PROPERTY OR SOCIAL ENTITY: REVISITING THE BUSINESS CORPORATION*

*William M. Varias***

INTRODUCTION

The origin of the term "corporation" can be traced back to the early fifteenth century when the townsmen of Plymouth petitioned to become a "*corps corporat.*"[1] This term, derived from the Latin word "*corporatus*" ("made into a body"), refers to a body of men joined together for a common design.[2] The word "company," on the other hand, originates from the twelfth century Latin term *"compagnia"* meaning "breaking bread together."[3] To be sure, this fictional entity has fascinated thinkers from every jurisdiction[4] that since its inception, the debate among jurists, scholars and the courts on the legal nature of the corporation[5] has never ceased. This paper is not an attempt to join that metaphysical tussle. Instead, the paper's approach will be pragmatic, examining signs and proofs that tell us whether the conventional notion on the corporation's legal nature is still true today.

Traditionally, it has been held that business corporations are established for purely private and financial reasons.[6] Corporate managers and directors must perform their duties in the interest of the company's shareholders. Corporations have one ultimate objective: profit maximization. In time, however, corporations came to wield enormous economic power,

* *Cite as* William Varias, *Property or Social Entity: Revisiting the Business Corporation,* 84 PHIL. L.J. 342 (page cited) (2009).

** Associate, Angara Abello Concepcion Regala & Cruz Law Offices (November 2006-present); Intern/Visiting Lawyer, Nagashima Ohno & Tsunematsu, Tokyo, Japan (October-December 2009); LL. M., Kyushu University, Japan (2009); LL.B., University of the Philippines College of Law (2006); B.A. Philosophy, *magna cum laude,* St. Louis University (1999).

1 ERNST FREUND, THE LEGAL NATURE OF CORPORATIONS 7 (1897).

2 *See* Sanford Schane, *The Corporation is a Person: The Language of a Legal Fiction*, 61 TUL. L. REV. 563, 566 (1987).

3 Joe Pitts III, *Corporate Social Responsibility: Current Status and Future Evolution*, 6 RUTGERS J.L. & PUB. POL'Y 334, 344 (2009).

4 The amount of literature devoted to the study of corporate personality is simply overwhelming. Some of the notable works on this subject include Arthur Machen, *Corporate Personality*, 24 HARV. L. REV. 253 (1911); FREDERICK HALLIS, CORPORATE PERSONALITY A STUDY IN JURISPRUDENCE (1930); Morton Horwitz, *Santa Clara Revisited: The Development of Corporate Theory*, 88 W. VA. L. REV. 173 (1986); David Millon, *Theories of the Corporation*, 1990 DUKE L.J. 201 (1990).

5 The subject of this paper is the business corporation. Thus, the words "corporation" and "business corporation" whenever they appear refer only to the business type of the corporation.

6 Milton Friedman is one of the staunch advocates of the traditional view. *See* Milton Friedman, *The Social Responsibility of Business Is to Increase Its Profits*, NEW YORK TIMES MAGAZINE, Sep. 13, 1970, *in* ETHICAL THEORY AND BUSINESS 87-91 (Tom Beauchamp and Norman Bowie ed., 3rd ed., Prentice Hall 1988).

shaping every aspect of life and affecting stakeholders other than corporate shareowners. Gradually, the business community began paying extra attention to constituencies other than company stockholders. Non-shareholder interests became prominent topics in boardroom meetings.

This paper will argue that the emergence and prominence of non-shareholder interests in the conduct of corporate business and boardroom decision-making, as well as the increase in corporate "giving" reveal a break from the traditional notions regarding the business corporation. Corporate "giving" is used here in a broader sense. It is not limited to charitable contributions. It also includes unconventional and "un-businesslike" strategies employed by corporations designed to impact not only their shareholders, but also the public or other constituencies.

In Part I, a background on some of the major theories regarding the nature of the corporation will be presented. Part II will discuss the fiduciary duties of corporate managers. The fiduciary duties owed to the corporation largely fall on the shoulders of directors. The term "corporate managers" will also be used, however, to refer to the individuals possessing fiduciary duties as corporate officers and other key personnel of the corporation also perform similar duties of care and diligence in the interests of the company. Part II also explores the expansion of corporate managers' duties to include non-shareholder or stakeholder interests. In Part III, we will look at the emergence of non-shareholder interests in the corporate domain as demonstrated in the development of stakeholder statutes, corporate codes of conduct and the OECD Principles of Corporate Governance. Part IV will discuss corporate "giving" in the form of data on corporate charitable contributions and avant-garde business methods employed by some of today's corporations that deliberately seek to make a difference on the lives of, in the words of Bill Gates, the "people who have been left out."

For practical reasons, the discussions in this essay will focus on developments and research in American corporate theory. It is in the United States where a sizable body of literature on corporate theory has developed and evolved over the past decades. However, whenever possible, reference to other jurisdictions' law and theory were made. The use of the terms "property" and "social entity" in the title of this paper was inspired by Chancellor William T. Allen's article based on a lecture he delivered in 1992 where he summarized the major conceptualizations of the corporation using those words.

I. THEORIES ON THE NATURE OF THE BUSINESS CORPORATION

Chancellor Allen pointed out that the takeover phenomenon in the 1980s became problematic for the legal theory of the corporation.[7] A drastic change in corporate control achieved through takeovers could have "dramatic effects on creditors, employees, management, suppliers, and communities,"[8] he said. But must corporate directors pay attention to matters other than the shareholders' interests? Can they resist the stockholders' desire to sell control of the corporation?[9] These questions seemed to provide a fitting backdrop for the revival of old debates in corporate theory at the time. But prior to these developments in corporate theory in the 1980s, scholars from different eras have already devoted hundreds of pages of their works dissecting the nature of the corporation.

A. Fiction Theory vs. Organic Theory

The corporation as a fictional entity

One of the early debates concerning the legal nature of corporations revolved around the concepts of the corporation as a *fictional* entity, on one hand, and as an *organic* creation, on the other hand. According to the influential nineteenth century jurist Friedrich Carl von Savigny, the original notion of a juristic person, or of the subject of a right, "must coincide with the idea of man."[10] Consequently, only the individual is juridically capable.[11] But Savigny contends that juridical personality may be expanded or restricted.[12] That is why not too long ago an individual may be denied personality by becoming a slave. In like manner, personality may be extended to an entity outside of the individual, the prime examples of which are associations or institutions.[13] This entity, however, is only "an artificially assumed subject,"[14] a fictitious being created by the state and granted the capacity to hold property. Having been granted existence and specific attributes by the state, the justification for this artificial entity's existence cannot be found in private law. Instead, the basis for its existence solely lies in the sphere of public law.[15]

---

[7] William Allen, *Our Schizophrenic Conception of the Business Corporation*, 14 CARDOZO L. REV 261, 274 (1992).
[8] *Id.*
[9] *Id.* at 274-75.
[10] Savigny, *La Personnalite Juridique* (2nd ed.), *cited in* HALLIS, *supra* note 4, at 4-5.
[11] *Id.*
[12] HALLIS, *supra* note 4, at 6.
[13] *Id.*
[14] *Id.* at 7.
[15] *Id.*

As a mere creation of the state, an artificial juridical entity can enjoy and exercise only those rights granted to it by the legislature and which rights must likewise be consistent with its property-holding capacity.[16] To subsist, the corporation depended entirely on what the law has conferred upon it and what its constituent charter contains, which is likewise confined within the bounds of law.

To Savigny's mind, the defining quality of a corporation consists in the idea "that the subject of the right does not exist in the individual members thereof (not even in all the members taken collectively), but in the ideal whole."[17] The individual constituents making up a corporation are irrelevant insofar as the corporation's legal existence is concerned. Hallis put it more bluntly by stating that the existence of the individuals making up a corporation is merely "a political fact to which the courts must show a polite indifference."[18]

Proponents of the fiction theory do not consider the corporation as a distinct legal person.[19] They maintain that ascribing to the corporation the attribute of separate existence contradicts the proposition that the aggregate is only the sum of its parts.

The corporation as an organic creation

In contrast, adherents of the organic theory of the corporation insist that the individual is not the only type of juridical person.[20] Personalities other than the flesh-and-blood individual are also capable of acting in a juridical capacity. The German jurist Otto von Gierke, the forerunner of the organic or real entity theory, asserted that the corporation and other groups were "real."[21] Corporations, like individuals, were naturally occurring entities in societies that exist on their own. "The corporation rests upon a substratum of physical persons, but it is not identical with them, for out of the association of the individuals the new personality arises, having a distinctive sphere of existence and a will of its own."[22]

---

[16] *Id.*; Hallis explains Savigny's idea on the corporation's property-holding capacity by stating that this property-capacity is all that the juristic person presents in private law and all other attributes of the corporation fall beyond the scope of private law.

[17] HALLIS, *supra* note 4, at 9.

[18] *Id.*

[19] FREUND, *supra* note 1, at 10.

[20] *Id.* at 13.

[21] Schane, *supra* note 2, at 566-67.

[22] *Id.*

Adherents of the organic theory also offer the rather metaphysical proposition that the law does not create the corporation, but rather, finding it in existence, brings such entity to life by investing it with a legal capacity.[23] In other words, corporations were extra-legal. They existed regardless of the law. Savigny, an ardent follower of Roman law that stressed universality and individuality, insisted that corporations are not like individual persons who have minds and volition. But Gierke, a disciple of Professor Georg Beseler who was a recognized leader of the Germanist branch of the historical school,[24] countered that corporations, like states, had natural, pre-existing attributes.[25] It is inevitable for the state to recognize the corporation's existence.[26]

While the fiction theory dominated in the nineteenth century in America, the organic theory later emerged as the most palatable of the two theories for American corporations.[27] As a real and separate person under the organic conception, the corporation was a free entity and bearer of important rights and duties, in contrast to the highly restricted version of the fiction theory. As a separate juridical entity, the corporation's liabilities could not attach to the individual incorporators and shareholders, which was a very convenient set-up that coincided with the growth and success of private enterprises in America beginning in the latter half of the nineteenth century.[28]

B. Natural Entity Theory vs. Artificial Entity Theory[29]

The discussion concerning the natural entity/artificial entity dichotomy focused on the corporation's justification for its existence. On one hand, the corporation was viewed as *artificial* in the sense that it owed its existence to the law of the state. On the other hand, proponents of the *natural entity* conception asserted that the corporation was the product of the private initiative of individual incorporators rather than state power.

---

[23] *Id.*

[24] Germanic law was communal and national, in contrast to Roman law which was universalistic and individualistic. Gierke considered fellowships central to the German spirit and society [Ron Harris, *The Transplantation of the Legal Discourse on Corporate Personality Theories: From German Codification to British Political Pluralism and American Big Business*, 63 WASH. & LEE L. REV. 1421, 1430 (2006)].

[25] *Id.*

[26] For a more historical comparison of Savigny and Gierke's theories, *see* Harris, *supra* note 24.

[27] Schane, *supra* note 2, at 568-69.

[28] *Id.*

[29] This section of the paper draws heavily on the work of Millon, *supra* note 4.

The corporation as an artificial creation

The understanding that the corporation was a product of state power rather than private initiative was exemplified in the early practice of requiring a specific legislative act for the incorporation of every corporation in the United States.[30] While the act of special chartering for every instance of incorporation was gradually replaced with general incorporation statutes, the fact that the creation of the corporation was made possible only through state action and state-granted charters further supported the thinking that corporations were artificial creations of the state.[31]

The nineteenth century saw the emergence of the notion that the state-granted privilege of incorporation is not simply for the private benefit of shareholders, but also to promote the welfare of the community. The main basis for such thinking was the business corporation's value as a "socially useful instrument of economic growth."[32] Public interest and public policy objectives were thus gradually reflected in legislations and regulations on corporations.

At a time when incorporation was completed solely through special charters granted by the legislature, public concern about equal opportunity and balance of economic power arose.[33] General incorporation laws later quelled such concerns as legislative discretion was eliminated. The monopolistic tendencies of certain firms were also avoided as general incorporation statutes paved the way for the incorporation of more enterprises.[34] In some states in America, regulations contained specific limitations aimed at preventing the concentration of harmful economic power such as restrictions on the scope of corporate activity.[35] Federal states likewise utilized corporate law to protect the interests of constituencies exposed to abusive corporate power. Thus, special provisions were designed for firms in the banking, insurance and transportation industry.[36] The courts likewise contributed to this growing body of public interest or general welfare regime in corporate law. The *ultra vires* doctrine clipped corporate powers whenever corporate acts that go beyond the corporation's charter were carried out.[37]

---

[30] Millon, *supra* note 4, at 206.
[31] *Id.*
[32] *Id.*
[33] *Id.* at 207.
[34] *Id.* at 208.
[35] *Id.*
[36] *Id.* at 210.
[37] *Id.* at 209.

