nace, *Gangs of America: The Rise of Corporate Power and the Disabling of Democracy* (San Francisco: Berrett-Koehler Publishers, 2003), pp. 19–23; J. Micklethwait and A. Wooldridge, *The Company: A Short History of a Revolutionary Idea* (New York: Modern Library Chronicles, 2005), p. 13 (stating that '[f]or much of the Middle Ages, guilds were the most important form of business organization'). On earlier forms of commercial organizations, see Micklethwait and Wooldridge, pp. 3–14, who describe partnership-like structures used by Sumerian families in Mesopotamia in 3,000 BC, and J. Barron Baskin and P. J. Miranti, *A History of Corporate Finance* (Cambridge: Cambridge University Press, 1997), pp. 29–54.

[3] Barron Baskin and Miranti, *supra* note 2, p. 59.

[4] Nace, *supra* note 2, p. 21.

[5] Ibid., pp. 19–23.

[6] See Barron Baskin and Miranti, *supra* note 2, pp. 59–63.

[7] Nace, *supra* note 2, p. 22.

[8] See P. Lawson, *The East India Company: A History* (Abingdon: Routledge, 1993), pp. 20–21; Barron Baskin and Miranti, *supra* note 2, pp. 58–59.

[9] Nace, *supra* note 2, p. 24.

[10] Ibid., pp. 24–25.

https://doi.org/10.1017/9781108377072.002 Published online by Cambridge University Press

East India Company, in particular, was immensely important for and in various ways intertwined with the state. Among others, a third of Parliament owned its shares, it provided payments to members of Parliament and the King to protect its continued existence against attacks by rivals, and a tax on its tea at one point constituted 10 per cent of the government's revenue.[11]

By the middle of the eighteenth century, however, the large British trading companies had collapsed and there was widespread hostility towards the concept of monopolistic trade companies, which also led to negative views on incorporated entities as vehicles for conducting business.[12] The Industrial Revolution that began around this time was thus not driven by the dominant players of the past but, instead, family enterprises, partnerships, and unincorporated joint stock companies.[13] The reference to the latter category of businesses requires some clarification. Until the end of the eighteenth century, the term 'company' did not necessarily signify that a business was *incorporated*. Both incorporated companies and *unincorporated associations*, which were also called companies, co-existed. The main difference between these two types of companies lay in the act of formation. Incorporated companies were formed through grant of a charter (by the crown and later by an Act of Parliament, in some cases also by way of statute), while unincorporated companies were formed through informal understandings between the members.[14]

Importantly, incorporated companies' charters implied certain public responsibilities or at least an association with the public good on the part of these entities, with early canal building schemes, the construction of railroad lines, and other infrastructure related ventures being prime examples.[15] Business companies, at this stage, were still closely connected to the state and the difference between private and public companies crystalized only later.[16] Additionally, some unincorporated companies were also used to carry out societal functions. Initially, this earned them a more lenient judicial approach towards enforcement of the Bubble Act 1720,[17] which, until its repeal in 1825, prohibited the sale of freely transferable shares by companies operating without charters. The Act eventually still ended the near similar treatment

11 Ibid., pp. 25–28.

12 See R. Harris, *Industrializing English Law: Entrepreneurship and Business Organization, 1720–1844* (Cambridge: Cambridge University Press, 2004), pp. 203–07. Critics of monopolistic merchant companies included Adam Smith, who believed that although they may have initially been useful, they 'have in the long run proved, universally, either burdensome or useless, and have either mismanaged or confined the trade'. A. Smith, *An Inquiry into the Nature and Causes of the Wealth of Nations*, vol. II (London: Macmillan and Co., 1869), pp. 316–17.

13 Nace, *supra* note 2.

14 L. Talbot, *Progressive Corporate Law for the 21st Century* (Abingdon: Routledge, 2013), p. 4.

15 Barron Baskin and Miranti, *supra* note 2, pp. 132–34, emphasizing the quasi-public nature of these ventures; see also Harris, *supra* note 12, pp. 216–24; Talbot, *supra* note 14, p. 7; P. Ireland et al., 'The Conceptual Foundations of Modern Company Law' (1987) 14:1 *Journal of Law and Society* 149.

16 Barron Baskin and Miranti, *supra* note 2, p. 132; Harris, *supra* note 12, pp. 112–14.

17 Talbot, *supra* note 14, p. 14.

https://doi.org/10.1017/9781108377072.002 Published online by Cambridge University Press

of unincorporated and incorporated companies.[18] After a few decades of uncertainty as to the legal treatment of unincorporated companies, the Joint Stock Companies Act 1844 clarified their status, improved financial transparency for outside investors in unincorporated companies and created a new class of public partnership. The Act also enabled the shift from chartering of specific companies to a *system of general incorporation*. While pre-1844 companies had all been public, the introduction of general incorporation paved the way for the ascent of private, closely held companies and a rapid rise in the number of incorporated entities.[19]

A series of company law legislation subsequently introduced further important changes. The Limited Liability Act 1855 introduced universal or general limited liability for UK company shareholders.[20] This was improved in the Joint Stock Companies Act 1856 and its abolishment of the previously strict capital requirements necessary to qualify for limited liability.[21] Interestingly, some commentators viewed limited liability as a tool to empower the poor by allowing them to set up businesses and, for this reason, established merchants and the upper class initially opposed the idea.[22] Later, the Companies Act 1862 and the Companies Act 1867 brought refinement of rules surrounding companies and facilitated outside investments. Supported by these developments, the corporate form became the dominant business vehicle by the end of the nineteenth century. During this time, manufacturing moved away from the use of partnerships to larger incorporated companies, which was often accompanied by the issuance of stock to a multitude of outside investors that began to hold shares in a broad range of companies.[23] Also during this time, the *Salomon* case confirmed the concept of a separate legal personality and limited liability, cementing the protections of the corporate shield for shareholders.[24]

A development similar to the one in England unfolded in America. The British trading companies and the English chartering system were the root of the American corporation, with the East India Company even being at the centre of one of the major events leading up to the birth of the USA, the Boston Tea Party protest. Indeed, the American Revolution was, in part, fuelled by anti-corporate sentiments, representing in one commentator's words 'directly and explicitly an *anti-corporate* revolt'.[25] This process was driven by intellectuals, which saw corporations as a vehicle through which wealthy elites profited at the expense of the public, but

18 On the Bubble Act and its background, see Harris, *supra* note 12, pp. 60–81.

19 This development is detailed in R. Harris, 'The Private Origins of the Private Company: Britain 1862–1907' (2013) 33 *Oxford Journal of Legal Studies* 339.

20 Certain forms of limited liability had previously been granted only to selected trading companies.

21 See Talbot, *supra* note 14, pp. 22–24.

22 Micklethwait and Wooldridge, *supra* note 2, pp. 50–51.

23 See Talbot, *supra* note 14, pp. 32–35.

24 *Salomon* v. A. *Salomon & Co. Ltd* AC 22 (1897). On the emergence of the separation of the company and its members, see P. Ireland, 'Capitalism without the Capitalist: The Joint Stock Company Share and the Emergence of the Modern Doctrine of Separate Corporate Personality' (1996) 17:1 *Journal of Legal History* 41.

25 Nace, *supra* note 2, p. 39.

https://doi.org/10.1017/9781108377072.002 Published online by Cambridge University Press

also in great part by local merchants who suffered under the limits imposed on them by British trade rules. Accordingly, although certain smaller corporations existed in the years after the American Revolution and became increasingly widespread thereafter, the USA sought to severely restrict these entities.

Restrictions on corporations were initially achieved through charters and supported by the prevailing view of corporations as quasi-public institutions that derived their powers solely from the state.[26] Indeed, the purpose of early US corporations was to exercise social functions for the state and to advance public welfare and '[t]he Framers ... took it as a given that corporations could be comprehensively regulated in the service of the public welfare'.[27] Building upon this basis, at the beginning of the nineteenth century, American political leaders had a 'vision ... to subordinate corporations to democratic oversight, then make use of this tamed institution as a tool for meeting the pent-up need for infrastructure'.[28] The political issue in this regard became the question to whom – states or the federal government – the authority to grant corporate charters should be assigned. As a result of fears that the English model of placing vast amounts of monopolistic power and wealth in a few trading companies and their wealthy shareholders would become prevalent – as the Supreme Court put it, there had been fear that corporations would bring various 'evils' to society[29] – the emerging US system entrusted the chartering function almost exclusively to the various state legislatures.[30] The states initially only granted small numbers of charters and, additionally, tended to limit them to corporations with quasi-public purposes that promoted the public good, such as roads, bridges, canals, banks, water works, schools, wharves, and other public services.[31] A public service function was, however, not a general requirement for businesses but rather only applicable to those that chose to incorporate.[32] An example for this is provided in an 1809 Virginia Supreme Court opinion, in which a charter application was rejected and the court noted the following:

> With respect to acts of incorporation, they ought never to be passed, but in consideration of services to be rendered to the public. This is the principle on which such charters are granted even in England ... and it holds *à fortiori* in this country ... It may be often convenient for a set of associated individuals, to have the privileges of a corporation bestowed upon them; but if their object is merely private

[26] See Talbot, *supra* note 14, pp. 71–75.
[27] *Citizens United* v. *FCC* 130 S. Ct. 876, 949–950 (2010) (Stevens, J.).
[28] Nace, *supra* note 2, p. 47.
[29] *Louis K. Liggett Co.* v. *Lee*, 288 U.S. 517, 548 (1933).
[30] Nace, *supra* note 2, p. 48.
[31] See, for example, I. Spier, 'Corporations, the Original Understanding, and the Problem of Power' (2012) 10 *Georgetown Journal of Law & Public Policy*, 115, at 126.
[32] See L. Johnson, 'Law and Legal Theory in the History of Corporate Responsibility: Corporate Personhood' (2012) 35 *Seattle University Law Review* 1135, 1145.

