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The Emerging Personality of the American Corporation

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THE EMERGING PERSONALITY OF THE AMERICAN CORPORATION

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ERIC W. ORTS, BUSINESS PERSONS: A LEGAL THEORY OF THE FIRM (2013). Pp. 291. Hardcover $ 65.00.

ROBERT E. WRIGHT, CORPORATION NATION (2014). Pp. 304. Hardcover $ 69.95.

Late last term, the U.S. Supreme Court issued its opinion in *Burwell v. Hobby Lobby*, holding that a closely-held, for-profit company is a "person" for purposes of exercising religious rights that can be protected by the Religious Freedom Restoration Act (RFRA) of 1996, as determined by its owner's sincerely-held religious beliefs and values.[1] In so holding, the Court upended the foundational corporate law principle that the incorporated firm is a separate juridical "person," and is not coterminous with its owners, a principle that has long been recognized even where there is only one person owning all of the incorporated firm's stock.[2] The Court's rationale also undermined views of the for-profit corporation as simply an economic entity with wealth-maximizing as its only legitimate purpose, recognizing that:

> While it is certainly true that a central objective of for-profit corporations is to make money, modern corporate law does not require for-profit corporations to pursue profit at the expense of everything else, and many

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1. Burwell v. Hobby Lobby Stores, Inc., 134 S. Ct. 2751, 2768 (2014).

2. In the common law countries of the UK, U.S., and Canada, this principle is traced to *Salomon v. Salomon & Co.*, [1897] AC 33 (HL). In that opinion, creditors of A. Salomon & Co., Ltd. sought payment from Aron Salomon for debts incurred by A. Salomon & Co., which the House of Lords construed as a "one-man firm" wholly owned by Aron Salomon. Lord Herschell, in ruling against the creditors, in one paragraph put into place concepts that remain foundational today, to whit:

> I am at a loss to understand what is meant by saying that A Salomon & Co, Ltd is but an alias for A Salomon. It is not another name for the same person; the company is *ex hypothesi* a distinct legal person. As little am I able to adopt the view that the company was the agent of Salomon to carry on his business for him. In a popular sense a company may in every case be said to carry on business for and on behalf of its shareholders, but this certainly does not on point of law constitute the relation of principal and agent between them or render the shareholders liable to indemnify the company against the debts which it incurs.

Id. As discussed below, economic accounts of the corporation continue to mistake the agency relationships within the firm by suggesting that the shareholders are the "principal" in the relationship and the board of directors their agent. *See infra* text accompanying note 28.

> do not do so. For-profit corporations, with ownership approval, support a wide variety of charitable causes, and it is not at all uncommon for such corporations to further humanitarian and other altruistic objectives. Many examples come readily to mind. So long as its owners agree, a for-profit corporation may take costly pollution-control and energy-conservation measures that go beyond what the law requires. A for-profit corporation that operates facilities in other countries may exceed the requirements of local law regarding working conditions and benefits. If for-profit corporations may pursue such worthy objectives, there is no apparent reason why they may not further religious objectives as well.[3]

While there is much to criticize in the Court's opinion from a corporate law perspective, particularly its misconception that shareholders have the power to approve—or not—of management decisions regarding charitable, social, environmental, or economic activities (except, perhaps, by using the legal fiction of approval by virtue of buying or selling shares based on the firm's social or political activities), this is not the place to develop those criticisms.[4] What is clear, however, is that the Court is continuing a trend begun in *Citizens Union v. Federal Election Commission*, one that construes the for-profit corporation as having a social and political nature beyond its economic purposes.[5]

Without suggesting that Professor Eric Orts would necessarily agree with the Court's holding in *Hobby Lobby*, the broader conception of the corporation that the Court relies upon is consistent with Orts' institutional theory of the firm, as developed in his book, *Business Persons: A Legal Theory of the Firm*.[6] In the preface to his book, Orts sets out a number of reasons to suggest that the purely economic theories of the firm that have dominated scholarship for the last several decades are not sufficient to capture the complex reality of the modern business firm.[7] Among those reasons, he argues that law is necessary for a full understanding of the social origins and foundations of firms,[8] is essential to considering the "multiple values" beyond efficiency that can "structure organizations" and be

3. *Hobby Lobby*, 134 S. Ct. at 2771.

4. The persuasive power of that legal fiction is undermined by the fact that shareholders do not have access to clear, comprehensive, comparable information about a firm's charitable, social, environmental or political activities, despite longstanding academic attention to the issue. *See, e.g.*, John C. Coates, IV, *Corporate Politics, Governance, and Value Before and After* Citizens' United, 9:4 J. OF EMP. L. STUD. 657, 659, 661 (2012) (showing that political contributions are negatively correlated with shareholder value, and thus arguing that the SEC should require disclosure of such contributions); Faith Stevelman Kahn, *Pandora's Box: Managerial Discretion and the Problem of Corporate Philanthropy*, 44 U.C.L.A. L. REV. 579, 586 (1997) (arguing that the SEC should require disclosure of corporate philanthropy, because managers of firms can use charitable giving to mask conflict of interest transactions and board vote buying); Cynthia A. Williams, *The Securities and Exchange Commission and Corporate Social Transparency*, 112 HARV. L. REV. 1197, 1204 (1999) (arguing that the SEC has the legislative authority to require expanded social and environmental disclosure, and that it should do so in order to provide investors with consistent, comparable facts about companies' social and environmental performance, domestically and globally).