Millon noted that the limitations on corporate activity and the *ultra vires* doctrine was a reflection of the continued distrust of corporate power and the desire to limit corporate ability to amass socially harmful economic power.[38] The mounting disdain for perilous corporate power provided the impetus for extensive regulation of corporate activity. The idea that the corporation was an artificial creation of state power thus provided the backbone for a regime within corporate law meant to regulate corporate activity for public welfare.[39]

The corporation as a naturally occurring entity

The natural entity theory rejected the idea that the corporation was an artificial entity completely dependent on state authority for its existence and privileges. Under the natural entity argument, corporations were viewed as natural products of individual initiative and enjoy powers conferred by individual incorporators and shareholders.[40]

Several developments in the United States during the early twentieth century provided support for the view that corporations were products of private initiative, rather than artificial creatures brought to life through state power. The gradual erosion of state power and regulation concerning incorporation and corporate activity facilitated fresh approaches concerning the relation of the state and corporations. State regulation and incorporation were viewed as mere formalities. State legislatures in the United States began to abolish significant corporate restrictions.[41] The *ultra vires* doctrine was also fading out of the picture as most jurisdictions in America accepted the view that a corporation could not invoke *ultra vires* in actions where the subject contract is wholly or partially executed.[42] The notion that corporations can only carry out their activity and exercise their powers within the borders of the state that chartered them was likewise rejected in several cases.[43] Regulation of the market through corporate law became less significant as competition in the market took on a more prominent role in determining market structures. The unprecedented growth of corporations reinforced the idea that corporations are not mere state creations but rather products of market competition and private entrepreneurial initiatives.[44]

---

[38] *Id.*
[39] *Id.* at 211.
[40] *Id.*
[41] *Id.* at 211-12.
[42] *Id.* at 212.
[43] *See* Southern Ry. v. Greene, 216 U.S. 400 (1910); Ludwig v. Western Union Tel. Co., 216 U.S. 146 (1910); Western Union Tel. Co. v. Kansas, 216 U.S. 1 (1910); Pullman Co. v. Kansas, 216 U.S. 56 (1910).
[44] Millon, *supra* note 4, at 213.

The twentieth century was thus replete with developments reflecting the shift from a regulatory notion of corporate activity to a private law perspective. Corporate activities came to be viewed as private affairs like ordinary individual commercial activities and thus free from legal regulations designed to promote public interest and protect general welfare.[45]

C. Property Theory v. Social Entity Theory

In a lecture given on 13 April 1992, Professor and Chancellor William T. Allen of the Delaware Court of Chancery[46] referred to the property conception and social entity conception as the two major conceptualizations of the nature of the business corporation over the course of the twentieth century.[47] Professor Allen summarized the hitherto centuries old debate on the legal nature of the corporation with his property-social entity dichotomy.

The corporation as private property

Under the property theory, the corporation is considered as the private property of its shareholders.[48] The function of directors, as agents of owners of the corporation, was to further the financial interests of the shareholders. The corporation exists for the creation of wealth and nothing else. Allen called this notion of the corporation the property conception because under this theory the corporation is seen as the property of its shareholders.

Beginning in the mid-nineteenth century, the legal landscape and prevailing state of affairs reflected only a weak sense of a distinctive, artificial corporate entity.[49] The focus instead was on the shareholders as individuals.[50] The corporations were viewed as similar to limited partnerships, where each member had a vote over matters concerning the corporate body's business and interests.[51] Significantly, and consistent with the prevailing idea at the time that the corporation was not really a distinctive entity, shareholders during this period only enjoyed a watered

---

[45] *Id.*
[46] A non-jury trial court established in 1792 and is considered the United States' only specialized court of corporation law.
[47] Allen, *supra* note 7, at 264.
[48] *Id.* at 264-65.
[49] *Id.* at 266.
[50] *Id.*
[51] *Id.*

down version of the limited liability protection[52]—unlike today where the legal independence of the corporation from the shareholders forming it is plain and clear: shareholders ordinarily are only at risk of losing their investment in the event of corporate failure and will not be further liable for debts owing to corporate creditors.

In 1919, the Michigan Supreme Court seemingly formalized the prevailing conception at the time that the corporation is a property of the shareholders. In *Dodge v. Ford Motor Co.*,[53] Ford Motor Company, through the leadership of Henry Ford, decided to suspend further dividend payments and retain $58 million in profits for business expansion and production of cheaper products. The Dodge brothers, as shareholders, sued the company. The brothers asserted that the shareholders owned the company and were entitled to force the directors to pay out more dividends. On the other hand, Ford, who controlled the board of directors, took the position that the purpose of the corporation was to produce cheap goods and provide jobs at good wages, and only incidentally to generate wealth. The Michigan Supreme Court disagreed with Ford:

> A business corporation is organized and carried on primarily for the profit of the stockholders. The powers of the directors are to be employed for that end. The discretion of directors is to be exercised in the choice of means to attain that end, and does not extend to a change in the end itself, to the reduction of profits, or to the nondistribution of profits among stockholders in order to devote them to other purposes.[54]

The corporation, albeit an artificial entity, was thus in reality the shareholders in a "special form."[55] Shareholders own the corporation. The assets of the corporation were equitably the assets of the shareholder-owners, and the directors, agents of the owners, were bound to act on behalf of shareholder interests.[56] The directors' primary duty was to maximize corporate earnings for the benefit of the shareholders. The main corporate agenda was the creation of more wealth regardless of who benefits.[57] Public and social policy questions were left to be dealt with by the state's taxing and regulatory power.[58] Noble pursuits as job creation, educational grants and

---

[52] Some state laws on corporations in the U.S. at the time imposed liability on shareholders in various instances and drastic corporate actions like merger or sale of all assets required unanimous shareholder approval (Allen, *supra* note 7, at 267).
[53] 170 N.W. 668 (Mich. 1919).
[54] *Id.* at 684.
[55] Allen, *supra* note 7, at 267.
[56] *Id.*
[57] *Id.* at 270.
[58] *Id.* at 269.

social interaction were regarded as mere by-products of the pursuit of wealth for shareholder benefit, but are nonetheless non-profit maximizing concerns that must not be undertaken using shareholders' money.[59]

The corporation as a social entity

Towards the end of the nineteenth century, however, an alternative conception of the corporation, captured in Henry Ford's unsuccessful argument in *Dodge v. Ford Motor Co.,*[60] was slowly emerging. The exceptional rise of business enterprises during this period required the infusion of massive funding from all possible sources. Dispersed stock ownership became the ideal solution for the huge capital investments required by corporations.[61] Securities markets in various jurisdictions were established and flourished. Thus, shareholders were seen more as mere investors and little by little became less significant in the corporate structure; while emerging large corporations began to stand out as "independent" and significant entities.[62] Professor Horwitz commented that "[b]y the time of the First World War, it was common for legal writers to observe that 'the modern stockholder is a negligible factor in the management of a corporation'."[63] Another commentator quipped, "stockholders today are primarily investors and not proprietors."[64]

Based on the social entity theory, the corporation is not an isolated entity that exists for its own benefit alone. Instead, the corporation has a social purpose.[65] While the shareholders are entitled to a fair rate of return on their investments, the corporation also owes non-shareholder constituents certain obligations including the production of products that will satisfy consumer needs, providing employment opportunities and making meaningful contributions to the community.[66]Allen points to several "constituency statutes" that further legitimated the entity conception in the late 1980s.[67] For instance, the Indiana and Pennsylvania constituency statutes, explicitly allowed corporate directors not to give preference to any particular interest, and therefore abandoning the conventional thinking that

[59] *Id.*
[60] 170 N.W. 668 (Mich. 1919).
[61] Allen, *supra* note 7, at 270.
[62] *Id.*
[63] *See supra* note 29.
[64] *Id.*
[65] *Id.* at 271.
[66] *Id.*
[67] Constituency or stakeholder statutes will be discussed more extensively later in this paper.

promoting the financial interests of shareholders is the primary duty of a director.[68]

The property-entity debate focused on the purpose of the corporation. Under the property conception, a corporate director's chief duty is to harness company resources for profit maximization. Shareholders own the company. As owners, they are entitled to the full benefits of their investments. The directors' job is to act in good faith in the interests of the company and the shareholders. In contrast, the social entity theory emphasizes the multi-faceted purpose of the corporation's existence. Corporate purpose is not limited to advancing the financial interests of shareholders. It includes the promotion of the general welfare. Directors owe a duty to both shareholders as well as non-shareholders affected by the corporation.

II. FIDUCIARY DUTIES OF CORPORATE MANAGERS

Professor Allen once observed that "The question, what is a corporation, has a correlative question: For whose benefit are those in control of a corporation supposed to act?"[69] To be sure, business corporations are private undertakings established mainly for one reason: maximization of wealth invested in the corporate enterprise. The individuals running the business are thus expected to devote company resources for the benefit of its owners, the shareholders. The responsibility of managing and growing shareholder investments largely fall on the shoulders of the company directors. Thus, most jurisdictions provide in their company laws or corporation statutes that the corporation and its affairs shall be managed under the direction of the board of directors.

The broad management powers granted to corporate managers place them in a unique position within the corporate structure. Because of this unique function and management responsibility, they owe a great deal of fidelity and loyalty to the company. Directors are thus fiduciaries bound to act in good faith in the interest of the company. Underlying such fiduciary duties is the primacy of shareholder interests. This traditional reality, however, has since evolved. Many corporations and corporate managers now recognize non-shareholder interests in the operation of their

[68] Allen, *supra* note 7, at 276. In addition, certain jurisdictions have traditionally taken into account company employees in their company laws. For instance, section 309 of the Companies Act 1985 of the United Kingdom required that directors of a company, in the performance of their functions, must also regard the interests of the company's employees in general. Section 172 of the UK's new Companies Act 2006 mentioned not only employees, but also the suppliers, customers, the environment and the community.

[69] Allen, *supra* note 7, at 264.

businesses. What follows is a discussion on the conventional duties of corporate directors and managers as trustees for the shareholders, as well as the trend towards citizenship or social responsibilities in the field of corporate governance.

A. Corporate Managers as Caretakers of the Corporation

i. Primacy of Shareholders

The basic legal duties of directors and corporate managers are to act in good faith in the interests of the company, and to exercise care and skill in managing the corporation. Corporate managers' primary goal is to maximize shareholder wealth. Professor E. Merrick Dodd's illustration in his influential work entitled *"For Whom Are Corporate Managers Trustees?"*[70] perhaps best summarizes this corporate law truism:

> An individual who carries on business for himself necessarily enters into business relations with a large number of persons who become either his customers or his creditors. **Under a legal system based on private ownership and freedom of contract, he has no duty to conduct his business to any extent for the benefit of such persons; he conducts it solely for his own private gain and owes to those with whom he deals only the duty of carrying out such bargains as he may make with them.**
>
> x x x
>
> Substitute several owners for one and the picture is scarcely altered, except that insofar as the owners take part in the conduct of the enterprise, there is a fiduciary relation between owner and owner, as well as between employee and owner. **Incorporate the enterprise, making the owners stockholders and some of them or persons selected by them directors, and—if we adopt the widely prevalent theory that the corporate entity is a fiction—our picture is substantially unchanged. The business is still a private enterprise existing for the profit of its owners, who are now the stockholders.** Its customers and creditors have contract rights, nominally against the corporation but in reality against the stockholders, whose liability is limited to the assets used in the business. The directors and other agents are fiduciaries carrying on the business in the sole interest of the stockholders.[71]

---

[70] 45 HARV. L. REV. 1145 (1932).
[71] *Id.* at 1145-46; emphasis supplied; internal citations omitted.

The relationship between the shareholders and the people responsible for running the corporation—officers, directors and managers, or simply "corporate managers"—is popularly described as "fiduciary." In particular, directors have been held by the courts to occupy a fiduciary position towards the company.[72] Every action and decision of a corporate manager must be made in the interest of shareholders.[73] Because of this peculiar nature of the director's job, he is said to possess fiduciary duties owed to the company shareholders.

A fiduciary is expected to act as his principal's alter ego.[74] In the same manner, a company director or manager acts as the shareholders' alter ego, managing the corporation and conducting the business in a manner consistent with the latter's interests and in line with the objective of maximizing company profit. While huge gains, much less any profit, are not always expected in every investment, corporate managers are expected to manage wisely the funds invested by shareholders in the company.

ii. The Duty to Act In the Company's Interests

The company law of almost every jurisdiction in the world contains provisions imposing upon the director the duty to conduct business in good faith in the interests of the company. The Companies Act of Austria requires directors, in carrying out their duties, to act with the care of a diligent and prudent businessman.[75] In England and Wales, the fiduciary position of the director implies obligations of trust and confidence between him and the company.[76] As such, a director is expected to act honestly and in good faith in the company's interests.[77] Section 174 of the UK Companies Act of 2006 states that a director of a company must exercise reasonable care, skill and diligence "that would be exercised by a reasonably diligent person with the general knowledge, skill and experience that may reasonably be expected of a person carrying out the functions carried out by the director in relation to the company", and "the general knowledge, skill and experience that the director has." Section 172 of the Act further provides that a director "must act in the way he considers, in good faith, would be most likely to promote the success of the company for the benefit of its members as a whole." The director's duty to promote the success of the company, however, does not

---

[72] Regal Hastings Limited v. Gulliver, 1 All ER 378 (1942).
[73] *See generally* Victor Brudney, *Contract and Fiduciary Duty in Corporate Law*, 38 B.C.L. REV. 595 (1997).
[74] *Id.* at 601-02.
[75] DIRECTORS' DUTIES AND LIABILITIES 2 (Paul Omar ed. 2000).
[76] *Id.* at 24.
[77] *Id.*

require him to do more than act in good faith and to exercise reasonable care, skill and diligence.[78]

The French Civil Code and its laws for general partnerships and limited liability companies mandate that all of the acts of directors must comply with the interests of the company, which encompasses the interests of both the majority and minority shareholders.[79] Directors who act against the interests of the company may be removed, replaced with provisional administrators and held liable for damages.[80] In Germany, Section 1, Article 93 of the "Aktiengesetz" of 6 September 1965 ("AktG") requires directors to carry out their duties with the care to be expected of a "proper and conscientious director."[81] Such duty of care is principally owed to the company and hence only the latter may claim damages for breach of that duty. However, where directors act in a grossly negligent manner, affected third parties like creditors may also bring a claim for damages against directors.[82]

Article 355 of Japan's Corporation Law provides that the "director shall perform his or her duties faithfully for the benefit of the *kabushiki-kaisha* (business corporation) in compliance with laws and ordinances, the articles of incorporation and resolutions of the general meeting of the shareholders."[83] Under Italian law, a director is obliged to perform his duty in accordance with the standard of diligence to be expected from a person to whom the management of property belonging to others has been entrusted, taking into consideration the experience, knowledge and professionalism required of a company director.[84]

Dutch laws require directors to manage the company properly, which duty includes the protection of capital and cooperation with legal bodies.[85] The Commercial Companies Code of Portugal provides that a director must act with the skill and care of a diligent manager in the interests of the company bearing in mind the interests of the shareholders and, interestingly, the employees.[86]

---

[78] Charles Mayo, *Directors' Duties*, *in* THE BUSINESS CASE FOR CORPORATE GOVERNANCE 126 (Ken Rushton ed., Cambridge University Press, 2008).
[79] DIRECTORS' DUTIES AND LIABILITIES, *supra* note 75, at 40.
[80] *Id.*
[81] The AktG is the law governing joint stock companies in Germany.
[82] DIRECTORS' DUTIES AND LIABILITIES, *supra* note 75, at 56-57.
[83] Law No. 86, Jul. 26, 2005.
[84] DIRECTORS' DUTIES AND LIABILITIES, *supra* note 75, at 72-73.
[85] *Id.* at 82.
[86] *Id.* at 95.