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> or selfish; if it is detrimental to, or not promotive of, the public good, they have no adequate claim upon the legislature for the privilege.[33]

The limitations on conducting business enterprises through the corporate form began to change from the 1830s onwards, when industrial and manufacturing output increased and created stronger demand for corporate charters from these businesses. Adapting to these circumstances, states granted charters more frequently and with more flexible terms, increasingly selling the chartering privilege for monetary benefits, including bribes.[34] The use of the corporate form for businesses was also supported by the US Supreme Court's 1819 *Dartmouth* decision.[35] In that decision, the Court held that while business corporations were 'artificial' entities and mere creatures of the law (in line with the concession and fiction theories of the corporation, which will be discussed in Chapter 6), they were still private institutions if they had been established by their founders for private purposes or pursued such goals based on their specified corporate purpose.

Between the 1850s and 1900, amid a political backlash against the current system, the chartering system began to decline and ultimately disappeared. Driven in part by lobbying on behalf of the emerging large railroad corporations – which became the 'first modern business enterprises'[36] – states grew more accommodating towards corporations and moved towards general incorporation in the form of automatic chartering.[37] As in England, this meant that corporations were largely liberated from state restrictions (as previously imposed via corporate charters). Corporations were now able to incorporate by simply filing certain documentation with one of the states. Among other benefits, unlimited duration was permissible, corporate acquisitions were allowed, and various restrictions on the size and scope of corporations and their activities were lifted. Notably, already by the 1830s, limited liability had become widely accepted in the most important corporate law jurisdictions.[38] States began to compete against each other in attracting businesses, with New Jersey gaining an early lead, although Delaware ultimately established the dominant position.

The above developments incentivized states to design corporate laws in a manner that would attract businesses, something that commentators refer to as a regulatory

[33] *Currie's Administration* v. *Mutual Assurance Society*, 14 Va. 315, 347–348 (1809) (footnotes omitted). The court went on to suggest that if the corporation's public service function should seize at a later point, the legislature would be allowed to repeal its charter.

[34] See Talbot, *supra* note 14, pp. 76–78.

[35] *Trustees of Dartmouth College* v. *Woodward*, 17 U.S. 518 (1819). This case is also a notable early milestone in the judicial recognition of corporations' constitutional rights. On this, see B. L. Garrett, 'Constitutional Rights of Corporations in the United States', in B. Choudhury and M. Petrin (eds), *Understanding the Modern Company* (Cambridge: Cambridge University Press, 2017).

[36] A. D. Chandler, *The Visible Hand: The Managerial Revolution in American Business* (Cambridge, MA: Harvard University Press, 1977), p. 81.

[37] Nace, *supra* note 2, p. 55.

[38] Barron Baskin and Miranti, *supra* note 2, p. 141.

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'race to the bottom'.[39] Along with a new conceptualization of the corporation (developing from the earlier concession theory to an aggregate view and finally the real entity theory), industrialization, and growing infrastructure, state competition facilitated the rise of modern corporations with dispersed ownership and a new class of professional managers that became increasingly insulated from direct influence by shareholders.[40] As business historian Alfred Chandler put it, Adam Smith's famous metaphor of the invisible hand of the market was being replaced by the 'visible hand' of corporate managers who began to dominate the coordination of flows of goods and resource allocation through their decisions at the top of increasingly large and powerful businesses.[41] This 'managerial capitalism', as Chandler called it, subsequently transformed Western economies and accelerated economic growth.[42]

2.1.2 The Shift to (and Prevalence of) a Private Welfare Focus

The advent of general incorporation meant that the former chartering system's emphasis on public functions of corporations faded and, in any event, was not enforceable anymore.[43] The use of the corporate form to conduct business for private gain grew strongly throughout the nineteenth century.[44] Together with the emerging investor-friendly company law framework, the combined effect was that, in both the UK and the USA, corporations firmly entered the investor-centric age. As a consequence, twentieth-century corporate governance in both jurisdictions – and indeed internationally – was largely oriented towards shareholders, not wider societal interests.[45] The changing structure of the shareholder franchise further accelerated this development. The shift from closely held or family-owned businesses towards larger corporations with institutional investors as controlling shareholders in the second half of the century was among the reasons for the transformed focal point for corporations, which became the enhancement of what is today known as 'shareholder value'.[46]

[39] See Nace, *supra* note 2, p. 68; Talbot, *supra* note 14, pp. 72, 82–86.
[40] See, for example, Micklethwait and Wooldridge, *supra* note 2, pp. 101–22.
[41] Chandler, *supra* note 36.
[42] He described the global aspects of this development in A. Chandler, *Scale and Scope: Dynamics of Industrial Capitalism* (Cambridge, MA: Harvard University Press, 1990).
[43] See Johnson, *supra* note 32, p. 1146.
[44] Ibid., p. 1144.
[45] See Talbot, *supra* note 14, pp. 41–70.
[46] On the development of this concept, see T. Kippenberger, 'The History of Shareholder Value' (1996) 1 *The Antidote* 8 (starting with certain US companies' focus on return on investment in the 1920s); P. L. Davies, 'Shareholder Value: Company Law and Securities Markets Law – A British View', in K. J. Hopt and E. Wymeersch (eds), *Capital Markets and Company Law* (Oxford: Oxford University Press, 2003), pp. 261–87; B. R. Cheffins, *Corporate Ownership and Control: British Business Transformed* (Oxford: Oxford University Press, 2008), pp. 338–44 (noting UK executives' initial reluctance to embrace shareholder value).

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Still, the twentieth-century legal framework that resulted in a sustained shift away from a public to a private (investor-oriented) function also faced various obstacles and opposition. In the UK, for instance, shareholder-centrism was notably interrupted between the 1950s and the 1970s, during which the government pursued a combined policy of a state-managed economy and provision of public welfare.[47] The policy's aim was to rely on nationalizing vital industries and developing them into large-scale operations, which was intended to provide employment and profits that could fund social benefits. Further, corporate governance was constructed around empowering labour as part of a conscious decision to give this constituency the power to counter corporate management's power.[48] This era, however, came to an end with the adoption of neoliberal policies in 1979. The role of labour was subsequently diminished, power was shifted back to shareholders and their demands, and instead of nationalization the order of the day was to privatize core industries. The corporate purpose reverted to shareholder value maximization, a development that was amplified with the hostile takeovers wave of the 1980s.[49]

In the USA, a notable movement of corporate 'progressivism' emerged during the earlier twentieth century. This movement, which included Presidents Theodore Roosevelt and Wilson, believed in the benefits of stricter market regulation and led to a phase of tightening competition and antitrust rules.[50] Also in this vein, Adolf Berle and Gardiner Means published *The Modern Corporation and Private Property*, in which they famously outlined the separation from ownership and control in corporations.[51] However, Berle and Means perceived this phenomenon as a potentially positive factor, suggesting that it could allow corporations to pursue the interests of the public at large. The conditions for this were legal reforms with changes, including limits on managers' determination of corporate goals, policies to empower employees, and certain enhanced shareholder rights.[52] From these measures, the latter two came to fruition when the USA introduced the Securities Act 1933, which provided investors with better information, and New Deal policies that strengthened unions and union members. Managerial power, however, remained mostly untamed.

In the following decades, commentators, particularly in the USA, engaged in debates over whether the reality of management-controlled corporations should be viewed as positive or negative based on its effects on society. In addition, they questioned whether management-led corporations (that is without significant checks by shareholders or the state) were pursuing – or capable of pursuing – only

47 See Talbot, *supra* note 14, pp. 41–70.
48 Ibid.
49 Ibid.
50 Ibid., pp. 87–90.
51 A. A. Berle, Jr, and G. C. Means, *The Modern Corporation and Private Property*, second edition (New York: Harcourt, Brace & World, Inc., 1968). Cheffins, *supra* note 46, provides an in-depth historical account of this process in the UK.
52 Berle and Means, *supra* note 51, p. 311.

https://doi.org/10.1017/9781108377072.002 Published online by Cambridge University Press

shareholder interests or other stakeholder interests as well.[53] During the 1960s, the voice of those sceptical of managers' ability to work in the interest of broader society gained the upper hand. Beyond academic critique of corporations, growing corporate power also led to a public backlash in the late 1960s to the late 1970s, with individuals' attitudes towards business deteriorating and many people beginning to believe that business failed to strike a fair balance between profits and the public interest. Corporations came under pressure from consumer and environmental organizations (and responded through lobbying and corporate advocacy) and a new wave of regulations under the Nixon administration curbed corporate activities.[54]

The growing regulatory and welfare role of governments in Western states led, as Zumbansen notes, to 'an important revitalisation and further consolidation' of stakeholderist and corporate social responsibility (CSR) thinking during the second half of the twentieth century.[55] The stakeholderist movement (as will be discussed in more detail in the following chapter) essentially disputed the private nature of corporations and argued that they – via their managers – owed duties to non-shareholder constituents such as employees, consumers, communities, and others. Yet what ultimately carried the day was the revived pro-managerial view of corporations, which argued that managerial power was justified based on its economic efficiency.[56]

Drawing upon theories developed by Ronald Coase and other pioneers,[57] scholars began to develop models of the firm that focused primarily on efficiency and the firm's role as a device to minimize transactions costs within production processes. These economics-based corporate law models were termed 'functional' theories and focused on corporations' (and corporate law's) ability to reduce transaction costs. The contractarian/nexus of contracts model, which has its roots in the aggregate view of corporations that was the prevailing model in earlier times, emerged from this foundation. As will be discussed in the next chapter, the nexus of contracts model is based on the idea that shareholder wealth maximization is the main corporate goal

[53] See Talbot, *supra* note 14, p. 102–13.