5. *See generally* Citizens United v. Federal Election Comm'n, 130 S. Ct. 876 (2010). This author has criticized *Citizens United* from a corporate law perspective. *See* Cynthia A. Williams & John M. Conley, *Trends in the Social [Ir]responsibility of American Multinational Corporations: Increased Power, Diminished Accountability*, 25 FORDHAM ENVIR. L. REV. 46 (2013).

6. ERIC W. ORTS, BUSINESS PERSONS: A LEGAL THEORY OF THE FIRM (2013).

7. *Id.* at ix.

8. *Id.* at x.

used to "resolv[e] disputes,"[9] and that these multiple underlying philosophical theories of the firm can "[un]shackle the imagination with respect to the purposes of firms."[10]

In this calm, thoughtful, important, and impeccably-sourced book, Orts constructs an institutional theory of the firm as a social and economic institution, one "both authorized and recognized by governments,"[11] as emphasized by top-down, concession theories of the firm, but also "managed by [and constructed by] individual participants,"[12] as emphasized by bottom-up, contractarian views. Chapter one is entitled "Foundations of the Firm I: Business Entities and Legal Persons," and in it Orts argues that we need not choose between these two competing versions of corporate theory. Orts relies upon H.L.A. Hart and John Dewey to suggest that what matters are the consequences for specific policy issues.[13] As he puts the point:

> At a minimum, the institutional theory assumes that both government and business participants have legitimate, substantive claims that deserve recognition . . . . The institutional theory of the firm is minimalist with respect to substantive political content because it leaves open for elaboration both (1) what substantive legal rules and restrictions government may impose; and (2) how far the aims and interests of business participants should be legally protected. In other words, the scope and breadth of substantive claims made by government (for regulation) and business participants (for limits on regulation and protection of their rights and interests) remain open for determination—both theoretically (through scholarly study and policy debate) and institutionally (through legal and political processes).[14]

While Orts may construe his institutional theory as minimalist with respect to substantive political content, as his discussion unfolds it becomes clear that the book is, in fact, an extended argument against the "standard [contractarian] economic view" that has considered "firms as merely 'fictions,'" and as first theorized by Eugene Fama as "a set of contracts among factors of production, with each factor motivated by its self-interest."[15] And that argument by Orts, within the discipline of corporate law scholarship, is political. Orts takes his argument forward by carefully showing the problematic aspects of every construct central to the contractarian view, while also demonstrating the necessity for legal, rather than purely economic, rules for constructing today's corporations.

In chapter one, Orts argues that even "the starting assumption of a natural human being as the relevant 'person' or unit assumed for economic analysis is problematic and

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9. *Id.* at xi.
10. *Id.* at xiii.
11. *Id.* at 14.
12. *Id.*
13. *Id.* at 17-19. *See also* H.L.A. HART, *Definitions and Theory in Jurisprudence, in* ESSAYS IN JURISPRUDENCE AND PHILOSOPHY 43-47 (1983); John Dewey, *The Historic Background of Corporate Legal Personality,* 35 YALE L.J. 655, 655-56, 660 (1926).
14. ORTS, *supra* note 6, at 18-19.
15. *Id*. at 27 (quoting Eugene F. Fama, *Agency Problems and the Theory of the Firm*, 88 J. POLIT. ECON. 288, 289 (1980)).

requires law for definition and recognition."[16] Orts relies upon Joseph Vining's work to show the many ways in which human beings have identities that shift depending on law and the legal context (such as a citizen versus a non-citizen in court, or with respect to the nation-state).[17] Even "if one concedes that firms are 'artificial legal fictions,' [comprised of human beings], they are legal fictions with social consequences that are real, practical, and large."[18] One can describe the business corporation as a legal fiction in the "sense that they are invented (in general) and created (in specific instances) by human beings who use established legal methods and processes to do so."[19] Once so invented, however, the corporation becomes "socially 'real'" in accordance with internal and external "legal rules, principles and understandings."[20] Connecting this discussion to the concept of "legal entities" (such as parent/subsidiary relationships, whose separate existence is also a "legal fiction") and "juridical persons," Orts demystifies the sense in which a corporation is a legal person, that is, a bearer of rights and duties, for some, but not all purposes.[21] Orts concludes, in chapter one, that "an institutional theory of the firm asserts that concepts of 'fictions,' 'entities' and '[juridical] persons' are foundational to understanding business enterprises,"[22] but also that these types of concepts are not unique to corporations or mysterious in the law.

In chapter two, Orts unravels the constructs of agents and agency law, contracts, and property, each of which is a foundational element in the standard economic view of the firm as a nexus of contracts. Orts starts the analysis by stating that "[f]irms of any complexity beyond a single individual cannot exist without the law of agency."[23] Agency law structures the relationships between principals (the firm acting as "juridical persons"), its agents (its governing body and CEO, as quasi-principals, and employees as agents and sub-agents) and third parties, both by imposing fiduciary duties on the quasi-principals and agents and by creating structures of authority and control.[24] Agency law can also provide some help in defining the boundaries of the firm,[25] although cannot completely accomplish that task, because in addition to internal agency relationships there are also external agency relationships, such as "arms-length contracts with services providers."[26] Determining the boundaries of the firm is difficult in a world enmeshed in a web of agency,[27] but is a particularly nettlesome problem for contractarians: if a firm is nothing but a nexus of contracts, how are we to know which of a firm's thousands or even millions of contracts are within the firm and which are not? The answer cannot be "it doesn't matter," because issues of fiduciary duties, authority, and responsibility between the firm and

