Washington University Law Review

Volume 92
Issue 2 *Midwestern People of Color Legal Scholarship Symposium*

2014

Toward a Critical Corporate Law Pedagogy and Scholarship

andré d. p. cummings
Indiana Tech Law School

Steven A. Ramirez
Loyola University Chicago School of Law

Cheryl L. Wade
St. John's University School of Law

Recommended Citation

andré d. p. cummings, Steven A. Ramirez, and Cheryl L. Wade, *Toward a Critical Corporate Law Pedagogy and Scholarship*, 92 WASH. U. L. REV. 397 (2014).
Available at: https://openscholarship.wustl.edu/law_lawreview/vol92/iss2/7

TOWARD A CRITICAL CORPORATE LAW PEDAGOGY AND SCHOLARSHIP

andré douglas pond cummings[*]
STEVEN A. RAMIREZ[**]
CHERYL L. WADE[***]

I. INTRODUCTION

In recent years, the publicly held corporation has assumed a central position in both the economic and political spheres of American life.[1] Economically, the public corporation has long acted as the key institution within American capitalism.[2] Politically, the public corporation now can use its economic might to sway electoral outcomes as never before.[3] Indeed, individuals who control public firms wield more economic power and political power today than ever before.[4] These truths profoundly shape

---

∗ Interim Dean and Professor of Law, Indiana Tech Law School; J.D. Howard University School of Law. Dean cummings expresses gratitude to Professors Steven Ramirez and Cheryl Wade for partnering superbly on this piece and for many other collaborations and insights provided over the years. Additional gratitude is expressed to Prosper Batinge, 2L Indiana Tech Law School, for excellent research support and to the Wash. U. Law Review editorial staff. Thanks also to the participants at the Midwestern People of Color Legal Scholarship Conference 2014 for providing critical feedback as well as the faculty at the Indiana Tech Law School where this piece was workshopped in 2014. Finally, much appreciation is due to Lavinia Mann Cummings, Cole Kaianuanu, Malia Ao'ilagi and Maxwell Keave for unconditional support and constant peace. Of course, as usual, any errors are the sole responsibility of the authors.

∗∗ Professor of Law, Associate Dean of Research & Faculty Development Director, Business & Corporate Governance Law Center, Loyola University Chicago School of Law (sramir3@luc.edu). Ronald Melton provided excellent research assistance for this article. This article also benefited from comments at the Midwestern People of Color Legal Scholarship Conference hosted by Indiana Tech Law School in April, 2014. I particularly thank Professor Kimberly Norwood for her efforts in making this Article a reality.

∗∗∗ Dean Harold F. McNiece Professor of Law, St. John's University School of Law (wadec@stjohns.edu).

1. Tom C.W. Lin, *The Corporate Governance of Iconic Executives*, 87 NOTRE DAME L. REV. 351, 372 (2011) ("Because corporations play such a vital role in the life of individuals and states, their governance can impact a whole host of prosaic and profound issues.").

2. STEVEN A. RAMIREZ, LAWLESS CAPITALISM 49 (2013) (terming the public corporation the "perfect capital aggregator under law" due to limited liability, perpetual investment horizon, centralized management, locked-in capital, and shareholder primacy).

3. *See, e.g.*, Citizens United v. Fed. Election Comm'n, 558 U.S. 310, 319, 339–40 (2010) (holding that the government cannot prohibit independent corporate expenditures and invalidating part of the Bipartisan Campaign Reform Act that restricted electioneering communications).

4. CEO compensation, for example, continues its inexorable upward trajectory. Gary Strauss et al., *The 0.1 Percent; Millions by Millions, CEO Pay Goes Up*, USA TODAY, Apr. 4, 2014, at 1B ("2013 median [CEO] pay . . . jumped 13% to $10.5 million . . . .").

American society.[5] The power, control, and role of the public corporation under law and regulation, therefore, hold more importance than ever before.[6]

Even though corporate law and regulation define all aspects of this central economic and political institution within the American system, the development of corporate law is impeded by a deficient pedagogy—and thus, to a certain degree, scholarship—that scarcely mentions the power and influence corporations hold. Critical voices, in particular, are excluded from virtually all corporate law textbooks. Many corporate law texts taught in law school classrooms treat the social role of the public corporation as a black box of corporate law pedagogy and, by extension, mainstream legal scholarship.[7] Indeed, a relentless stream of legal scholarship challenging the law and regulation of the public firm from the perspective of its broader social and economic implications receives little to no mention in the key textbooks adopted and taught from in law schools today.[8] This Article challenges the dominant corporate law master

5. Indeed, corporate and financial elites now constitute about half of the top .01 percent (or one in 10,000) of the income distribution, and virtually all of the growth over the most recent decades accrued to this group. JACOB S. HACKER & PAUL PIERSON, WINNER-TAKE-ALL POLITICS 1–13, 22–28, 46, 48 (2010). Corporate law fuels economic inequality. THOMAS PIKETTY, CAPITAL IN THE TWENTY-FIRST CENTURY 302 (2014) ("Recent research, based on matching declared income on tax returns with corporate compensation records, allows me to state that the vast majority (60 to 70 percent, depending on what definitions one chooses) of the top 0.1 percent of the income hierarchy in 2000–2010 consists of top managers.").

6. Modern economic and financial scholarship agrees. For instance, in recent years, experts in finance and financial economics have increasingly studied the importance of corporate law and corporate governance on firm performance and macroeconomic performance. *Compare* Harold Demsetz, *The Firm in Economic Theory: A Quiet Revolution*, 87 AM. ECON. REV. 426, 426 (1997) (stating that under "neoclassical theory" the firm is a "black box" in that its functioning is assumed to be optimal), *with* M. Andrew Fields & Phyllis Y. Keys, *The Emergence of Corporate Governance from Wall St. to Main St.: Outside Directors, Board Diversity, Earnings Management, and Managerial Incentives to Bear Risk*, 38 FIN. REV. 1, 12–13 (2003) (giving an overview of empirical evidence regarding the impact of diversity and other elements of corporate governance variation on financial performance).

7. This Article reviewed five major corporate law texts: MELVIN ARON EISENBERG & JAMES D. COX, BUSINESS ORGANIZATIONS: CASES AND MATERIALS (11th ed. unabr. 2014); CHARLES R.T. O'KELLEY & ROBERT B. THOMPSON, CORPORATIONS AND OTHER BUSINESS ASSOCIATIONS: CASES AND MATERIALS (7th ed. 2014); JESSE H. CHOPER ET AL., CASES AND MATERIALS ON CORPORATIONS (8th ed. 2013); WILLIAM KLEIN ET AL., BUSINESS ASSOCIATIONS: CASES AND MATERIALS ON AGENCY, PARTNERSHIP, AND CORPORATIONS (8th ed. 2012); DAVID EPSTEIN ET AL., BUSINESS STRUCTURES (3d ed. 2010).

8. Such critical scholarship, for example, includes: Paul S. Miller, *Shareholder Rights:* Citizens United *and Delaware Corporate Governance Law*, 28 J.L. & POL. 53, 91 (2012) (arguing that shareholders must submit to coerced speech directed by managers under current Delaware law and *Citizens United*); john a. powell & Stephen Menendian, *Beyond Public/Private: Understanding Excessive Corporate Prerogative*, 100 KY. L.J. 43, 66–74 (2011–2012) (arguing against excessive privatizations and corporate prerogatives); andré douglas pond cummings, *Procuring "Justice"?:*

narrative perpetuated in all of the major business law textbooks. This master narrative prevents law students and legal scholars from fully understanding and analyzing the changing nature and evolution of law and power in the United States.

In challenging the status quo narrative, law students and scholars today must consider the fact that at the apex of the modern public firm stands the Chief Executive Officer ("CEO").[9] CEOs act as the new potentates in American society and manage their firms as "personal fiefdoms."[10] The pay of CEOs and senior executives at the largest firms proves their power, as they now command enormous salaries beyond most athletes or movie stars and far beyond any ordinary citizen or employee.[11] Never before has the American economy produced so much for the benefit of so few—most of whom are corporate or financial elites.[12] Recently, data on current inequality affirms that wealth gaps have again reached the historically high

---

Citizens United, Caperton*, and Partisan Judicial Elections*, 95 IOWA L. REV. BULL. 89, 97–99 (2010) (showing pernicious impact of *Citizens United* on judicial independence); Thuy-Nga T. Vo, *To Be or Not to Be Both CEO and Board Chair*, 76 BROOK. L. REV. 65, 126–29 (2010) (concluding that combining of chairman and CEO roles contributes to excessive CEO power and diminished financial performance); Nancy Levit, *Megacases, Diversity, and the Elusive Goal of Workplace Reform*, 49 B.C. L. REV. 367, 414–27 (2008) (noting that class action lawsuits are necessary to assure corporate diversity); George W. Dent, Jr., *Academics in Wonderland: The Team Production and Director Primacy Models of Corporate Governance*, 44 HOUS. L. REV. 1213, 1215 (2008) ("[T]he status quo is not director primacy, shareholder primacy, or team production, but CEO primacy—governance by managers largely for their own benefit."); Steven A. Ramirez, *Games CEOs Play and Interest Convergence Theory: Why Diversity Lags In America's Boardrooms and What To Do About It*, 61 WASH. & LEE L. REV. 1583, 1613 (2004) (concluding that CEOs work to place cronies on the board of their firms and forgo diversity).

9. Legendary mutual fund founder John Bogle claims that a "pathological mutation" has gripped the public corporation, transmogrifying traditional "owners' capitalism" into "managers' capitalism." JOHN C. BOGLE, THE BATTLE FOR THE SOUL OF CAPITALISM 28 (2005).

10. According to economist and Nobel laureate Joseph Stiglitz, American CEOs manage corporations as a "personal fiefdom, not for the shareholders, but for their own benefit." In particular, immediately preceding the financial crisis of 2007–2009 firms "reported high profits, gave big bonuses, big stock options, but in fact there were huge risks buried off-balance sheet and those chickens have now come home to roost." *Talk of the Nation: Economists Explain 'How to Save Capitalism'*, NPR (Oct. 20, 2008), http://www.npr.org/templates/story/story.php?storyId=95906243.

11. For example, a joint study of CEO compensation at the largest firms conducted by Equilar Inc. "found that the median 2012 pay package came in at $15.1 million—a leap of 16 percent from 2011." Gretchen Morgenson, *An Unstoppable Climb in C.E.O. Pay*, N.Y. TIMES, June 30, 2013, at BU1.

12. HACKER & PIERSON, *supra* note 5, at 1–4 (showing how high inequality, arising largely from high payouts to corporate and financial elites, operated to create a rigged economic system); JOSEPH E. STIGLITZ, THE PRICE OF INEQUALITY: HOW TODAY'S DIVIDED SOCIETY ENDANGERS OUR FUTURE 119–22 (2012) (economic account of the causes and consequences of high inequality with a focus on economic power as a tool to corrupt the political system).

levels last seen in the chaotic days just prior to the financial collapse of 2008.[13]

Even when chief executives who constitute this new economic royalty fail badly in their supposed primary task of shareholder wealth maximization, as they did during the financial market crisis of 2008, they are still richly paid through stock options or golden parachutes.[14] These arrangements exist with the consent of their handpicked confederates on the Board of Directors who too often serve as nominal supervisors.[15] Yet, issues of CEO power, CEO compensation, golden parachutes, and the crony capitalism that gives rise to board members with close affinity to the CEO, ostensibly supervising the CEO, get little discussion in the most widely used corporations textbooks today.[16] The manifest costs of CEO primacy in the public firm are not mentioned at all.[17] Today's law students will become tomorrow's business leaders, advisors, and policymakers, but

13. Emmanuel Saez, Striking it Richer: The Evolution of Top Incomes in the United States (Updated with 2012 Preliminary Estimates) 9 Figure 3 (Sept. 3, 2013) (unpublished manuscript) (archived at http://perma.cc/Z4EE-5XNH).

14. Recently, the former CEO of Target garnered about $55 million in severance pay after being ousted for a major breach in data security at that firm. Gary Strauss, *Ousted Target CEO Could Collect $55M-Plus*, USA TODAY, May 6, 2014, *archived at* http://perma.cc/448C-8N9F.

15. One infamous example:

> Stanley O'Neal, former CEO of Merrill Lynch . . . spent much of his career at Merrill Lynch and became CEO in 2002, presiding over the company as it began to place huge bets on subprime mortgages and risky derivatives that generated billions in losses, nearly sank the firm, and led to a takeover by Bank of America in 2008. In 2006—the year Merrill made many of the deals that led to its downfall—O'Neal earned $91 million, according to the Financial Crisis Inquiry Commission. When O'Neal resigned in 2007, Merrill gave him a severance package worth another $161 million.

Rick Newman, *How 11 Corporate Titans Profited After Failure*, U.S. NEWS (June 29, 2011), *archived at* http://perma.cc/9N5Q-VE4R.

16. *See* KLEIN ET AL., *supra* note 7, at 907–10 (discussing directors, the Dodd-Frank say on pay provision, and executive compensation in general but omitting critical analysis of the way compensation decisions are made); O'KELLEY & THOMPSON, *supra* note 7, at 1171–73 (discussing directors, golden parachutes, and executive compensation in general but omitting critical analysis of the way compensation decisions are made). For a discussion of the potential biases arising from CEOs' relationship with the board of directors, see Antony Page, *Unconscious Bias and the Limits of Director Independence*, 2009 U. ILL. L. REV. 237, 248 (quoting Kristina A. Diekmann et al., *Self-Interest and Fairness in Problems of Resource Allocation: Allocators Versus Recipients*, 72 J. PERSONALITY & SOC. PSYCHOL. 1061, 1061 (1997)) ("As self-interested actors in a world of limited goods and opportunities, we are motivated to promote and justify resource distributions that favor us and those to whom we are linked by ties of kinship or group membership.").

17. Joseph Stiglitz, on the other hand, traces the CEO's power to set his or her own compensation to accelerating inequality, and then to a corrupted legal system and other macroeconomic ills associated with too much CEO power. STIGLITZ, *supra* note 12, at 31–39, 40–41, 66–67, 271. *See also* PIKETTY, *supra* note 5, at 334 ("The most convincing proof of the failure of corporate governance and . . . extremely high executive pay is that when we collect data about individual firms . . . it is very difficult to explain the observed variations in terms of firm performance.").

their legal education regarding corporations suffers from crucial blind spots. This black hole of knowledge will lead to an intolerable ignorance on the part of those who propose to lead on global economic issues in the future.

The ability of the CEO to stack the board of directors with cultural clones is key to the new power of the CEO. Essentially, in most public corporations, management selects management under the federal proxy rules.[18] The board of the public firm is a product of "homosocial reproduction" whereby socially important cultural traits such as gender and race play a decisive role in board membership.[19] This dynamic contributes to the fact that the governing heights of the American economy continue to be the last bastion of white male supremacy.[20] Again, despite important emerging critical scholarship on this fact,[21] no major Business

18. Under state law, shareholders putatively select directors. In public corporations, however, "[b]efore directors' elections, companies distribute proxy materials that allow shareholders who do not attend annual meetings to vote their shares. Typically, these proxy materials include only those director candidates nominated by the existing board . . . ." Recent Case, *Administrative Law—Corporate Governance Regulation—D.C. Circuit Finds SEC Proxy Access Rule Arbitrary and Capricious for Inadequate Economic Analysis—*Business Roundtable v. SEC, *647 F.3d 1144 (D.C. 2011)*, 125 HARV. L. REV. 1088, 1088 (2012).