[54] Nace, *supra* note 2, pp. 137–38.

[55] P. Zumbansen, The Evolution of the Corporation: Organization, Finance, Knowledge and Corporate Social Responsibility (2009) *CLPE Research Paper No. 6/2009*, available at https://papers.ssrn.com/sol3/papers.cfm?abstract_id=1346971, accessed 4 June 2018, p. 17. For further details, see A. B. Carroll, 'A History of Corporate Social Responsibility: Concepts and Practices', in A. Crane et al. (eds), *The Oxford Handbook of Corporate Social Responsibility* (Oxford: Oxford University Press, 2008), pp. 20–42 (using the Industrial Revolution as a reasonable starting point for the discussion of CSR but also noting that '[t]hough the roots of the concept that we know today as corporate social responsibility have a long and wide-ranging history, it is mostly a product of the twentieth century, especially from the early 1950s up to the present time'). See also Micklethwait and Wooldridge, *supra* note 2, p. 187, who note that the debate concerning the corporate purpose and the emergence of the diverging stakeholder and the shareholder primacy views dates back to the mid-nineteenth century.

[56] Talbot, *supra* note 14, p. 107.

[57] The groundbreaking work is R. Coase, The Nature of the Firm (1937) 4 *Economica (n.s.)* 386.

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and tends to include the view that only people have responsibilities, not corporations as fictional entities. Indeed, through the lens of economics-based corporate governance theories, the corporation has no public role to play beyond its efficiency-enhancing effect, which arguably would result in aggregate benefit for society at large. Consequently, the nexus of contracts theory and modern corporate law itself have, as Lyman Johnson observed, little to say about the public responsibilities and duties of corporations, which are left to be governed by external, non-corporate laws and regulations.[58]

What prevailed in the end was the vision of free markets and the contractarian/nexus of contracts concept of corporations. Politicians adopted deregulatory policies from the late 1970s onwards and shareholder value and profit maximization, as underpinning aims of corporations, carried the day in the various statutes, rules, and codes that now make up the body of corporate and corporate governance law. In terms of the question of the corporate purpose, the UK and USA both have shareholder wealth maximization as the default and primary corporate aim. While – as we will see in the next chapter – there is room for corporations to deviate from this norm, the fundamental fact remains that today both the law and the realities of business practice make it clear that corporations are private entities with private goals, while the public character and public duties have mostly fallen by the wayside.

2.1.3 *Developments Since the Turn of the Millennium*

Around the turn of the millennium, various corporate accounting scandals as well as the (partially related) crash of the 'dot-com bubble' tarnished corporations' public standing, leading to legal reforms such as the Sarbanes–Oxley Act, which aimed to increase managerial accountability.[59] However, while at least the occurrences surrounding the accounting scandals could be explained by pointing to individual misconduct or greed on the part of certain senior managers, the more fundamental systemic issue of corporations' focus on investor gains entered the spotlight more clearly in the wake of the 2008–2009 global financial crisis. The fallout from the crisis negatively affected societies around the globe, directly – such as through the loss of employment and pensions – or indirectly, including through the impact of taxpayer-funded governmental 'bail outs' of financial institutions. After decades of private gains, the public was forced to absorb the downside of corporate activities.

[58] L. Johnson, Law and Legal Theory in the History of Corporate Responsibility: Corporate Personhood (2012) 35 *Seattle University Law Review* 1135, 1139–40.

[59] According to Nace, the Act's relatively weak political response was due to the large campaign contributions – over $1 billion – that businesses had made during the decade preceding the scandals, which meant that neither political party 'had any incentive to rock the boat'. Nace, *supra* note 2, p. 184.

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In the years following the crisis, diversified investors were quickly able to recover from their losses. Major stock market indices have experienced a sustained ascent, beginning from 2009, and still mostly continuing at the time of this writing. Yet, the structural changes and effects caused by the financial crisis proved to be profound and continued to negatively affect at least certain employees and industries. Together with the impact from globalized trading, those who lost their employment, homes, or experienced a substantial decline in their economic welfare, became increasingly discontent. A growing segment of the public perceived – and continues to perceive today – the corporate world as unfair, resenting that those who were bailed-out are back to making profits and earning high salaries.[60] This wave of discontent is said to have led most recently, among other factors, to the momentous events of Brexit and the victory of Donald Trump in the 2016 US presidential election, with especially the latter highlighting not only anti-globalist but also (in many ways related) anti-corporate tendencies among the American population.[61]

Guardian columnist Aditya Chakrabortty described the connection between the financial crisis and the UK electorate's political mood in 2017 as follows:

> First, it was working- and middle-class Britons who paid for the mess, who are still paying for it now and who will keep paying for it decades from now. Second, the crash has prompted almost no fundamental reckoning or reform. And, most importantly, the combination of those first two factors means the crash that began in 2007 cannot be consigned to the past. Today's politics – from Brexit to Trump and the collapse of centrism – is just one of its products. For politicians and financiers to treat the crash as history brings to mind Stephen Dedalus in Ulysses: 'History is a nightmare from which I am trying to awake.'[62]

Chakrabortty posits that despite reforms that followed on from the crash, the economic and business model that created it remains intact. Instead of using nationalized banks to direct credit to strategic industries and regions, he observed,

[60] The United Nations stated in *The Global Social Crisis: Report on the World Social Situation 2011* (New York: United Nations, 2011) that the recovery following the financial crisis 'has been uneven and still remains fragile' and that '[e]stimates suggest that between 47 million and 84 million more people fell into, or remained trapped in, extreme poverty because of the global crisis'. On this, see also I. Ötker-Robe and A. M. Podpiera, 'The Social Impact of Financial Crises: Evidence from the Global Financial Crisis', Policy Research Paper 6703 (Washington, D.C.: World Bank, 2013).

[61] See, for example, R. Partington, *Brexit will hit north of England the hardest, says thinktank*, The Guardian (9 Nov. 2017) ('Many Britons voted to leave the EU feeling the economic recovery since the financial crisis had failed to improve their lives, made worse by government cuts.'); P. Augar, *A call for corporate boards to overturn the status quo*, Financial Times (3 Jan. 2018) (linking the pursuit of shareholder value with the Trump presidency and Brexit); P. Ghemawat, 'Globalization in the Age of Trump' (2017) 95 *Harvard Business Review* 112 (noting, among others, that the backlash against globalization is also partially a backlash against big business); J. O'Reilly et al., 'Brexit: Understanding the Socio-Economic Origins and Consequences' (2016) 14 *Socio-Economic Review* 807–54 (highlighting anti-business sentiment and corporate neglect of societal issues as contributing factors that led to Brexit).

[62] A. Chakrabortty, *Ten years after the crash, there's barely suppressed civil war in Britain*, The Guardian (15 Aug. 2017).

https://doi.org/10.1017/9781108377072.002 Published online by Cambridge University Press

'Labour and the Tories insisted on treating them as if they were still private sector industries.'[63] In Chakrabortty's words, the crisis and its consequences for the UK public can be summed up as follows: 'The banks got bailed out. Their bosses still get paid out. The rest of us get austerity.'[64]

On the other side of the Atlantic, Bloomberg columnist Justin Fox has suggested that the growing anti-corporate mood has become a great uniting force of our times, with voters' hatred of big business being the emerging major political theme across US party lines. In Fox's view, corporates may soon become one of the most disdained elements of society:

> Voters around the Western world have already been expressing disdain for things that big corporations like, such as immigration and free trade. What's to stop them from focusing their ire more directly at the corporations themselves? Ronald Reagan did such a brilliant job in the 1980s of focusing ire on 'big government' that Americans still see it as the greatest threat facing the nation ... But when the pollsters phrase things differently and ask if respondents are satisfied with 'the size and influence of major corporations,' 58 percent aren't. If another Great Communicator comes along who finds a way to make scheming corporate executives the villains of the national narrative instead of intrusive government bureaucrats, watch out.[65]

The events since the turn of the millennium have, as we describe in the following chapter, revitalized academic thinking and initiatives by certain policy-makers and business representatives on alternatives to the shareholder value model. The regulatory response, however, was not to strengthen the position of nonshareholder stakeholders and to reorient the corporate purpose, but rather to engage in approaches that strengthen 'shareholder democracy'. For instance, already in 2003, the European Union (EU) identified the establishment of 'real shareholder democracy' as one of its medium- to long-term political goals,[66] and the push towards stronger shareholder rights has only gathered steam since then, both in Europe and the USA. Among the most visible signs in this respect are enlarged shareholder rights in the area of executive remuneration, discussions surrounding short-termism and shareholder engagement, efforts to give shareholders more control over board appointments and increased opportunities to submit proposals.