16. *Id*.
17. *Id.* at 28.
18. *Id.* at 29.
19. *Id.* at 30.
20. *Id.*
21. *Id*. at 30-49.
22. *Id.* at 51.
23. *Id.* at 54.
24. *Id.* at 54-60.
25. *Id.* at 62.
26. *Id.* at 61.
27. *See* Samuel Issacharoff & Daniel R. Ortiz, *Governing Through Intermediaries*, 85 VA. L. REV. 1627, 1635 (1999).

those outside it depend on where those boundaries are drawn. Contrary to the standard economic theory of the firm, an accurate understanding of agency law shows that shareholders are not the principal in the corporate firm, except perhaps in a controlled corporation where one or a few shareholders own a controlling block of shares. As stated by the *Restatement (Third) of Agency Law, "*a 'true agency' is 'not present' in the 'relationship between a corporation's shareholders and its directors."[28] Fundamental to a true agency is the ability of the principal to control the agent's actions, which is not a power that shareholders in a public corporation have.

Orts next discusses not only the importance of contracts within firms, but also their insufficiency in explaining all aspects of the firm. Missing in such an account are organizational realities such as hierarchies and management authority (some of which are grounded in contracts, some in agency law, some by actions of corporate officials, some in norms such as fairness, relationship, trust, and so forth);[29] collective ownership of property within the firm; and the legal recognition of the firm as an entity separate from its constituents.[30] Orts also shows that property and its ownership (and management) is not simple and so cannot provide the seed around which a nexus of contracts can form and a reasonable facsimile of a firm crystalize. Firms possess tangible property,[31] intangible property (which critically depends on rights of legal recognition, as conflicts between Chinese and U.S. intellectual property regimes show),[32] and fractured ownership interests with rights to various capital flows, as elaborated by Berle and Means, with various governance implications that follow particularly from the use of debt versus equity.[33] Moreover, simple contractarian views of the firm miss important, real-world fracturing of ownership and control, such as that provided by parent/subsidiary pyramidal ownership, which permits financial as well as operational control of controlled companies with far less than majority ownership, and which account for "more than one-quarter of the largest companies in the world."[34] And contractarians, who obsess about the agency costs of the separation of ownership from control, have not sufficiently encompassed in their theories "the large, self-organizing, and significantly 'autonomous' firm," whose growth is made possible by retained earnings and thus is not selling either new equity or debt and so not taking on new capital ownership obligations.[35] Far from being a minor character in the corporate finance *dramatis personae,* studies have shown that retained earnings are "'the primary method of finance' in most developed countries, including France, Germany, Japan, the United Kingdom, and the United States."[36] Thus, even a sophisticated understanding of the classic implications of "the separation of ownership from and control," as developed by Berle and

28. ORTS, *supra* note 14, at 60.

29. *Id.* at 65-68 (citing, *inter alia,* Robert C. Clark, *Contracts, Elites, and Traditions in the Making of Corporate Law,* 89 COLUM. L. REV. 1703, 1705 (1989); Robert C. Clark, *Agency Costs Versus Fiduciary Duties, in* PRINCIPALS AND AGENTS: THE STRUCTURE OF BUSINESS 60-61 (John W. Pratt & Richard J. Zeckhauser, eds., 1990); Melvin Aron Eisenberg, *The Structure of Corporation Law,* 89 COLUM. L. REV. 1549 (1989)).

30. *Id*. at 65.

31. *Id.* at 71, 73.

32. *Id.* at 75-78.

33. *Id.* at 78-90.

34. *Id.* at 92-93 (citing Rafael La Porta, Florencio Lopez-de-Silanes & Andrei Shleifer, *Corporate Ownership around the World,* 54 J. FIN. 471, 499-500 & tbl. IV (1999), for estimates of pyramidal ownership).

35. *Id.* at 102-04.

36. *Id.* at 103 (citing FRANKLIN ALLEN & DOUGLAS GALE, COMPARING FINANCIAL SYSTEMS 363 (2000);

Means in the 1930s, misses much of the complexity of ownership of rights in today's business firm, Orts argues.[37]

Chapter three, entitled "The Public/Private Distinction: Two Faces of the Business Enterprise," rejects the view that the public/private distinction is "unhelpful" in understanding the modern business corporation.[38] In response to the "unhelpful" claim, Orts discusses a number of different ways to understand "the public/private distinction," such as between government or private ownership of shares in companies; or between public (regulation) versus private (contract) sources of control within the firm: he connects those concepts to his institutional theory of the firm, arguing "that business enterprises are neither entirely 'private' nor entirely 'public.'"[39] Sustaining that latter argument is central to Orts' project, and so an extended quote is in order:

> To accept the importance of the public/private distinction does not mean to say that business enterprises are to be understood as only 'private' rather than 'public' entities . . . Instead, firms have two faces: public *and* private. They are created, recognized, and regulated by public authorities, namely, governments. They are also composed of private interests and private participants who deserve some level of legal recognition by and protection from government. The relative balance between the public and the private elements of firms are continually contested in both theory and practice . . . . The hard choices of regulation focus on the scope of recognition to be given to private organizations and the extent to which they should be required to shoulder public obligations of one kind or another.[40]

The first aspect of the public/private distinction that Orts discusses is with respect to the ownership of firms by either private investors or the state.[41] While it is clear that some property is public and some private, business firms in different societies "present a shifting mix of state-owned and privately-owned enterprises, as well as hybrid forms," even including state-owned or hybrid businesses in the U.S. (such as Fannie Mae and Freddie Mac, taxpayer-funded bailouts of financial firms, Amtrak, the U.S. Post Office, and the Corporation for Public Broadcasting), versus state capitalism in China which also exhibits thriving private-firms.[42] The implications of these different ownership structures for his central theory are not clearly articulated, but perhaps are obvious.