19. Lin, *supra* note 1, at 363 ("With regards to directors, executives often engage in 'homosocial reproduction' and select like-minded individuals to work with them and to execute their visions. Thus, it should not be surprising that many current and former corporate executive officers serve on corporate boards, even interlocking firms in their service.").

20. James D. Westphal & Edward J. Zajac, *Who Shall Govern? CEO/Board Power, Demographic Similarity, and New Director Selection*, 40 ADMIN. SCI. Q. 60, 77, 79 (1995) (finding that "in firms in which CEOs are relatively powerful, new directors are likely to be demographically similar to the firm's incumbent CEO" and that cultural similarity leads to higher compensation). While some may argue that the problem of white male domination of America's boardrooms arises from recruitment difficulties or lack of sufficient candidates for board membership, others suggest more traditional causes of exclusion of diverse voices. According to one leader in the African American business community because "there is a surplus of black executive talent with sterling professional credentials and reputations for unmatched performance at the highest levels" the fact that "an overwhelming number of boards of publicly traded companies still lock African Americans out of the boardroom" constitutes "a detestable statement that they seek to maintain these preserves of white male privilege and dominance." *Black Enterprise Publishes Exclusive Registry of African Americans on Corporate Boards*, BLACK ENTERPRISE, Aug. 4, 2014, http://www.blackenterprise.com/career/black-enterprise-publishes-exclusive-registry-of-african-americans-on-corporate-boards/ (quoting *Black Enterprise* CEO Earl "Butch" Graves Jr.). We posit that the white male domination of the boardroom, whether conscious or unconscious, is simply a numerical fact. Thus, according to the latest survey conducted by *Black Enterprise*, 74 of the nation's 250 largest public companies still have zero African-American directors as of May of 2014. *Id.*

21. *E.g.*, Michael R. Siebecker, *Bridging Troubled Waters: Linking Corporate Efficiency and Political Legitimacy Through a Discourse Theory of the Firm*, 75 OHIO ST. L.J. 103, 110–11, 127–29 (2014) (arguing that allowing shareholder access to management's proxy solicitation can enhance engagement and ultimately corporate legitimacy); Bo Becker et al., *Does Shareholder Proxy Access Improve Firm Value? Evidence from the Business Roundtable's Challenge*, 56 J.L. & ECON. 127, 157 (2013) (finding that shareholder proxy access is valued in equity markets); Grant M. Hayden & Matthew T. Bodie, *The Bizarre Law and Economics of* Business Roundtable v. SEC, 38 J. CORP. L.

Associations textbook mentions the social realities behind the legal mechanisms that belie any notion of a meritocracy at the commanding heights of the economy. Textbooks treat this costly crony capitalism as if it does not exist, or as if there is no problem with the status quo.[22] This failure is a critical one.

Corporate governance failings manifest themselves in massive social costs and reckless risks. Consider the enormous costs of the Enron series of scandals in 2001-2002,[23] the subprime debacle,[24] or the BP oil spill in the Gulf of Mexico.[25] Each of these instances demonstrates that the costs of misgoverned public corporations with poor risk management policies and procedures can reach the trillions.[26] The key to effective corporate governance is to maximize the benefits of the corporate form while minimizing costs.[27] This, in turn, requires a candid discussion of the role

101, 120–22 (2012) (arguing that the decision to deny shareholders access to proxy materials for purpose of director elections rested upon weak law and economics).

22. *See* KLEIN ET AL., *supra* note 7, at xi–xxi; O'KELLEY & THOMPSON, *supra* note 7, at ix–xxiv.

23. *See* Urska Velikonja, *The Cost of Securities Fraud*, 54 WM. & MARY L. REV. 1887, 1914, 1937–38 (2013) (describing broad externalities associated with securities fraud beyond market capitalization losses—including an increase in the cost of capital for even honest firms—and illustrating such costs through the experience of Enron's and WorldCom's bankruptcy in 2001–2002); Erica Beecher-Monas, *Marrying Diversity and Independence in the Boardroom: Just How Far Have You Come, Baby?*, 86 OR. L. REV. 373, 377 (2007) (noting that Enron's 14 member board included 12 white males).

24. *See generally* Christopher J. Miller, Note, *Don't Blame Me, Blame the Financial Crisis: A Survey of Dismissal Rulings in 10b-5 Suits for Subprime Securities Losses*, 80 FORDHAM L. REV. 273 (2011) (discussing cases involving securities fraud in the context of mortgage-related securities created during the financial crisis and noting $2.2 trillion in bank losses alone from the financial crisis).

25. *See* Joseph Karl Grant, *What Can We Learn from the 2010 BP Oil Spill?: Five Important Corporate Law and Life Lessons*, 42 MCGEORGE L. REV. 809, 814 (2011) (recounting the loss of over 50 percent of BP's market capitalization in the wake of the Gulf oil spill). BP's losses amount to $42 billion. Selina Williams, *BP Views Higher Oil-Spill Costs as Profit Declines*, MARKETWATCH (July 30, 2013), http://www.marketwatch.com/story/bp-views-higher-oil-spill-costs-as-profit-declines-2013-07-30. The damage to the Gulf ecosystem as a result of the BP oil spill is literally incalculable. Gaia J. Larsen, *Skewed Incentives: How Offshore Drilling Policies Fail to Induce Innovation to Reduce Social and Environmental Costs*, 31 STAN. ENVTL. L.J. 139, 140 (2012). An acoustic switch to trigger a well shutdown could have prevented the Deepwater Horizon blowout and costs around $500,000. *Id.* at 171–72.

26. The governance of corporations formed a core cause of the financial crisis. *See* FIN. CRISIS INQUIRY COMM'N, THE FINANCIAL CRISIS INQUIRY REPORT xviii (2011) (finding that "dramatic failures of corporate governance and risk management" drove the crisis) [hereinafter FCIC REPORT]; GRANT KIRKPATRICK, THE CORPORATE GOVERNANCE LESSONS FROM THE FINANCIAL CRISIS 2 (OECD 2009) (finding that "to an important extent" the financial crises arose from "failures and weaknesses in corporate governance," particularly in the areas of compensation incentives and risk management). Losses from the crisis include lost wealth of $9 trillion, and forgone GDP could approach $10 trillion. *See* U.S. GOV'T ACCOUNTABILITY OFFICE, GAO-13-180, FINANCIAL CRISIS LOSSES AND POTENTIAL IMPACTS OF THE DODD-FRANK ACT 15, 21 (2013).

27. *See* Steven A. Ramirez, *The End of Corporate Governance Law: Optimizing Regulatory Structures for a Race to the Top*, 24 YALE J. ON REG. 313, 316 n.23 (2007) ("[O]ptimal corporate governance would minimize net agency costs.").

of the corporation in our economy and political system with appropriate critiques of manifest shortcomings.[28] This Article seeks a more critical discourse regarding the public corporation and its social and political impact.

Poorly governed corporations recently posed even greater problems than the massive economic costs exacted by the crises of recent years. The corporation now holds a central position in our political system—beyond the contemplation of any of the nation's Founders[29]—and that position has enabled the corporation to seize new profit opportunities in important social realms. For example, corporations recently emerged as a prime political player and profiteer in America's mass incarceration campaign.[30] Today, even education has been corporatized at some schools.[31] Should profit maximizing corporations hold such key social roles such as prison sentry or school administrator? Are there any limits on the privatization of government functions through the corporation? Should the corporation be tethered to its original policy contemplation of fostering business formation and directly funding innovation? Critical corporate scholars

28. Traditionally, corporations were viewed with healthy skepticism and confined only to activities that they were specifically chartered to pursue—there were no general business corporations, much less corporations pursuing business traditionally left to the state or exercising constitutional rights. *See* Citizens United v. Fed. Election Comm'n, 558 U.S. 310, 428 (2010) (Stevens, J., concurring in part and dissenting in part) ("Even 'the notion that business corporations could invoke the First Amendment would probably have been quite a novelty,' given that 'at the time, the legitimacy of every corporate activity was thought to rest entirely in a concession of the sovereign.'"(citations omitted)). In other words, corporations possessed limited powers defined by the state, not constitutional rights the state could not infringe.

29. Jonathan A. Marcantel, *The Corporation as a "Real" Constitutional Person*, 11 U.C. DAVIS BUS. L.J. 221, 265 (2011) ("[W]hile the drafters and ratifiers of the federal organic documents perhaps used words that if defined broadly could encompass corporations, the drafters and ratifiers did not, at least during the debates, use those words in a manner consistent with protecting juridical beings as real constitutional entities.").

30. PRISON PROFITEERS: WHO MAKES MONEY FROM MASS INCARCERATION ix–x (Tara Herivel & Paul Wright eds., 2007) (providing overview of private interests that earn profits from incarceration including prison managers, prison builders, prison suppliers, firms that tap into low-cost prison labor, transportation firms, weapons makers, and bankers and lawyers who structure prison-related deals and bond offerings).

31. *See* KLEIN ET AL., *supra* note 7, at xi–xxi (ignoring privatization); O'KELLEY & THOMPSON, *supra* note 7, at ix–xxiv (same). According to recent reports:

> Critics see the newest rush to private vendors as more worrisome because school districts are outsourcing not just supplies but the very core of education: the daily interaction between student and teacher, the presentation of new material, the quick checks to see which kids have risen to the challenge and which are hopelessly confused. At the more than 5,500 charter schools nationwide, private management companies—some of them for-profit—are in full control of running public schools with public dollars.

Stephanie Simon, *Private Firms Eyeing Profits from U.S. Public Schools*, REUTERS INDIA (Aug. 2, 2012), *archived at* http://perma.cc/J3TL-989D.

wrestle with these very questions regarding the proper role of the corporation in our society while corporate textbooks completely ignore such quandaries.[32]

This Article challenges the benign view of all aspects of corporate law now prevalent in most major texts in this area and, by implication, much of the corporate law teaching that goes on in U.S. law schools today. "Law schools train many of the nation's leaders."[33] Textbooks play a central role in the education of law review editors for their role as gatekeepers to legal scholarship.[34] And, for the business law professoriate, the content of corporate law textbooks effectively tethers most to very narrow constructions of American business law, leaving very little space for critical assessments in the classroom.[35] Excessive deference to corporate domination and the power of the CEO marginalizes critical scholarship that raises uncomfortable questions for those claiming leadership over our economy.[36] Critical analysis of corporate law and governance in Business Associations casebooks will help students and future business leaders to question the role of the public corporation and understand its advantages and limitations.

More than ever, CEOs and the public corporations they control exert a decisive influence over the American economy and political system—and by extension society itself.[37] The policy basis for this massive "mission

32. Until relatively recently, corporate law textbooks spent significant effort on the role of the corporations in society and early efforts to contain the corporation to limited spheres. *See, e.g.*, NORMAN D. LATTIN, THE LAW OF CORPORATIONS §§ 54, 63–66 (2d ed. 1971); HARRY G. HENN & JOHN R. ALEXANDER, LAWS OF CORPORATIONS §§ 4–12 (3d ed. 1983).

33. Susan Sturm, Commentary, *Law Schools, Leadership, and Change*, 127 HARV. L. REV. F. 49, 49 (2013), *available at* http://perma.cc/RT24-QV4S.

34. According to Richard Posner, the student-edited law review is "not well-equipped to select, and through editing to improve, articles outside of the core of legal doctrinal analysis." Richard A. Posner, *The Decline of Law as an Autonomous Discipline: 1962–1987*, 100 HARV. L. REV. 761, 779 (1987).

35. *Cf.* Juan F. Perea, *Race and Constitutional Law Casebooks: Recognizing the Proslavery Constitution*, 110 MICH. L. REV. 1123, 1149 (2012) (concluding that the failure to include critical perspectives in constitutional law textbooks "will deter" teaching such perspectives and training future lawyers to critically question evidence).

36. *Id.* at 1148–52 (noting that accurate and balanced pedagogy as manifest in casebooks is key to understanding current inequities, including the subtle racism that continues to pervade U.S. society, and failure to teach evidence in a balanced fashion "perpetuates widespread ignorance" as well as "unquestioning reverence" to the Founders).

37. *See, e.g.*, Janis Sarra, *Class Act: Considering Race and Gender in the Corporate Boardroom*, 79 ST. JOHN'S L. REV. 1121, 1121–25 (2005) (arguing that lack of diversity of corporate boards exacerbates race and gender discrimination issues); Jayne W. Barnard, *Corporate Boards and the New Environmentalism*, 31 WM. & MARY ENVTL. L. & POL'Y REV. 291 (2007) (assessing corporate leaders' decision making and its impact on the environment); Janis Sarra, *The Gender Implications of Corporate Governance Change*, 1 SEATTLE J. SOC. JUST. 457 (2002) (exploring impact of corporate governance on women); Kent Greenfield & D. Gordon Smith, *Debate: Saving the World with*

creep" is currently non-existent, or at least unarticulated.[38] Largely this is because the natural forum for analyzing and critiquing the legal and regulatory changes giving rise to this reality—the basic corporations law school class—fails to raise or meaningfully discuss these developments.[39] This permits corporate law to veer away from fundamental values.[40] This Article suggests that the black box of corporate law controversies be opened and that a full discussion of winners, losers, and policy underlying the public corporation be discussed and debated.

Corporations constitute a key prop to a modern and dynamic capitalist economy. Crucially, they operate to channel passive capital into productive entrepreneurial and innovative conduct.[41] In a capitalist system, if corporations did not exist they would need to be invented.[42] Some commentators rightfully consider the public corporation to be one of the greatest legal innovations in history.[43] Rather than contesting this assertion, this Article seeks to vindicate it by insisting upon a balanced critique of the proper legal and regulatory definition of the public

Corporate Law?, 57 EMORY L.J. 947 (2008) (examining the impact of corporate law on poverty, the environment and labor).

38. Indeed, the Court previously has denied the corporation certain constitutional rights. *See* First Nat'l Bank of Bos. v. Bellotti, 435 U.S. 765, 778 n.14 (1978) ("Corporate identity has been determinative in several decisions denying corporations certain constitutional rights, such as the privilege against compulsory self-incrimination, or equality with individuals in the enjoyment of a right to privacy . . . . Certain 'purely personal' guarantees, such as the privilege against compulsory self-incrimination, are unavailable to corporations and other organizations because the 'historic function' of the particular guarantee has been limited to the protection of individuals.") (citations omitted).

39. As Professor Perea aptly asks, "When did 'thinking like a lawyer' come to require ignoring important evidence . . . and avoiding rigorous analysis of the possible ramifications of that evidence?" Perea, *supra* note 35, at 1149–50.

40. Thirty-one years ago a leading corporate law treatise raised questions about American corporations and their relationship to the apartheid regime in South Africa. HENN & ALEXANDER, *supra* note 32, at 32–33. Professor Lynne Dallas' textbook about law, policy and socioeconomics explores the societal impact of business, economics and corporate decision-making and would enrich a corporation's course. LYNNE L. DALLAS, LAW AND PUBLIC POLICY: A SOCIOECONOMIC APPROACH (2005).