For proponents of shareholder empowerment, corporate scandals as well as the financial crisis have bolstered the case for stronger shareholder rights. From this perspective, directors and managers – particularly in financial institutions – and

[63] Ibid.

[64] Ibid.

[65] J. Fox, *The Emerging Anti-Corporate Majority*, BloombergView (28 Dec. 2017) (footnotes omitted).

[66] European Commission, 'Modernising Company Law and Enhancing Corporate Governance in the European Union – A Plan to Move Forward' (2003) 284 *COM* 14.

https://doi.org/10.1017/9781108377072.002 Published online by Cambridge University Press

other gatekeepers are to blame for the crisis and its effects.[67] Commentators have suggested that directors and managers – emboldened by their near-absolute control – behaved inappropriately, took excessive risks, and drove their companies into the ground, sometimes enriching themselves at the shareholders' expense. Consequently, and in line with the concept of agency costs or the general need for 'owners' to monitor 'controllers', it arguably follows from this perspective that shareholders should be given more powers to control companies and keep managers in check.

There is also an opposing view.[68] Focusing on the recent financial crisis as a test case for shareholder empowerment, William Bratton and Michael Wachter, along with numerous other scholars, have argued that the financial crisis in fact supports the case for the current model, not one that would shift the balance of board and shareholder powers towards the latter.[69] They contend that shareholders push directors to an unhealthy focus on their companies' share price, which – as more risk translates into higher financial returns – leads (and has already led) to ever-increasing levels of risk. This, in itself, is not necessarily problematic, at least as long as shareholders are aware of and comfortable with these risks. The problem, Bratton and Wachter argue, is the lack of risk internalization. Should risk manifest itself in economic rescue costs and other negative effects, the risk-taker (shareholders who, for example, pushed companies towards aggressive lending practices) should ideally bear the entire risks. However, in the case of corporations, such risk internalization does not (or not fully) take place as governments – ultimately the taxpayers – may step in to 'bail out' important companies, and shareholders' downside risk is limited due to limited liability. For Bratton and Wachter, this lack of risk internalization, coupled with shareholders' lack of information (which they argue is often limited to market pricing information), does not bode well for shareholder empowerment.

Moreover, institutional investors have at least so far generally not proven to be willing to act as proactive and engaged stewards,[70] not to mention that they also

[67] On this, see J. G. Hill, 'The Rising Tension between Shareholder and Director Power in the Common Law World' (2010) 18:4 *Corporate Governance: An International Review* 344, 346.

[68] As Jennifer Hill has noted, '[t]he global financial crisis added a new layer of ambiguity, with shareholders alternatively viewed as victims or collaborators in the crisis'. J. G. Hill, 'Images of the Shareholder – Shareholder Power and Shareholder Powerlessness', in J. G. Hill and R. S. Thomas (eds), *Research Handbook on Shareholder Power* (Cheltenham: Edward Elgar, 2015), p. 53.

[69] W. W. Bratton and M. L. Wachter, 'The Case against Shareholder Empowerment' (2010) 158 *University of Pennsylvania Law Review* 653. There is ample literature on this topic, both in the USA and UK. From the latter, see for example J. Mukwiri and M. Siems, 'The Financial Crisis: A Reason to Improve Shareholder Protection in the EU' (2014) 41 *Journal of Law and Society* 51; A. Dignam, 'The Future of Shareholder Democracy in the Shadow of the Financial Crisis' (2013) 36 *Seattle University Law Review* 639; B. R. Cheffins, 'Did Corporate Governance "Fail" During the 2008 Stock Market Meltdown? – The Case of the S&P 500' (2009) 65 *Business Lawyer* 1; A. Keay, 'Risk, Shareholder Pressure and Short-termism in Financial Institutions: Does Enlightened Shareholder Value Offer a Panacea?' 5 *Law and Financial Markets Review* 435 (2011).

[70] With reference to the UK, B. R. Cheffins, 'The Stewardship Code's Achilles' Heel' (2010) 73 *Modern Law Review* 1004.

https://doi.org/10.1017/9781108377072.002 Published online by Cambridge University Press

pursue their own, often short-term-oriented goals.[71] Additionally, insofar as institutional shareholders rely on proxy advisors, shifting power to shareholders means shifting power to these advisory firms, raising a host of new accountability and conflict of interest issues. At the same time, individual shareholders remain constrained by the well-known issues stemming from collective action problems, information asymmetries, and rational apathy. In light of the example of the recent financial crisis and its lessons it seems that shareholder empowerment proponents should be mindful of the fact that shareholders are among those thought to have contributed to the financial crisis. In this vein, the European Commission observed that 'confidence in the model of the shareholder-owner who contributes to the company's long-term viability has been severely shaken'.[72] Giving these same shareholders, with their proven appetite for risk and quick profits, more power may lead to increased pressures on boards to justify their pay with short-term gains, eviscerating the thrust of ongoing efforts to curb short-termism.

2.2 JUSTIFYING CORPORATE DUTIES

The preceding brief history of the corporation and its modern developments reminds us of the shortcomings with the existing corporate model. It also points us to the need to view corporations through a broader public lens given the numerous effects corporations have had, and will likely have in the future, on the public. However, a historical analysis is insufficient, in and of itself, to capture the reasons why corporations should bear duties to the public. In this part, we take a closer look at the justifications for imposing duties on the corporation *vis-à-vis* the public. These include the power of corporations, the role of corporations as rule makers, international arbitrage, and externalities stemming from corporate activities.

2.2.1 *Power*

In 1932, Berle and Means predicted the continuation of the rise and corresponding importance of the corporation to the public. In *The Modern Corporation and Private Property*, they posited that the corporation would become 'completely dominant' in the lifetime of their children and that its impact on the lives of every individual would be 'certain to be great'.[73] Berle and Means' predictions certainly have come

[71] J. Kay, *The Kay Review of UK Equity Markets and Long-Term Decision Making: Final Report* (Brussels: European Corporate Governance Institute, July 2012) (citing evidence from the Institute of Directors); C. Villiers, 'Controlling Executive Pay: Institutional Investors or Distributive Justice?' (2010) 10 *Journal of Corporate Law Studies* 309, 341 (concluding that shareholders are part of the problem of escalating executive salaries).

[72] European Commission, 'Green Paper: Corporate Governance in financial Institutions and Remuneration Policies' (2010) 284 *COM* 8. Still, the EU Commission's conclusion in this paper was that strengthening shareholders would provide the adequate cure to the malaise.

[73] Berle and Means, *supra* note 51, p. 3.

https://doi.org/10.1017/9781108377072.002 Published online by Cambridge University Press

true and today are echoed by countless commentators and sources. A Google search for the term 'corporate power' generates over 23 million hits. Similarly, newspaper articles boast countless headlines such as those proclaiming '*How corporate dark money is taking power*', '*The latest sneaky attempt to increase corporate political power*', and '*What the Facebook hearings reveal about corporate power in Washington*'. There are also over 45,000 books with the term 'corporate power' in some form or other in their title.

Further proof of the ubiquitous nature of the subject of corporate power can be found in the periodic ranking of corporations versus states. For instance, a 2016 survey comparing the annual revenue of corporations to a number of different countries found that Walmart's annual revenue outstripped that of Spain, Australia, and the Netherlands; Royal Dutch and Shell's revenue exceeded that of Mexico and Sweden; and Apple's revenue exceeded that of Belgium, Switzerland, Austria, and Denmark.[74] Indeed, of the top 100 economies surveyed, only 31 belonged to countries while the remainder belonged to corporations. A 2009 survey conducted by the World Bank comparing countries' gross domestic product (GDP) to companies' revenues found similar results. The survey found that Royal Dutch and Shell had higher revenues than Pakistan's, Austria's, or Switzerland's GDP; that Exxon Mobil and Walmart both had higher revenues than Colombia, Malaysia, or Belgium's GDP and that BP, Total, Toyota and Chevron all had higher revenues than Denmark, Israel, Ireland, and Finland's GDPs.[75]

Commentators have questioned the methodological relevance of comparing GDP with corporate revenue, generating thoughts of comparing apples to oranges.[76] One commentator argues that a corporation's power is better evaluated by comparing corporate net sales figures with a state's budget or by looking to its market capitalization as a proxy for its influence on the political process.[77] A second commentator goes even farther, suggesting that comparing GDP with revenue as a means of evaluating corporate power is 'reckless'.[78]

While we offer no comment on the use of one form of statistics over another to evaluate corporate power, we agree with the critics that the idea of whether corporations have power is more complex than comparing GDP with revenues; it requires a more thorough evaluation. Fundamentally, this is because power is one of the bases for demanding responsibility from corporations. As Berle and Means have noted, there has been a constant warfare between those wielding power and those

74 Corporations vs governments revenues: 2015 data, Global Justice Now (2016), www.globaljustice.org.uk/sites/default/files/files/resources/corporations_vs_governments_final.pdf.