The next difference between public and private that Orts articulates is with respect

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Colin Mayer, *Corporate Governance, Competition, and Performance*, 24 J.L. & SOC'Y 152, 164-65 (1997) (showing that retained earnings leads all other sources of new financing in those five countries).

37. *Id.* at 79.

38. *Id.* at 109 (citing Morton J. Horwitz, *The History of the Public/Private Distinction*, 130 U. PA. L. REV. 1423 (1982) and Duncan Kennedy, *The Stages of the Decline of the Public/Private Distinction*, 130 U. PA. L. REV. 1349 (1982), for the concept that the distinction is "unhelpful").

39. *Id.* at 123.

40. *Id.*

41. *Id.* at 110.

42. *Id.* at 110-11.

to how law treats and justifies "private property" and "private contract," relying upon Morris Cohen's work.[43] Beyond property and contract, the distinction matters in evaluating "the rights to self-organize and various freedoms that are recognized in the workplace," as well as determining the sources and permissible ambit of social control within the business firm.[44] Having concluded that the distinction matters does not imply that it is easy to draw the line between matters of public versus private concern, particularly given "privatization" of traditionally public institutions (the military or prison administration, for instance).[45] That difficulty implies that the line-drawing can only be sensibly done with respect to particular issues (such as "whether employees should possess 'public' rights of free speech in 'private' workplaces"), and with reference to social values outside of the law.[46] This latter point is Orts' response to the "indeterminacy" argument concerning the public/private divide.

In response to structural critiques that arguments of private rights of contract and property can be used as "show-stoppers," for instance as against labor rights or environmental considerations, Orts contends that "arguments invoking private rights may favor different groups that have historically had less influence (such as employees or dispersed shareholders) as well as groups that have usually held greater social power (such as top managers or wealthy owners."[47] How that might be done is not developed in any detail. Rather than a Marxist argument that:

> den[ies] any zone of legal coverage to private rights, the more moderate position adopted here seems preferable and more persuasive, namely: to recognize the legal distinction between public and private as salient—and then to allow and encourage policy debates with respect to where the lines should be drawn.[48]

While Orts' argument that public values can be—and should be—permitted to affect the internal workings of the firm is persuasive, at least to this reader, Orts is less persuasive in his discussion of the opposite concern: the private business firm's ability to participate in and shape public regulation. As he puts the point:

> In principle at least, it is not clear why the possession of wealth or other resources should disqualify citizens from influencing the political process of regulation, as long as these resources are not used coercively to

43. *Id.* 112-13 (citing Morris R. Cohen, *Property and Sovereignty*, 13 CORNELL L. Q. 8 (1927); Morris R. Cohen, *The Basis of Contract*, 46 HARV. L. REV. 553 (1933)).

44. *Id.* at 113. He recognizes that this point is, in effect, a recapitulation of the general conundrum of whether one construes the business firm as a top-down creature of public law, as in *Dartmouth College*, or as a bottom-up relationship among the participants in any one individual firm.

45. *Id.* at 117.

46. *Id.* at 118-19 (citing Ruth Gavison, *Feminism and the Public/Private Distinction*, 45 STAN. L. REV. 1 (1992), while recognizing that the existence of a public/private distinction is a highly-contested issue in feminist legal theory). *See, e.g.,* Frances Olsen, *Constitutional Law: Feminist Critiques of the Public/Private Distinction*, 10 CONST. COMMENT. 319 (1993).

47. ORTS, *supra* note 6, at 121.

48. *Id.*

> silence or buy off other less well-endowed citizens and thereby control political results. These concerns support legal prohibitions against politically motivated coercion, such as bribery and vote-buying in elections, for example—and may support limitations on campaign contributions as well (taken up in Chapter Seven). A general political concern is warranted that an oligarchy of business-connected wealth could arise and exert a controlling influence on political process and legal regulation. This is an ancient and continuing concern in political theory, and it is an important theme, though one that lies mostly outside the scope of this book.[49]

The power of private business interests to shape public regulation and "control political results" in accordance with self-interested conceptions of the good goes beyond coercion or silencing, however, as too many recent analyses have shown.[50] Moreover, economic inequality in the U.S. is growing in significant part because of the rise of the "super-managerial elite" within U.S. business,[51] and we see a convergence in policy preferences between the ultra-wealthy and business interests, which is having a demonstrable effect on policy outcomes at the federal level.[52] Thus it seems more consideration of this aspect of the public/private distinction should have been in order.

To be fair, in ending the chapter with a lengthy discussion of *Trustees of Dartmouth College v. Woodward* as a "concluding example of the social importance of the public/ private distinction,"[53] Orts recognizes the importance of the question of whether "empowering private corporations too much would threaten to corrupt the public political process" and states again that it is an "important political dimension of the public/private distinction" that is "not addressed at length in this book."[54] And he states that he hopes to take up these difficult "issues regarding politics and business enterprises in future work."[55] Given

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49. *Id.* at 122 (describing "oligarchy" as a perverse form of government "directed to the interest of the well-to-do" as opposed to healthy forms of government "directed to the advantage of the whole body of citizens") (internal citation omitted).