In Spain, directors are required to carry out their duties "with the diligence that may be reasonably expected from a responsible businessman and from a trustworthy representative of the company".[87] The Swiss Federal Code of Obligations requires directors to perform their duties with diligence, be loyal to and act in the interests of the company to the best of their ability.[88] Every director is expected to act in a manner that may reasonably be expected of an ordinary person in the same situation.[89]

In the United States, each state typically has its own corporation law. But a majority of *Fortune* 500 corporations are incorporated in Delaware[90] as most corporations consider that state's corporate law and specialized courts attractive; hence, that state's reputation as a corporate haven. "Delaware director fiduciary duties are derived from a statutory obligation to manage the business and affairs of the corporation. Thus, Delaware law creates an obligation for directors to manage the business affairs of a corporation on behalf of the shareholders."[91] The duty of care is also set out in the Revised Model Business Corporation Act[92] sections 8.30 and 8.31. Under section 8.30 of the Revised Model Business Corporation Act, a director must discharge his duties "(1) in good faith; and (2) in a manner he reasonably believes to be in the best interests of the corporation."

In addition, the basic relationship between the company and its directors in the United States, true to its common law roots, has been established by common law rather than statute. The test laid down in the leading case of *Selheimer v. Manganese Corp. of America*[93] is widely quoted: directors must perform their duties with that degree of diligence, care and skill "which ordinarily prudent men would exercise under similar circumstances in their personal business affairs." The broad language of this test has been rarely followed, however, in actual cases. Instead, different rules and tests have been formulated and applied depending on the facts of the case. In *Unocal Corporation v. Mesa Petroleum Co.*,[94] where the Delaware Supreme Court upheld the use of a self-tender to resist a hostile tender offer from a minority shareholder, an "enhanced business judgment rule" was

---

[87] *Id.* at 119.
[88] *Id.* at 131.
[89] *Id.* at 132.
[90] Constance Bagley, *Shareholder Primacy Is a Choice, Not a Legal Mandate*, *in* THE ACCOUNTABLE CORPORATION VOL. 1 CORPORATE GOVERNANCE 86 (Marc Epstein and Kirk Hanson ed. 2006).
[91] Carter Bishop, *The Deontological Significance of Nonprofit Corporate Governance Standards: A Fiduciary Duty of Care Without a Remedy*, 57 CATH. U.L. REV. 701, 728 (2008).
[92] *The Model Business Corporation Act, available at* http://www.abanet.org/buslaw/library/onlinepublications/mbca2002.pdf
[93] 224 A.2d 634 (Pa. 1966).
[94] 493 A. 2d 946 (Del. 1985).

applied.[95] This enhanced rule sets out that the board of directors must show that its action was performed in good faith and after reasonable investigation, and that any defensive action by the board must be reasonable vis-à-vis the threat posed.[96] Under this reasonability requirement, the board was required to examine how the perceived threat will affect the corporation, including the impact on non-shareholder constituencies.[97]

The rule in *Unocal* was later modified in the case of *Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc.*[98] In this case, the management of Revlon resisted attempts to takeover the company by granting another company a lock-up option and a no-shop provision.[99] Under the *Revlon* rule, while non-shareholder interests may also be considered in responding to a takeover threat, board actions taken to protect non-shareholder interests must also benefit shareholders.[100] Wai Shun Wilson Leung pointed out that the two later cases of *Paramount Communications, Inc. v. Time, Inc.*[101] and *Paramount Communications, Inc. v. QVC Network Inc.*[102] were no different from the rulings in *Unocal* and *Revlon*: *Time* and *QVC* also upheld the shareholder primacy doctrine.[103] Under these four Delaware cases, directors may generally act only for the benefit of shareholders.[104] Thus, Leung adds, when shareholder and non-shareholder interests conflict, board action must prioritize shareholder interests.[105]

What is relevant in these four Delaware cases is the primacy of shareholder interests. Corporate managers carry out their fiduciary duties and run the affairs of the firm, first and foremost, to benefit shareholders.

B. Corporate Managers with Social Responsibilities

Donations for charitable and educational purposes were the earliest form of corporate social activity in the United States.[106] Federal tax legislation in 1935 allowing companies to deduct from taxable income up to 5 percent on account of corporate contributions spurred the growth of

---

[95] Wai Shun Wilson Leung, *The Inadequacy of Shareholder Primacy: A Proposed Corporate Regime that Recognizes Non-Shareholder Interests*, 30 COLUM. J. L. & SOC. PROBS. 587, 610 (1997).
[96] *Id.*
[97] *Id.*
[98] 506 A.2d 173 (Del. 1986).
[99] *Id.* at 175.
[100] Leung, *supra* note 95, at 611.
[101] 571 A.2d 1140 (Del. 1990).
[102] 637 A.2d 34 (Del. 1994).
[103] Leung, *supra* note 95, at 612.
[104] *Id.*
[105] *Id.* at 613.
[106] NEIL JACOBY, CORPORATE POWER AND SOCIAL RESPONSIBILITY 198 (1973).

corporate giving.[107] The case of *A.P. Smith Manufacturing Co. v. Barlow et al.*[108] later supported this legislation when the New Jersey court in that case held that corporate gifts were desirable despite management's failure to demonstrate any direct benefit to the donor company.[109] Despite these developments, corporate social responsibility was not universally accepted.

i. Profit Maximization: Friedman's Idea of "Corporate Social Responsibility"

Professor Milton Friedman's famous 1970 commentary in the New York Times Magazine entitled *"The Social Responsibility of Business Is to Increase Its Profits"*[110]placed the nascent notion of corporate social responsibility at the forefront of the debate on corporate management theory. Professor Friedman was a renowned free-market economist and staunch advocate of shareholder primacy in the theory of the corporation.

Friedman rejected the idea that the scope of corporate managerial responsibilities included non-shareholder parties and interests.[111] To Friedman's mind, corporate managers have the obligation of protecting and promoting the interests of the owner-shareholders. These interests are purely financial and, thus, corporate managers must preoccupy themselves only with profit-maximization work.[112] Friedman acknowledged that contractual arrangements between the company, employees, customers, suppliers and the local government underlie corporate business.[113] But, according to him, these contractual relationships benefit everyone. Each party to the contractual arrangement receive what is due to him: return on investments for shareholders, products and services to customers, and wages for employees, among others.[114]

Friedman asserted that an inanimate entity like "business" cannot have responsibilities. More importantly for Friedman, corporate managers are employed by shareholders and thus their responsibilities must only be to the owners of the corporation. This responsibility owed to the owners of the business is, Friedman insisted, to carry on the business pursuant to the desires of the shareholders, "which generally will be to make as much money

---

[107] *Id.*
[108] 98 A. 2d 581 (N.J. 1953).
[109] JACOBY, *supra* note 106, at 198.
[110] Friedman, s*upra* note 6.
[111] Tara Radin, *700 Families to Feed: The Challenge of Corporate Citizenship*, 36 VAND. J. TRANSNAT'L L. 619, 636 (2003).
[112] *Id.*
[113] *Id.* at 636-37.
[114] *Id.* at 637.

as possible while conforming to the basic rules of the society, both those embodied in law and those embodied in ethical custom."[115]

Friedman believed that social responsibilities have no place in company business. Such activities eat into company profits and are not consistent with the corporate manager's responsibility to shareholders. Thus, for him, a corporate activity for social responsibility is a waste of shareholders' money. Corporate managers funding such activities are unjustifiably spending other people's money.[116] Friedman argued that sometimes those who implement social responsibility projects merely do so to pursue legitimate business decisions. Social responsibility is only used as a "cloak" or mere "window dressing."[117]Friedman concluded his now famous article with an emphatic reiteration of his shareholder primacy argument: "there is one and only one social responsibility of business–to use it resources and engage in activities designed to increase its profits so long as it stays within the rules of the game, which is to say, engages in open and free competition without deception or fraud."[118]

However, as pointed out by Professor Tara Radin, Friedman's fervent defense of shareholder primacy was not sufficient to hold back efforts in the academe and in practice in favor of corporate social responsibility.[119] Radin stated that part of the reason for this is Friedman's failure to adequately explain the underlying stakeholder relationships in the business structure and the need to recognize and manage these relationships for sustainable success.[120] Professor Neil H. Jacoby also remarked that:

> Unfortunately, Friedman failed to add that social involvement is consistent with self-interest, and that corporate managers need a sophisticated understanding of business-societal relationships in order to operate on that principle. Those economists and businessmen who assert that the purpose of business is 'business' and not social 'do-gooding' are as much in error as the radicals of the New Left who would compel business to concentrate on social improvement.[121]

---

[115] *Id.*
[116] *Id.*
[117] *Id.* at 637-38.
[118] Friedman, s*upra* note 6, at 33.
[119] Radin, *supra* note 111, at 638.
[120] *Id.*
[121] JACOBY, *supra* note 106, at 197-98.

ii. Stakeholder Theory and Non-Shareholder Interests

Stakeholder theory is an approach used to recognize the social responsibilities of a corporation on top of its profit-making objectives. Stakeholders refer to "people whose financial well-being is tied to the corporation's success, such as employees, suppliers, charities, and communities."[122] In the 1970s and 1980s, legal thinkers, mainly in Germany, engaged in a "wider discussion of the organization of a business enterprise in which stakeholders participate in various activities."[123] What became clear from this debate was that workers were considered as the principal stakeholders, but the focus of the discussion soon turned to "integrating a wider spectrum of 'interests' (the so called "*Unternehmensrecht*") into the legal organization of corporations."[124]

Professor Radin once explained in much detail that stakeholder management (or the notion that there are other entities that have "stakes" in company affairs) is not inconsistent with the law. She pointed out that stakeholder thinking "signifies the recognition that the corporation has responsibilities to people or entities in addition to shareholders."[125] Radin acknowledged R. Edward Freeman's contribution to the development of stakeholder theory with the release of the latter's book entitled *Strategic Management: A Stakeholder Approach* in 1984.[126] Freeman challenged the theory of shareholder primacy and argued that shareholder interests should be seen as only one element of an expansive web of stakeholder interests. Companies owe both shareholders and other stakeholders equal responsibilities, Freeman argued.[127] Freeman developed the diagram below to illustrate the stakeholders in a typical large corporation:[128]

---

[122] Kathleen Hale, *Note: Corporate Law and Stakeholders: Moving Beyond Stakeholder Statutes*, 45 ARIZ. L. REV. 823, 825 (2003).

[123] Peter Nobel, *Social Responsibility of Corporations*, 84 CORNELL L. REV. 1255, 1259 (1999).

[124] *Id.* Professor Nobel noted that this debate resulted only in the consolidation of workers' co-determination rights.

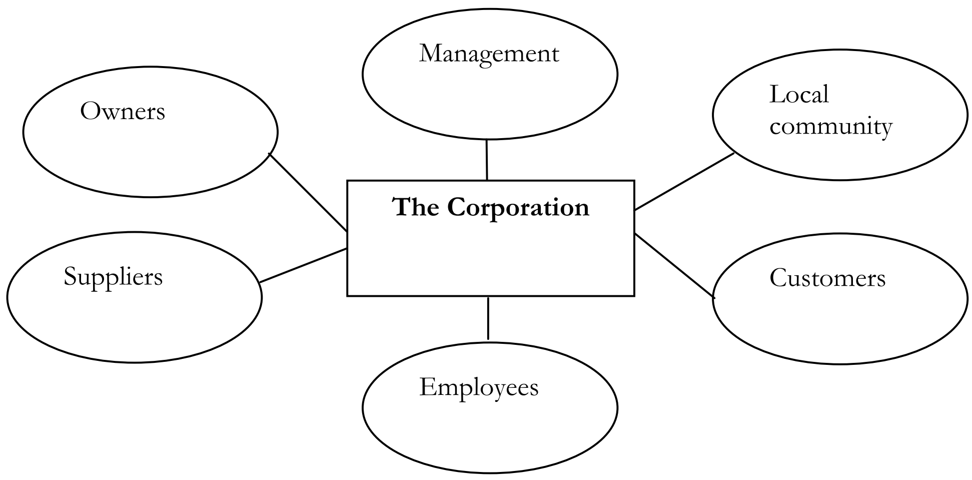
[125] Radin, *supra* note 111, at 639.