41. *See* Steven A. Ramirez, *Rethinking the Corporation (and Race) in America: Can Law (and Professionalization) Fix "Minor" Problems of Externalization, Internalization, and Governance?*, 79 ST. JOHN'S L. REV. 977, 978–79 (2005) (arguing that the essential elements of the modern corporation may maximize the flow of capital from passive investors to productive enterprises despite structural problems).

42. JOHN MICKLETHWAIT & ADRIAN WOOLDRIDGE, THE COMPANY: A SHORT HISTORY OF A REVOLUTIONARY IDEA xv (2003) ("[The corporation is] the basis of the prosperity of the West and the best hope for the future of the rest of the world.").

43. *See, e.g.*, 1 WILLIAM MEADE FLETCHER, CYCLOPEDIA OF THE LAW OF PRIVATE CORPORATIONS § 21 (1917) ("[T]he limited liability corporation is the greatest single discovery of modern times . . . ." (quoting Nicholas Murray Butler, President, Columbia Univ., Address at the 143rd Annual Banquet of the Chamber of Commerce of the State of New York (Nov. 16, 1911))).

corporation. Because of its manifest importance, this critical approach seeks to perfect the corporation, particularly its deeply suboptimal governance frameworks.[44]

This Article will unfold as follows: in Part II, the Article highlights the continued domination of corporate governance by elite white males. Next, in Part III, the Article will assess the impact of the new political power granted public firms by the federal judiciary through its decision in *Citizens United*.[45] In Part IV, this Article will demonstrate the meaning of the enhanced power of CEOs. Part V will discuss the role of the corporation in managing prisons and public schools as an example of how the relaxation of traditional constraints on corporate power have combined for profoundly un-American outcomes: jailing citizens and educating children for profit. Part VI will show the economic senselessness and continuing reality of the Too Big To Fail ("TBTF") corporation.

The conclusion of the Article is that current corporate law pedagogy, as evinced in widely adopted and longstanding texts that are published by traditional law presses, avoids grappling with important issues in corporate law: who actually controls corporations and why; whether corporations should undertake traditional government functions for profit; the political role of the corporation; and the recent devolution of law and regulation in favor of corporate managers.[46] In short, the public corporation in these texts stands immune from critical analysis and should simply be accepted as immutable. Evidence to the contrary is simply ignored.

We concede that the list of potential topics for discussion in a Business Associations class is already impossibly crowded. But Business Associations is a survey course, and the goals in this kind of law school class include introducing students to a broad range of discourse about large and small business organizations. Sometimes, Business Associations professors must opt for breadth rather than depth when choosing what to cover. Most important, a more balanced and inclusive text gives the law professor who adopts it the ability to more easily choose the most appropriate topics and perspectives for his or her students. This can be

44. *E.g.*, Thomas Piketty et al., *Optimal Taxation of Top Labor Incomes: A Tale of Three Elasticities*, AM. ECON. J.: ECON. POL'Y, Feb. 2014, at 230 (finding that the prevalence of CEO pay for luck increases with lower tax rates as CEOs face greater incentives to use their power to enhance compensation); George W. Dent, Jr., *Toward Unifying Ownership and Control in the Public Corporation*, 1989 WIS. L. REV. 881 (1989) (arguing that proxy reform would resolve the governance problems inherent in the separation of ownership and control).

45. Citizens United v. Fed. Election Comm'n, 558 U.S. 310, 428 (2010).

46. *See* KLEIN ET AL., *supra* note 7, at xi–xxi (failing to provide critical analysis of corporations); O'KELLEY & THOMPSON, *supra* note 7, at ix–xxiv (same).

done without having to resort to supplemental reading that students consider onerous. The refusal to provide critical evidence and critical analysis skews the business law education of U.S. law students and biases the knowledge base of emerging lawyers and leaders. We conclude by proposing a critical approach to corporate law pedagogy and scholarship.

II. THE PUBLIC CORPORATION AND WHITE MALE SUPREMACY

Virtually absent in all leading business law texts published by traditional law presses is any discussion of the continuing dominance of white male supremacy at all leadership levels of public corporations.[47] This occurs even though corporations profoundly influence the social reality of race and class in the United States.[48] In fact, the public corporation is a key engine of racial disparities in economic outcomes in America.[49] Nothing illustrates this reality more powerfully than the subprime mortgage crisis.[50] Most of the key players in the crisis operated as public corporations subject to American corporate governance laws.[51] Numerous official inquiries have identified defective corporate governance and risk management as a key cause of the subprime debacle.[52]

47. *See* EISENBERG & COX, *supra* note 7, at v–xvii, 1080–84; KLEIN ET AL., *supra* note 7, at xi–xxi; O'KELLEY & THOMPSON, *supra* note 7, at ix–xxiv; *see also* RICHARD ZWEIGENHAFT & G. WILLIAM DOMHOFF, THE NEW CEOS: WOMEN, AFRICAN AMERICAN, LATINO, AND ASIAN AMERICAN LEADERS OF FORTUNE 500 COMPANIES xii, xxiii (paperback ed. 2014) (showing that women and minorities now lead only about 10 percent of the Fortune 500 as CEOs and hold only about 25 percent of directorships despite comprising nearly 64 percent of the population).

48. For example, researchers found that tobacco firms competed to market menthol cigarettes in poor minority communities, and this contributed to the racialized geography of today's tobacco-related health disparities. Valerie B. Yerger et al., *Racialized Geography, Corporate Activity, and Health Disparities: Tobacco Industry Targeting of Inner Cities*, J. HEALTH CARE FOR POOR & UNDERSERVED, Nov. 2007, at 10 .

49. Leadership positions at the top of the public corporation carry power, prestige and wealth, as evidenced by the fact that about half of the top .01 percent of the income distribution consists of corporate and financial elites. *See supra* note 5. CEO compensation, in particular, constitutes one of the few positions where compensation can soar as high as $100 million or even over $1 billion per annum. Strauss et al., *supra* note 4.

50. *See* Natasha Lennard, *A Record High Wealth Gap Between Whites and Minorities*, SALON (July 26, 2011), *archived at* http://perma.cc/3N8Q-AAY7.

51. FCIC REPORT, *supra* note 26, at xvii ("The very nature of many Wall Street firms changed—from relatively staid private partnerships to publicly traded corporations taking greater and more diverse kinds of risks."). The FCIC highlights "stunning" corporate governance failures at AIG, Merrill Lynch, Fannie Mae and Citigroup, each of which was a publicly traded corporation. *Id.* at xix.

52. *See supra* note 26. *See also* S. COMM. ON HOMELAND SEC. AND GOVERNMENTAL AFFAIRS, PERMANENT SUBCOMM. ON INVESTIGATIONS, 112TH CONG., WALL STREET AND THE FINANCIAL CRISIS: ANATOMY OF A FINANCIAL COLLAPSE 65–68 (Comm. Print 2011), *archived at* http://perma.cc/8BS-CC4T [hereinafter Levin-Coburn Report] (finding that Washington Mutual

The subprime crisis caused the most massive destruction and transfer of wealth in U.S. history.[53] That wealth transfer—from Main Street taxpayers to Wall Street bankers, executives and investors—ultimately led to the highest recorded racial wealth gap in recent U.S. history.[54] "By one measure, the white-to-black median wealth ratio increased from eleven to one in 2005 to twenty to one in 2009. By this same measure, the white-to-Hispanic median wealth ratio increased from seven to one in 2005 to eighteen to one in 2009."[55] Naturally, these devastating changes in household wealth caused by the subprime mortgage fiasco result in fewer educational opportunities, less secure retirements, less economic mobility, and a lower quality of life in minority communities.[56]

The financial crisis also spawned differential outcomes in income status. "[B]y one measure, African Americans and Hispanics as a whole were downwardly mobile and net losers in terms of their income status during the period of 2001-2011, while whites were net winners."[57] And, the gap between white unemployment and minority unemployment reached higher levels after the crisis than before the crisis.[58] More Americans of color live in poverty today as a direct result. When compared to white Americans, twice as many Americans of color live in

---

("WaMu") embarked on high-risk mortgage lending in early 2005, even as the bank's own Chief Risk Officer stated that the condition of the housing market signifies a "bubble" with risks that "will come back to haunt us" and that WaMu forged ahead despite repeated warnings that the risks were excessive, its lending standards and risk management systems were deficient, and many of its loans were tainted by fraud.). The Levin-Coburn report found that WaMu was typical of home mortgage lenders in terms of risk. *Id.* at 4.

53. According to National Public Radio (NPR):

> [T]he proximate cause of the Great Recession was the collapse of the housing market. When things went south, blacks and Latinos—who had more of their family wealth wrapped up in housing —were absolutely throttled. Blacks lost half of their household wealth, Latinos lost two-thirds, and home ownership rates fell to numbers not seen since the Reagan era.

Gene Demby, *What Do We Do About America's Racial Wealth Gap?*, NPR: CODE SWITCH (Apr. 30, 2013), http://www.npr.org/blogs/codeswitch/2013/04/30/179907029/what-do-we-do-about-americas-racial-wealth-gap.

54. *See* SIGNE-MARY MCKERNAN ET AL., URBAN INST., LESS THAN EQUAL: RACIAL DISPARITIES IN WEALTH ACCUMULATION 1 (2013), *archived at* http://perma.cc/TDH4-PZU2.

55. Thomas W. Mitchell, *Growing Inequality and Racial Economic Gaps*, 56 HOW. L.J. 849, 858 (2013) (citing PEW RESEARCH CTR., TWENTY-TO-ONE: WEALTH GAPS RISE TO RECORD HIGHS BETWEEN WHITES, BLACKS AND HISPANICS, 7, 14 (2011), *archived at* http://perma.cc/4QL8-46S2).

56. *See id.* at 861–68.

57. *Id.* at 851 (citing PEW RESEARCH CTR., FEWER, POORER, GLOOMIER: THE LOST DECADE OF THE MIDDLE CLASS, 12 (2012), *archived at* http://perma.cc/M4B6-RPTE).

58. In 2011, the white unemployment rate was 7.9 percent lower than the black unemployment rate and 3.6 percent lower than the Hispanic unemployment rate. U.S. BUREAU OF LABOR STATISTICS, LABOR FORCE CHARACTERISTICS BY RACE AND ETHNICITY, 2011 41 tbl.12 (2012), *archived at* http://perma.cc/8TG7-4PSQ. In contrast, in 2001, the white unemployment rate was 4.4 percent lower than the black unemployment rate and 2.4 percent lower than the Hispanic unemployment rate. *Id.*

poverty.[59] *Even more troubling is the fact that 37.9 percent of African* American children now live in poverty and 33.8 percent of Hispanic children live in poverty.[60] A more economically senseless destruction of human capital is difficult to imagine.

This economic inequality was no accident. Flawed corporate law, governance and policy played a major role.[61] For example, executives were able to harvest huge gains at the expense of shareholders and the disempowered, as well as society in general.[62] Predatory lenders targeted the most unsophisticated borrowers, who, historically, have been denied access to capital and credit, for noxious home loans.[63] A Federal Reserve study found that predatory lenders frequently targeted less educated Americans.[64] Another study by the *Wall Street Journal* found that of all subprime borrowers, 61 percent of them actually qualified for prime loans.[65] The most nefarious of the subprime lending was concentrated largely in areas that had sizeable minority populations.[66] The high up-front fees and interest costs associated with subprime loans accelerated executive compensation even while leading to higher borrower-default

59. In 2011, 12.8 percent of whites lived in poverty while 27.6 percent of blacks and 25.3% of Hispanics lived in poverty. CARMEN DENAVAS-WALT ET AL., U.S. CENSUS BUREAU, INCOME, POVERTY, AND HEALTH INSURANCE COVERAGE IN THE UNITED STATES: 2011, at 14 tbl.3 (2012), *available at* https://www.census.gov/prod/2012pubs/p60-243.pdf.

60. Valerie Strauss, *New Census Data: Children Remain America's Poorest Citizens*, WASH. POST: THE ANSWER SHEET BLOG (Sept. 17, 2013, 5:26 PM), *archived* http://perma.cc/KJW5-29ZF ("Those hardest hit are children of color: 37.9 percent of black children lived in poverty in 2012, and 33.8 percent of Hispanics did as well. Compare that to 12.3 percent for white, non-Hispanic children.").

61. *See* PIKETTY, *supra* note 5, at 302.

62. We were warned, albeit not through corporate law casebooks. No less an authority than Fed Chair Alan Greenspan stated in 2002, in reference to the Enron scandals, that CEOs would seek to harvest gains without respect to shareholder value. FED. RESERVE BOARD'S SEMIANNUAL MONETARY POL'Y REP. TO THE CONG. (July 16, 2002), *archived at* http://perma.cc/4XQB-MREA (testimony of Chairman Alan Greenspan) (stating that lax corporate governance law contributed to CEO primacy and permitted CEOs to "harvest" illicit gains through manipulation of stock prices).

63. Christopher L. Peterson, *Fannie Mae, Freddie Mac, and the Home Mortgage Foreclosure Crisis*, 10 LOY. J. PUB. INT. L. 149, 168 n.128 (2009) ("The mortgage foreclosure crisis was driven not by lending to poor people, but by lending to poor people with terms designed to extract short term profits through abusive fees.").

64. *See generally* Kristopher Gerardi et al., *Financial Literacy and Subprime Mortgage Delinquency: Evidence from a Survey Matched to Administrative Data* (Fed. Reserve Bank of Atlanta, Working Paper No. 2010-10, Apr. 2010), *available at* http://www.frbatlanta.org/documents/pubs/wp/wp1010.pdf.

65. Rick Brooks & Ruth Simon, *Subprime Debacle Traps Even Very Credit-Worthy*, WALL ST. J., Dec. 3, 2007, at A1.

66. Elvin Wyly et al., *Cartographies of Race and Class: Mapping the Class-Monopoly Rents of American Subprime Mortgage Capital*, 33 INT'L J. URBAN & REGIONAL RES. 332, 339–40 (2009) (finding that subprime lending was concentrated in areas with high prime loan rejection rates and areas of historic minority marginalization such as the Texas border area).

levels.[67] Overwhelming evidence demonstrates that much of the crisis was rooted in widespread race-based subprime lending to non-subprime borrowers of color.[68]

All the while, corporations and their executives profited from this subprime lending. Take Countrywide Financial Corp., for example. Countrywide paid CEO Angelo Mozilo $102 million in 2006 and $229 million in 2007, including $127 million that Mozilo reaped from exercising stock options in 2007, the same year that Countrywide announced massive mortgage losses.[69] The Financial Crisis Inquiry Commission ("FCIC"), a congressionally authorized commission charged with investigating the financial crisis, found that as early as 2006, Mozilo termed Countrywide's subprime loans "poison" and "toxic," and stated they were likely to lead to bankruptcy.[70] Countrywide ultimately settled predatory lending claims for $8.4 billion, the largest predatory lending settlement in history.[71] Meanwhile, Angelo Mozilo and others settled securities fraud claims with the Securities and Exchange Commission ("SEC") for over $70 million—essentially for selling shares to the investing public without disclosing the "poisonous" lending at Countrywide.[72] Mozilo, however, personally only paid $22.5 million of

67. High-cost subprime loans default at eight times the default rate on prime loans, even after controlling for credit characteristics. CLAUDIA COULTON ET AL., CTR. ON URBAN POVERTY & CMTY. DEV., PATHWAYS TO FORECLOSURE: A LONGITUDINAL STUDY OF MORTGAGE LOANS, CLEVELAND AND CUYAHOGA COUNTY, 2005-2008, at 1 (2008), *available at* http://blog.case.edu/msass/2008/06/23/Pathways_to_foreclosure_6_23.pdf.