50. *See, e.g.*, JACOB S. HACKER & PAUL PIERSON, WINNER TAKE ALL POLITICS (2010) (describing how policy positions supported by a majority of Americans fail to become law today given the influence of elite preferences and money in politics); SIMON JOHNSON & JAMES KWAK, 13 BANKERS: THE WALL STREET TAKEOVER AND THE NEXT MELTDOWN (2010) (discussing how federal economic policies have been driven by "ideological capture" and the revolving door between Washington and Wall Street).

51. *See, e.g.,* CHRYSTIA FREELAND, PLUTOCRATS: THE RISE OF THE NEW GLOBAL SUPER-RICH AND THE FALL OF EVERYONE ELSE 14, 130-40 (2012) (discussing the escalation in CEO pay); THOMAS PIKETTY, CAPITAL IN THE TWENTY-FIRST CENTURY 315-21 (2014) (presenting data showing that, in all the English-speaking countries including in the U.S., "the primary reason for increased income inequality in recent decades is the rise of the supermanager in both the financial and nonfinancial sectors").

52. *See* Martin Gilens & Benjamin I. Page, *Testing Theories of American Politics: Elites, Interest Groups and Average Citizens,* 12 PERSPECTIVES ON POLITICS 564 (2014) (evaluating the response of Congress on 1,779 policy issues, and finding evidence of economic elite domination and biased (business plus wealthy individuals) pluralism affecting the policies adopted).

53. ORTS, *supra* note 6, at 126; Dartmouth College v. Woodwards, 17 U.S. 518, 636 (1819). In *Dartmouth College*, the Supreme Court recognized the authority of government to "determine the rules of the game with respect to the formation of private organizations," but also held that once organized there are constitutional limits on how the state may change the rules of the game for organizations already formed. *Id.*

54. ORTS, *supra* note 7, at 130.

55. *Id.* at 122 n.68.

his thoughtful contributions to a legal theory of the firm in this book, Orts should be encouraged in that regard.

Chapters four and five, while replete with excellent sources and statistics, are more descriptive chapters geared, it seems, to a general or an interdisciplinary audience than they are theoretical or conceptual chapters engaging with legal academics' arguments over the nature of the corporation. That said, both introduce new developments in the business world and suggest avenues for future analysis and policy development, and so are likely to engage the attention of even expert readers. Chapter four, "Enterprise Liability, Business Participant Liability, and Limited Liability," discusses each of these concepts in turn, noting the ability of companies to structure their enterprises in ways that can have the effect of allowing uncompensated harm (such as by the use of separately-incorporated subsidiaries in various countries in which the enterprise does business, or by the use of franchise structures or independent contractors rather than employees to adjust the borders of enterprise liability).[56] Orts is more normative in this discussion than in many other parts of the book, asserting that "[i]n general, business enterprise conducted through the use of multiple entities requires an updating of principles of enterprise liability to focus on the nature of firms operating at this level of complexity and integration,"[57] while recognizing that enterprise liability has been recognized more broadly in Germany and the European Union than it has been in the United States or Great Britain.[58] While *Hobby Lobby* is likely to be *sui generis*, one potential implication of that opinion, if carried forward, would be to soften the borders of separate existence between shareholders (such as parent companies) and separately incorporated subsidiaries.[59] We are a long way from that outcome, but principles of enterprise liability bear serious reconsideration given the global reach of the country's largest companies, concerns that global corporate accountability has been undermined by the Supreme Court in *Kiobel v. Royal Dutch Petroleum*, and the inconsistent and financially beneficial treatment of global firms as enterprises for tax and transfer pricing purposes.[60]

Chapter five continues Orts' methodological institutionalism, recognizing the importance of both institutions and the individuals within them, to describe the range of business firms today in terms of interactive dimensions of capital ownership, governance, and agency authority.[61] Data and analysis using those "interactive dimensions" are provided on the "standard range" of business entities, including sole proprietorships, partnerships, cooperatives, limited liability partnerships (LLPs), limited liability companies (LLCs), small and large firms (which roughly, but not entirely, track closely-held corporations and

56. *Id.* at 137-44.

57. *Id.* at 145-46 (relying on PHILIP I. BLUMBERG ET AL., BLUMBERG ON CORPORATE GROUPS (2005)). Professor Blumberg has been a pioneer in the (so-far unsuccessful) effort to persuade courts in the U.S. of the importance of enterprise liability.

58. *Id.* at 146.

59. Burwell v. Hobby Lobby Stores, Inc., 134 S. Ct. 2751 (2014).

60. Kiobel v. Royal Dutch Petroleum, 133 S. Ct. 1659 (2013) (holding that the Alien Torts Claims Act ("ATCA") does not apply extraterritorially). The ATCA had been the primary statute giving subject matter jurisdiction to U.S. federal courts to hear claims against companies for alleged violations of plaintiffs' international human rights abroad.