[126] *Id.*

[127] *Id.*

[128] William Evan and R. Edward Freeman, *A Stakeholder Theory of the Modern Corporation: Kantian Capitalism*, in ETHICAL THEORY AND BUSINESS 101 (Tom Beauchamp and Norman Bowie ed., 3rd ed., 1988).

Figure 1.1 Stakeholders



Under Freeman's model, every stakeholder is important; the business corporation cannot exist without the stakeholders as each part of the whole is necessary. All stakeholders are necessary for the survival and success of the firm.[129]

Radin asserted that corporate managers, by law, also owe the employees, the consumers and the environment, among others, a responsibility. She stated that some laws prioritize non-shareholder interests and show that stockholder interests are not inherently the most important in corporate management.[130] Professor Nobel likewise observed that "a consensus seems to exist that a corporation must consider the interests of all stakeholders (and not simply shareholders)" and "under a long-term view, even profit maximizing might demand that a corporation consider an optimal combination of all contributing factors."[131] And, as will be shown later, international organizations also recognize non-shareholder constituencies' interests.[132]

Stakeholder theory's expansive approach is thus able to address both the concern for shareholder benefit and the fact that multiple relationships involving non-shareholder parties support and affect the business structure. Shareholders are important, but they are not the only ones important. As Professor Radin noted, evidence suggests that non-shareholder entities have

[129] *Id.* at 101-02.
[130] Radin, *supra* note 111, at 641.
[131] Nobel, *supra* note 123, at 1260.
[132] *See generally* the April 1998 OECD advisory group's report on corporate governance.

legitimate claims because of their relationship with the corporation.[133] For instance, company workers invest in the company through labor, commitment and loyalty.[134]

As can be gleaned from the earlier discussions in this paper, the conventional notion that the corporate manager is a fiduciary bound to protect and promote the financial interest of shareholders has made it difficult to consider non-shareholder interests in the management of the business. But Radin pointed out that fiduciary law does not in fact exclude the accommodation of non-shareholder interests, as she argued that, on the contrary, the idea of fiduciary duty was founded upon concern for managerial indiscretion.[135] It was developed "to prevent managers from self-dealing, more than in an effort to distinguish between stakeholders and preclude attention to non-shareholder considerations."[136]

Radin further maintains that stakeholder relationships can co-exist with fiduciary relationships.[137] Corporate managers can pay attention to the interests of non-shareholder constituencies while carrying out their primary duty of looking after the financial welfare of shareholders. Moreover, it is fair to state that stakeholder relationships must be taken into account in order to satisfy fiduciary obligations and profit-maximizing duties owed to shareholders. "Paying attention only to shareholders limits the ability of managers to counter relationships that threaten (the company's) performance, and to recognize and develop relationships that can protect the firm over the long-term."[138] The UK Company Law Review steering group, in a report, likewise concluded that "the present scheme of the law fails adequately to recognize that businesses normally best generate wealth where…managers…recognize the wider interests of the community in their activities."[139]

iii. Corporate Citizenship Theory

Under the corporate citizenship theory, corporations are seen as members of society with similar rights and duties like other citizens.[140] The corporation's social responsibility is founded upon its existence in civil

---

[133] Radin, *supra* note 111, at 640-41.
[134] *Id.* at 641.
[135] *Id.* at 649.
[136] *Id.*
[137] *Id.*
[138] *Id.* at 655; internal citation omitted.
[139] Mayo, *supra* note 78, at 121.
[140] MARVIN BROWN, CORPORATE INTEGRITY: RETHINKING ORGANIZATIONAL ETHICS AND LEADERSHIP 20 (2008).

society.[141] Professor Peter Nobel explains that corporations, in a sense, are "social persons" as corporate law's history suggests that the creation of a separate corporate legal personality has always been linked to the achievement of social goals.[142]

Radin has this to say on corporate citizenship:

> Citizenship provides the vehicle for translating stakeholder responsibilities for managers. As a citizen, an individual receives benefits and acquires certain responsibilities. Business enterprises, as citizens, receive benefits such as tax breaks and constitutionally-protected freedoms. In addition, they receive protection from harm, as individuals do, through local fire and police protection agencies. In return, business enterprises have the same sorts of responsibilities as individuals, such as treating others with respect and to acting responsively. What the notion of citizenship offers stakeholder thinking is a community-based conception of reciprocity. In other words, while stakeholder thinking suggests that firms should pay attention to stakeholders because they affect or are affected by the firm's operations, citizenship more broadly indicates that, even if the effects are not clear, responsibilities to stakeholders also exist as a result of the membership of the firm in a community in which others are also citizens (with similar benefits and responsibilities).[143]

Based on Radin's analysis, the concept of corporate citizenship offers a more complete approach than stakeholder thinking in explaining the social responsibility of corporations in the communities in which they operate. While stakeholder theory may, in a sense, be limited in that it only draws attention to the fact that corporate existence rests on a bedrock of indispensible stakeholder relationships, corporate citizenship theory reinforces this idea by indicating that the corporation's membership in the community implies responsibilities to the other members of the community, including the stakeholders affecting and affected by the corporation. Indeed, as the Supreme Court of New Jersey declared in *A.P. Smith Manufacturing Co. v. Barlow et al.*,[144] "modern conditions require that corporations acknowledge and discharge social as well as private responsibilities as members of the communities within which they operate."[145]

---

[141] *Id.* at 21.
[142] Nobel, *supra* note 123, at 1257.
[143] Radin, *supra* note 111, at 668; internal citations omitted.
[144] *Supra* note 108.
[145] *Id.* at 586.

iv. The UK's Enlightened Shareholder Value Approach

Finally, the United Kingdom's approach to corporate management deserves attention in this section especially with the passage of its new company law. The United Kingdom's Companies Act 2006 received Royal Assent on 8 November 2006 and replaced existing company legislation,[146] including the Companies Act 1985. The Act codified existing common law principles, such as those relating to directors' duties.

The Act, as well as its predecessor the Companies Act 1985, requires that directors, in the performance of their functions, must also give regard to the interests of the company's employees.[147] Section 172 of the UK Companies Act 2006 specifically provides:

> A director of a company must act in the way he considers, in good faith, would be most likely to promote the success of the company for the benefit of its members as a whole, and in doing so have regard (amongst other matters) to:
>
> (a) the likely consequences of any decision in the long term,
> (b) the interests of the company's employees,
> (c) the need to foster the company's business relationships with suppliers, customers and others,
> (d) the impact of the company's operations on the community and the environment,
> (e) the desirability of the company maintaining a reputation for high standards of business conduct, and
> (f) the need to act fairly as between members of the company.

Charles Mayo observed that the United Kingdom government decided to adopt the 'enlightened shareholder value' approach because this method is "most likely to drive long-term company performance and maximise overall competitiveness and wealth and welfare for all."[148] The Company Law Review steering group preferred this concept over 'enlightened self-interest' and explained its reasons therefor as follows:

---

[146] *available at* http://www.companieshouse.gov.uk/companiesAct/companiesact.shtml (last visited May 30, 2009).
[147] Mayo, *supra* note 78, at 122.
[148] *Id.*

> We consider the most appropriate formulation of directors' duties is to give effect to the enlightened shareholder value perspective. The argument is that these duties, as currently expressed, and as interpreted in practice, often tend to lead to an undue focus on the short term and the narrow interest of members at the expense of what is in a broader and a longer-term sense the best interest of the enterprise, and thus its value to them as ultimate controllers able to realise that value.
>
> The key company law provision is for the fiduciary duties of directors. These require them honestly ('in good faith') to manage the undertaking for the benefit of the company. That benefit is defined by case law as the interest of members present and future. The duties of directors to exercise their powers for their proper purpose are also relevant. These, for example, prevent directors from using their powers to impede the exercise by members of their rights to dispose of their shares, such as by issuing new shares to allies to defeat a takeover bid.
>
> **It is in our view clear, as a matter of policy, that in many circumstances directors should adopt the broader and longer-term ('inclusive') view of their role. This is indeed now widely acknowledged.** But we do not accept that there is anything in the present law of directors' duties which requires them to take an unduly narrow or short-term view of their functions. **Indeed they are obliged honestly to take account of all the considerations which contribute to the success of the enterprise.**
>
> There is nevertheless considerable evidence that the effect of the law is not well recognised and understood. This may be in part because the relevant principles are not enacted, but have to be derived from quite extensive case law, developed over 250 years and rooted in the eighteenth century law of trusts.[149]

The steering group saw that the law concerning directors' duties is not obvious enough and even widely misunderstood, and thus deemed it necessary to explicitly set it out in the new Act.[150] For the group, the aim of the law should be to make sure that directors understood their obligation to consider the need, where appropriate, to build long-term and trusting relationships with employees, suppliers, customers and other parties, to secure the success of the business over time.[151]

---

[149] *Id.* at 121-22; emphasis supplied; internal citation omitted.
[150] *Id.* at 122.
[151] *Id.*

The enlightened shareholder value concept found in English common law and now explicitly outlined in the Companies Act 2006 shows that giving regard to non-shareholder interests in managing the affairs of the corporation is not incompatible with the profit-maximizing duties of the corporate manager, but, in fact, ensures long-term benefits for the enterprise.

III. EMERGENCE OF NON-SHAREHOLDER INTERESTS

In 1932, Herbert Hoover lost the United States presidential election to Franklin Delano Roosevelt.[152] It was widely considered that Hoover's inability to prevent the U.S. from heading towards the "Great Depression" led to his downfall. That same year, when the U.S. was grappling with the crippling effects of recession, Professor Dodd made a seemingly prophetic observation:

> [P]ublic opinion, which ultimately makes law, has made and is today making substantial strides in the direction of a view of the business corporation as an economic institution which has a social service as well as a profit-making function, that this view has already had some effect upon legal theory, and that it is likely to have a greatly increased effect upon the latter in the near future.[153]

This dual function or dual capability of the corporation—the ability to generate wealth and carry out social responsibilities—captured in the enduring words of Professor Dodd can be seen today in several forms.

A. Stakeholder Statutes

Almost all states in the United States have enacted legislation known as stakeholder statutes.[154] These laws, drafted in virtually identical

[152] www.nps.gov, *Herbert Hoover, at* http://home.nps.gov/heho/historyculture/herbert-hoover.htm (last visited Jun. 5, 2009).

[153] Dodd, *supra* note 70, at 1148.

[154] Hale, *supra* note 122, at 827. The following are constituency statutes adopted in thirty states in the U.S.: Ariz. Rev. Stat. Ann. §10-2702 (2004); Conn. Gen. Stat. §33-756 (2004); Fla. Stat. §607.0830 (2005); Ga. Code Ann. §14-2-202(b)(5) (2004); Haw. Rev. Stat. §414-221 (2004); 805 Ill. Comp. Stat. 180/15-15 (2005); Idaho Code §30-1602 (Michie 2005); Ind. Code §23-1-35-1 (Michie 2004); Iowa Code Ann. §491.101B (West 2004); Ky. Rev. Stat. Ann. §271B.12-210 (Michie 2004); La. Rev. Stat. Ann. §12:92 (West 2005); Mass. Gen. L. ch. 156-D §8.30 (West 2005); Me. Rev. State. Ann. tit. 13-C §831 (2005); Minn. Stat. §302A.251 (2004); Miss. Code Ann. §79-4-8.30 (2005); Mo. Rev. Stat. §351.347 (2005); N.J. Rev. Stat. §14-A:6-1 (West 2005); N.M. Stat. Ann. §53-11-35 (Michie 2005); N.Y. Bus. Corp. Law §717 (Consol. 2005); N.D. Cent. Code, §10-19.1-50 (2005); Nev. Rev. Stat. §78.138 (Michie 2004); Ohio Rev. Code Ann. §1702.30 (Anderson 2005); Or. Rev. Stat. §60.357 (2003); 15 Pa. Cons. Stat. §§1 715, 1716 (2004); R.I. Gen. Laws §7-5.2-8 (2005); Tenn. Code Ann. §48-103-204 (2004); Wash. Rev. Code Ann. §23B.19.010 (West 2005); Wis. Stat. §180.0827 (2004); Vt. Stat.

language,[155] allow corporate managers to consider non-shareholder interests without breaching fiduciary duties to shareholders.[156] The enactment of the early versions of these statutes was seen as "a dramatic departure from the norms of corporate law."[157] These statutes are also referred to as "nonshareholder" statutes, "constituency" statutes[158] and "other-constituency" statutes.[159]

The forerunner of stakeholder statutes was the various corporate governance statutes enacted by state legislatures in the United States during the 1980s.[160] These statutes gave legal imprimatur for corporate managers to consider the interests of non-shareholder constituencies in business-decision making.[161] To recall, the long-standing notion in corporate theory was that corporate managers' fiduciary duties required them to carry out their functions in accordance with shareholder interests. Thus, prior to the passage of the aforementioned statutes, it was not clear whether it was legally permissible for managers to give regard to non-shareholder interests.[162]

The development of the first stakeholder statutes is tied to the prevalence of hostile takeovers in the 1980s.[163] Stakeholders, or non-shareholder constituencies, suffered the most during the hostile takeovers of that time: massive layoffs; lost tax benefits, employment opportunities and other advantages for many communities; ruined customer relationships; and weakened security between creditors, suppliers and corporations.[164] Corporate managers who wanted to resist such takeover bids ran the risk of breaching their duty to maximize shareholder wealth. Thus, to resolve this legal quandary, stakeholder statutes were developed in an attempt to provide a new approach in corporate management that allowed for stakeholder consideration.[165]

The State of Pennsylvania passed the first stakeholder statute in 1983.[166] Forty other U.S. states have enacted similar statutes.[167] Notably,

---

Ann. Tit. 11A. § 8.30 (2004); and Wyo. Stat. Ann. § 17-16-830 (Michie 2005). *See* LAWRENCE MITCHELL, LAWRENCE CUNNINGHAM & JEFFREY HAAS, CORPORATE FINANCE AND GOVERNANCE 549 (3rd ed. 2006.).

