

The Utility of the Business Organizations Class

Daniel JH Greenwood¹ – January 4, 2014

Panel: Tamar Frankel, Boston U; Christyne Vachon, U. N. Dakota; Robert Reder, Milbank (ret.), Vanderbilt; Tamara Piety; Daniel Greenwood

Comments:

Prof. Vachon emphasizes the importance of the ethical dilemma in storytelling. Bus Orgs, it seems to me, is a key locus of rhetoric in the law. We begin the course with morality plays of ownership, contract, property, democracy – and then we challenge them all, replacing ownership with (per share) voting, contract with the radically different norms of agency, democracy with market.

As Prof. Frankel emphasizes, our largest corporations are institutions of power and influence resembling states. Yet they are not fully under the control of either state or citizen – we can think of them as competing power structures organized under quite different principles.

The key issue Frankel raises, and one that we need to place front and center, is how the internal decisionmaking processes of these institutions press them to behave in the public sphere.

The internal norms of business corporations are an odd amalgam of Cardozo’s “highest punctilio of an honor the most fine” – the “abnegation of self” of agency law – with the greed-is-good arms-length self-promotion of market and contract. Neither set of norms takes much notice of the justice, equality, common welfare or patriotic norms of the public sphere.

While we assume that most citizens comply with the law because they share or have internalized its norms, we have not designed our corporations along the same lines: while they are quite effective at ensuring that their decisionmakers and actors internalize corporate norms, we have fewer mechanisms for assuring that corporate norms do not stray from social ones. As Larry Mitchell has written, corporations can become “externalization machines” – devices for allowing people to act in ways that most of us, and most of them, would find abhorrent in other contexts.

Public law enters the corporate decision process as a constraint: through Prof. Frankel’s compliance officer and through the advice of Prof Reder and his former colleagues. It is stunningly absent from the stories that Prof. Vachon and other lawyers tell, which nearly always emphasize profit maximization above ordinary decency and even despite the law.

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In my view, the business organizations course is critical in the law school curriculum precisely because of this issue. Law school tends to be somewhat triumphalist: we have enshrined the liberal ideals of liberty, equality and prosperity into the rule of law, embodied in a happy confluence of tradition, professional debate and judicial reasoning, and democratic legislative course corrections. [To be sure, the system has often been less than perfect – our nation was founded half slave, after all – but the workings of history refine the dross and have left us with something pretty good. Even if we disagree on abortion, we agree on the basic values that form our constitutional and common law systems.]

The business organizations course is a leading reminder of how far we have to go to reach the eighteenth century paradise of Lockean liberty.

First, of course, agency rejects equality and democracy as fundamentally as it rejects the strangers of the state of nature and our first year curriculum. Agents and their principals -- servants and masters -- are always in relationship, never strangers and, as the terms make clear, never equal in the eyes of the law. [The XIII Amendment may have abolished involuntary servitude, but Bus Orgs reminds us that for 40 hours or so a week, nearly all of remain – or aspire to remain – in voluntary servitude, servants to a master that is entitled, as a matter of law, to direct our actions, appropriate our products, and invade our privacy.]

In the state of nature, people may acquire property rights by mixing their labor with its objects. In American law, however, at least during the working day, the product of our labor belongs to our employers. Under the law of agency, much as in our national politics, it is the takers who are deemed the makers, while the actual makers are left out of the picture altogether.

Second, the law of organizations undermines the stories of personal responsibility that seem to underpin the first year curriculum. [To be sure, as we teach our students, tort, contract, criminal law, conlaw and so on create rights and duties for legal persons. But] it is only in Bus Orgs that we clarify that lawyers have virtually complete discretion to create the relevant legal persons, determine who controls them, and endow them with the assets and powers that mean that there is a there there – or there isn't.

As Lynn LoPucki has eloquently pointed out, regulatory law beginning with tort and contract has a radically counterintuitive meaning if we can easily make the relevant legal actor insolvent or simply dissolve and re-form it after any liability-creating event.

Conversely, constitutional rights have very different meanings if we can create rights-bearing persons at will – if Corporations are Fourteenth Amendment persons for the purpose of participating in politics by advertising and lobbying, or asserting that unregulated speech trumps essential economic self-government, doesn't the same Fourteenth Amendment also

grant them the right to be counted in apportionment? As we've known since Hobbes, at least, many rights are zero sum; granting them to easily replicated organizations and purely fictional shell corporations diminishes what real citizens retain.

Third, the law of business organizations challenges commonplace economic ideals of the market and the political ideals of self-governing democratic republicanism.

Our corporations are managed by ordinarily self-perpetuating elites that are, however, ultimately responsive to an anonymous stock market dominated by computerized trading and arbitrageurs (at least in the case of publicly traded corporations). Although we call this "shareholder democracy" it has nothing to do with democracy – votes for sale is plutocracy or corruption -- and little to do with shareholders: prices are set by buyers and sellers, not holders – rule by immigration and emigration, not members.

And we offer rationalizations for why corporations, at least those with public shareholders, often seem to be managed at least partly in the interest of shareholders – even though ordinary economic theory tells us that as purely fungible providers of a purely fungible commodity (money) shareholders should have no claim on profits. And as sunk costs, they should not be able to obtain payment at all.

Corporate law, that is, is the great mystery play of the curriculum. We teach self-interest and self-abnegation, and yet expect and predict that self-interested self-abnegating agents – managers who ought to set aside their own interests -- will make uncompelled gifts of the product of other people's work to an anonymous collection of pension funds and the international kleptocracy. We call shareholders owners, and demand that they receive the surplus created by the cooperative activity in the firm – but deny them the rights or responsibilities of ownership. We teach the rhetoric of mechanical self-interest, while practicing faith-based economics, in which we expect insiders to give gifts of dividends just because it is expected.

And we pit the strong incentives of the stock market against the equally strong but more diffuse incentives of morality and wonder why, so often, compliance officers become trail-guides to evasion.