61. Orts, *supra* note 6, at 182.

widely-held corporations).[62] Orts also devotes substantial attention to types of enterprises that are often ignored, at least in many law professors' business associations classes, including government and state-owned enterprises,[63] charitable and nonprofit enterprises,[64] and hybrid social enterprises.[65] This chapter is stuffed with excellent data on numbers of these entities, total revenues, total payrolls, trends and comparative data covering a wide range of countries. Orts includes a separate sub-chapter to what he calls "complex relational firms,"[66] including corporate groups, franchise firms (with data showing that franchise firms accounted for over one-third of retail sales in the U.S. in 2010), joint ventures, marketing alliances, cooperatives and so forth.[67] Again, Orts returns to the questions of the boundaries of the firm, whether arrangements of ownership and control "amount to 'integration' sufficient to perceive a coherent enterprise," and how companies' formations of complex business relationships can or should be used to limit liability and reduce taxes.[68] Orts' general argument is that "an economic decision to structure a business enterprise to avoid potential liability should not dispose of questions about whether the method of avoidance should be legally respected as a matter of public policy."[69] The chapter ends with a discussion of corporate responsibility and the range of ethical cultures within firms.[70] As throughout the book, this chapter contains a wide range of sources for further development of the ideas and arguments for interested readers.

The final chapters in the book are short. Chapter six, "Managing and Regulating the Shifting Boundaries of the Firm," summarizes the author's arguments in the rest of the book, emphasizing how the boundaries of firms have important implications for questions of responsibility, liability and regulatory design. In his summary, Orts asserts that in constructing regulatory regimes "[t]he legal theory of the firm advanced here is . . . compatible with an array of normative orientations and approaches" including law and economics, which emphasizes economic efficiency, or with "others [who] may argue that the normative principles of democracy and political equality should take precedence."[71] Given how much of the book is an argument against law and economics and the contractarian views of the business firm, at least insofar as those views would purport to be a complete description of the firm, that assertion of compatibility is mysterious. Clarifying that comment is Orts'

> own intuition that competing values—including economic efficient, democracy, deontological duties (such as honesty and loyalty), and distributive justice—will prove more or less compelling in different situations. At least descriptively, it is inaccurate to say that any one particular value

62. *Id.* at 175-91.
63. *Id.* at 194-200.
64. *Id.* at 200-06.
65. *Id.* at 206-15.
66. *Id.* at 191.
67. *Id.* (citing Robert W. Emerson, *Franchise Encroachment*, 47 AM. BUS. L.J. 191, 196-97 (2010)).
68. *Id.* at 192-93.
69. *Id.* at 192.
70. *Id.* at 222.
71. *Id.* at 228.

> (such as overall social welfare maximization as determined from an economic perspective) is dominant in current legal practice.[72]

To the extent that he is distinguishing here between legal practice and academic theory, then his compatibility statement makes more sense, given that corporate law decisions emphasize the fiduciary duties of care and loyalty,[73] and do not try to tie them to a concept of economic efficiency. Still, since most of the book has been an argument against the law and economics' conception of the firm, Orts perhaps should have been more careful in how he summarized his argument in this chapter.

Chapter seven, entitled "Two Applications," shows two examples of how having a broader theory of the firm can help in thinking about difficult issues involving business corporations: levels of executive compensation and the constitutional rights of political speech for corporations. Regarding executive compensation, Orts argues that a theory of the firm that is concerned only with shareholders and top managers, as is the relationship of interest if the "separation of ownership from control" is one's analytic framework, misses important implications in evaluating excessive levels of executive compensation.[74] Direct concerns include the effects on employees' productivity and morale generally from compensation structures deemed unfair.[75] Indirect concerns include the potential negative effects on the long-term investments of the firm, including in research and development, from an excessive focus on share price that can occur when top managers are compensated with stock options, as well as concerns that "high-powered incentives" for top managers have also created "temptations to commit accounting fraud."[76] Orts asserts that "[o]nce the mainstream principal-agent economic model of the firm is rejected as too narrow, simple, and naïve (at least with respect to many firms), a path towards other possible law reform opens."[77] This assertion seems undoubtedly true, since a theory that emphasizes the institutional aspects of the firm has both internal and external consequences. Internally, such a theory yields concerns about the ethical climate of the firm, employees' perceptions of fairness and the effects of those perceptions on productivity and "employee citizenship." And externally, an institutional theory allows a broader role for regulation to import public values, since the firm is understood to be more than a nexus of (privately-developed and enforced) contracts. Yet the examples Orts provides of other possible law reforms to address executive compensation are not particularly persuasive since they do not go beyond either existing measures (disclosure) or ideas already discussed and/or rejected: enhanced disclosure of executive compensation, enhanced judicial scrutiny of executive compensation as self-interested, and more progressive income taxation—the latter of which he essentially takes off the table as "overinclusive" since it would address "broader concerns of inequality."[78] Thus, this application ends up being unsatisfying, although the fundamental point—that an institutional theory of the firm allows more room for policy invention—

72. *Id.* at 229.
73. *Id.* at 70.
74. *Id.* at 233.
75. *Id.* at 234 n.19.
76. *Id.* at 235-37.
77. *Id.* at 237.
78. *Id.* at 238-39.

remains powerful.

Regarding constitutional protections for political speech, Orts' application of his theory is somewhat more satisfying: he articulates the problem of where to draw the line of permissible regulation of corporate political speech with specificity, relying upon his institutional theory.[79] Using the competing majority and dissenting opinions in *Citizens United v. Federal Election Commission*, Orts treats Justice Kennedy's majority decision's broad protection of corporations' political free-speech rights as consistent with the bottom-up, participant view of the corporation, even as the majority goes beyond pre-existing precedent and "does not . . . provide a full-fledged legal theory to explain why business corporations should have a right of political free speech equivalent to individual citizens."[80] Orts suggests that the rights of persons and firms should not necessary be coterminous, given compelling governmental concerns of corruption of the political process that are more cogent with the advantages of the business firm than with wealthy individuals, but since "business firms are composed of people [they] therefore should, derivatively, have their constitutional rights recognized."[81] The Stevens' dissent, Orts suggests, is consistent with the top-down view of the concession theory, with its long-standing concern for political corruption, and greater ambit for regulatory power.[82]