[155] Radin, *supra* note 111, at 644.
[156] Hale, *supra* note 122, at 827.
[157] *Id.* at 854.
[158] *Id.* at 829.
[159] Leung, *supra* note 95, at 613.
[160] Hale, *supra* note 122, at 829.
[161] *Id.*
[162] *Id.* at 829-30.
[163] *Id.* at 831.
[164] *Id.*
[165] *Id.* at 832.
[166] *Id.* at 833.

Delaware, the acknowledged corporate haven in the United States, has not adopted any stakeholder statute.[168] However, it must be noted that Delaware case law has made it clear that directors, in carrying out their duty to manage the business in the best interests of the company, may consider the effects of their decisions on constituencies other than shareholders.[169]

The basic premise underlying stakeholder statutes was that stakeholders—like employees, customers, creditors, suppliers, and communities—also have a stake in the business. Non-shareholder constituencies have legitimate claims on the business as a result of their relationship with the company.[170] Stakeholder statutes thus paved the way for corporate managers to legally consider not only shareholder interests in business-decision making, but also the interests of non-shareholder constituencies.[171]

While these statutes were based on the same premise, the statutes enacted by the different states varied in the scope and applicability of the law. Wyoming's version of the law, for instance, employs a rather broad language and is an example of a comprehensive stakeholder statute:

> For purposes of subsection (a) of this section, a director, in determining what he reasonably believes to be in or not opposed to the best interests of the corporation, shall consider the interests of the corporation's shareholders and, in his discretion, may consider any of the following: (i) The interests of the corporation's employees, suppliers, creditors, and customers; (ii) The economy of the state and nation; (iii) The impact of any action upon the communities in or near which the corporation's facilities or operations are located; (iv) The long-term interests of the corporation and its shareholders, including the possibility that those interests may be best served by the continued independence of the corporation; and (v) Any other factors relevant to promoting and preserving public or community interests.[172]

Out of all the legislated stakeholder statutes in the United States, Connecticut's statute is the only one mandatory in nature, expressly requiring corporate managers to consider non-shareholder interests.[173] All

---

[167] *Id.*
[168] *Id.*
[169] Bagley, *supra* note 90, at 86-87.
[170] Radin, *supra* note 111, at 640-41.
[171] Hale, *supra* note 122, at 833.
[172] *Id.* at 833-34.
[173] *Id.* at 834.

other states have permissive stakeholder laws: whether or not stakeholder interests are to be considered in business-decision making is left to the discretion of corporation managers.[174] Moreover, some statutes grant the permission to consider stakeholder interests only to directors, while others extend such authority to both directors and other corporate officers.[175] The Illinois statute, for instance, provides that "the board of directors, committees of the board, individual directors and individual officers" may consider non-shareholder constituencies in discharging their respective duties.[176]

Significantly, the Pennsylvania and Indiana statutes placed non-shareholder interests at par with that of the shareholders: "The board of directors…shall not be required, in considering the best interests of the corporation or the effects of any action, to regard any corporate interest or the interests of any particular group affected by such action as a dominant or controlling interest or factor."[177]

Notably, most stakeholder statutes allow corporate managers to consider stakeholder interests in any circumstances, while the statutes in nineteen states, on the other hand, allow stakeholder consideration only during takeover situations.[178]

Stakeholder statutes thus marked a remarkable departure from conventional corporate thinking. The statutes explicitly recognized that people other than shareholders have legitimate stakes in the business and corporate conduct, and that companies therefore must take into account the interests of these stakeholders. Indeed, there has been a trend in recent years toward emphasizing stakeholder relationships.[179] However, it has been observed that stakeholder statutes alone cannot promote proper stakeholder consideration.[180] Radin asserts that "[s]takeholder thinking does not offer a formula for management."[181] Stakeholder thinking expands the areas of concern of a corporate manager, but it does not specify which stakeholder relationships should be prioritized when they conflict.[182]

---

[174] *Id.*
[175] *Id.* at 834-35.
[176] *Id.* at 835.
[177] Leung, *supra* note 95, at 615.
[178] Hale, *supra* note 122, at 836.
[179] *See generally* Jeanne Logsdon and Donna Wood, *Business Citizenship: From Domestic to Global Levels of Analysis*, 12 BUS. ETHICS Q. 155 (2002).
[180] *See generally* Hale, *supra* note 122. Hale, in her article, has proposed the adoption of "stakeholder meeting statutes" which will provide a mechanism and an opportunity for corporate managers to meet and interact with stakeholders, and thereby facilitate consideration of stakeholder interests.
[181] Radin, *supra* note 111, at 669.
[182] *Id.*

Moreover, several problems lay within the current versions of the stakeholder laws themselves:

(a) All existing statutes (with the exception of Connecticut's) are permissive.[183] Since stakeholder consideration is discretionary, this discretion may never be used;[184]

(b) The statutes are not enforceable.[185] No mechanisms exist by which failure on the part of directors to consider stakeholder interests would be remedied;[186]

(c) The statutes focus on takeovers when in fact stakeholders are also vulnerable in other situations;[187] and

(d) The statutes are vulnerable to abuse by managements planning to entrench themselves in power as some statutes give board of directors an absolute "just say no" defense to takeover bids.[188]

B. Codes of Conduct and Non-Shareholder Interests

Increasing concern for the interest of non-shareholders such as employees, customers, suppliers or business partners, creditors and the community is also manifested in corporate information materials like company profiles, annual reports, corporate websites and codes of conduct.[189]

A code of conduct refers to "any written statement of ethics, law, or policy (or some combination thereof), delineating the obligations of one or more classes of corporate employees."[190] They are also referred to as "corporate codes of behavior," "corporate codes of ethics," or "standards of a corporation."[191] These codes consist of corporate governance rules voluntarily adopted by companies, as opposed to rules imposed by law.[192] Such codes have been widely adopted by transnational corporations (TNCs) to regulate working conditions and the management of their production

[183] Leung, *supra* note 95, at 617.
[184] *Id.* at 622-23.
[185] *Id.* at 617.
[186] *Id.*
[187] *Id.* at 618.
[188] *Id.*
[189] Lisa Fairfax has observed that "corporate 'stakeholder rhetoric'…permeates corporate websites and documents from annual reports to mission statements." *See* Lisa Fairfax, *Easier Said Than Done? A Corporate Law Theory for Actualizing Social Responsibility Rhetoric*, 59 FLA. L. REV. 771, 773 (2007).
[190] *Note: The Good, The Bad, and Their Corporate Codes of Ethics: Enron, Sarbanes-Oxley, and the Problems with Legislating Good Behavior*, 116 HARV. L. REV. 2123, 2125 (2003).
[191] *Id.* at 2124.
[192] *Id.* at 2125-26.

facilities and factories.[193] The first codes of conduct were in fact developed in response to criticisms and growing problems concerning labor conditions in the factories of TNCs located in developing countries.[194] But the codes of conduct created and adopted by corporations have since evolved to specifically include express provisions or principles covering a broad category of non-shareholder constituents including the community, suppliers or business partners and even customers.

i. Development of Codes of Conduct

Corporate scandals in the 1960s, 1970s, and 1980s in the United States contributed to the development of corporate codes of behavior.[195] These corporate crises "reinforced the conclusion that corporate codes should be part of the repertoire of corporate self-governance."[196] Some companies adopted codes because of these scandals, while others did so for public relations purposes.[197]

Ans Kolk and Rob Van Tulder pointed out three events involving multinational companies that contributed to the use of transnational codes in promoting corporate social responsibility, namely, (1) the outsourcing of manufacturing plants to low-wage countries with poor labor conditions, (2) ties between multinational corporations and oppressive regimes, and (3) large-scale environmental damages caused by operations of multinational enterprises.[198]

The use of sweatshops and production facilities employing child labor has been widely documented. Kolk and Van Tulder noted that companies relocate their production facilities in other countries to take advantage of the latter's poor labor regulations.[199] Companies resort to child labor, pay very low wages and refuse to provide basic workers' rights such as collective bargaining and freedom of association. Later on, however, Levi Strauss & Company became the first company to draw up a corporate code of conduct "that placed the management of ethics and labor rights in the context of international supplier relations."[200] Thus, the worsening working

---

[193] Koji Ishikawa, *The Rise of the Code of Conduct in Japan: Legal Analysis and Prospect*, 27 LOY. L.A. INT'L & COMP. L. REV. 101, 101 (2005).
[194] *Id.*
[195] Note, *supra* note 190, at 2126.
[196] *Id.*
[197] *Id.*
[198] Ans Kolk & Rob Van Tulder, *International Responsibility Codes*, in The Accountable Corporation: Corporate Social Responsibility 149 (Marc Epstein and Kirk Hanson ed., Vol. 3, Praeger Perspectives, 2006).
[199] *Id.*
[200] *Id.*

conditions in the factories of TNCs in developing countries is considered the principal cause of the development of transnational codes of conduct.[201]

The second event linking the use of transnational codes of conduct to corporate social responsibility involves multinational corporations' association to human rights abuses and oppressive regimes in countries where they operate. Royal Dutch Shell was embroiled in an ugly and highly-publicized case concerning its operations in Nigeria. The company was criticized for its ties with the Nigerian military regime.[202] Public disapproval also met the plans of Carlsberg and Total to set up operations in Myanmar.[203] Hence, in 1997, Shell adopted a code providing that it is fully adhering to the principles found in the 1948 Universal Declaration of Human Rights making it the first multinational company to do so.[204]

Finally, Kolk and Van Tulder likewise observed that large-scale environmental damage beginning in the 1970s also led to greater focus on the activities of multinational companies. The *Amoco Cadiz* and *Exxon Valdez* oil spills, Union Carbide factory explosion in Bhopal, pollution of the Rhine by *Sandoz*, and relocation of multinationals to pollution havens, among others, all drew greater public attention on industrial activities.[205] This spate of environmental disasters most likely played a huge role in driving companies to review their operations and introduce changes in the way they conduct their business, including the adoption of codes of conduct.

ii. The First Codes of Conduct

1. International responsibility codes

While an overwhelming number of corporate codes of conduct were adopted only in the 1990s, the first responsibility codes were developed almost simultaneously by international organizations in the 1970s.[206] The drafting of the United Nations' Code of Conduct for Transnational Corporations ("UN Code") began in 1974 when the United Nations Economic and Social council set up a commission tasked to study the economic role of TNCs in the international community and to draft a code of conduct for said corporations.[207] The UN Code did not impose specific obligations on TNCs but merely contained general principles. Developed

[201] *See generally* Ishikawa, *supra* note 193.
[202] Kolk and Van Tulder, *supra* note 198, at 149.
[203] *Id.*
[204] *Id.*
[205] *Id.*
[206] *Id.* at 150.
[207] Ishikawa, *supra* note 193, at 103.

countries, especially the United States, strongly opposed the UN Code despite its weak substance and was therefore never adopted.[208]

In 1976, the Organisation for Economic Cooperation and Development (OECD) drafted the Guidelines for Multinational Enterprises ("OECD Guidelines"), which provides standards on several areas including employment, industrial relations, human rights, and the environment.[209] The OECD Guidelines was revised in 2000 and contains recommendations coming from the thirty OECD member countries.[210]

The International Labor Organization (ILO) drafted the Tripartite Declaration of Principles Concerning Multinational Enterprises ("ILO Code") in 1977.[211] The ILO Code's coverage extends to job creation, investments in the local economy and job contracting, and is thus considered broader than the scope of the OECD Guidelines.[212]

During the World Economic Forum in 1999, then UN Secretary-General Kofi Annan appealed to business leaders to support international efforts aimed at promoting human rights, improving working conditions and protecting the environment.[213] Thus, the Global Compact came out of this conference. However, it was to suffer the same fate as the 1974 UN Code. Despite receiving support from various UN agencies and several TNCs, the Global Compact received criticism from a number of states, especially from the United States, the business community and academic scholars.[214]

Obviously, the aforementioned draft codes and guidelines were not successful. While one company voluntarily adopted the ILO Code, no other company adopted or used the Code after workers' groups invoked the code in an industrial dispute.[215] The UN Code, as noted above, met strong opposition and was never adopted.