75 The World's Top 100 Economies, World Bank (2009), http://siteresources.worldbank.org/INTUWM/Resources/WorldsTop100Economies.pdf.

76 J. Tullberg, 'Illusions of Corporate Power: Revisiting the Relative Powers of Corporations and Governments' (2004) 52:4 *Journal of Business Ethics* 325 at 326; C. May, *Global Corporations in Global Governance* (Abingdon: Routledge, 2015), pp. 1–19.

77 May, *supra* note 76, pp. 1–19.

78 Tullberg, *supra* note 76, p. 328.

https://doi.org/10.1017/9781108377072.002 Published online by Cambridge University Press

who are subjects of that power and just as there is a need for power, there is a corresponding desire to make that power the servant of the individuals it affects.[79] Tullberg similarly argues that the high estimate of corporate power begets the expectations, commitments and demands from corporations.[80] Power theorist Steven Lukes elaborates on the relationship between power and responsibility. He argues:

> … an attribution of power is … an attribution of … responsibility for certain consequences. The point, in other words, of locating power is to fix responsibility for consequences held to flow from the action, or inaction, of certain specifiable agents.[81]

The duties of corporations that we espouse in this book flow naturally from the idea that corporations possess power. Since power has become one of the central reasons for imposing duties on corporations, it becomes imperative to study the notion of corporate power in a more in-depth manner.

Breaking Down Power

The definition of power is open to interpretation.[82] Max Weber offers a useful basic definition of power, describing it as the possibility of imposing one's will onto the behaviour of others.[83] Following this definition, it could be said that corporate power is manifested in the different ways in which corporations have the possibility of imposing their will on others, including members of the public. Beyond Weber's basic definition, power theorists have broken down the definition of power into its constituent elements.[84] These elements provide a deeper understanding of power in general and corporate power as a subset thereof.

Theorists argue that power is composed of a number of different facets. The first facet of power is the possibility to make decisions that affect others.[85] This is the behavioural aspect of power – actors making decisions that affect others[86] – but it also reflects the direct influence of an actor over another.[87] Galbraith argues that this

79 Berle and Means, *supra* note 51, p. 310.
80 Tullberg, *supra* note 76, p. 325.
81 S. Lukes, *Power: A Radical View*, second edition (Basingstoke: Palgrave MacMillan, 2005), p. 56.
82 As Tolstoy noted, power is a word the meaning of which we do not understand. See L. Tolstoy, *War and Peace* (Ware: Wordsworth Editions, 1869), p. 940.
83 M. Weber, *Max Weber on Law in Economy and Society* (Cambridge: Cambridge University Press, 1954), p. 323. Galbraith agrees with this definition noting, 'someone or some group is imposing its will and purpose(s) on others including on those who are reluctant or adverse. The greater the capacity to impose such will and achieve the related purpose, the greater the power'. See J. K. Galbraith, *The Anatomy of Power* (Boston, MA: Houghton Mifflin Harcourt, 1983), p. 2.
84 See, for example, Lukes, *supra* note 81; R. A. Belliotti, *Power: Oppression, Subservience, and Resistance* (Albany, NY: State University of New York Press, 2016).
85 R. A. Dahl, 'The Concept of Power' (1957) 2:3 *Behavioral Science* 201; P. Bachrach and M. Baratz, 'Two Faces of Power' (1962) 56 *The American Political Scientist Review* 947, 948.
86 M. Haugaard, *Power: A Reader* (Manchester: Manchester University Press, 2012), p. 26.
87 D. Fuchs, *Business Power in Global Governance* (Boulder, CO: Lynne Rienner Publishers, 2007), p. 56.

https://doi.org/10.1017/9781108377072.002 Published online by Cambridge University Press

type of power can be exercised in a condign or compensatory manner. If exercised in a condign manner, the party holding the power will inflict or threaten adverse consequences for another's failure to submit. For instance, the employees that became victims of the Rana Plaza disaster (discussed in Chapter 8) were subject to condign power when their employers threatened to fire them unless they agreed to work in a collapsing building. Alternatively, power can also be exercised by offering an affirmative reward for submission, for example, where an individual submits to a corporation in return for compensation.[88] In both scenarios, Weber's hallmark of power, the imposition of one's will onto others, is ultimately achieved.

The second facet of power pertains to institutional neutrality or, more precisely, the absence thereof. As Bacharatz and Betz explain, power is exercised when an actor creates or reinforces 'social and political values and institutional practices that limit the scope' of decision-making to only those issues either promoted by or innocuous to the actor. By doing so, the actor is able to prevent another from raising issues that are seriously detrimental to the actor's set of preferences.[89] The second facet thus stresses an actor's control over the political agenda as well as the ways in which potential issues are kept out of the decision-making process altogether.[90] For instance, corporations can set the political agenda by lobbying political actors to promote certain interests and to resist interests that are detrimental to the corporation's own interests. Thus, businesses successfully lobbied the Bush administration in the USA to resist the usage of a statutory mechanism for holding corporations accountable,[91] while in Australia, gaming corporations managed to silence reforms to poker machine gambling.[92] Corporations even persuaded the United Nations to refrain from including anti-tax avoidance practices as part of its Sustainable Development Goals.[93]

The third facet of power is the ability to influence, shape or determine another actor's very wants, or as Galbraith terms it 'conditioned power'.[94] This is 'the supreme exercise of power to get another or others to have the desires you want them to have – that is, to secure their compliance by controlling their thoughts and

88 Galbraith, *supra* note 83, pp. 4–5.
89 Bachrach and Baratz, *supra* note 85, p. 948.
90 Lukes, *supra* note 81, p. 25.
91 See K. R. Carter, 'Amending the Alien Tort Claims Act: Protecting Human Rights or Closing off Corporate Accountability' (2007) 38 *Case Western Reserve Journal of International Law* 629; EarthRights International, *In Our Court: ATCA, Sosa, and the Triumph of Human Rights* (Washington, D.C.: EarthRights International, July 2004).
92 W. Smith, '*Political donations corrupt democracy in ways you might not realise*', The Guardian (11 Sept. 2014).
93 The significance and subversion of SDG 16.4: Multinational tax avoidance as IFF, A. Cobham (2017), www.un.org/esa/ffd/ffdforum/wp-content/uploads/sites/3/2017/05/ED1-Cobham.pdf; T. Murphy, '*Corporations secretly lobbying UN to allow tax avoidance in its anti-poverty agenda*', Humanosphere, 23 June 2017.
94 Galbraith, *supra* note 83, p. 6; W. LaFeber, *Michael Jordan and the New Global Capitalism* (New York, NY: Norton, 1999), p. 157.

https://doi.org/10.1017/9781108377072.002 Published online by Cambridge University Press

desires'.[95] This facet of power is more than an attempt to ensure that potential conflicts of interest or countervailing considerations will not be present in and influence decision-making, which is seen in the first two facets of power. Rather it is an attempt to ensure that conflicts of interest will not even be perceived as such.[96] This facet provides more depth to power issues, for example, by considering the institutional and social conditions that have prevented individuals over whom power is being exercised from being able to participate in decision-making altogether.[97] For instance, the power to influence and shape desires is evidenced by the corporate power to determine the areas in which they will focus their research and development activities and which of these developments will be rendered into new products and services. In this way, it is corporate preferences rather than consumer needs that can determine available goods and services.

Power in general, therefore, is characterized by the presence of one of three elements. First, the possibility to make decisions that affect others; second, the creation or reinforcement of social, political, and institutional values and practices that limit outsiders' participation in decision-making; and third, the ability to influence, shape or determine another actor's desires. Moreover, each of the three facets of power enhances one another, meaning that an individual facet of power will benefit from the presence of another facet.[98]

Notions of Corporate Power

Scholarly attention has been directed, in addition, at corporate power as a specific instance of power. In some aspects, corporate power theorists have drawn from the three main elements of power observed above, but these elements either have been further clarified in the corporate context or serve as the basis for describing corporate power more specifically.

Parkinson, for example, argues that corporations exercise control, decision-making, and discretionary and political power. As he explains, corporations exercise control or strong bargaining positions, such as in relation to their employees.[99] They further exercise decision-making power in the sense of having discretion to make choices that have significant effects over others.[100] In addition, corporations exercise discretionary power over the allocation of resources between different uses as well as over production-related decisions.[101] They also exercise political power in terms of being able to influence government policy as well as exercise 'structural

95 Lukes, *supra* note 81, p. 23.
96 Ibid., pp. 27–29; Fuchs, *supra* note 87, p. 61.
97 Lukes, *supra* note 81, pp. 27–29.
98 Fuchs, *supra* note 87, p. 65.
99 J. E. Parkinson, *Corporate Power and Responsibility: Issues in the Theory of Company Law* (Oxford: Oxford University Press, 1993), p. 8.
100 Ibid., p.10.
101 Ibid., p. 15.