68. For example, a recent study found:

> Consistent with previous research, blacks and Latinos were more likely and Asians less likely to receive subprime loans than whites were. Income was positively associated with receipt of subprime loans for minorities, whereas the opposite was true for whites. When expensive (jumbo) loans were excluded from the sample, regressions found an even stronger, positive association between income and subprime likelihood for minorities, supporting the theory that wealthier minorities were targeted for subprime loans when they could have qualified for prime loans.

Jacob W. Faber, *Racial Dynamics of Subprime Mortgage Lending at the Peak*, 23 HOUSING POL'Y DEBATE 328, 329 (2013). *See also* RAMIREZ, *supra* note 2, at 147–51 (collecting studies).

69. James L. Bicksler, *The Subprime Mortgage Debacle and Its Linkages to Corporate Governance*, 5 INT'L J. DISCLOSURE & GOVERNANCE 295, 296–97 (2008).

70. FCIC REPORT, *supra* note 26, at 20.

71. Gretchen Morgenson, *Countrywide to Set Aside $8.4 Billion in Loan Aid*, N.Y. TIMES, Oct. 6, 2008, at B1.

72. Press Release, SEC, Former Countrywide CEO Angelo Mozilo to Pay SEC's Largest-Ever Financial Penalty Against a Public Company's Senior Executive (Oct. 15, 2010), *archived at* http://perma.cc/3YC3-A5V2 (noting that the SEC settled based upon allegations that Mozilo (and others) "failed to disclose to investors the significant credit risk that Countrywide was taking on as a result of its efforts to build and maintain market share" and that "Mozilo engaged in insider trading in the securities of Countrywide by establishing four 10b5-1 sales plans in October, November, and

the settlement.[73] The Mozilo and Countrywide fraud demonstrate the flawed legal structure of the public firm that permitted, even facilitated, the ability of CEOs and other senior executives to profit mightily from predatory and race-based lending while defrauding the public.[74]

What would have happened if corporate leadership in America embraced and reflected diversity? Could these kinds of catastrophic losses for society, communities of color, and shareholders have been averted? Recent empirical studies demonstrate that firms with diverse boards suffered fewer subprime losses during the mortgage meltdown.[75] Still, despite evidence that meaningfully diverse boardrooms improve corporate governance and bestow significant financial benefits,[76] the apex of corporate leadership remains a bastion of white male supremacy.[77]

A survey of the demographic make-up of corporate leadership reveals continued white male privilege rather than the operation of competitive meritocracy.[78] Fifty years after the Civil Rights Act of 1964,[79] which formally outlawed racial and gender discrimination, the commanding heights of the American economy still look more like an old boys' club

---

December 2006 while he was aware of material, non-public information concerning Countrywide's increasing credit risk").

73. Walter Hamilton & E. Scott Reckard, *Angelo Mozilo, Other Former Countrywide Execs Settle Fraud Charges*, L.A. TIMES (Oct. 16, 2010), *archived at* http://perma.cc/58U7-YKGU.

74. *See* Gretchen Morgenson, *Gimme Back Your Paycheck: After the Losses, Who Shares the Pain?*, N.Y. TIMES, Feb. 22, 2009, at BU1 ("Executives at seven major financial institutions that have collapsed, were sold at distressed prices or are in deep to the taxpayer received $464 million in performance pay since 2005" even while their shareholders suffered staggering losses).

75. *E.g.*, Maureen I. Muller-Kahle & Krista B. Lewellyn, *Did Board Configuration Matter? The Case of US Subprime Lenders*, 19 CORP. GOVERNANCE: AN INT'L. REV. 405, 405 (2011) ("We find that the board configurations of those financial institutions that engaged in subprime lending were significantly different from those that did not. Specifically, subprime lenders had boards that were busier, had less tenure and were less diverse with respect to gender."); Marion Hutchinson et al., *Who Selects the 'Right' Directors? An Examination of the Association Between Board Selection, Gender Diversity and Outcomes*, 55 ACCT. & FIN. (forthcoming 2015) (finding that Australian companies with "greater gender diversity moderate[d] excessive firm risk which in turn improve[d] firms' financial performance").

76. *See* RAMIREZ, *supra* note 2, at 145–47 (citing authorities which find diversity improves boardroom performance).

77. As will be discussed in the next section the problem is essentially that CEOs exercise too much control over the public firm's proxy solicitation, which they continue to use to control board composition and indirectly their compensation. *See* Ramirez, *supra* note 8, at 1600–12 (collecting authorities that demonstrate link between director and CEO affinity and compensation); Richard Clune et al., *The Nominating Committee Process: A Qualitative Examination of Board Independence and Formalization,* 31 J. CONTEMP. ACCT. RES. 748 (2014) (finding that CEOs continue to exercise influence over director nominations notwithstanding nominally independent nominating committees).

78. *See generally* ALLIANCE FOR BOARD DIVERSITY, MISSING PIECES: WOMEN AND MINORITIES ON *FORTUNE 500* BOARDS (2013), *available at* http://theabd.org/2012_ABD%20Missing_Pieces_Final_8_15_13.pdf.

79. 42 U.S.C. §§ 2000a–2000h-6 (2006 & Supp. V. 2011).

than a thriving modern capitalistic meritocracy.[80] Only a genuine or unintended belief in white male supremacy can ignore the fact that meaningful racial, gender, or worldview diversity has failed to take hold in the modern corporate governance of the public firm.[81]

For example, according to one recent survey, males hold over 80 percent of Fortune 100 board seats and whites hold nearly 85 percent of such seats.[82] At Fortune 500 firms these numbers increase to nearly 85 percent and 87 percent, respectively.[83] Progress for women and minorities on this front continues at a glacial pace, as women and minorities accounted for only 26.7 percent of all seats in 2012 at Fortune 500 firms, barely more than the 25.5 percent seen in 2010.[84] Women and minorities continue to be dramatically underrepresented at all leadership levels of the world's most powerful public corporations.[85]

While public firms in the U.S. lag, diversity in the boardroom commands the attention of lawmakers in other parts of the world. For example, in 2003, Norway imposed quotas requiring that women occupy 40 percent of the board seats of public firms.[86] Other countries followed suit shortly thereafter.[87] The EU proposed a directive in 2012 requiring that 40 percent of non-executive directors on corporate boards be female by January 1, 2020.[88] Diversity in the boardroom, thus, is a global issue.

---

80. *See* Gary Strauss, *Good Old Boys' Network Still Rules Corporate Boards*, USA TODAY, Nov. 1, 2002, at 1B (quoting Stephen Baum, CEO of Sempra Energy, that board diversity "provides diversity of opinion and a different perspective. It causes us to think a little more. The quality of our decision-making is better. If we were all right-wing Republicans, we might miss opportunities.").

81. Professor Cheryl Wade states the reality well:

> [C]orporate diversity discussions are misleading because they imply that companies work hard to ensure race and gender equity. . . . The *implied contextual message*, however, is that it may be true that many men and whites are promoted more frequently and earn more, but these decisions are based on merit. The implication is that even with diversity training, diversity officers, and codes of conduct that prohibit discrimination, whites and males climb to the top of the corporate hierarchy anyway. It is an implied message of white male supremacy.

Cheryl L. Wade, *Transforming Discriminatory Corporate Cultures: This Is Not Just Women's Work*, 65 MD. L. REV. 346, 349, 372 (2006).

82. ALLIANCE FOR BOARD DIVERSITY, *supra* note 78, at 2 fig.1.

83. *Id.* at 7 fig.7.

84. *Id.* at 7.

85. According to the most recent census data, non-Hispanic whites now constitute only 63 percent of the U.S. population and are declining. Hope Yen, *Census: White Majority in U.S. Gone by 2043*, NBC NEWS (June 13, 2013), *archived at* http://perma.cc/W593-M4PW. Thus, white males constitute only about 30 percent of the general population but hold nearly 75 percent of the board seats.

86. Fawn Lee, Note, *Show Me the Money: Using the Business Case Rationale to Justify Gender Targets in the EU*, 36 FORDHAM INT'L L.J. 1471, 1488 (2013).

87. *Id.* at 1492–94.

88. *Id.* at 1494–96.

Lawmakers in the U.S. recently acted to encourage diversity on corporate boards, among senior executives, and in the corporate world in general. In 2009, the SEC imposed disclosure requirements on public firms to state the role of diversity in the board nomination process.[89] More recently, federal banking regulators in the U.S. released a joint rulemaking initiative requiring virtually all financial institutions to embrace diversity pursuant to the Dodd-Frank Wall Street Reform and Consumer Protection Act[90] ("Dodd-Frank Act").[91] These recent legislative and regulatory changes supplement already-existing anti-discrimination law that indirectly encourages business leaders to embrace diversity.[92]

Lawmakers undertook these initiatives as a result of increased acceptance of a business rationale in support of diversity.[93] Diversity extends greater informational elaboration to firms.[94] More diverse boards can draw upon distinct perspectives and experiences.[95] As a result,

89. SEC Diversity Disclosure Rule, 17 C.F.R. § 229.407(c)(2)(vi) (2011); Proxy Disclosure Enhancements, 74 Fed. Reg. 68,334 (Dec. 23, 2009) (requiring disclosure of diversity policies in corporations).

90. Pub. L. No. 111-203, 124 Stat. 1376 (2010).

91. Proposed Interagency Policy Statement Establishing Joint Standards for Assessing the Diversity Policies and Practices of Entities Regulated by the Agencies and Request for Comment, 78 Fed. Reg. 64052 (Oct. 25, 2013). *See also* Dodd-Frank Act § 342 (codified at 12 U.S.C. § 5452(a)(1)).

92. *See* Faragher v. City of Boca Raton, 524 U.S. 775, 780 (1998) (holding that "an employer is vicariously liable for actionable discrimination caused by a supervisor, but subject to an affirmative defense looking to the reasonableness of the employer's conduct as well as that of a plaintiff victim"). Naturally, policies that impose and enforce an obligation to embrace diversity upon all employees would satisfy the affirmative defense articulated in *Faragher*. *See* El-Bakly v. Autozone, Inc., No. 04 C 2767, 2008 WL 1774962 at *12 (N.D. Ill. 2008) ("Given the law in this area, the Court agrees that the signed diversity mission statements are relevant to a potential affirmative defense for Defendant AutoZone, because they might support a finding that Defendant AutoZone exercised reasonable care to prevent and correct promptly the harassing behavior.").

93. *E.g.*, Toyah Miller & María del Carmen Triana, *Demographic Diversity in the Boardroom: Mediators of the Board Diversity—Firm Performance Relationship*, 46 J. MGMT. STUD. 755, 755 (2009) (finding in a sample of Fortune 500 firms "a positive relationship between board racial diversity and both firm reputation and innovation. We find that reputation and innovation both partially mediate the relationship between board racial diversity and firm performance. In addition, we find a positive relationship between board gender diversity and innovation."); Niclas L. Erhardt et al., *Board of Director Diversity and Firm Financial Performance*, 11 CORP. GOVERNANCE 102, 102 (2003) ("Correlation and regression analyses indicate board diversity is positively associated with these financial indicators of firm performance.").

94. Of course, cognitive diversity and information elaboration is not limited to diverse cultural perspectives or experiences associated with race or gender. *See, e.g.*, Lubomir P. Litov et al., *Lawyers and Fools: Lawyer-Directors in Public Corporations*, 102 GEO. L.J. 413 (2014) (finding that lawyer-directors add diversity to the board, give the board access to more elaborate information, and thereby add value).

95. Miller & del Carmen Triana, *supra* note 93, at 775 ("These findings suggest that firms may benefit from the diverse human and social capital on diverse boards . . . because racial and gender diversity (proxies for richness of information in the decision-making process) are both related to innovation.") (citations omitted).

diversity enjoys a powerful association with innovation.[96] Diversity logically operates to effectively counter groupthink as well as affinity bias and thereby proves to be particularly relevant in the boardroom.[97] More diverse groups often hold dissimilar views, even on basic issues such as risk.[98] Although, as might be expected, evidence is not uniform, there is strong empirical evidence that supports the tangible business benefits of diversity in the boardroom.[99]

Notwithstanding the empirical strength of the business case for diversity in the boardroom, mainstream corporate law casebooks ignore the issue altogether.[100] Finance and economics scholars research and write about diversity, and many reports support diversity in the corporate boardroom. However, the authors and publishers of mainstream casebooks simply omit this discourse.[101] The authors of these texts overlook the actions of the SEC,[102] the federal banking authorities,[103] Congress,[104] and other lawmaking bodies to improve diversity in U.S. corporate boardrooms and the public sector.[105] The leading corporate law texts

96. Mariateresa Torchia et al., *Women Directors on Corporate Boards: From Tokenism to Critical Mass*, 102 J. BUS. ETHICS 299, 299 (2011) (conducting tests on 317 Norwegian firms and finding "that attaining critical mass—going from one or two women (a few tokens) to at least three women (consistent minority)—makes it possible to enhance the level of firm innovation.").

97. Regina F. Burch, *Worldview Diversity in the Boardroom: A Law and Social Equity Rationale*, 42 LOY. U. CHI. L.J. 585, 594 (2011) ("This Article proposes that greater worldview diversity on corporate boards may lead to better governance and mitigate bias and unfairness in corporate decision making.").

98. *Id.* at 610 (citing Dan M. Kahan et al., *Culture and Identity-Protective Cognition: Explaining the White-Male Effect in Risk Perception*, 4 J. EMPIRICAL LEGAL STUD. 465, 466 (2007)).

99. *Compare* CREDIT SUISSE RESEARCH INSTITUTE, GENDER DIVERSITY AND CORPORATE PERFORMANCE 12 (2012) (finding enhanced board diversity was associated with a 26 percent gain in corporate valuation from 2005 to 2012), *with* Lissa Lamkin Broome & Kimberly D. Krawiec, *Signaling Through Board Diversity: Is Anyone Listening?*, 77 U. CIN. L. REV. 431, 433–34 (2008) (discussing gaps in empirical evidence of business benefits). Diversity gains seem particularly robust when a board achieves a critical mass of diverse directors rather than just tokenism. *E.g.*, Jasmin Joecks et al., *Gender Diversity in the Boardroom and Firm Performance: What Exactly Constitutes a "Critical Mass?"*, 118 J. BUS. ETHICS 61 (2013) (finding evidence that critical mass of gender diversity is associated with higher financial performance).

100. *See* EISENBERG & COX, *supra* note 7, at 1470–71, 1472, 1482 (failing to mention diversity or demographic characteristics of board or management in index); O'KELLEY & THOMPSON, *supra* note 7, at 1169–75 (same); CHOPER ET AL., *supra* note 7, at 1157–1170 (same); KLEIN ET AL., *supra* note 7, at 895–928 (same); EPSTEIN ET AL., *supra* note 7, at 635–39 (same).

101. *See* Fields & Keys, *supra* note 6.

102. *See supra* note 89.

103. *See supra* note 91.