2. Independent and Private Codes of Conduct

There were also private initiatives to formulate norms for corporate conduct during the 1970s. In 1976, Leon H. Sullivan, a pastor and member of General Motors' board of directors, advocated for norms and principles

---

[208] *Id.* at 103-04.
[209] *Id.* at 104-05.
[210] *Id.* at 104.
[211] Kolk & Van Tulder, *supra* note 198, at 150.
[212] Ishikawa, *supra* note 193, at 105.
[213] *Id.* at 104. *See also* Kolk & Van Tulder, *supra* note 198, at 156-57.
[214] Ishikawa, *supra* note 193, at 104.
[215] Kolk & Van Tulder, *supra* note 198, at 150.

to guide American TNCs in South Africa during the apartheid era, namely: anti-discrimination, fair employment, equal wages, the promotion of non-white management, and improvement of the quality of life outside the workplace.[216] Twelve big American TNCs supported the *Sullivan Principles*,[217] but it suffered the same fate as the draft codes formulated by the international organizations at the time. Sullivan himself declared the Principles a failure when discrimination persisted in South Africa.[218]

The *MacBride Principles* is another code developed in the private sector. The Irish statesman Sean MacBride developed these principles to address discrimination against Catholic workers in American companies in Protestant-dominated Northern Ireland.[219] The Principles championed non-discrimination, affirmative action, and protection of the workers.[220]

A code of conduct for TNCs in the former Soviet Union was also formulated in 1988. A private foundation formulated the *Slepak Principles*, named after a Soviet dissident, in 1988 to provide multinationals operating in the Soviet Union a standard code of conduct.[221] American Congressman, John Miller, introduced a bill in the United States Congress in 1991 to do the same in China by way of the *Miller Principles*.[222]

3. Corporate Codes of Conduct

In the 1980s, the discussion on responsibility codes was limited to "business ethics" and largely took place only in the United States.[223] But in the 1990s significant attempts at establishing norms for corporate conduct resurfaced.[224] Corporations joined international organizations, governments, and non-governmental organizations (NGOs) in drawing up codes of conduct. TNCs felt increasing pressure from all sectors regarding their international operations and the working conditions in their overseas facilities. Hence, in 1991, Levi Strauss & Company became the first TNC to adopt a code of conduct through its adoption of its Business Partner Terms of Engagement and Guidelines for Country Selection.[225] This set of

---

[216] Ishikawa, *supra* note 193, at 107.
[217] Frederick Jonassen, *A Baby-Step to Global Reform: Corporate Codes of Conduct and the Child*, 17 MINN. J. INT'L L. 7, 36 (2008).
[218] *Id.*
[219] *Id.* at 37.
[220] *Id.*
[221] *Id.* at 37-38.
[222] *Id.* at 38.
[223] Kolk & Van Tulder, *supra* note 198, at 150.
[224] *Id.*
[225] Ishikawa, *supra* note 193, at 107. *See also* Kolk & Van Tulder, *supra* note 198, at 149-51.

guidelines covered key areas, including, ethical standards, environmental requirements, community involvement and employment standards.[226]

Nike's Code of Conduct is another high profile code that came into being after Levi Strauss & Company's introduction of its own code. Nike's code was adopted in 1992 in response to accusations of unfair labor practices in its Indonesian operations.[227] Nike's code contains provisions on child labor, compensation and benefits, work hours, the environment, and health and safety, among others.[228] Nike complemented the adoption of this code with enforcement and monitoring measures when it established a Labor Practices Department in 1996 to examine whether contractors met the Code, and hired Ernst & Young to independently monitor pay records, overtime compensation and compliance with local laws.[229]

The Rugmark code of conduct, which is a labeling program, was not initiated by a specific corporation. Instead, this movement targeted, and later on successfully partnered with, carpet retailers and manufacturers. Kailash Satyarthi, an Indian activist, fought against child labor in the carpet industry of South Asia.[230] He founded the Rugmark Foundation. Under the Rugmark code of conduct, carpet retailers and manufacturers agreed to replace child labor with adult labor and provide for the education of the children. The companies who agree to abide by the code pay a licensing fee and are subject to inspection by Rugmark monitors. Companies that passed the screening may use and attach the Rugmark label to their products, certifying that the carpet was not produced with child labor.[231] This labeling program was considered successful in Germany as well and soon gained popularity in the United States.[232]

iii. Wave of Corporate Codes of Conduct

As discussed, concerns about the working conditions in the factories of TNCs in developing countries led to international efforts of formulating principles for corporate conduct. Indeed, the first responsibility codes focused on addressing rampant unfair labor practices and the use of child labor. But this development may also be viewed as an unspoken recognition that maximizing overall firm value for the shareholders is not absolute.

---

[226] Ishikawa, *supra* note 193, at 107.
[227] *Id.* at 108.
[228] *Id.*
[229] *Id.*
[230] Jonassen, *supra* note 217, at 38.
[231] *Id.* at 39.
[232] *Id.*

Corporate activity can be tempered, and the interests of other parties can be taken into account in the operation of the business.

The latter part of the twentieth century saw the increase in the number of companies formulating and adopting codes of conduct. Companies "have taken the lead in the 'voluntary' introduction and implementation of codes of conduct." [233] And this time codes were adopted for various reasons. A 1996 United States Deparment of Labor study likewise noted this emergence of corporate codes and observed the variety of forms that these codes take: from guidelines to letters stating company policies to compliance certificates and clauses in formal documents.[234]

Corporate governance and accounting scandals put companies in the spotlight and created additional pressure for companies to adopt codes.[235] Some companies introduced codes frequently in response to stakeholder concerns.[236] Kolk and Van Tulder even noted that in some business sectors, especially the sporting goods and coffee industries, the adoption, modification or updating of codes were direct responses of companies to stakeholder concerns.[237] They observed that the interaction between business and their stakeholders was an important factor in the development of international responsibility codes.[238] "Codes of conduct are part of the bargaining relations between companies' managers and their stakeholders around the world," they said.[239] This indicates the significant role of company stakeholders. Businesses cannot simply ignore them. Profitability and responsibility must go hand in hand.

In a survey cited by Frederick Jonassen, "78 percent of the respondents said that they would prefer to shop at retail stores that had committed themselves to ending garment-worker abuse; 84 percent said they would pay $1 extra on a $20 item to ensure that the garment had been made in a worker friendly environment."[240] This demonstrates that there is in reality a socially-conscious sector of the market. Corporations have seized on this development and fighting very hard for this segment of the market. They have taken an interest in social responsibility because there are consumers who are in fact influenced by political and social concerns, and are willing to pay a premium for products that are made, for instance,

[233] Kolk & Van Tulder, *supra* note 198, at 151.
[234] Jonassen, *supra* note 217, at 46.
[235] *Id.*
[236] Kolk & Van Tulder, *supra* note 198, at 151.
[237] *Id.*
[238] *Id.* at 152.
[239] *Id.* at 166.
[240] Jonassen, *supra* note 217, at 49.

without exploitative child labor.[241] The case of Levi Strauss is another proof that corporations no longer take lightly stakeholder concerns in making business decisions. Levi Strauss, pursuant to its Guidelines, committed to contract only in countries where workers' rights can be improved.[242] Otherwise, Levi Strauss will pull out its investments and leave the country that fails to improve its laws on workers' rights.[243]

There is no doubt that the first corporate codes of conduct were formulated in response to accusations of unfair labor practices and to address the series of corporate scandals that rocked companies beginning in the 1960s. Its acceptance and popularity in the corporate community since the 1990s, however, reveal that a business-as-usual only approach is not enough. Corporations began to pay attention to non-shareholder concerns and, in some cases, fully embraced this development. In the following section, we will look at examples of codes of conduct of some big corporations and highlight how they treat non-shareholder interests.

iv. Example Codes of Conduct of Top Global Companies

90% of *Fortune* 500 companies and about half of all other companies have adopted their own codes of conduct.[244] In fact, a study showed that almost 90% of companies around the world have adopted mission or value statements that contain principles associated with stakeholders.[245]

In 2008, *Fortune 500* lists the following corporations as the world's ten biggest companies: Wal-Mart Stores, Exxon Mobil, Royal Dutch Shell, BP, Toyota Motor, Chevron, ING Group, Total, General Motors, and ConocoPhillips.[246] All these companies have adopted some form of code of conduct. Wal-Mart Stores has a Global Statement of Ethics;[247] Exxon Mobil

---

[241] *Id.*

[242] *Id.* at 56.

[243] *Id.*

[244] Note, *supra* note 190, at 2125. Lisa Fairfax has provided more specific data in one of her articles: "My study of Fortune 100 companies reveals that the vast majority of corporations espouse stakeholder rhetoric in some official corporate arena. All but two Fortune 100 companies feature such rhetoric within their annual reports, separate 'citizenship' reports, or on their corporate websites. Eighty-eight percent of these companies include stakeholder rhetoric within their annual report, 28% adopting such rhetoric on the very first page of the report, and 68% addressing stakeholder concerns within the first five pages. Moreover, many annual reports devote entire sections to spotlight the company's commitment to improving employees' quality of life, enhancing the environment, or engaging in community activities. The websites of 90% of Fortune 100 companies highlight issues associated with a group other than shareholders. Thus, the websites include discussions of stakeholders under such headings as 'social responsibility,' 'corporate citizenship,' 'our values,' or 'our commitment.'" See Fairfax, *supra* note 189, at 780; internal citations omitted.

[245] Fairfax, *supra* note 189, at 781.

[246] www.cnn.com, *World's 25 Biggest Companies (2008), at* http://money.cnn.com/magazines/fortune/global500/2008/snapshots/2255.html (last visited Jul. 12, 2009).

[247] http://walmartstores.com/AboutUs/281.aspx (last visited Jul. 12, 2009).

follows a Standards of Business Conduct;[248] Royal Dutch Shell has a General Business Principles,[249] a Code of Conduct[250] and a Code of Ethics;[251] BP is implementing a Code of Conduct;[252] Toyota Motor has a broad CSR Policy;[253] Chevron follows a Business Conduct and Ethics Code;[254] ING Group implements its own Business Principles;[255] Total has a Code of Conduct;[256] General Motors uses the Global Sullivan principles;[257] and ConocoPhillips follows a Code of Business Ethics and Conduct.[258] The contents of the codes of conduct of these companies vary and in some cases their commitments to social responsibility or stakeholder welfare are found not in their code of conduct but elsewhere. For instance, ConocoPhillips' Code of Conduct contains no elaboration on stakeholder values.[259] Instead, the company's website has a whole section on social responsibility covering areas like governance and ethics, community engagement, sustainable development, health and safety, and the environment.[260]

Toyota's CSR Policy contains commitments towards customers, employees, business partners (such as suppliers), shareholders, the environment, the community and on social contribution.[261] In addition, its company website also devotes a whole section on corporate responsibility providing detailed information on CSR Initiatives, the environment, social contribution and even traffic safety.[262]

---

[248] http://www.exxonmobil.com/Corporate/about_operations_sbc.aspx (last visited July 12, 2009).

[249] http://www.shell.com/home/content/aboutshell/who_we_are/our_values/sgbp/sgbp_30032008.html (last visited Jul. 12, 2009).

[250] http://www.shell.com/home/content/aboutshell/who_we_are/our_values/code_of_conduct/code_of_conduct_30032008.html (last visited Jul. 12, 2009).

[251] http://www.shell.com/home/content/aboutshell/who_we_are/our_values/code_of_ethics/code_of_ethics_30032008.html (last visited Jul. 12, 2009).

[252] http://www.bp.com/sectiongenericarticle.do?categoryId=9003494&contentId=7006600 (last visited Jul. 12, 2009).

[253] http://www.toyota.co.jp/en/csr/principle/index.html (last visited Jul. 12, 2009).

[254] http://www.chevron.com/documents/pdf/chevronbusinessconductethicscode.pdf (last visited Jul. 12, 2009).

[255] http://www.ing.com/group/showdoc.jsp?docid=350057_EN&menopt=cre|pol|bus (last visited Jul. 12, 2009).

[256] http://www.total.com/static/en/medias/topic1608/Total_code_conduct_en.pdf (last visited Jul. 12, 2009).

[257] http://www.gm.com/corporate/responsibility/reports/06/700_social/3_thirty/730.html (last visited Jul. 12, 2009).

[258] http://www.conocophillips.com/NR/rdonlyres/147E8B57-9169-4FA7-BB23-A41207B26D2D/0/13_CodeofEthics.pdf (last visited Jul. 12, 2009).

[259] *See* ConocoPhillips Code of Conduct, *supra* note 258.

[260] *See* the "Social Responsibility" section of ConocoPhillips' website *at* http://www.conocophillips.com/social/Governance/index.htm (last visited Jul. 12, 2009).

[261] *See* Toyota Guiding Principles and CSR Policy, *supra* note 253.

[262] *See* the "Corporate Responsibility" section of Toyota *at* http://www.toyota.co.jp/en/index_responsibility.html (last visited Jul. 12, 2009).

Total states in its Code of Conduct that it will strive to uphold the principles of the Universal Declaration of Human Rights, the key conventions of the International Labour Organization, the OECD Guidelines for Multinational Enterprises, and the principles of the United Nations Global Compact.[263] The company also declares in its Code of Conduct that its "business principles are (its) reference point and go hand-in-hand with the objective of continued growth, benefiting shareholders, customers and employees, and contributing to the economic and social development of the countries."[264]

Chevron, in its Business Conduct and Ethics Code, considers "partnership" as one of its values and towards this end it has "an unwavering commitment to being a good partner focused on building productive, collaborative, trusting and beneficial relationships with governments, other companies, (its) customers, (its) communities and each other."[265]

ING Group declares in its Business Principles that it accepts its responsibility for the sustainable development of society.[266] The company further states that it will take into account "a range of social, ethical and environmental considerations" while respecting its clients' desires.[267] Moreover, ING considers good relations with local communities are fundamental to the company's long-term success.[268]

BP's Code of Conduct covers a broad range of areas including the environment, health, safety and security, fair treatment and equal employment opportunity, working with suppliers, and community engagement.[269] Wal-Mart's Statement of Ethics encompasses a similarly broad scope of commitments and further states that the vision of its Global Ethics Office is to promote ownership of the company's ethical culture to all stakeholders globally.[270]

---

[263] *See* Total's Code of Conduct, *supra* note 256, at 8.
[264] *Id.* at 5.
[265] *See* Chevron's Business Conduct and Ethics Code, *supra* note 254, at 1.
[266] *See* ING Group's Business Principles, *supra* note 255, at 8.
[267] *Id.*
[268] *Id.* at 10.
[269] *See generally* BP's Code of Conduct, *supra* note 252.
[270] *See* Wal-Mart's Statement of Ethics, *supra* note 247, at 5.