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power' by shaping the 'economic environment within which the government must operate'.[102]

Kaysen's view on corporate power begins with his definition of power, which he characterizes as 'the significant choice open to an actor; thus an actor's power over another is the scope of the actor's choices which significantly affects others'.[103] For Kaysen, 'the giant corporation manifest[s] its power', through the dimensions of choice open to it, such as in relation to 'prices and price-cost relations, investment, location, research and innovation, and product character and selling effort'.[104] Kaysen notes that the corporation's choice in regard to each of these dimensions affects not only the markets in which the firm operates, but more broadly may affect the economy as a whole as well.[105] He further observes that corporate power is exercised through innovation as the corporation decides which technical areas will be focused on by research and development and which 'scientific and technical novelties will be translated into new products and new processes'.[106]

Edward Epstein has similarly found that corporate power is a function of specific individual elements. Epstein argues that corporate power involves power over participants, or the capacity to determine or influence the behaviour of others (either intentionally or consequentially)[107] and this power is manifested in six spheres: economic, social and cultural, power over the individual, technological, environmental, and political.[108] Epstein contends that economic power is the ability to control the nature, quality, prices and conduction of production, and distribution of scarce resources. Social and cultural power, on the other hand, is the corporation's impact on the character of other social institutions and cultural values and lifestyles. The third manifestation, power over the individual, is the corporation's effects on those individuals it has direct relationships with and their impact on 'social character and the nature of individualism' in society. The final three manifestations are technological power, which is the corporation's role in shaping technological change within society; environmental power, which is the corporation's effects on the environment; and political power, or the capacity of corporations to influence governmental decision-making.[109]

Power scholar Dowding similarly contends that business power takes six forms. These are: local; to define the agenda; to gain disproportionate effects from the political process; to benefit from elected officials that 'pander' to business interests; the superior ability to mobilize political resources; and the overarching system of

[102] Ibid., p. 19.
[103] C. Kaysen, 'The Corporation: How Much Power? What Scope?' in E. S. Mason (ed.), *The Corporation in Modern Society* (Cambridge, MA: Harvard University Press, 1959), p. 85.
[104] Ibid., pp. 91–92.
[105] Ibid.
[106] Ibid., p. 93.
[107] Ibid., p. 13.
[108] Ibid., pp. 14–15.
[109] Ibid.

https://doi.org/10.1017/9781108377072.002 Published online by Cambridge University Press

capitalism that privileges business interests over other interest.[110] For Dowding, local power is the power of business to affect the interests of its local community by providing jobs, supplier contracts, local government taxes, etc.[111] For the other forms of power, Dowding sees these sources arising from business' ability to threaten disinvestment if their needs are not met and the government's reliance on them for the overall functioning of the economy.[112] Because of these twin factors, Dowding argues that business decides what is best for politicians rather than vice versa.[113]

Conversely, business power scholar Fuchs disaggregates corporate power into, what she sees as, its three constituent elements: instrumental, structural, and discursive power. Fuchs defines instrumental power as the direct means by which the corporation exercises its influence.[114] Exercise of this type of power is linked to a change in outcomes due to the influence being exercised over another.[115] Instrumental power also describes corporations' abilities to influence policy makers and includes both corporate (direct) lobbying efforts as well as corporations' ability to harness resources and networks to support supranational and network efforts at lobbying or other political work.[116]

Second, Fuchs argues that corporations exercise structural power by being able to shift policy deliberations towards corporate preferences and exert control over actors' choice sets.[117] This is the influence corporations have over 'setting agendas and making proposals as a product of their material position within states and the global economy' and derives from corporations' ability to 'reward and punish country's policy choices' by relocating capital and jobs.[118] Structural power is also reflected in the increasing ability of corporations to make governance decisions themselves through mechanisms that enable them to set, implement, and enforce private rules.[119] Not only does this practice enable corporations to specify the content of the rules but it also enables them to influence which rules are adopted.[120]

Finally, drawing on the work of power scholar Lukes, Fuchs argues that corporations exercise discursive power. This power draws from the recognition that power is a function of norms and ideas and is reflected in discourse and cultural values and

[110] K. Dowding, 'Business and Power' in K. Dowding, ed., *Encyclopedia of Power* (Thousand Oaks, CA: Sage, 2011), pp. 79–80.
[111] Ibid., pp. 79–80.
[112] Ibid., p. 80.
[113] Ibid., p. 81.
[114] Fuchs, *supra* note 87, pp. 84–85.
[115] J. Clapp and D. A. Fuchs, 'Agrifood Corporations, Global Governance, and Sustainability: A Framework for Analysis' in J. Clapp and D. A. Fuchs (eds), *Corporate Power in Global Agrifood Governance* (Cambridge, MA: MIT Press, 2009), p. 8.
[116] Fuchs, *supra* note 87, pp. 84–85.
[117] Ibid., pp. 108–09.
[118] Clapp and Fuchs, *supra* note 115, pp. 8–9.
[119] Ibid., p. 9.
[120] Ibid.

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institutions.[121] Fuchs argues that corporations play a 'role in constituting and framing policies, actors, and broader societal norms and ideas'; that is to say, corporations frame issues in public discourse.[122] This discourse can influence the way the issue is debated by the public and, accordingly, the choices that are given to society to address such problems.[123] Fuchs further maintains that corporate contributions to discourse may also enhance their political legitimacy.[124] This is because legitimacy is intertwined with discourse and the exercise of discursive power is reliant on the willingness of 'message recipients to listen and to place trust in the validity of the message'.[125] Fuchs argues that corporations thus obtain political legitimacy from the trust the public places in their 'expertise, capacities and intentions'.[126]

From these different conceptions of corporate power, several consistent elements emerge. First, corporations have instrumental or direct power; that is, they have the power to make decisions that affect others or the discretion to choose between different decisions that will affect others. This is akin to the power to make decisions that affect others that Weber and others have described. From a corporate perspective, this is the element of power that is probably most commonly attributed to corporations. For example, corporations can decide where they will locate their business. This will determine which individuals, community and even which country will benefit from the corporation's presence and which will not.

Second, corporations have structural power by being able to 'set the agenda' and by their ability to shape the economic environment. Relatedly, they also have political power, which is tied to their structural power, and more specifically refers to their disproportionate influence over the political process and their superior ability to mobilize political resources. This element of corporate power draws from the second element of power described above; that is, the creation or reinforcement of social, political, and institutional values and practices that limit outsiders' participation in decision-making. In the corporate sphere, this is exercised through corporate influence over the political agenda, a practice that is exemplified, for instance, in the USA through the National Rifle Association's impact on the Republican Party.[127] Moreover, corporations can exercise structural power through their ability to influence the political agenda with threats of exit from the country, if their preferences are not realized, as well as their ability to set the rules themselves through the growing practice of corporate self-regulation.

[121] Ibid., p. 10.
[122] Ibid.
[123] Ibid.
[124] Ibid., pp. 10–11.
[125] Ibid., p. 11.
[126] Ibid.
[127] See, for example, B. Orr, *My party, tragically, is beholden to the NRA*, Charlotte Observer (22 Feb. 2018); K. Lee and M. Moore, *The NRA used to be a bipartisan campaign contributor, but that changed in 1994. Here's why*, Los Angeles Times (3 Mar. 2018).

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Finally, corporations have the power to influence and shape the wants of others. This can be through social conditioning or advertising, as Galbraith argued,[128] or by framing the discourse, as Fuchs argues. In either case, it reflects the ability of corporations to shape the economic market to sustain its position. Again, this draws from the third element of power, described above, or the ability to influence, shape or determine another actor's desires. We see exercises of this power in corporations framing the discourse by promoting the idea of self-regulation as superior to government regulation in relation to environmental issues,[129] in companies shaping product choices through decisions where to innovate, and in removing those affected from corporate decision-making altogether, as has been the practice of establishing corporate facilities on indigenous lands.[130]

Moreover, while these elements of power can be exercised in relation to a variety of areas, it becomes clear that corporations exhibit particular strengths in certain areas. These include economic (in relation to pricing, investment, etc.); social (in being able to dictate the market's preferences and lifestyles mainly by relying on shaping power); and politics (in determining the governance of issues as well as whether certain issues will be governed at all). In addition, corporations are exercising considerable power in relation to technology through their role in driving change in this area. As Kaysen has observed, exercises of corporate power in relation to technology has the ability to profoundly affect 'the whole material fabric of society, the structure of occupations, [and] the geographic distribution of economic activity and population'.[131] Thus, this aspect of power may be one of the strongest manifestations of corporate power.

Repercussions of Power

As we have seen, corporate power is a composite of direct/instrumental power, structural/political power, and influence/conditioning power directed at economic, social, political, and technological issues, among others. Thus, if the objective of identifying the constructs of corporate power, and its particular areas of focus, is to impose 'responsibility for consequences' that flow from the exercise of such power,[132] this would suggest that corporations should be held responsible in these areas. While the discussion of power does not, in and of itself, suggest the ways in which corporations should be held responsible, at the

[128] Galbraith, *supra* note 83, pp. 132–42.

[129] Clapp and Fuchs, *supra* note 115, p. 10.