104. Dodd-Frank Act, Pub. L. No. 111-203 § 342 (2010) (codified at 12 U.S.C. § 5452(a)(1)).

105. Not one of the leading texts studied even mentions the word diversity either in the context of the corporate boardroom or as important from a profit maximizing perspective. *See* EISENBERG & COX, *supra* note 7, at 1470, 1485; CHOPER ET AL., *supra* note 7, at 1160–61; O'KELLEY & THOMPSON, *supra* note 7, at 1169–1175; EPSTEIN ET AL., *supra* note 7, at 147–57; KLEIN ET AL., *supra* note 7, at

certainly need not accept uncritically the benefits of diversity; but completely ignoring the debate as if it is nonexistent does a disservice to both law students and a society mired in racial privilege and disempowerment.[106] Indeed, these texts implicitly accommodate the racial pseudo-science of yesteryear that white male domination is not just acceptable but natural and unworthy of critique or analysis.

While each of the leading corporate casebooks disregards critical assessment of corporate leadership and diversity goals, there are some meager exceptions. To its credit, the *Choper* text *Cases and Material on Corporations* at least acknowledges that the boardrooms of public firms in America may be culturally monolithic.[107] But even *Choper* fails to discuss any reason for this continued exclusion of diverse voices from the boardroom or critically examine why this remains true in the modern U.S. economy.[108] Students are given no context for this homogeneity, no evidence demonstrating the benefits of diversity, and are essentially invited to conclude that white male supremacy is simply the natural order of American society.[109] At the very least there is a manifest failure of the primary business law text authors to voice any objection to the continued over-representation of white males in the boardroom.[110]

895–928. Compare this absence of discussion with the actual approach of the financial world. Barclay's recently launched an investment fund that seeks to capitalize upon the financial edge enjoyed by diverse firms. Michael Leibel, *Barclays Launches Women in Leadership Index and ETNs*, REUTERS (July 9, 2014), *archived at* http://perma.cc/YAA5-JW9W.

106. As Professor Wade highlights:

> In the business setting, the equitable treatment of women and people of color depends on the commitment of corporate officers, directors, managers, and senior executives, almost all of whom are white and male. In spite of the difficulties inherent in discussing racism and sexism, it is important that the discourse not occur among women and people of color only. Whites and men must participate, and the discourse should start in law-school classes about business and corporate governance.

Cheryl L. Wade, *Teaching Gender as a Core Value in Business Organizations Class*, 36 OKLA. CITY U. L. REV. 545, 549 (2011).

107. CHOPER ET AL., *supra* note 7, at 10 (stating that boards remain populated "primarily" by white males).

108. *Id.*

109. *Id.*

110. Progressive corporate law scholars have long argued that the continuation of white male supremacy at the apex of the public corporation is totally without justification and that diversity is associated with a variety of business justifications. *See, e.g.*, DOUGLAS M. BRANSON, NO SEAT AT THE TABLE: HOW CORPORATE GOVERNANCE AND LAW KEEP WOMEN OUT OF THE BOARDROOM 151 (2007) ("The scarcity of women in corporate governance roles is curious, because women have been entering the professional and managerial ranks in great numbers for nearly three decades now."); Lisa M. Fairfax, *Board Diversity Revisited: New Rationale, Same Old Story?*, 89 N.C. L. REV. 855, 884 (2011) ("However, the empirical evidence suggests that the increased reliance on the business case has not translated into any appreciable gains in board diversity. Instead, there has been a relative stagnation in board diversity efforts even as more corporations and regulators appear willing to

The *Klein* text *Business Associations: Cases and Materials on Agency, Partnership, and Corporations*, arguably the most widely adopted Business Associations textbook on the market, makes no mention of diversity or the fact that board and executive leadership is dominated by privileged white males.[111] By ignoring this important corporate governance issue, the *Klein* authors leave law professors who adopt their text completely adrift on this matter, forcing them to manufacture meaningful classroom conversation in connection with diversity in the boardroom and its proper place in corporate governance policymaking.[112] Most professors using this text are forced to leave the subject unconsidered and students uninformed.

The *O'Kelley* business law text, *Corporations and Other Business Associations: Cases and Materials*, potentially opens a door to concrete discussion of board and executive makeup in connection with race and gender, but then slams the door abruptly by eschewing the opportunity to critically assess the monolithic makeup of corporate leadership.[113] Disappointingly, the text pays only passing lip service to gender diversity by describing the CEO as "she" when differentiating between officers and directors, no doubt well understanding that only 22 of Fortune 500 CEOs (4 percent) are female.[114] The text, however, provides no further critical analysis as to why the corporate boardrooms and corner offices continue to be dominated by entrenched white males in the United States.[115]

None of the other leading corporations' texts mentions the domination of white males at the apex of the public firm, the potential benefits of cultural and worldview diversity, or the manifest costs of the corporations' presumed racially neutral structures.[116] Exacerbating the problem of white

---

rhetorically embrace the business case."); Lissa Lamkin Broome, *The Corporate Boardroom: Still a Male Club*, 33 J. CORP. L. 665, 679–80 (2008) ("Too often, directors follow the path of least resistance and nominate their acquaintances with whom they feel comfortable and these candidates necessarily often resemble the incumbent directors in terms of gender, race, social status, background, and experience."); Marleen A. O'Connor, *The Enron Board: The Perils of Groupthink*, 71 U. CIN. L. REV. 1233, 1241 (2003) (arguing that diversity can stem groupthink which arises from homogeneity).

111. *See* KLEIN ET AL., *supra* note 7, at 907–09.

112. Law professor adopters of *Klein* are seemingly forced to shoehorn considerations of board diversity into existing text sections on board duties (Chapter 5), including perhaps the duty of care. One can imagine how this results in awkward syllabus construction and, at many times, leaves students with the false impression that the subject is unimportant or *ultra vires* for purposes of corporate law study. This has been the experience of two authors of this Article, and likely countless law professors around the country.

113. *See* O'KELLEY & THOMPSON, *supra* note 7, at 150–51.

114. ZWEIGENHAFT & DOMHOFF, *supra* note 47, at xii.

115. *See* O'KELLEY & THOMPSON, *supra* note 7, at 151.

116. *See supra* note 100.

male domination in the corporate boardroom is the new electioneering power granted this powerful, but culturally monolithic, group by the Supreme Court of the United States in *Citizens United*. Indeed, the upper echelons of the public corporation may well qualify as one of the most enduring bastions of white male supremacy in the U.S.

III. *CITIZENS UNITED* AND THE NEW POLITICAL POWER OF THE PUBLIC FIRM

On January 10, 2010, the United States Supreme Court rendered its decision in *Citizens United v. Federal Election Commission*.[117] The Court ruled that corporations enjoy the same free speech rights as individuals, and therefore, governmental restrictions on a corporation's political speech must survive strict scrutiny, the most demanding level of judicial review of governmental actions.[118] More specifically, the Court held that corporations are entitled to first amendment free speech protections, and as a result, corporate money spent on political electioneering independent of a campaign cannot be limited by campaign finance restrictions.[119] Previously, corporate funds could not be used for electioneering purposes, forcing CEOs and corporate leaders to finance politicking for their chosen candidates from their own capital (typically through Political Action Committees ("PACs")).[120] Now, CEOs and corporate leadership can essentially use corporate monies in an unfettered manner to campaign for and help elect the political candidates of their choice.[121]

---

117. 558 U.S. 310 (2010).

118. *Id.* at 342–43.

119. *Id.* at 372 (holding 2 U.S.C. § 441b's restriction of corporate independent electioneering expenditures unconstitutional). The Court ultimately overruled two of its precedents on this point. *Id.* at 365–66. The statutory section found unconstitutional was part of the Bipartisan Campaign Reform Act of 2002. Pub. L. No. 107-155, 116 Stat. 81 (codified in scattered sections of 2, 8, 18, 28, 36, and 47 U.S.C).

120. *See generally* Bret Shaw, Note, It's the End of the World as We Know It (And I Feel Fine)*: How Comparative Campaign Finance Suggests that* Citizens United *May Not Be the End of the World . . . and that the United States Should Consider Other Policy Alternatives*, 31 ARIZ. J. INT'L & COMP. L. 159, 161–64 (2014) (describing the evolution of regulating corporate political activity).

121. Shareholders have no power to influence the management of the corporation under state law and are generally limited to voting for directors. *See, e.g.*, DEL. CODE ANN. tit. 8, § 141(a) (2011) ("The business and affairs of every corporation organized under this chapter shall be managed by or under the direction of a board of directors . . . ."); DEL. CODE ANN. tit. 8, § 211(b) (2011) ("[A]n annual meeting of stockholders shall be held for the election of directors . . . ."). High profile corporate law experts almost immediately attacked the Court's decision because it misapprehended the nature of the corporation as an instrument of public policy with no inherent powers not ceded by the state for public purposes. *See, e.g.,* Robert A.G. Monks, *Corporate Governance Redux in the Light of* Citizens United, HARV. L. SCH. F. ON CORP. GOVERNANCE & FIN. REG. (May 7, 2010, 9:24 AM), *archived at* http://perma.cc/JG2T-9YL5.

This change in law represents a massive transfer of political power from ordinary citizens to the CEOs of the most colossal capital aggregations in the history of the world.[122] Modern public corporations in America hold value approaching $20 trillion.[123] One U.S. Senator stated that the *Citizens United* ruling has moved the U.S. toward an economic and political oligarchy whereby a small handful of "billionaire families" control the economy and political system.[124] Another former Senator reflected upon the scale of resources available to public corporations and described the decision's implications as "scary."[125] A leading election law scholar called the day the opinion was issued "a very bad day for American democracy."[126]

CEOs' power over the political activities of the corporation is now unlimited. Surprisingly, there is no mandatory disclosure obligation of a public firm's political activities.[127] There is no enforceable mandate that the CEO consider shareholder interests when deploying for political ends the extraordinary capital available to the public firm.[128] It is virtually

---

122. *See* Douglas M. Spencer & Abby K. Wood, Citizens United, *States Divided: An Empirical Analysis of Independent Political Spending*, 89 IND. L.J. 315, 316 (2014) ("Indeed, during the 2012 federal election cycle, independent spending related to all federal races exceeded $1 billion, which was approximately three times more than spending in 2008 and approximately six times more than spending in 2004."). Professors Spencer and Wood examined those states whose election laws were most affected by *Citizens United*. They found that independent corporate electioneering expenditures in state elections since *Citizens United* doubled. *Id.* at 361 ("[W]e . . . systematically examined the effect of [*Citizens United*] on spending at the state level. We found that independent spending increased at twice the rate in states whose laws were affected by the decision.").

123. The current total market value of publicly traded firms in the US amounts to $19.8 trillion. WILSHIRE, THE WILSHIRE 5000 TOTAL MARKET INDEX: FUNDAMENTAL CHARACTERISTICS, http://web.wilshire.com/Indexes/Broad/Wilshire5000/Characteristics.html (last visited Dec. 4, 2014), *archived at* http://perma.cc/T5MS-DXRK.

124. Natasha Bach, *Bernie Sanders: Citizens United Is Creating An 'Oligarchic Form Of Society'*, HUFF. POST (Mar. 27, 2014, 6:04 PM), *archived at* http://perma.cc/5Q95-KN97.

125. Bob Kerrey, *The Senator from Exxon-Mobil?*, HUFF. POST (Mar. 23, 2010, 5:12 AM), *archived at* http://perma.cc/8BEP-R5W3 ("With $85 billion in profits during the 2008 election, Exxon Mobil would have been able to fully fund over 65,000 winning campaigns for U.S. House or outspend every candidate by a factor of 90 to 1. That's a scary proposition when you consider that the health of our planet is at stake.").

126. Rick Hasen, Citizens United: *What Happens Next?*, HUFF. POST (Mar. 23, 2010, 5:12 AM), *archived at* http://perma.cc/JX92-VMGB.

127. Delaware law fails to even authorize political expenditures much less regulate them. *See* DEL. CODE ANN. tit. 8, § 122 (2011) (detailed listing of corporate powers without authorizing political contributions and activities).

128. At best, the campaign expenditures and political activity of a CEO is subject to review only under the very promiscuous business judgment rule, which only imposes fiduciary duty liability for gross negligence—meaning egregious, near intentional wrongdoing. *See, e.g.*, Smith v. Van Gorkom, 488 A.2d 858 (Del. 1985) (imposing liability upon finding that the CEO negotiated sale of company without authority from board, settled upon a price without basis and without expert analysis, signed

impossible for shareholders to hold corporate leaders accountable in this context, even if executives put their personal interests before those of the corporation and its shareholders. In order to enforce fiduciary duties owed to the corporation, a shareholder must proceed derivatively and can generally only do so upon a showing of bad faith.[129] Indeed, state law provisions that effectively abolished the duty of care for most public corporations fail to provide means to hold directors accountable even when they act recklessly.[130] These statutes typically require a showing of "conscious disregard" of duty.[131] Thus, the Supreme Court through *Citizens United* expanded the power of CEOs, already insulated under statutory law, to use shareholder wealth—and to thereby coerce shareholder speech—to further management's political goals with little or no accountability.[132]

In fact, while state law generally takes great care to delineate the power of the corporation, those powers generally do not include the power to

---

merger agreement without reading document, and failed to assure that board conditions to transaction were properly secured).

129. *See, e.g.*, Stone v. Ritter, 911 A.2d 362, 373 (Del. 2006) ("Accordingly, we hold that the Court of Chancery properly . . . dismissed the plaintiffs' derivative complaint for failure to excuse demand by alleging particularized facts that created reason to doubt whether the directors had acted in good faith in exercising their oversight responsibilities."); Beam *ex rel.* Martha Stewart Living Omnimedia, Inc. v. Stewart, , 1044, 1054 n.37 (Del. 2004) (quoting Aronson v. Lewis, 473 A.2d 805, 815 (Del. 1984) ("[I]n the demand context even proof of majority ownership of a company does not strip the directors of the presumptions of independence, and that their acts have been taken in good faith and in the best interests of the corporation. There must be coupled with the allegation of control such facts as would demonstrate that through personal or other relationships the directors are beholden to the controlling person.")) (dismissing derivative action).

130. *E.g.*, DEL. CODE ANN. tit. 8, § 102(b)(7) (2011) (authorizing an exculpatory provision in a corporation's articles of incorporation for money damages for "acts or omissions not in good faith or which involve intentional misconduct or a knowing violation of law"). *See also* Lawrence A. Hamermesh, *Why I Do Not Teach* Van Gorkom, 34 GA. L. REV. 477, 490 (2000) (finding that 98% of sampled Fortune 500 companies that incorporated under state laws that permit insulation of directors for duty-of-care liability had adopted insulating charter provisions, and that 100% of Delaware firms sampled had adopted such provisions).

131. *In re* Walt Disney Co. Derivative Litig., 906 A.2d 27, 63, 67 (Del. 2006) (holding that a "conscious disregard of one's responsibilities" shows bad faith for purposes of director liability).

132. *See* discussion of CEO primary *infra* Part IV. *See also* Miller, *supra* note 8, at 91. In his opinion, Justice Stevens articulated the point:

> It is an interesting question "who" is even speaking when a business corporation places an advertisement that endorses or attacks a particular candidate. Presumably it is not the customers or employees, who typically have no say in such matters. It cannot realistically be said to be the shareholders, who tend to be far removed from the day-to-day decisions of the firm and whose political preferences may be opaque to management. Perhaps the officers or directors of the corporation have the best claim to be the ones speaking . . . .