Bringing these perspectives together into a coherent whole is the difficult task that Orts attempts. He does this primarily by focusing on the point that business corporations are constructed to advance economic purposes, which does not imply shared political perspectives, nor do internal corporate governance mechanisms "work to transmit political preferences."[83] Thus, at the least Orts would support "a robust regulatory system of 'disclaimers and disclosure' of the organizations and individual identities of donors to political campaigns and political media operations," as discussed in Justice Kennedy's majority opinion in *Citizens United*.[84] To address the problem of corruption "requires at least some direct substantive regulation, such as the prohibition of bribery."[85] Again, as with respect to executive compensation, Orts' ultimate policy solutions seem more restrained than his theory would require. The system of disclosure of political contributions does not address the point that the for-profit corporation is not constructed to aggregate political preferences, and bribery is not the only concern with for-profit corporations' direct involvement in the electoral process.

A more persuasive analysis of the problem of identifying the proper scope of corporate political constitutional rights was that recently provided by Margaret Blair and Elizabeth Pollman, who show that prior to *Citizens United*, corporations' free speech constitutional rights were understood to be derivative rights.[86] Thus, such rights were either necessary to protect the property interests of the individuals comprising the corporation

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79. *Id.* at 245.

80. *Id.* at 241, 244.

81. *Id.* at 245. This argument does not address the point that the people who invest in and work for corporations can assert their electoral political rights and views directly.

82. *Id.* at 244-45.

83. *Id.* at 246.

84. *Id.* at 249.

85. *Id.* at 250.

86. Margaret M. Blair & Elizabeth Pollman, *The Derivative Nature of Corporate Constitutional Rights*, 56 WM. & MARY L. REV. (forthcoming 2015).

(as in speaking about a corporate tax issue, in *First National Bank of Boston v. Bellotti*),[87] or were necessary to provide information to the hearers of commercial speech (as in *Virginia Pharmacy*).[88] They would argue that, in determining when political free speech rights should be extended to juridical persons, the courts should pay attention to differences in the type of "person": non-profits and ideological political action campaigns can be understood as aggregates of their members from whom political rights can be derived; for-profit corporations can generally not be so construed.[89]

And yet, to say that this reader would have liked to have seen Orts go further in developing solutions in both examples is not to suggest that this undermines his institutional theory. His general points remain persuasive: first, that an institutional theory of the corporation more accurately describes the legal, social, political and organizational reality of the modern business firm than does a nexus of contracts, participant-based conception; and second, that this broader conception "represents a new beginning rather than an end of legal and political debate."[90] In that debate, Orts' book is an important and provocative intellectual contribution.

In somewhat of a contrast, Robert Wright's book *Corporation Nation* develops the implications of his solid historical research too aggressively.[91] The book is a deeply researched historical treatment of the development of business firms in the United States from the earliest days of the republic. The core chapters (four through six) present wonderful detail, painstakingly gathered, to inform and perhaps modify the standard view among corporate law professors about the problems with special state grants of authority necessary to incorporate a company, and the effects of general incorporation statutes starting to be adopted by the states in the late 1800s. What Wright shows in chapter four, entitled "Corporate Ubiquity," is that thousands of companies were given special charters by state governments before general incorporation statutes, and thus, "the ubiquity of corporations" between 1790 and 1860, and the amount of capital, conservatively estimated, that these companies represented was significant.[92] He also provides data about the 22,419 "specially chartered corporations" and their capitalization, state by state over the same period,[93] and also by type of industry.[94] Through these materials Wright provides a much more specific, and accurate, picture of the state of corporate America in the era of special charters.

In chapter five, "The Benefits of Big," Wright argues that the costs of obtaining a special charter were not generally a problem, and therefore there was no serious limitation on the number of companies.[95] Rather, the monopoly power once granted was problematic,

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87. First National Bank of Boston v. Bellotti, 435 U.S. 765 (1978).

88. Virginia State Pharmacy Bd. v. Virginia Citizens Consumer Council, 425 U.S. 748 (1976).

89. Blair & Pollman, *supra* note 86, at 46.

90. *Id.* at 250 (discussing *Citizens United* as "representing the beginning rather than an end of political debate").

91. ROBERT WRIGHT, CORPORATION NATION (2014).

92. *Id.* at 49-59.

93. *Id.* at 58-59, Tbl. 1.

94. *Id.* at 62-63, Tbl. 2.

95. *Id.* at 80-115.

as was the entanglement of the state in business, concomitant lobbying, and political involvement by the firms.[96] So in some instances, charters were not granted because the state was invested in one company and did not want to allow competition, or a state (such as New York) might refuse to charter a bank based on the purported political affiliations of the bank's founders.[97] Wright argues, however, that if entrepreneurs could not obtain a special charter, they could still conduct business as an unincorporated joint stock company.[98] The major factor that determined when industries shifted to a preference for transacting business using an incorporated form was when mechanization affected that industry, and thus there developed a need for larger amounts of capital.[99] Throughout the 1800s, and even as early as the mid-1700s, though, companies in various industries recognized the value of economies of scale, scope and market power, which developments Wright traces in many industries (printing, textiles, turnpikes, railroads, insurance, ferries, canals, and so on).[100] Foreshadowing an argument that comes to play a central role in Wright's analysis, he concludes this chapter by asserting:

> [i]t was difficult to rail against railroad 'monopolies' [when costs to consumers were falling and the time to travel between cities was becoming so much shorter], especially when the railroads were well-governed. Later in the nineteenth century, when railroad rates rose and many roads had clearly fallen into the grasp of cabals of directors or executives, matters would be different.[101]

Chapter six, entitled "Governance Principles," is a most interesting chapter, discussing governance principles before the Civil War that gave shareholders far more direct influence in companies than they have today. Thus, shareholders had power to develop policies for companies, to appoint committees to investigate various matters, to review financial statements and make decisions about the capital structure of companies, and to convene meetings to change managers.[102] Shareholders could buy shares in installments, which then had governance implications, since the subscriptions would only be paid in full if shareholders agreed with the direction of the company.[103] Directors and officers were concomitantly constrained, in some cases with officers even being required to pay performance bonds to secure their work.[104] Many of these governance principles worked to ensure that "everyone conceded that stockholders were the true owners of the corporation in which they owned stock."[105]

After this point in the book, Wright's perspective that "state-centered regulation proved itself to be more costly and less responsive than stockholder governance" begins

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96. *Id.* at 82.
97. *Id.*
98. *Id.* at 83.
99. *Id.* at 100-01.
100. *Id.* at 100-15.
101. *Id.* at 115.
102. *Id.* at 117-22, 132-33, 136-37.
103. *Id.* at 143-44.
104. *Id.* at 127.
105. *Id.* at 132.

to play a central role in his analysis, with negative consequences for the objectivity of his analysis, at least so far as this reader is concerned.[106] In chapter eight, "Regulation Rising," Wright concludes that increasing calls for safety, labor, and consumer protection statutes in different industries, including railroads, ferries, insurance, and banking, were successful in expanding the role of government in shaping corporate governance, a development he summarizes negatively as follows: "[m]ost state-directed regulations stuck, however, because they benefited governments, legislators, and, all, too often, the regulated companies themselves, with much of the cost falling on their respective constituents and customers."[107] Corporate governance after the Civil War increasingly saw shareholder power diminished; as the size of companies grew, the number of shareholders in companies expanded, and management increasingly became the province of paid executives with reasonably low shareholdings.[108] Drawing upon Berle and Means' separation of ownership from control, Wright decries the erosion of shareholder "checks such as the concept of ultra vires and caps on capitalization [which had previously] prevented railroad directors from furthering their managerial empires by straying into other lines of business."[109]

In applying his analysis of the governance failures after the Civil War to the corporate governance challenges of today, Wright's view is that "stockholder monitoring and sound management by directors and executives" have been "crowded out" by "the sordid history of government regulation."[110] Thus, he criticizes Glass-Steagall's separation of commercial and investment banking because the restriction "solved no economic problems but helped legislators get reelected by purportedly fixing a presumed cause of the Great Depression."[111] What Wright thinks was a more productive system was having investment banks playing a governance role by monitoring companies, extracting private financial information, and acting as reputational intermediaries on whom retail investors could rely; but this role was dismantled by the Clayton Act of 1914 and policies informed by "Brandeis's anti-investment bank diatribe *Other People's Money.*"[112] Rather than more "state-centered regulation,"[113] moreover, what Wright suggests are policies to "restore the principles of [stockholder] governance common in the antebellum period."[114] He would like to see institutional investors playing a larger role in corporate governance,[115] directors being more active as monitors, executives forbidden from owning shares in their companies (so as not to manipulate the prices), but being required to put their "familial assets" in their companies; and voting by proxy, banned.[116]

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106. *Id.* at 171.
107. *Id.* at 189. "Constituents," apparently, means shareholders in this quote.
108. *Id.* at 192-98.
109. *Id.* at 194.
110. *Id.* at 220.
111. *Id.* at 203.
112. *Id.* at 202-03.
113. Certainly pluralist or new governance legal scholars recognize norms, soft law, commercial standards, voluntary initiatives, certification regimes, and many other varieties of non-state-centered regulation. Yet Wright's consistent use of the term "state-centered regulation" in these concluding chapters of the book has a strong implication of regulatory animus, in context, rather than an implication of a distinction being drawn between state and non-state varieties of regulation.
114. *Id.* at 216.
115. *Id.* at 226.
116. *Id.* at 227-29.

These ideas show a potential risk for any serious academic of interdisciplinary scholarship. While the core of the book evidences careful historical investigation, these corporate governance ideas are deeply problematic. Some are redundant (institutional investors are already playing a large role in corporate governance, and encouraging boards to be more active monitors has been suggested as a reaction to corporate governance problems for the last four decades); some inconsistent (why would it make a difference if executives did not own the stock of their company but their "familial assets" were invested in those same stocks?); and some just silly and impractical (no proxy voting?). Generally, Wright wants to return to antebellum governance, when companies had very few shareholders (100 to 1000 at most),[117] and most shareholders lived so close to the company in which they owned shares that they could participate in the annual meeting in person rather than by proxy, carefully watching the management of their investments.[118] This social and historical context is so far from the world we live in today that suggesting we go back to the governance mechanisms that worked then is a suggestion only an idealistic historian could love. That said, Wright has compiled impressive data on the growth of companies in the U.S. and on how companies' corporate governance arrangements used to work when those companies were smaller and locally owned and managed, so the book is of value notwithstanding the weaknesses of the last three chapters.

117. *Id.* at 90-94.
118. *Id.* at 91.