C. The OECD Principles of Corporate Governance

The OECD released in 1999 and 2004 the OECD Principles of Corporate Governance.[271] The Principles are intended to assist governments, corporations and other parties in evaluating and improving corporate governance frameworks.[272] The Principles are non-binding but "represent a common basis that OECD member countries consider essential for the development of good governance practices."[273] The guidelines contained in the Principles include common elements identified in both OECD and non-OECD countries.[274]

The Principles' Preamble explicitly provides that "(e)mployees and other stakeholders play an important role in contributing to the long-term success and performance of the corporation."[275] It then devotes an entire section on the Role of Stakeholders in Corporate Governance, which is reproduced in full below:

> IV. The Role of Stakeholders in Corporate Governance
>
> *The corporate governance framework should recognise the rights of stakeholders established by law or through mutual agreements and encourage active co-operation between corporations and stakeholders in creating wealth, jobs, and the sustainability of financially sound enterprises.*
>
> A. The rights of stakeholders that are established by law or through mutual agreements are to be respected.
>
> B. Where stakeholder interests are protected by law, stakeholders should have the opportunity to obtain effective redress for violation of their rights.
>
> C. Performance-enhancing mechanisms for employee participation should be permitted to develop.
>
> D. Where stakeholders participate in the corporate governance process, they should have access to relevant, sufficient and reliable information on a timely and regular basis.
>
> E. Stakeholders, including individual employees and their representative bodies, should be able to freely

---

[271] Organization for Economic Co-operation and Development (OECD), OECD Principles of Corporate Governance 2004 (hereafter the "OECD Principles"), *available at* http://www.oecd.org/dataoecd/32/18/31557724.pdf (last visited Jul. 13, 2009).

[272] *See* the Preamble of the OECD Principles, *id.* at 11.

[273] *Id.*

[274] *Id.*

[275] *Id.* at 12.

> communicate their concerns about illegal or unethical practices to the board and their rights should not be compromised for doing this.
>
> F. The corporate governance framework should be complemented by an effective, efficient insolvency framework and by effective enforcement of creditor rights.[276]

The Annotations to the Principles provide that companies should realize that stakeholder contributions are essential in establishing successful enterprises.[277] Corporations would do well to foster "wealth-creating cooperation among stakeholders" which will contribute to the long-term success of the business.[278] Thus, corporations are encouraged to adopt a governance framework that recognizes stakeholder interests and contributions.[279]

Assessment of developments discussed in this section

The developments in the last few decades studied in this section show a more pronounced engagement of stakeholder interests at the level of international regulation, state regulation and self-regulation of the corporation. There is even empirical evidence suggesting that corporations themselves have come to embrace the notion of responsibility to groups and interests other than shareholders. Fairfax noted that corporate commitment to stakeholders in various company documents is proof that stakeholders now have a more distinct role in the corporate domain.[280] Fairfax adds that "while the extent and nature of stakeholder rhetoric varies among corporations, when viewed as a whole, it seems clear that stakeholders represent a central component of corporate discourse."[281] Notably, some corporations have even expressed that they have a dual commitment to shareholders and non-shareholders.[282] Such rhetoric is a "conscious acknowledgement of the corporate obligation to non-shareholders"[283] beyond the traditional objective of maximizing overall firm value for shareholders. But it must be noted that this development is not pure rhetoric. Many corporations do translate stakeholder rhetoric into actual company practice.[284]

---

[276] *Id.*, Part IV, at 21.
[277] *Id.*, Annotations to the OECD Principles, Part IV, at 46.
[278] *Id.*
[279] *Id.*
[280] Fairfax, *supra* note 189, at 782.
[281] *Id.* at 783.
[282] *Id.*
[283] *Id.* at 784.
[284] *Id.* at 817.

IV. THE RISE OF CORPORATE GIVING

In a report published in 2008 by the New York-based Committee Encouraging Corporate Philanthropy ("CECP"), 84% of corporate executives surveyed from around the world "believe that society now expects businesses to take a much more active role in environmental, social, and political issues than it did five years ago."[285] The report quoted one CEO as saying: "There is a quasi-public responsibility placed on private-sector companies and their leaders."[286] 75% of the respondents surveyed declared that "corporate philanthropy is one effective way to meet society's new expectations."[287]

The study further revealed that "[c]ompanies are developing more sophisticated initiatives to address the three levels of their contract with society (laws and regulations, implicit nonlegal expectations, and frontier issues such as obesity or human rights) and employing broader resources for community impact, including volunteerism, product donations, and capacity building."[288]

These findings are strong indications that corporations do admit the larger role that they play in society, and that they are embracing and taking concrete steps to fulfill this role. Corporations' fulfillment of this role is seen in the increase in recent years in the amount of corporate contributions, and innovative, if not unconventional and "un-businesslike," business methods like social entrepreneurship and Bill Gates' "creative capitalism."

A. Corporate Giving By the Numbers

The Conference Board[289] reported that based on its annual survey of giving, corporate contributions in the United States and abroad among 189 leading companies and corporate foundations amounted to $10.2 billion in 2006, up from $9.8 billion in 2005.[290] The report also revealed that

---

[285] Committee Encouraging Corporate Philanthropy, *Business's Social Contract: Capturing the Corporate Philanthropy Opportunity*, at 9, *available at* http://corporatephilanthropy.org/pdfs/research_reports/SocialContract.pdf (last visited Jul. 29, 2009).

[286] *Id.*

[287] *Id.*

[288] Committee Encouraging Corporate Philanthropy, *Research Reports* (on the study "Business's Social Contract: Capturing the Corporate Philanthropy Opportunity), *available at* http://corporatephilanthropy.org/index.php?option=com_content&view=article&id=502&Itemid=329 (last visited Jul. 29, 2009).

[289] A nonprofit membership and research organization. *See* www.conference-board.org (last visited Jul. 15, 2009).

[290] The Conference Board, *Corporate Contributions Rise Again,* Jan. 31, 2008, *at* http://www.conference-board.org/utilities/pressDetail.cfm?press_ID=3315 (last visited Jul. 15, 2009).

pharmaceutical companies are the top donors in the United States during that period.[291] In 2007, American corporations gave away $6.8 billion in cash and in-kind giving.[292]

CECP, "the only international forum of business CEOs and chairpersons focused exclusively on corporate philanthropy,"[293] reported that corporate giving in 2007 was higher than in 2006. Its finding, contained in an analysis of 2007 corporate philanthropy, is based on corporate contributions data from 155 leading corporations, including 69 of the *Fortune* 100 companies.[294] CECP reported that the "median total giving climbed from $24.67 million to $26.05 million based on matched-set data; giving as a percentage of pre-tax profit increased from 0.93% to 0.96%; and 66% of companies gave more in 2007 than in 2006."[295] 71% of *Fortune* 100 corporations gave more in 2007 than in 2006, with 39% of them increasing their contributions by 10% or more.[296] Some of the reasons it gathered for increased giving from corporations include continued strong profits, greater emphasis on philanthropy by senior management, and improved contributions tracking.[297]

Interestingly, CECP's report notes that not all companies that increased profits in 2007 gave more, while a majority of corporations that experienced a decline in company profits increased their corporate contributions. This, according to the report, is an indication that a company's financial performance is only one of many factors influencing corporate giving.[298]

In 2008, in the aftermath of the cyclone that wreaked havoc in Myanmar's delta region and the earthquake that devastated China's Sichuan Province, donations from American corporations were a combined $120.1 million for both China and Myanmar, while British companies' financial aid to the earthquake victims in China was said to be almost four times larger than the British government's official aid.[299]

---

[291] *Id.*

[292] Carol Adelman, *Global Philanthropy and Remittances: Reinvigorating Foreign Aid*, at 28, *available at* http://www.hudson.org/files/publications/BJWA_15%202_Adelman.pdf (last visited Jul. 15, 2009).

[293] *See* CECP's profile at http://corporatephilanthropy.org/about-cecp.html, (last visited 15 Jul. 2009).

[294] Committee Encouraging Corporate Philanthropy (CECP), *Giving in Numbers 2008 Edition*, at 4, *available at* http://corporatephilanthropy.org/pdfs/benchmarking_reports/GivinginNumbers2008.pdf (last visited Jul. 15, 2009).

[295] *Id.* at 8.

[296] *Id.* at 15.

[297] *Id.* at 9.

[298] *Id.* at 7, 10.

[299] Carol Adelman, *The Boom In Private Giving*,, INT'L HERALD TRIBUNE, Jun. 4, 2008, *available at* http://www.nytimes.com/2008/06/04/opinion/04iht-edadelman.1.13460679.html?_r=1.

Carol Adelman, Director of the Center of Global Prosperity at the Hudson Institute, notes that compared to the 1950s and 1960s when government aid dominated funding for developing countries, 75 percent of the financial flows from donor countries to poor nations today come from private sources: philanthropy, investments and remittances.[300] It can be safely concluded that corporations—the ones capable of generating vast capital resources—account for a substantial portion of these private fund inflows to poor countries.

LBG Research Institute[301] reported that the majority of corporations that it surveyed in November 2008 "anticipate no change or an increase in charitable giving for 2009."[302] Despite the declaration by 42% of corporations and 37% of corporate foundations surveyed that their charitable giving will decrease in 2009, the Institute predicted that the overall decrease in 2009 will be far less than the 12.1% drop in 2001 reported by Giving USA in 2002.[303] 80% of the corporations surveyed by the LBG Research Institute shared that their giving will be more strategic in 2009 meaning the their contributions will go to where it can have the greatest impact.[304] One respondent revealed that they will give "more dollars to fewer groups for greater impact and greater efficiency at work."[305]

Despite the bleak economic conditions, 24% of those surveyed said they will increase their giving for environmental causes, while 23% said they will increase support for basic needs, i.e. food, clothing and shelter. 16% of the corporations surveyed likewise declared that they will increase their giving for education and literacy causes, and another 14% of those surveyed said they will provide more funding for health in 2009. [306]

B. Social Entrepreneurship

Social entrepreneurship is perhaps the most radical evidence that many corporations today no longer pursue conventional for-profit only objectives. Social entrepreneurship is about merging noble social goals into business strategies. It is not very different from the typical business goal of

---

[300] *Id.*

[301] A nonprofit organization that conducts research on community investment. *See* http://www.lbgresearch.org/.

[302] LBG Research Institute, *Not All Doom and Gloom for Corporate Charitable Giving in 2009*, 6 January 2009, *available at* www.csrwire.com/PressReleasePrint.php?id=14182 (last visited March 26, 2009).

[303] *Id.*

[304] *Id.*

[305] *Id.*

[306] *Id.* The complete text of LBG Research Institute's report, *"Doing More with Less: How the Economic Downturn Will Impact Corporate Giving in 2009,"* may be purchased by visiting the "Publications" section of LBG's website *at* http://www.lbgresearch.org.

earning profits. The idea first developed in the 1990s from among the ranks of mostly technology investors who thought about "how philanthropy might work (differently and) about how they could take what made them rich in business and apply those tactics to charity."[307] Social entrepreneurship follows closely the "double bottom line" approach.[308] The enterprise simultaneously focuses on financial profits and social good.[309] The double bottom line concept considers profit "as having financial and social components."[310] It generates financial returns and social progress at the same time.[311]

Janet Kerr has called social entrepreneurship as "smart business, not charity or profit-sacrificing behavior."[312] She asserts that the upsurge in and sudden popularity of social entrepreneurship signals the end of the Milton Friedman business model and is a recognition by enterprises that "business cannot succeed if society fails."[313]

In her 2007 article, Kerr described several successful social entrepreneurship ventures, including the following.[314]

1. eBay

Even before eBay became public, its founders, Pierre Omidyar and Jeff Skoll, already talked about "the community" and what they can do for it. The duo decided to donate to a charitable foundation pre-initial public offering stocks.[315] Skoll later put up the Skoll Foundation which established the Skoll Centre for Social Entrepreneurship, Institute for Oneworld Health, Benetech and The PBS Foundation Social Entrepreneurship Fund.[316] Skoll also established Participant Productions, a production company that invests in films written and produced to promote social goals.[317]

But the more interesting strategy of the eBay founders is that of Omidyar's. Omidyar looked for for-profit ventures that promoted social

---

[307] Janet Kerr, *Sustainability Meets Profitability: The Convenient Truth of How the Business Judgment Rule Protects a Board's Decision To Engage in Social Entrepreneurship*, 29 CARDOZO L. REV. 623, 624 (2007).
[308] *See generally* Kerr, *id.*
[309] *Id.* at 632.
[310] *Id.* at 633.
[311] *Id.* at 634.
[312] *Id.*
[313] *Id.* at 642, *quoting* Bradley Googins, *A New Business Model for the 21st Century, Boardroom Briefing*, Winter 2006, at 6, *available at* http://www.directorsandboards.com/DBEBRIEFING/December2006/Winter06BB.pdf.
[314] Kerr, supra note 307.
[315] *Id.* at 624.
[316] *Id.* at 625.
[317] *Id.*

goals, and non-profit enterprises that earned money like for-profit businesses.[318] His Omidyar Network invested in enterprises that help communities by building playgrounds and sports fields, and an entity that assist teachers who need support for school projects, among others.[319] Omidyar Network has also worked in the area of microfinance, which was famously promoted by Nobel Peace Prize Winner Muhammad Yunus, considered the father of microcredit and Grameen Bank founder.[320]

2. Google

Google founders Larry Page and Sergey Brin, inspired by eBay, expressed that they consider Google as having obligations not only to its customers, employees and stockholders, "but also to the greater global community."[321] In an unprecedented move, Page and Brin informed prospective investors that they would invest 1% of Google's equity and profit in charitable work. This initial commitment alone amounted to over $1 billion.[322]