Citizens United v. Fed. Election Comm'n, 558 U.S. 310, 467 (Stevens, J., concurring in part, dissenting in part).

influence politicians and elections.[133] Only the U.S. Supreme Court endows these artificial legal fictions with such power.[134] Historically, the corporation existed as a matter of the state's imperative to facilitate macroeconomic growth.[135] This implied concentrated economic power, and legislatures exercised caution accordingly, limiting the power of the corporation by imposing limits on its duration, number of shareholders, capitalization, and powers.[136] There is no evidence, however, that at the framing of the U.S. Constitution anyone contemplated that the corporation would act as a key political player that is controlled almost entirely by the CEO.[137]

Noted constitutional law scholars have raised important objections to allowing CEOs to plumb shareholder wealth to fund their political objectives.[138] They note that the Supreme Court's expansion of the power of corporate managers to use shareholder wealth for management's political agenda is at odds with the Court's insistence that unions be deprived of the same power with respect to union members.[139] These scholars also recognize that the Court could have easily resolved the compelled speech issue with respect to shareholders simply by mandating institutional assurances that shareholders have some voice in the expenditure of their wealth by corporate leadership for political

133. *See, e.g.*, DEL. CODE ANN. tit. 8, § 122 (2011).

134. Leading texts of decades past wrestled only with the charitable donations that corporations made and did not contemplate them as political actors. LATTIN, *supra* note 32, at § 64. Indeed, the nature of the historic roots of the corporation was that the sovereign dispensed concessions to the corporation as its creator and that these could contravene constitutional rights. *Id.* § 174–75.

135. Thus, corporations existed in England and the American colonies to generate revenue for the government and assist in the creation of infrastructure such as bridges, roads, ferries, wharfs, banks, water suppliers and other basic public goods. *Id.* § 175.

136. *Id.* § 54.

137. Prior to the Constitution only about 30 special purpose corporations even existed in the American colonies. HENN & ALEXANDER, *supra* note 32, at 24. General incorporation statutes did not appear until 1795 (with many restrictions) and broad general business corporations did not exist until the late 19th century. *Id.* at 24–27. *See also* Carol R. Goforth, *"A Corporation Has No Soul"—Modern Corporations, Corporate Governance, and Involvement in the Political Process*, 47 HOUS. L. REV. 617, 659 (2010) ("Given the accepted notion that the Framers were indeed concerned with individual rights, they never would have contemplated giving [modern public corporations] free speech rights.").

138. *See, e.g.*, Catherine L. Fisk & Erwin Chemerinsky, *Political Speech and Association Rights After* Knox v. SEIU, Local 1000, 98 CORNELL L. REV. 1023, 1024–25 (2013) ("When the Supreme Court held in *Citizens United v. FEC* that corporations have a First Amendment right to make unlimited, independent campaign expenditures, it dismissed in a few sentences the idea that the corporate leadership's use of corporate resources on politics might infringe the rights of dissenting shareholders.").

139. *Id.* at 1026 ("The dissimilar treatment of unions as compared to almost all other organizations for purposes of the compelled speech restriction on associational free speech rights cannot be justified by law or logic.").

purposes.[140] Instead, the Court's mandate that state-created artificial entities enjoy First Amendment speech rights to spend shareholder money for electioneering simply shifted massive political power to CEOs.

The Supreme Court's holding in *Citizens United* invited leading corporate law scholars to address the issue of compelled speech of shareholders and the crafting of innovative structural adaptations to address this issue. Some scholars answered the call admirably.[141] These commentators urge more robust accountability of managers, under traditional fiduciary duties, for political expenditures.[142] Fundamentally, however, the issue is a more urgent incarnation of a longstanding corporate governance and shareholder concern: "how to ensure that [a] corporation['s] political activities are actually in the interest of shareholders."[143]

Consider the observations made in the preceding paragraphs along with the dearth of women or minority leaders who are CEOs or on boards of Fortune 500 companies. It becomes clear that the new political and economic power granted to CEOs and boards by *Citizens United* is simply a grant of additional power to entrenched white males and the white male perspective that has dominated economic policy in the United States for so long.[144] Put simply, the Supreme Court transferred power from the diverse body politic as a whole to a small handful of non-diverse corporate elites.

Consider also one disturbing example of a CEO's abuse of the power given to corporate executives under *Citizens United.* The CEO of Massey Coal in West Virginia hand-picked a West Virginia Supreme Court judicial candidate, used corporate funds to see him elected, and then reaped the reward when that judge cast the deciding vote in a case that spared Massey Coal from a $50 million verdict for allegedly interfering

140. *Id.* at 1023 ("Nor does it consider what kinds of internal organizational governance mechanisms are necessary to ensure a fair allocation of speech protections between those who wish the organization to promote one message and those who wish it to promote another.").

141. *See, e.g.*, Lucian A. Bebchuk & Robert J. Jackson, Jr., *Corporate Political Speech: Who Decides?*, 124 HARV. L. REV. 83, 117 (2010) ("We have put forward rules based on a combination of shareholder voting, oversight by independent directors, and detailed transparency requirements that include robust disclosure of spending through intermediaries.").

142. *See, e.g.*, William Alan Nelson II, Esq., *Post-*Citizens United*: Using Shareholder Derivative Claims of Corporate Waste to Challenge Corporate Independent Political Expenditures*, 13 NEV. L.J. 134, 155–67 (2012); Jonathan Romiti, Note, *Playing Politics with Shareholder Value: The Case for Applying Fiduciary Law to Corporate Political Donations Post-*Citizens United, 53 B.C. L. REV. 737, 769–73 (2012).

143. James Kwak, *Corporate Law Constraints on Political Spending*, 18 N.C. BANKING INST. 251, 253 (2013).

144. *See* cummings, *supra* note 8, at 108.

tortiously in a business relationship.[145] The *Citizens United* decision has enabled CEOs to select and elect state judges who are amenable to the business law policies favored by the CEOs.[146]

Most business law textbooks fail to question or even mention the political role of the corporation, the recent expansion of that role, the fact that the expansion enjoys a weak state law basis, and the implications in terms of CEO power arising from the expanded political role of the public firm. The *Eisenberg* text mentions the *Citizens United* case immediately following materials concerning corporate power to make charitable contributions, but it offers no explicit opportunity to critique or analyze the expansion of corporate political power.[147] The text also raises corporate governance questions regarding corporate political activity but does not attempt to spark discussion about whether such activity is something that corporations should pursue.[148] The *Choper*, *O'Kelley*, *Epstein*, and *Klein* texts all fail to mention or make reference to *Citizens United*.[149] Despite multiple entry points in the current corporate law canon, textbooks generally ignore the political role of the corporation.[150] These omissions make it difficult to have thoughtful classroom discussions on the proper political status of the public corporation or the role of the CEO in directing the prodigious spending of corporations for political purposes.

145. *Id.* at 99–102. *See also* Caperton v. A.T. Massey Coal Co., 556 U.S. 868 (2009) (holding that West Virginia Supreme Court of Appeals judge should have recused himself as matter of due process because president and CEO of corporation appearing before him contributed some $3 million to his election campaign following trial court's entry of $50 million judgment against corporation when it was likely that corporation would be seeking review in Supreme Court of Appeals).

146. *See* cummings, *supra* note 8, at 102–09; *see also* Michael H. LeRoy, *Do Partisan Elections of Judges Produce Unequal Justice when Courts Review Employment Arbitrations?*, 95 IOWA L. REV. 1569 (2010).

147. EISENBERG & COX, *supra* note 7, at 267.

148. *Id.* The Supreme Court's decision in *Hobby Lobby* provides another important illustration of the judiciary's acquiescence to the arguably unreasonable expansion of corporate power and influence. The Court held that the religious beliefs of the owners of small family-owned businesses could be attributed to the corporation itself. Burwell v. Hobby Lobby Stores, Inc., 573 U.S. ___ (2014) (holding that corporations could not be compelled by law to do anything they find religiously objectionable). A group of corporate lawyers and professors signed onto an amicus brief explaining that this holding eviscerated the fundamental notion in corporate law that a corporation is an entity or person that is separate from its owners or shareholders. Brief of Corporate and Criminal Law Professors as Amici Curiae Supporting Petitioners, *Hobby Lobby*, 573 U.S. ___ (2014) (Nos. 13-354, 13-356), 2014 WL 333889.

149. *See* CHOPER ET AL., *supra* note 7, at 1130; O'KELLEY & THOMPSON, *supra* note 7, at 1164; EPSTEIN ET AL., *supra* note 7, at xxi; KLEIN ET AL., *supra* note 7, at xxiv.

150. *See* Michael D. Guttentag, *Teaching* Citizens United v. FEC *in the Introductory Business Associations Course*, 8 J. BUS. & TECH. L. 163, 165–66 (2013) (arguing that *Citizens United* can be integrated into the typical Business Associations course when discussing shareholder primacy, agency costs between managers and owners, and when discussing the risk management role of transactional attorneys).

This kind of discussion can occur only if supplemental material is assigned. Thus, at a time when high-profile commentators demonstrate that America has devolved into an aristocracy of CEOs, students will be ill-equipped to assess whether the new political power of the CEO contributes to this new reality.[151]

IV. CEO PRIMACY AND AMERICA'S NEW ECONOMIC ROYALTY

Noticeably missing from all major business law texts is a discussion connecting the reckless mismanagement of many corporate leaders with the mortgage crisis of 2008. After the financial crisis of 2007-2009, many experts and commentators concluded that CEOs and senior executives at major financial firms received excessive compensation for pursuing reckless lending and investment activities, which led to catastrophic losses for the firms and huge paydays for senior executives.[152] In fact, the head of the Office of the Comptroller of the Currency ("OCC"), which supervises all national banks and federally chartered thrifts, concluded that underlying the entire debacle was "the worst mortgage underwriting in our nation's history."[153] These reckless mortgages added huge risks to an already over-leveraged financial sector, meaning that small losses could

151. *See* Robert J. Samuelson, *The CEO Aristocracy: Big Bucks for the Big Boss*, WASH. POST, June 22, 2014, *archived at* http://perma.cc/83DM-JBZV.

152. *E.g.*, Claire A. Hill & Brett H. McDonnell, *Reconsidering Board Oversight Duties After the Financial Crisis*, 2013 U. ILL. L. REV. 859, 859–60 ("The financial crisis helps make the case that boards should do more monitoring. Corporate behavior in the crisis yielded enormous negative externalities for the greater society. Corporations were able . . . [to] incentivize risky behavior that yields negative externalities, [so] it seems appropriate that boards do more to prevent the abuse of [limited liability]."); Lucian A. Bebchuk et al., *The Wages of Failure: Executive Compensation at Bear Stearns and Lehman 2000–2008*, 27 YALE J. ON REG. 257, 257–60 (2010) (finding that "the top executive teams of Bear Stearns and Lehman" derived billions in compensation, "exceed[ing] the value of the executives' [stock] holdings at the beginning of the period," such that "the bottom-line payoffs of these executives during 2000–2008 were not negative but rather decidedly positive."); Kenneth R. Davis, *Taking Stock—Salary and Options Too: The Looting of Corporate America*, 69 MD. L. REV. 419, 419–20 (2010) ("Too many managers appointed to protect the interests of shareholders are looting their companies. . . . Even in 2008, a year of shriveling corporate profits and plummeting stock prices, more CEOs saw pay increases than cuts. Despite the ravages of the financial crisis, average CEO pay in 2008 declined only modestly."); Morgenson, *supra* note 74 ("Executives at seven major financial institutions that have collapsed, were sold at distressed prices or are in deep to the taxpayer received $464 million in performance pay since 2005. . . . Yet these firms have reported losses of $107 billion since 2007 . . . . And $740 billion in stock market value has been lost since these companies' shares peaked in 2007, just before the housing bubble burst.").

153. John C. Dugan, Comptroller of the Currency, Office of the Comptroller of the Currency, Remarks Before the Exchequer Club 6 (July 21, 2010), *available at* http://www.occ.gov/news-issuances/speeches/2010/pub-speech-2010-84a.pdf ("[T]he recent financial crisis was caused by a number of factors . . . [including,] at the heart of it all, the worst mortgage underwriting in our nation's history.").

wipe out equity and lead to mass insolvency.[154] All of this led to massive losses for shareholders and the economy at large.[155] CEOs essentially manipulated risk to pump up short-term profits, saddling the entire financial sector with a very high probability of systemic failure.[156] The FCIC confirmed that compensation rewarded high-risk short-term gains and resulted in long-term threats to firms' financial viability.[157] Little mention of this lethal mismanagement is included in major business law texts today, even though they may include extended discussions of compensation issues.[158] It is as if the crisis simply did not happen, or corporate governance played no role—and these texts foreclose any debate

---

154. As the FCIC explains:

> By one measure, [the five major investment banks'] leverage ratios were as high as 40 to 1, meaning for every $40 in assets, there was only $1 in capital to cover losses. Less than a 3% drop in asset values could wipe out a firm. To make matters worse, much of their borrowing was short-term, in the overnight market—meaning the borrowing had to be renewed each and every day.

FCIC REPORT, *supra* note 26, at xix.

155. Losses from the crisis include lost wealth of $9 trillion and foregone GDP could approach $10 trillion. *See* U.S. GOV'T ACCOUNTABILITY OFFICE, *supra* note 26.

156. *See supra* notes 9 and 10 and accompanying text. *See also* Raghuram Rajan, *Bankers' Pay is Deeply Flawed*, FIN. TIMES, Jan. 8, 2008, at 11, *available at* http://us.ft.com/ftgateway/superpage.ft?news_id=fto010920081142101282 ("[U]nless we fix incentives in the financial system we will get more risk than we bargain for. Unless bankers offer these better explanations, their enormous pay, which has been thought of as just reward for performance, will deservedly come under scrutiny."); Paul Krugman, *Banks Gone Wild*, N.Y. TIMES, Nov. 23, 2007, at A37, *available at* http://www.nytimes.com/2007/11/23/opinion/23krugman.html?_r=0 ("Executives are lavishly rewarded if the companies they run seem successful: last year the chief executives of Merrill and Citigroup were paid $48 million and $25.6 million, respectively. But if the success turns out to have been an illusion—well, they still get to keep the money.").

157. *See* FCIC REPORT, *supra* note 26, at xix ("Compensation systems . . . too often rewarded the quick deal, the short-term gain—without proper consideration of long-term consequences. Often, those systems encouraged the big bet—where the payoff on the upside could be huge and the downside limited. This was the case up and down the line—from the corporate boardroom to the mortgage broker on the street."). Both the Chair of the FDIC and the Chair of the SEC concurred in this basic conclusion. *Id.* at 64 (quoting SEC Chair Mary Schapiro: "Many major financial institutions created asymmetric compensation packages that paid employees enormous sums for short-term success, even if these same decisions result in significant long-term losses or failure for investors and taxpayers.").

158. Fed Chair Ben Bernanke explained just how lethal the risk manipulation was:

> As a scholar of the Great Depression, I honestly believe that September and October of 2008 was the worst financial crisis in global history, including the Great Depression. . . . [O]ut of maybe the . . . 13 of the most important financial institutions in the United States, 12 were at risk of failure within a period of a week or two.