[130] Food and Agriculture Organization of the United Nations, '*Free Prior and Informed Consent: An indigenous peoples' right and a good practice for local communities – Manual For Project Practitioners*' (Rome, Italy: Food and Agriculture Organization of the United Nations, 2016), p. 6 (noting 'the focus on profits has seen companies convince municipal and national authorities to accelerate extractive and economic projects, without the consent of indigenous peoples who have lived there for hundreds of years').

[131] Kaysen, *supra* note 103, p. 93.

[132] Lukes, *supra* note 81, p. 56.

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very least, it raises the discussion of whether there should be repercussions for exercising those powers.

Galbraith has stressed, for instance, the importance of restraining corporate power. As he observed, 'power on one side of a market creates the need for the exercise of countervailing power from the other side' since countervailing power operates to prevent the misuse of business power.[133] Indeed, without this countervailing power, he cautioned, 'private decisions could and would lead to the unhampered exploitation of the public'.[134] Similarly, Berle and Means reasoned that the power bestowed on corporations required them to serve not only their owners and managers but society as well.[135] They concluded that this societal goal was necessary in order to preserve the survival of the corporate system.[136]

Accordingly, if we draw from the idea that the attribution of responsibility flows from the notion of power, Galbraith's concerns over the effects on the public of unadulterated corporate power, and Berle and Means' argument that corporate power requires corporations to serve society as well, then it becomes apparent that the power of the corporation justifies the corresponding imposition of public duties on it.[137] In particular, corporate power has been especially acute in relation to several of the issues we examine in this book. Thus, corporate exercises of direct/instrumental power have shaped their ability to affect tort and criminal law victims, while exercises of structural/political power have been common in relation to environment, corruption, and tax issues and influence/conditioning power has been used in connection with both human rights and corporate governance issues. Duties are therefore needed in these areas as a counter to the exercises of corporate power.

2.2.2 *Corporations as Rule Makers*

Closely related to the discussion of the structural or political power of corporations, described above, is the increasing role of corporations as rule makers. While the discussion of the structural or political power of corporations has emphasized the more indirect role of corporations in agenda setting or influencing the political process, the ability of corporations to act as actual rule makers highlights how they can actively engage in governance.[138]

133 Galbraith, *American Capitalism: The Concept of Countervailing Power* (Piscataway, NJ: Transaction Publishers, 1993), pp. 113 and 167.
134 Ibid., p. 167.
135 Ibid., pp. 307–12.
136 Ibid., pp. 312–13.
137 Due to the limited scope of the book, we focus mainly on economic and social issues, leaving politics and the burgeoning issues of technology to others.
138 K. Webb, 'Corporate Citizenship and Private Regulatory Regimes: Understanding New Governance Roles and functions' in I. Pies and P. Koslowski (eds.), *Corporate Citizenship and New Governance: The Political Role of Corporations* (Berlin: Springer, 2011), pp. 39, 41; J. S. Nye, *The Paradox of American Power: Why the World's Only Superpower Can't Go It Alone* (Oxford: Oxford University Press, 2003), p. 106.

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Today, corporations play an active role in creating rules and standards. In many areas, corporations are either contributing to rule formation or application in combination with other actors, such as in private–public relationships, alongside non-governmental organizations or other stakeholders as part of multi-stakeholder initiatives, or entirely by themselves through industry organizations.[139] Examples of areas where corporations develop their own rules include *lex mercatoria*, the governance of merchant relationships developed entirely by medieval merchants;[140] international commercial arbitration, described as 'basically a private justice system';[141] international concession agreements where terms are interpreted according to industry practice;[142] investor–state contracts, through which investment arbitration can be transformed into international legal rights;[143] aboriginal land rights claims relating to oil sands;[144] the ISO 14001 norm;[145] and credit-rating agencies, which have been described as 'private gate-keeping systems'.[146]

The reasons for corporate activity in rule generation are myriad. They may involve enhancing the (perceived) legitimacy of their actions, improving or maintaining the credibility and confidence of their partners, minimizing transaction costs and reducing ambiguity in terms of disruptions, boycotts, etc.[147] However, regardless of the precise reason for their engagement, corporations' increased role in rule-making emphasizes the shift from their being governed to their governing. It also reminds us that this mode of governance does not (or at least not directly) have its authority rooted in a country's government.[148] Indeed, by adopting a governance function, corporations may be appropriating the role of governments in some scenarios and, certainly, when the issues at hand concern the public, they may also be privately appropriating the public interest. In this book, we take a particular look at the role of corporations as rule makers in connection with corporate governance, human rights, environmental, and corruption issues. In these areas, corporations are developing

[139] L. Cata Backer, 'Private Actors and Public Governance Beyond the State: The Multinational Corporation, the Financial Stability Board and the Global Governance Order' (2011) 18 *Indian Journal of International Law* 751; D. Hess, 'Social Reporting and New Governance Regulation: The Prospects of Achieving Corporate Accountability Through Transparency' (2007) 17:3 *Business Ethics Quarterly* 453.

[140] Nye, *supra* note 138, p. 55.

[141] Ibid.

[142] V. Lowe, 'Corporations as International Actors and International Law Makers' (2004) 14:1 *The Italian Yearbook of International Law* 23.

[143] J. Arato, 'Corporations as Lawmakers' (2015) 46:2 *Harvard International Law Journal* 229.

[144] T. I. Wanvik, 'Governance Transformed into Corporate Social Responsibility (CSR): New Governance Innovations in the Canadian Oil Sands' (2016) 3:2 *The Extractive Industries and Society* 517.

[145] R. MacLean and B. Nalinakumari, 'The New Rule Makers: The Paradigm Shift in Environmental, Health, Safety, and Social Responsibility "Regulations" Now Underway' (2004) 11:8 *Corporate Environmental Strategy: International Journal for Sustainable Business* 2–183.

[146] S. Sassen, *Losing Control?: Sovereignty in an Age of Globalization* (New York, NY: Columbia University Press, 1996), p. 17.

[147] Webb, *supra* note 138, p. 47.

[148] Cata Backer, *supra* note 139, p. 759.

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particular niches either as self-regulators or as part of the team dictating the rules in multi-stakeholder initiatives.

2.2.3 *International Arbitrage*

A third reason for the growing connectedness between corporations and the public is their ability to engage in international arbitrage. In finance, the idea of international arbitrage focuses on the profit that a trader can make from buying and selling foreign securities on two different exchanges. However, in the context of this book, we define international arbitrage to mean the growing practice of multinational corporations exploiting differences in national regulatory regimes by virtue of being a global actor. Thus, corporations headquartered in Country X can choose to establish manufacturing facilities in Country Y (due to lower labour requirements), extraction facilities in Country Z (due to lower environmental regulations), and subsidiaries in Country ABC (due to lax tax rules).

While situating aspects of a multinational corporation around the world has contributed to growth in many countries, it has also spread the power and rule-making abilities of corporations exponentially. Indeed, the aforementioned aspects of corporate power are intensified dramatically through the tentacle-like reach of multinational corporations. Corporations are now not only affecting the public through direct/instrumental power, structural/political power, and influence/conditioning power in the country in which they are established but may also be doing so in any of the countries in which they have established their business.

More importantly, drawing from Hirschman's theory of exit, voice, and loyalty, corporations – in addition to employing structural/political power through their 'voice' – are also, in the context of international arbitrage, exhibiting their power through 'exit'.[149] That is, corporations who are not provided favourable investment conditions by one country can choose to establish aspects of their business elsewhere.[150] Moreover, this 'threat' of exit may underlie corporations' voice with national governments, thereby amplifying corporate power.

At the same time, countries are competing for foreign investment from multinational corporations. This can result in countries lowering their national regulations in order to attract investment,[151] becoming tax havens, or relinquishing their sovereign powers in key regulatory areas through the conclusion of free trade and investment agreements.[152] Although this interest in attracting multinational

[149] A. O. Hirschman, *Exit, Voice, and Loyalty: Responses to Decline in Firms, Organizations, and States* (Cambridge, MA: Harvard University Press, 1970).

[150] A. C. Aman, Jr, 'The Globalizing State: A Future-Oriented Perspective on the Public/Private Distinction, Federalism, and Democracy' (1998) 31 *Vanderbilt Journal of Transnational Law* 769.

[151] C. Villiers, 'Corporate Law, Corporate Power and Corporate Social Responsibility' in N. Boeger et al. (eds.), *Perspectives on Corporate Social Responsibility* (Cheltenham: Edward Elgar, 2008), p. 102.

[152] See, for example, A. Kulick, *Global Public Interest in International Investment Law* (Cambridge: Cambridge University Press, 2012); B. Choudhury, 'Recapturing Public Power: Is Investment

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corporate investment can stimulate healthy competition among countries, encouraging governments to be careful with costly or overzealous regulation, it can also drive a 'race to the bottom' by limiting government discretion to set appropriate levels of regulation for public interest issues.[153] Thus, the very nature of inviting corporations in via globalization is requiring a readjustment of corporate versus public interests.