Google.org, a for-profit enterprise directed towards addressing social issues in the world including global poverty, health, the environment and energy, was the beneficiary of the money set aside from Google's equity and profits.[323] Google.org has partnerships with various for-profit and non-profit groups. What made Google's strategy unique from other corporations' strategy in philanthropy work is its commitment to support and invest in charitable work from the very beginning of the company's establishment, instead of waiting to generate profits that can be used in supporting social causes.[324] Moreover, the financial commitment is sourced directly from the money of Google's investors. The acceptance within the company of this unprecedented move is bolstered by the Google Board of Directors' support of a 20-year financial commitment to Google.org and approval of a faster payout rate of funds, which amounts to $175 million over a two-year period.[325]

---

[318] *Id.*
[319] *Id.*
[320] *Id.* at 625-26.
[321] *Id.* at 626-627.
[322] *Id.* at 627.
[323] *Id.*
[324] *Id.* at 628.
[325] *Id.*

3. Project Impact

David Green's Project Impact has been hailed as remarkable and revolutionary for the nonprofit entity's work in helping developing countries produce high-quality but affordable medicines.[326] The first project of Project Impact was a non-profit company in India called Aurolab. Aurolab was able to produce cheap surgically implanted artificial lenses for cataract patients especially the poor in developing countries. These lenses were sold for $4 to $6 each, compared to the exorbitant average industry price of $100 to $150.[327] Project Impact's strategy with Aurolab not only helped six million individuals, but also reaped substantial profits as Aurolab became the second biggest manufacturer of the lenses that it developed.[328]

4. GlaxoSmithKline and Toyota

GlaxoSmithLine and Toyota's strategies were directly aimed at their respective products. The big drug manufacturing company decided to slash the prices of their vaccines at or below cost in developing countries. Toyota, on the other hand, invested heavily in producing fuel-efficient vehicles, which has led to increase in brand value and company profits since it introduced its gas-electric hybrid car, Prius.[329] Kerr notes that the experiences of GlaxoSmithKline and Toyota show that business can benefit and reap huge profits by investing in social entrepreneurship.[330]

Perhaps more than the charitable and social responsibility projects that Toyota has since implemented, its standing today as the world's largest automaker shows the magnitude of its significance and impact on thousands of employees and families dependent on the company for their existence. The company's phenomenal growth even led the town of Koromo in Aichi Prefecture, Japan (where the company was first established by Mr. Kiichiro Toyoda) to change its name to "Toyota" in 1959.[331] Today, Toyota city, 25 times bigger than it was in the 1930s, is home to twelve of the car manufacturing giant's fifteen plants in Japan.[332]

---

[326] *Id.* at 631, citing David Green, *at* http://www.ashoka.org/node/3146.
[327] *Id.* at 631.
[328] *Id.*
[329] *Id.* at 629.
[330] *Id.*
[331] The Yamasa Institute, *Toyota Motor Company*, *available at* http://www.yamasa.org/japan/english/destinations/aichi/toyota.html (last visited August 7, 2009).
[332] *Id.*

5. Unilever

Unilever's case is an example of a leading global company employing socially-responsible and eco-friendly business strategies. The company has set up "a free community laundry, financing for eco-friendly drip irrigation, and waste recycling in Sao Paulo, Brazil."[333] The company's strategy is broad and diverse. It has also established a free hospital in Bangladesh, helps communities in Ghana by providing potable water, and assists women in India set up their own small business.[334]

6. Venture Capital firms

Venture capital firms, or "outside investors who fund and advise new, growing or struggling businesses,"[335] have also taken advantage of the social projects market. The venture capital firms Kleiner Perkins Caufield & Byers ("KPCB") and Khosla Ventures, founded by Vinod Khosla who was originally with KPCB, have been successful in investing and supporting social projects.[336]

KPCB's website declares that it is "actively investing in Greentech innovation and entrepreneurs."[337] On the other hand, Khosla Ventures invests in technologies that have beneficial effect and economic impact on society. The firm declares on its website that:

> Making a difference is a core value of khosla ventures and we have pledged some of any investment proceeds to achieving this difference. In particular, Vinod will donate 100% of his general partner profit from khosla ventures to these and other similar causes. Some of our "social impact" interests also make for great businesses, such as alternative energy, or can at least be viable businesses ("no loss" self sustaining businesses that don't need continued outside support, they are impact maximizers instead of being profit maximizers) even if profit is not the primary goal, such as microfinance and affordable housing.[338]

---

[333] Kerr, *supra* note 307, at 631-632.
[334] *Id.* at 632.
[335] *Id.* at 654.
[336] *Id.* at 657.
[337] *See* KPCB Initiatives, Greentech, *at* http://www.kpcb.com/initiatives/greentech/index.html (last visited Jul. 15, 2009).
[338] *See Khosla Ventures, The Things We Care About*, *at* http://khoslaventures.com/nonprofit.html (last visited Jul. 15, 2009).

C. Bill Gates' Creative Capitalism

Bill Gates is clearly one of the most recognizable names in the world today and perhaps in modern history. A billionaire entrepreneur and now retired founder of tech giant Microsoft Corporation, Bill Gates currently spends most of his time and fortune on philanthropy work, principally with the Bill & Melinda Gates Foundation, and preaching on "creative capitalism." Richard Stengel, *Time* Managing Editor, said of Bill Gates:

> Last January (2008) Bill Gates gave a groundbreaking speech on 'creative capitalism' at the World Economic Forum in Davos, Switzerland. Here's what we heard: one of the greatest capitalists in the history of the world suggesting that capitalism wasn't working all that well for almost half the people on the planet. He was in effect proposing a third way—the notion that profit and social responsibility were not mutually exclusive.[339]

Gates emphasizes that corporations are in a position to benefit not only investors and shareholders, but society in general as well. Gates' theory reminds us of the social entity conception of the corporation discussed in the first part of this paper. To recall, the social entity conception considers the corporation not as mere private property of its stockholders, but as a social entity with a public purpose. Gates admits that governments and nonprofit groups play a key role in helping billions of people suffering from poverty and preventable diseases, among others.[340] He argues, however, that:

> It is mainly corporations that have the skills to make technological innovations work for the poor. To make the most of those skills, we need a more creative capitalism: an attempt to stretch the reach of market forces so that more companies can benefit from doing work that makes more people better off. We need ways to bring far more people into the system—capitalism—that has done so much good in the world.[341]

Gates notes that creative capitalism is already at work in today's world. He points to the examples of cell phone companies utilizing selling arrangements in markets primarily composed of poor people, and businesses pledging a percentage of company profits to fight AIDS.[342] The social entrepreneurship business models described above may even represent Gates' notion of creative capitalism. Barbara Kiviat, in a short piece entitled *A Brief History of Creative Capitalism,* listed down examples of creative

[339] Richard Stengel, *To Our Readers, Creative Capitalism*, TIME, Aug. 11, 2008, at 2.
[340] Bill Gates, *How to Fix Capitalism*, TIME, Aug. 11, 2008, at 24.
[341] *Id.*
[342] *Id.*

capitalism throughout history including Henry Ford's famous move to increase the wages of his company, as well as Professor Merrick Dodd's argument that there is room in a for-profit venture like the corporation to take into consideration non-shareholder constituencies such as employees, customers and communities.[343]

Gates, in explaining creative capitalism, indicates that such an approach is a way to answer an important question: "How can we most effectively spread the benefits of capitalism and the huge improvements in quality of life it can provide to people who have been left out?"[344] Gates, therefore, does not directly impose on the corporation a separate obligation, unlike the profit-social responsibility dichotomy and the traditional debates concerning the nature and objective of the business corporation. Instead, he is telling corporations that there are probably ways for them to conduct business and maximize profit that, at the same time, directly impacts the "people who have been left out." Hence, Gates is not espousing pure charity but in fact states that earning a return on ventures that benefit those who have been left out is "the heart of creative capitalism."[345] "It's not just about doing more corporate philanthropy or asking companies to be more virtuous. It's about giving them a real incentive to apply their expertise in new ways, making it possible to earn a return while serving the people who have been left out,"[346] Gates adds. For this to happen, Gates suggests that businesses can look for these new ways or opportunities on their own, or governments and nonprofit groups can help provide such opportunities for businesses.[347]

As Gates has pointed out, companies can bring and introduce technology to those who cannot get it otherwise under normal market conditions. He draws attention not only to Microsoft's monetary and software donations "to bridge the digital divide," but also to the company's work developing software to enable illiterate or semi-illiterate people to use computers with minimal training.[348] Gates likewise cites Safaricom's business strategy which has helped make mobile phone telephony accessible to and affordable for the people of Kenya. Safaricom, to serve the low-income groups in Kenya, charge customers by the second rather than by the minute.[349] This type of creative selling arrangement is likewise used by

---

[343] *See generally* Barbara Kiviat, *A Brief History of Creative Capitalism*, TIME, 11 August 2008, at 26-27.
[344] Gates, *supra* note 340, at 26.
[345] *Id.* at 26-27.
[346] *Id.* at 27.
[347] *Id.*
[348] *Id.*
[349] *Id.*

mobile phone companies in the Philippines—a country where a majority of its population live on less than $2 a day.

Concluding observations on corporate giving

Earlier in this paper we referred to developments and cases indicating a growing recognition that the corporation is no longer viewed as a purely for-profit entity (e.g., stakeholder statutes, codes of conduct, social entrepreneurship). These developments show that to achieve long-term success and profitability, companies should take into account both shareholders and other stakeholders' interests. Gates' creative capitalism is distinct in this respect. Gates' theory is not merely promoting a stakeholder view of the corporation. He is not just imploring corporations to go beyond the interests of shareholders. Gates is suggesting that business strategies be tailored in such a way that will benefit people who have been left out—not mere corporate stakeholders—in addition to ensuring that the business is able to generate a handsome return for its investments and maximize overall firm value for the shareholders. One may argue that this is similar to the idea of social entrepreneurship. But no matter how we define Gates' brainchild, the notion of creative capitalism is yet another strong indicator of how today's business leaders view the corporation, its capacity and potential to do more, and the role that it can play in today's world.

CONCLUSION

There is no doubt that wealth creation is still the fuel that drives present day business corporations. Investors and entrepreneurs set up a company to grow the funds invested therein and rightly so. However, history and the development of corporate legal theory suggest that profit-making need not be the sole and ultimate objective of the corporation. Families, communities and even an entire nation are built, sustained and maintained on the foundations of successful corporations. A community of hundreds of thousands may be sustained by a single corporation and may even change its name after that of the corporation operating within it, as in the case of Toyota City in Japan. This broad, all-encompassing reach of the corporation shows that groups other than company shareholders affect and are affected by the corporation.

As Millon noted, the business corporation is viewed as a "socially useful instrument of economic growth."[350] This thought supported the view in the nineteenth century that the state-granted privilege of incorporation is

[350] Millon, *supra* note 4, at 206.

not simply for the private benefit of shareholders, but also to promote the welfare of the community. Earlier, we covered the development in the United States of regulations designed to prevent the concentration of harmful economic power, and laws aimed at protecting the interests of constituencies exposed to abusive corporate power.[351] American jurisprudence likewise contributed to the body of public interest and general welfare regime in corporate law with the development of the *ultra vires* doctrine,[352] the court's approval of corporate giving despite management failure to demonstrate any direct benefit to the donor company,[353] and recognition of non-shareholder interests,[354] among others. Allen himself has observed that "both our courts and, more importantly, our legislatures have, in effect, endorsed the entity view."[355]

Apart from the evolution in legislation and jurisprudence of a corpus of general welfare regime in corporate law, stakeholder and social responsibility theories also developed to support the thinking that corporations owe responsibilities to groups other than stockholders. These theories demonstrated that multiple relationships involving non-shareholders support and affect the corporation. Legal scholars further dissected the nature of the corporation and the scope of management duty to reveal the view that duties toward non-shareholder constituencies also exist. Thus, we saw the creation of stakeholder statutes and corporate codes of conduct.

Business leaders themselves—from Henry Ford to Bill Gates—have acknowledged and declared the business corporation's other, non-profit making side. Data on corporate giving have supported this recognition by corporations and their leaders. The continued rise and institutionalization of corporate giving throughout the years is a testament to corporations' acceptance of the broad expectations of society. Corporations now accept the larger role that they play in the social order. Indeed, corporate commitment to stakeholders in various company documents is proof that stakeholders now have a more distinct role in the corporate domain.[356]

For sure, these insights might appear as mere repetitions of what we perhaps knew all along, i.e., corporations do contribute something to the community where they operate. But this thought is too simplistic. It does

---

[351] *Id.* at 210.
[352] *Id.* at 209.
[353] A.P. Smith Manufacturing Co. v. Barlow, et al., *supra* note 108.
[354] Unocal Corporation v. Mesa Petroleum Co., *supra* note 94, Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc., *supra* note 98, and Paramount Communications, Inc. v. Time, Inc., *supra* note 101.
[355] Allen, *supra* note 7, at 276.
[356] Fairfax, *supra* note 189, at 782.

not fully explain why a company can fulfill stakeholder duties or contribute to charitable causes using shareholder money or company funds that were, in the first place, invested to grow wealth. While searching for the justification to this query was not the goal of this paper, this question was perhaps fortuitously addressed throughout the discussion herein.

The developments in corporate law theory and empirical evidence discussed throughout this essay suggest that corporations—or at least many of them—no longer confine themselves to purely private and wealth-maximization concerns. The emergence of non-shareholder interests in corporate affairs and business operation, as well as the increase in corporate "giving" confirm the trend away from conventional notions regarding the corporation. However, whether or not senior management actively pursue and consider stakeholder or other-constituency interests in actual boardroom decision-making is beyond the scope of this paper.

-o0o-