Id. at 354. *See also* CHOPER ET AL., *supra* note 7, at xxv, 7–8, 647–49 (mentioning in short discussions scattered throughout the text the financial crisis as well as raising the possibility of risk manipulation to seek enhanced compensation and Congress' response to the problem in the form of the Dodd-Frank Act); O'KELLEY & THOMPSON, *supra* note 7, at xxv, 7–8, 248–49 (mentioning the financial crisis but failing to mention links to risk manipulation and compensation arrangements encouraging excessive risk).

on this point.[159] The problem of excessive executive compensation and incentives to manipulate risk continues to plague public firms, yet the subject is ignored in business law texts and classrooms.

To address the problem of excessive compensation, Congress included a provision within the Dodd-Frank Act that gave shareholders a "say on pay."[160] More precisely, the Act mandated that shareholders have an advisory vote on executive pay.[161] This precatory vote, however, has not been an effective mechanism for controlling CEO pay.[162] In the past two years since say on pay took effect, CEO pay has soared—in some cases exceeding $1 billion in a single year.[163] Executive compensation now stands at a level that exceeds pre-crisis highs.[164] The core problem is that say on pay lacks teeth—a no vote is next to meaningless. And when shareholders do approve high payouts it serves to encourage excessive pay.[165]

Progressive corporate law scholars have argued that the "say on pay" rules should have been an occasion for state courts to reinvigorate state fiduciary duty standards as a mechanism for imposing more effective corporate governance.[166] The prospects for this kind of change in any meaningful sense are dim at best.[167] Instead, this modest reform seems to have backfired as managers use shareholder votes to justify larger pay

159. *See, e.g.*, EISENBERG & COX, *supra* note 7, at 730–56 (discussing compensation but not financial crisis); CHOPER ET AL., *supra* note 7, at 131–54 (same).

160. *See* Dodd-Frank Act, Pub. L. No. 111-203 § 951, 124 Stat. 1376, 1899–1900 (2010) (codified at 15 U.S.C. § 78n-1 (2012)).

161. This was only the most recent federal effort to reign in corporate excesses. LOUIS LOSS, JOEL SELIGMAN ET AL., FUNDAMENTALS OF SECURITIES REGULATION 55–57 (6th ed. 2011) (historical overview of federal efforts to reign-in corporate excesses under the federal securities laws.).

162. Jesse Eisinger, *Ixnay on 'Say on Pay'*, PROPUBLICA (June 26, 2013, 12:00 PM), *archived at* http://perma.cc/JXR2-9T2B.

163. *See supra* notes 4 and 11 and accompanying text. The high end of CEO pay soared to unprecedented levels recently, as ten CEOs made over $100 million, and two made over $1 billion. Dina ElBoghdady, *Two CEOs Break a Billion-Dollar Record*, WASH. POST, Nov. 8, 2013, *archived at* http://perma.cc/4J94-29AF.

164. Eisinger, *supra* note 162.

165. *See* John Carney, *Why 'Say on Pay' Failed and Why That's a Good Thing*, CNBC (July 3, 2013, 6:00 AM), *archived at* http://perma.cc/PNU6-3F3D.

166. *See, e.g.*, Lisa M. Fairfax, *Sue on Pay: Say on Pay's Impact on Directors' Fiduciary Duties*, 55 ARIZ. L. REV. 1, 25 (2013).

167. The most significant corporate law jurisdiction, Delaware, continues to insist that senior managers of public firms hold immunity for misconduct short of intentional wrongdoing. It also seeks more risk in public firms while being incapable of comprehending that too much risk can pose lethal dangers to firms and the economy as a whole. *See In re* Citigroup Inc. S'holder Derivative Litig., 964 A.2d 106, 114 n. 6 (Del. Ch. 2009) ("[T]he threat of personal liability may discourage beneficial risk taking.").

packages.[168] In sum, the say on pay effort to control perverse compensation incentives is a bust.[169]

Another Dodd-Frank Act failure is the effort by Congress to reform proxy access so that shareholders could access management's proxy solicitation to nominate directors and run candidates against management's own selections.[170] The SEC attempted to implement the power Congress expressly gave it to allow shareholders expanded proxy access.[171] In *Business Roundtable v. SEC*,[172] the D.C. Circuit Court held that the SEC's effort to implement this part of Dodd-Frank was not valid because the SEC failed to perform an adequate cost-benefit analysis, and its rule was therefore arbitrary and capricious.[173] Consequently, in the public firm today, management still selects management, meaning that shareholder supervision is not possible and compensation soars ever higher.[174]

Despite broad consensus that perverse compensation incentives drove the financial crisis and the resulting Dodd-Frank legislation, corporate law textbooks largely ignore the links between compensation and the crisis.[175] For example, the *Klein* text declines a perfect platform to take up the issue of skewed corporate executive compensation when it examines *Disney*.[176] In that case, Disney shareholders sued the Disney board of directors for entering into an astonishing contract with former Disney President Michael Ovitz that turned out to pay Ovitz more money when he was terminated from the company without fault than it would have paid out

---

168. *See* Minor Myers, *The Perils of Shareholder Voting on Executive Compensation*, 36 DEL. J. CORP. L. 417, 461 (2011) ("Shareholder approval has the potential to insulate directors from criticism for compensation decisions, which may perversely lead directors at some firms to offer pay packages that are higher and less sensitive to performance than the current baseline.").

169. *See* Eisinger, *supra* note 162.

170. Dodd-Frank Act, Pub. L. No. 111-203 § 971 (codified as amended at 15 U.S.C. § 78n) (2012) (authorizing the SEC to adopt a proxy access rule).

171. Facilitating Shareholder Director Nominations, 75 Fed. Reg. 56,668, 56,753–76 (Sept. 16, 2010) (codified at 17 C.F.R. pt. 240.14a-11).

172. 647 F.3d 1144 (D.C. Cir. 2011).

173. *Id.* at 1148 ("We agree with the petitioners and hold the Commission acted arbitrarily and capriciously for having failed once again . . . adequately to assess the economic effects of a new rule.").

174. *See supra* notes 17–19. *See also* 17 C.F.R. 240.14a-8(i)(8) (2013) (allowing management to exclude shareholder proposals from management's proxy solicitation materials if the shareholder proposal relates to a director election). Thomas Piketty argues the ability of CEOs to set their own compensation (or have other CEOs set CEO pay) has caused an explosion in manager salaries leading to soaring inequality. PIKETTY, *supra* note 5, at 331–32.

175. *See supra* notes 9, 10, 152, 156 and 157.

176. *In re* Walt Disney Co. Derivative Litig., 907 A.2d 693 (Del. Ch. 2005), *aff'd sub nom.*, Brehm v. Eisner, 906 A.2d 27 (Del. 2006).

had he performed the life of his contract.[177] Ovitz took home close to $130 million for his fourteen months of service to Disney—roundly considered a failed tenure.[178] Noted commentators concluded that, in the end, the *Disney* litigation resulted in yet another judicial power transfer to CEOs to enter into dubious compensation arrangements with other officers.[179]

When presented with the opportunity to critically examine executive compensation and the perverse incentives that motivate executives to take excessive and reckless risks based on astonishing pay packages, the *Klein* text eschews the opportunity.[180] Rather, the text reads as if astonishing executive compensation is natural, even appropriate, and board members are rightly protected from shareholder inquiry if an excessive pay package is approved by a compensation committee and compensation expert.[181] The message is that corporate executives deserve the hundreds of millions of dollars of compensation, even if their tenure is deemed a failure.

While *Klein* fails to critically examine enormous executive-compensation payouts and the attendant consequences, it does take note of the Dodd-Frank Act's "say on pay" provisions to alert students to the fact that shareholders now have the right to take a periodic "non-binding" advisory vote on executive pay.[182] In noting that Dodd-Frank tries to address not only "Wall Street Banks" but also corporate compensation generally in the United States, *Klein* matter-of-factly reports that "[t]he results of the [say on pay] vote are not binding on the board of directors. Indeed, the Act makes clear that the vote shall not be deemed either to effect or affect the fiduciary duties of directors."[183]

As the *Klein* text is perhaps the most widely adopted Business Associations textbook in the United States, thousands of law students annually are given no critical analysis of executive compensation as currently practiced in corporate America, nor are they encouraged to think

177. *Disney*, 907 A.2d at 704.

178. *Brehm*, 906 A.2d at 35.

179. *See, e.g.*, Marc I. Steinberg & Matthew D. Bivona, *Disney Goes Goofy: Agency, Delegation, and Corporate Governance*, 60 HASTINGS L.J. 201, 230 (2008) ("The *Disney* case recognized Eisner's unilateral actual authority to terminate without cause the company's president, causing the issuance of a $130 million severance payment. This event took place with no board of director discussion or approval."). The judicial grant of arguably unreasonable levels of power to CEOs is embodied in the court's holding that the board of Disney acted in good faith and with no duty of care breach when they hired and fired Michael Ovitz.

180. KLEIN ET AL., *supra* note 7, at 374–90.

181. *Id.* at 389.

182. *Id.* at 390 (discussing Dodd-Frank pay reforms without any context regarding the financial crisis). This appears to be the only discussion of the financial crisis and the Dodd-Frank Act in *Klein*. *Id.* at 909.

183. *Id.* at 390.

about the possibility that executive compensation paradigms may have helped to precipitate the financial crisis.[184] One of the most controversial issues in corporate law today, excessive executive compensation and its manifest costs, is nearly invisible in one of the most widely adopted business law texts on the market.[185] Not only is the subject left unaddressed, but if a business law professor that uses the *Klein* text intends to examine executive compensation and the perverse incentives that motivate so many business leaders today, that professor is forced to supplement the text and bring in a significant amount of outside reading. This can alienate students, already burdened with significant amounts of work, and cause discordance for a professor who assigns materials some students may deem inappropriate because it is "not in the book."

No other mainstream business law textbook adequately considers the issue of excessive executive compensation insofar as the financial crisis and CEO power is concerned. There is a mention of excessive executive compensation in the *Epstein* text, but no serious critical consideration of it or link to the financial crisis.[186] No substantial discussion at all of links between excessive risk-taking incentives in executive compensation and the financial crisis appears in the *Choper* text,[187] the *Eisenberg* text[188] or

---

184. Inclusion of this topic in the text (or any topic discussed herein) obviously does not mean that the authors of the text endorse any particular position or that these professors teach any particular position. Instead, it only means that students may engage in thoughtful discussion on the topic if a given professor deems the topic worth the time given what else must be covered. *See* Joan MacLeod Heminway, *Teaching Business Associations Law in the Evolving New Market Economy*, 8 J. BUS. & TECH. L. 175, 190 (2013) (articulating four primary goals for the basic business organizations course: "(1) efficiently use available resources, (2) build from individual strengths, (3) meet institutional curricular and degree requirements, and (4) educate our students for the short-term and long-term demands of a business law or other practice in a rapidly changing legal employment and education setting"). With respect to the issue of the excessive compensation and the financial crisis, lawmakers, influential commentators and a consensus of economists concluded that excessive compensation was "partly responsible for the financial crisis." John Cassidy, *Wall Street Pay: Where's the Reform?*, NEW YORKER, July 23, 2010, *archived at* http://perma.cc/N2JN-F9R4. Thus, future business leaders should at least hold the possibility of an unencumbered discussion of the issue.

185. *See supra* note 182.

186. EPSTEIN ET AL., *supra* note 7, at 261–70, 311–12, 315–18 (discussing the financial crisis but failing to link executive compensation to excessive risk and risk manipulation). *See also id.* at 658 (discussing how the business judgment rule operates to protect subprime mortgage investments in Delaware).

187. The *Choper* text includes a credible discussion on the power of CEOs and executive compensation. CHOPER ET AL., *supra* note 7, at 5–17, 131–35, 142–44, 533–38. *Choper* also footnotes a reference to potential director liability for investment in subprime mortgages, but with no discussion of the role of such lax oversight in the financial crisis of 2008. *Id.* at 98 n.44, 139 n.101. As previously demonstrated, while the *Choper* text does in fact mention excessive risk taking and perverse compensation incentives during the financial crisis, no student would have any clue that numerous experts and legal inquiries target these factors as a key driver of the crisis. *Id.* at xxv, 7–8, 647–49 (mentioning in short discussions scattered throughout the text the financial crisis as well as raising the

the *O'Kelley* text.[189] Leading corporate law professors who draft the most adopted business law textbooks in the country provide no assessment of the verdict of the FCIC, Nobel laureates, or a wide array of other economists that corporate law allows CEOs to pillage their firms to attain massive compensation payments.

Excessive CEO compensation has now figured prominently in a series of corporate fiascos this century. First, in 2001–2002, a battery of public firms collapsed amid accounting frauds rooted in efforts by senior managers to increase their options-based compensation.[190] Second, in 2006, options back-dating emerged as another way for CEOs to take for themselves millions of dollars from shareholders.[191] Third, during the subprime debacle, senior executives received huge incentive-based compensation payments for manipulating risk, even though these risks ultimately sank the entire financial sector and led to the Great Financial Crisis of 2007–2009.[192] The costs of this misconduct are measured in the trillions.[193]

Yet, perhaps the greatest cost of CEO dominance is not the occasional massive macroeconomic disruption implicit in financial crises. Instead, CEO primacy inflicts a daily toll on the economy in the form of compromised financial performance.[194] CEOs simply hold too much

---

possibility of risk manipulation to seek enhanced compensation and Congress' response to the problem in the form of the Dodd-Frank Act).

188. *See* EISENBERG & COX, *supra* note 7, at 1465, 1475.

189. *See* O'KELLEY & THOMPSON, *supra* note 7, at 325–326, 379–395. The *O'Kelley* text includes a limited discussion of the financial crisis of 2008, but no mention of perverse compensation incentives or risk manipulation for higher compensation. *Id.* at 7–8.

190. *See generally* andré douglas pond cummings, *"Ain't No Glory in Pain": How the 1994 Republican Revolution and the Private Securities Litigation Reform Act Contributed to the Collapse of the United States Capital Markets*, 83 NEB. L. REV. 979 (2005) (describing the accounting frauds at Enron, WorldCom, and many others resulting from corporate executives attempting to maintain high stock value to enhance executive compensation payouts).

191. *See* M.P. Narayanan et al., *The Economic Impact of Backdating of Executive Stock Options*, 105 MICH. L. REV. 1597, 1641 (2007) ("[O]ur evidence suggests that managerial theft is not a zero-sum game, but involves huge dead-weight losses for the shareholders.").

192. *See* Philip Coggan, *The Bonus Racket*, THE ECONOMIST, Jan. 31, 2009, at 79 ("In effect, executives and employees were given a call option on the markets by the banking system. They took most of the profits when the market was booming and shareholders bore the bulk of the losses during the bust."). In the three years prior to the crisis, Bear Stearns paid $11.3 billion in compensation and benefits while the shareholders were wiped out in bankruptcy; Lehman Brothers paid $21.6 billion and went bankrupt; finally, Merrill Lynch paid compensation and benefits of $45 billion while its shareholders got $9.6 billion in Bank of America stock. *Id.*

193. *See supra* note 26.