A prime example of this is provided by foreign direct investment (FDI). Countries hungry for FDI are eagerly signing on to free trade and investment agreements that prioritize the property interests of corporations.[154] However, these agreements often contain an enforcement provision allowing corporations directly to sue countries for damages in connection with national regulations that interfere with their foreign investments in an international arena. This device, known as investment arbitration, has been used as a 'sword' by corporations to challenge countries' public interest regulations on a host of issues.[155] For instance, Phillip Morris instigated arbitration proceedings against both Uruguay and Australia, challenging their anti-smoking legislation[156] while Italian investors used it to challenge South Africa's apartheid-redressement regulations.[157] The quest to attract foreign corporations, engaging in international arbitrage, has therefore directly pitted corporate interests against public interests in a litigious forum.

Relatedly, Stiglitz argues that corporations may be engaging in international arbitrage as a means of escaping accountability. As he observes, '[i]n old cowboy movies, the sheriff chases the bandits to the state border – the bandit knows that once he crosses the border he is safe. So too for the modern corporation'.[158] In fact, corporations can escape accountability in a jurisdiction simply by moving their assets out of that jurisdiction to another, thereby thwarting enforcement efforts arising from any future lawsuits against it in that jurisdiction.[159] Some corporations even deliberately establish themselves as contractual networks rather than corporate groups in order to increase their

Arbitration's Engagement of the Public Interest Contributing to the Democratic Deficit?' (2008) 41 *Vanderbilt Journal of Transnational Law* 775.

[153] See, for example, the arguments in *Worldbeater Inc*. The Economist, 1997. See also J. E. Stiglitz, 'Multinational Corporations: Balancing Rights and Responsibilities' (2007) 101 *Proceedings of the Annual Meeting (American Society of International Law)* 3, 15. For a good discussion on the conditions necessary for a race to the bottom see D. Spar and D. Yoffie, 'Multinational Enterprises and the Prospects for Justice' (1999) 52:2 *Journal of International Affairs* 557, 564 et seq.

[154] D. Aguirre, *The Human Right to Development in a Globalized World* (Abingdon: Routledge, 2008), p. 8; D. Schneiderman, *Constitutionalizing Economic Globalization* (Cambridge: Cambridge University Press, 2008), p. 2.

[155] Choudhury, *supra* note 152, p. 781 et seq.

[156] *Philip Morris Brands Sàrl, Philip Morris Products S.A. and Abal Hermanos S.A.* v. *Oriental Republic of Uruguay*, ICSID Case No. ARB/10/7, Award (8 July 2016); *Philip Morris Asia Limited* v. *The Commonwealth of Australia*, UNCITRAL, PCA Case No. 2012–12, Final Award (8 July 2017).

[157] *Piero Foresti, Laura de Carli & Others* v. *The Republic of South Africa*, ICSID Case No. ARB(AF)/07/01 (2006).

[158] Stiglitz, *supra* note 153, p. 18.

[159] Ibid.

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flexibility to operate in multiple jurisdictions and limit their liability in such jurisdictions.[160]

Without a global regulatory body overseeing the arbitrage activities of corporations, there is a constant push by corporations to exploit regulatory advantages with tangential impacts on the public without a corresponding force to counteract such pushes. This enables corporations to operate in a 'transnational context of incomplete legal and moral regulation'.[161] As a result, this has led to a 'whack-a-mole' scenario in which assorted bodies – such as the Organisation for Economic Co-operation and Development or the EU – make (reactive) attempts to counter corporate arbitrage activities impinging on the public in one area while new arbitrage possibilities pop up and draw corporations into others.

In this book, we examine particular instances of international arbitrage. For instance, the human rights, environment, corruption, and tax chapters discuss how globalization has allowed corporations to operate in fragile and incomplete regulatory environments that allow them to commit harms in these areas with impunity. Moreover, in the chapter on parent company liability, we examine how the establishment of a subsidiary structure may impede the ability of tort victims from holding the corporation accountable. In short, international arbitrage highlights the ability of corporations to affect the public on a multitude of issues while similarly being able to thwart accountability. It therefore leaves the interests of the public potentially opposed to the interests of corporations without a proper protector for the public.

2.2.4 *Externalities*

A final reason for the growing intersection between corporations and the public is the rise of negative corporate externalities.[162] Ranging from imposing human rights or environmental consequences on unsuspecting tort victims to fostering corrupt cultures to necessitating reductions in public spending in tax haven states, corporate impacts on unrelated third parties, namely the public, are clearly increasing.

According to Coase, these types of negative externalities are best addressed by the market by assigning clear property rights and allowing the participants to bargain efficient outcomes. However, such an analysis assumes perfect market conditions and no information asymmetries, both assumptions that have been proved false.[163] As Stiglitz observes,

160 A. Beckers, *Enforcing Corporate Social Responsibility Codes: On Global Self-Regulation and National Private Law* (Oxford: Hart, 2015), p. 13.

161 G. S. Palazzo and A. G. Scherer, 'Towards a Political Conception of Corporate Responsibility: Business and Society Seen from a Habermasian Perspective' (2007) 32:4 *Academy of Management Review* 1096, 1108.

162 An externality is the unintentional effect of an economic decision on an outside party that is not part of the original decision. See R. C. Free, *21st Century Economics: A Reference Handbook*, vol.1 (Thousand Oaks, CA: Sage, 2010), p. 228.

163 Stiglitz, *supra* note 153, p. 21.

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> The externalities associated with imperfect information (and incomplete markets) are so diffuse and pervasive that it is inconceivable that they could be addressed through Coasian bargaining; but the information imperfections themselves mean that the kind of compensation envisioned in Coasian bargaining (where, in a world with well-defined property rights, those imposing external costs on others compensate them for the damage they suffer) is impossible.[164]

For that reason, Stiglitz recommends government intervention to address externalities. Thus, leaving the market aside, correction of negative externalities should be in the domain of individual, country governments. However, as the discussion on international arbitrage has highlighted, the agency of corporations often extends beyond national borders. This can leave regulatory gaps that enable corporations to act with impunity. As a result, even though responsibility for controlling the activities of corporations lies primarily with governments, where deficiencies in a 'state's apparatus'[165] exists, there may be a more pressing need to enmesh corporate and public interests.

Scherer and Palazzo make this argument cogently. As they observe, while corporations traditionally operate within a framework defined by the government, this assumption does not hold true due to globalization. Rather they contend that '[t]he global framework of rules is fragile and incomplete. Therefore, business firms have an additional political responsibility to contribute to the development and proper working of global governance'.[166] The authors are quite explicit in what they expect from corporations. They argue that where the 'legal system is imperfect or legal rules are incomplete' or when 'the enforcement body is weak' corporations should not only obey the law but 'go beyond what is required by law'.[167] This, they argue, is not only because of the ability of corporations to cross national boundaries but also because of the emergence of global risks, such as global warming or global diseases, which cannot be governed by one country.[168]

Some scholars have even recognized that corporations should bear public interest duties as one method of addressing externalities that cannot be curbed by governments alone. Schwarz, for instance, argues that problems of systemic risk, highlighted by the last financial crisis, can put in peril the entire financial system, which harms the public.[169] Accordingly, he recommends that corporations bear 'a public governance duty' that would require them not to engage in excessive risk taking that could systemically harm the public.[170] Hart and Zingales similarly argue that

164 Ibid., p. 22.
165 Palazzo and Scherer, *supra* note 161, p. 1101.
166 A. G. Scherer and G. Palazzo, 'Globalization and Corporate Social Responsibility' in Crane et al., *supra* note 55, p. 414.
167 Ibid.
168 Ibid.
169 S. L. Schwarcz, 'Misalignment: Corporate Risk-Taking and Public Duty' (2016) 92:1 *Notre Dame Law Review* 17.
170 Ibid., p. 28.

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corporations should seek to maximize shareholder welfare by taking social factors into account and internalizing their own externalities.[171] While not adopting a public interest model for corporations, Bratton and Wachter blame a shareholder-centric approach for firms' excessive risk taking.[172] Accordingly, they caution against empowering shareholders for fear of doing so will further incentivize corporations not to minimize externalities, such as market risks. Thus, the authors advocate in favour of the importance of corporations internalizing at least some externalities.

In this book, we will take a particular look at several examples of externalities – ranging from those in the area of tort and criminal law to human rights, environment, and corruption issues to issues relating to tax. Indeed, the presence of externalities in such a diverse range of areas, which corporations may be able to control and which governments – who bear traditional primacy in the area – may not, presents a strong argument for imposing corporate duties to the public.

2.3 CONCLUSION

The relationship between corporations and the public is not new. Rather, this is a long-standing relationship, which was unbundled during a period of increased focus on private welfare, but which is becoming pronounced once again. The coupling of corporate and public interests is not surprising given the many links between these two areas. Whether it is the ubiquitous power of corporations, their ability to act as rule makers, their movement as global actors, and/or their ability to commit negative externalities, corporations are strongly intertwined in public issues. This intermingling of corporate and public interests therefore demands that corporations bear public duties. What the scope of that duty is, however, will be laid out in greater detail in the following chapters as we traverse some of the most important public issues in which corporations have become involved, including issues of corporate, tort, criminal, human rights, the environment, corruption, and tax law. However, we begin, first, with a discussion of the corporate purpose and how it shapes the very basis of corporate duties to the public.

[171] O. Hart and L. Zingales, 'Companies Should Maximize Shareholder Welfare Not Market Value' (2017) 2:2 *Journal of Law, Finance, and Accounting* 247.

[172] Bratton and Wachter, *supra* note 69.

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