194. *See* Paul Gompers et al., *Corporate Governance and Equity Prices*, 118 Q. J. ECON. 107, 145 (2003) (finding that potential gains from improvements in corporate governance "would be enormous").

power.[195] For example, the simple expedient of splitting the CEO position from the Chair of the Board results in dramatic performance gains at the worst performing companies.[196] And there are other fundamental corporate governance matters that should be addressed and assessed in Business Associations casebooks. An independent risk-management committee is associated with superior financial performance, particularly in financial firms.[197] Diverse boardrooms have also been linked to valuation gains.[198] Shareholders value the ability to exercise votes in a meaningful way in the context of shareholder access to management's proxy for director elections.[199]

The political power of CEOs is the linchpin of CEO primacy. Economists have modeled how CEOs are able to wield political power to entrench and enrich themselves at shareholder expense. These models are consistent with extant empirical evidence.[200] This observation draws further support from the devolution of law and regulation in favor of managers that coincides with their runaway compensation, as discussed above. For example, in Delaware and most other jurisdictions, the law now provides for the elimination of liability for breach of the directors' duty of care.[201] This makes it less likely that boards will supervise CEOs.

---

195. Steven A. Ramirez, *Lessons From the Subprime Debacle: Stress Testing CEO Autonomy*, 54 ST. LOUIS U. L.J. 1, 52 (2009).

196. Vo, *supra* note 8, at 126–29. *See also* Ryan Krause & Matthew Semadeni, *Apprentice, Departure, and Demotion: An Examination of the Three Types of CEO-Board Chair Separation*, 56 ACAD. MGMT. J. 805, 805 (2013) ("In a study of Standard & Poor's (S&P) 1500 and *Fortune* 1000 firms, we find that separation of the two leadership roles positively impacts future firm performance when current performance is poor, but negatively impacts future firm performance when current performance is high. We find that this effect is most dramatic for demotion separations.").

197. *E.g.*, Ryan J. Baxter et al., *Enterprise Risk Management Program Quality: Determinants, Value Relevance, and the Financial Crisis*, 30 CONTEMP. ACCT. RES. 1264 (2013) (finding that superior Enterprise Risk Management (ERM) is associated with superior accounting performance and firm value); Robert E. Hoyt & Andre P. Liebenberg, *The Value of Enterprise Risk Management*, 78 J. RISK & INS. 795 (2011) (finding that insurance firms practicing ERM enjoy a 20 percent valuation premium.).

198. *See supra* notes 93–99 and accompanying text. *See also* Torchia et al., *supra* note 96 (finding that firms with a critical mass of women on the board are more innovative).

199. *See* Becker et al., *supra* note 21 (finding that sophisticated shareholders value proxy access).

200. *See* Lucian A. Bebchuk & Zvika Neeman, *Investor Protection and Interest Group Politics*, 23 REV. FIN. STUD. 1089 (2010) (articulating a model of sub-optimal corporate governance based upon lobbying resources and incentives and concluding that a CEO primacy model is consistent with extant empirical evidence).

201. Delaware essentially abolished liability under the duty of care for directors of public firms in 1987, through the passage of Delaware General Corporation Law (DGCL) section 102(b)(7). DEL. CODE ANN. tit. 8, § 102(b)(7) (2011). The synopsis of the bill indicated that the legislature was animated by the concerns of the insurance industry. *See* Michael Bradley & Cindy A. Schipani, *The Relevance of the Duty of Care Standard in Corporate Governance*, 75 IOWA L. REV. 1, 43 (1989). This is odd given that the market value of such insurance companies rose significantly after the *Smith v.*

Corporate leadership has also escaped liability for securities fraud because plaintiffs are now required to plead a "strong inference" of scienter without the benefit of discovery.[202] And big business leaders consistently exercise political power in a way that deprives shareholders of any real voice in the selection of board directors.[203]

The political power of CEOs reached its zenith in the aftermath of the financial market crisis of 2007–09. Despite proof of massive fraud, no individual corporate leader faced any real criminal accountability for the misconduct underlying the crisis.[204] In particular, no senior executive of any Wall Street bank faced indictment for the wrongdoing that precipitated the crisis.[205] The Department of Justice has failed to accurately justify this apparent immunity.[206] A lack of accountability for the most powerful does violence to the rule of law and encourages lawlessness throughout our society.[207] While there may be some colorable basis for declining to pursue criminal charges against banks backed by the full faith and credit of

---

Van Gorkom decision. *Id.* at 74. It appears insurance companies were able to use the decision to enhance their premium revenues with little real additional risk. *Id.*

202. Steven A. Ramirez, *Arbitration and Reform in Private Securities Litigation: Dealing with the Meritorious as Well as the Frivolous*, 40 WM. & MARY L. REV. 1055, 1076, 1084 (1999) ("The . . .'reforms' of private securities litigation are a betrayal of . . . the federal securities laws and expose our financial system to risks that are not fully appreciated. A more reactionary cycle could hardly have been imagined by the promulgators of the federal securities laws in the early 1930s."). Most major texts at least mention the Private Securities Litigation Reform Act in passing while failing to link the Act to the massive securities fraud underlying the subprime debacle. *See, e.g.*, EISENBERG & COX, *supra* note 7, at 863–66; O'KELLEY & THOMPSON, *supra* note 7, at 1030–59; CHOPER ET AL, *supra* note 7, at 407–13.

203. The Business Roundtable and the United States Chamber of Commerce—lobbying organizations that operate to further the interests of CEOs—recently stymied the SEC's efforts to give shareholders access to management's proxy for the purpose of participating in the director-selection process insofar as proxy voting is concerned. *See* Bus. Roundtable v. SEC, 647 F.3d 1144, 1146–47 (D.C. Cir. 2011).

204. *See* Steven A. Ramirez, *The Virtues of Private Securities Litigation: An Historic and Macroeconomic Perspective*, 45 LOY. U. CHI. L.J. 669 (2014) (reviewing evidence of massive securities fraud).

205. *Id.* at 723 n.362 ("In early 2013, Frontline investigated 'why Wall Street's leaders have escaped prosecution for any fraud related to the sale of bad mortgages.' . . . Among its findings was an apparent lack of criminal Grand Jury investigations . . . .") (citing *Frontline: The Untouchables* (PBS television broadcast Jan. 22, 2013), *archived at* http://perma.cc/MQ4-6GT6).

206. *Id.* (citing U.S. DEP'T. OF JUST., AUDIT OF THE DEPARTMENT OF JUSTICE'S EFFORTS TO ADDRESS MORTGAGE FRAUD, OFFICE OF THE INSPECTOR GENERAL AUDIT DIV., AUDIT REPORT 14–12, at 29 (Mar. 2014), *available at* http://www.justice.gov/oig/reports/2014/a1412.pdf.) ("The Inspector General of the Department of Justice also found that the Department mislead [sic] the public with regard to its prosecutorial efforts against financial and mortgage fraud. . . . Thus, the criminal response to the frauds underlying the Great Financial Crisis of 2008–2009 has been weaker than reported.").

207. *See* Mary Kreiner Ramirez, *Criminal Affirmance: Going Beyond the Deterrence Paradigm to Examine the Social Meaning of Declining Prosecution of Elite Crime*, 45 CONN. L. REV. 865, 871 (2013).

the U.S. government,[208] there is no basis for individual immunity for top financial executives. Moreover, this immunity from prosecution and the recklessness that presaged the market crisis are not mentioned in any of the leading corporations' textbooks to date.[209]

The irrational deviations from traditional norms described in the preceding paragraphs speak volumes about the power of CEOs.[210] But, little to nothing is mentioned in leading business law texts that would challenge the new primacy of the CEO.

V. CORPORATIZATION OF PRISONS AND SCHOOLS

Also absent in any Business Associations textbook is discussion of the disquieting trend whereby traditional governmental functions are turned over to profit-seeking firms.[211] For example, one increasingly popular

208. *See* Gregory M. Gilchrist, *The Special Problem of Banks and Crime*, 85 U. COLO. L. REV. 1 (2014) (arguing that externalities to prosecutions justify declination of prosecutions of banks).

209. While the issues of CEO power and accountability squarely implicate basic corporate governance principles, criminal exposure for acts surrounding the financial crisis is arguably less central to corporate law. Nevertheless, as an indicator of the political power of CEOs, and the impact of that political power on the fabric of basic corporate law, criminal immunity for top executives must warrant discussion to some extent. The most likely placement for this discussion is either in sections discussing executive compensation or the effort to reduce agency costs within the corporation through fiduciary duties. *See, e.g.*, EISENBERG & COX, *supra* note 7, at 299–314; CHOPER ET AL., *supra* note 7, at 32–35. Unfortunately, reading these sections of the texts, one would not even know the crisis of 2007–2009 ever occurred. *See also* O'KELLEY & THOMPSON, *supra* note 7, at 1169–75; KLEIN ET AL., *supra* note 7, at 895–928; EPSTEIN ET AL., *supra* note 7, at 635–39. The *Epstein* text was published in 2010, before it became clear that zero criminal prosecutions against personnel at the largest firms would occur.

210. CEO power thus explains soaring compensation. Prominent economists cannot find any performance-related basis for CEO pay. PIKETTY, *supra* note 5, at 334 ("The most convincing proof of the failure of corporate governance . . . is that when we collect data about individual firms . . . it very difficult to explain the observed variations [in pay] in terms of firm performance."). *See also* Piketty et al., *supra* note 44, at 232 (finding that soaring CEO pay resulted from CEO power to set pay independently from performance and incentives to exploit lower marginal tax rates).

211. Scholars increasingly contest the move of traditionally government functions to the corporate space. They argue that corporations do not operate with respect for individual rights but do operate without the checks and balances applicable to government actions. *E.g.*, powell & Menendian, *supra* note 8, at 121–24. They are not subject to anti-discrimination laws to the same extent as government actors due to the State Action doctrine. *See id.* at 121–22. Corporations represent highly concentrated power, not diffused power like that associated with democracy. As Professors powell and Menendian state:

> [C]orporations make good servants, but bad masters. To paraphrase Rawls, we can have either a corporatist welfare state or democracy, property respecting state. The rapid expansion of corporate prerogative and growth of corporate space is not only a threat to individual liberty and democratic accountability, it is a threat to the broadest public good. The concentration of wealth and influence in corporate form is an increasingly evident structural distortion in our economy and our politics.

Id. at 123.

privatization trend involves the transfer of the operation or ownership of correctional facilities from local, state, or federal governments to for-profit corporations.[212] Another significant privatization effort involves for-profit companies that operate or manage primary and secondary public schools.[213] These companies control the lives and futures of vulnerable constituencies—prisoners and students. These vulnerable individuals serve as a source of shareholder wealth.

At its legal optimum, the public firm aggregates capital from passive investors to fund ideas, innovation and entrepreneurial activities.[214] It fuels growth by lowering the cost of capital and eliminating the need for expensive capital intermediation.[215] There are, however, limits to the activities society should wish to capitalize through the economic benefits of the public firm.[216] Some activities do not warrant a lower cost of capital, nor high-powered lobbying and electioneering efforts, as there exists a zone of activities that may be best left to public funding.[217]

A. The Prison Industrial Complex

The prison industrial complex in the U.S. illustrates this limit.[218] The inherent problems of privatizing traditionally public functions are

212. The privatization of prisons is not a new phenomenon. In 1995, seven percent of the operators of state and federal facilities were private contractors. JAMES J. STEPHAN, U.S. DEP'T OF JUSTICE, CENSUS OF STATE AND FEDERAL CORRECTIONAL FACILITIES, 1995, at 2 (1997). Typically, one company "is responsible for everything that goes on in the prison, from the food that's served and the vocational courses that are taught to the discipline that's meted out to inmates." Penelope Lemov, *Jailhouse Inc.*, GOVERNING MAGAZINE, May 1993, at 44. Lemov described one of the prison companies, Corrections Corporation of America, and the fact that it sold its stock on a major stock exchange. *See id.*

213. For-profit companies have also been retained to distribute social services program benefits. *See generally* U.S. GEN. ACCOUNTING OFFICE, SOCIAL SERVICE PRIVATIZATION: EXPANSION POSES CHALLENGES IN ENDURING ACCOUNTABILITY FOR PROGRAM RESULTS (1997) (examining the policy implications of privatization of social services for children).

214. *See* RAMIREZ, *supra* note 2, at 51.

215. *Id.* at 49–51.

216. In decades past, corporate law textbooks addressed the limitations and restrictions imposed upon corporate activities by states. *E.g.*, WILLIAM L. CARY & MELVIN ARON EISENBERG, CASES AND MATERIALS ON CORPORATIONS 5–12 (5th ed. unabridged 1980). As Justice Brandeis recognized, these restrictions were based upon "apprehension of corporate domination." Louis K. Liggett Co. v. Lee, 288 U.S. 517, 549, 555 (1933) (Brandeis, J., dissenting) (noting that traditionally corporations only existed for a limited number of purposes and their powers were "sparingly conferred and strictly construed").

217. This is particularly so in the wake of *Citizens United*. *See supra* Part III. We explain the reasons why certain government functions are best left to the public sector in the subsections that follow.

218. *See* Patrice A. Fulcher, Hustle *and* Flow*: Prison Privatization Fueling the Prison Industrial Complex*, 51 WASHBURN L.J. 589, 589 (2012) ("The Prison Industrial Complex . . . is a profiteering

particularly evident in the context of carceral policy.[219] Should passive investors profit from incarcerating fellow citizens? Should society capitalize incarceration through the capital aggregation power of the public firm? Is the use of the public firm to operate prisons acceptable, particularly in light of the enhanced political power of the firm to influence legislation and incarceration policies?

Consider the following facts. The U.S. currently incarcerates more citizens than any nation on earth,[220] outpacing such autocratic regimes as China, Russia and Rwanda.[221] African Americans suffer disproportionately from this excessive incarceration rate, accounting for more than forty percent of the nation's inmates but only thirteen percent of the population.[222] This stunning percentage is exacerbated when you consider that most incarcerated African Americans are males. Nearly one in three African-American males can now expect to face some time in prison.[223] Latino males similarly make up large percentages of the U.S. prison population even though they make up a much smaller percentage of our nation's citizenry.[224] Additionally, the federal government holds approximately 34,000 immigration law violators in detention facilities that

---

system fueled by the economic interests of private corporations, federal and state correctional institutions, and politicians."). *See also* Eric Schlosser, *The Prison-Industrial Complex*, THE ATLANTIC, Dec. 1998, *available at* http://www.theatlantic.com/magazine/archive/1998/12/the-prison-industrial-complex/304669/ ("The prison-industrial complex is not only a set of interest groups and institutions. It is also a state of mind. The lure of big money is corrupting the nation's criminal-justice system, replacing notions of public service with a drive for higher profits.").

219. andré douglas pond cummings, "*All Eyez On Me": America's War on Drugs and the Prison-Industrial Complex*, 15 J. GENDER RACE & JUST. 417, 419 (2012) ("The 'tough on crime' political posturing and War on Drugs rhetoric have further led to an eruption in prison profiteering, in what has come to be known, per Angela Davis, Cornel West, and Talib Kweli, as the 'prison-industrial complex.'").

220. Michael B. Kelley & Christina Sterbenz, *This World Map Shows the Enormity of America's Prison Problem*, BUS. INSIDER (Jan. 24, 2014, 12:58 PM), http://www.businessinsider.com/world-map-of-incarceration-rates-2014-1#ixzz2vyEV26eA.

221. Fulcher, *supra* note 218, at 591.

222. Michael B. Kelley, *13 Signs That America's Prison System Is out of Control*, BUS. INSIDER (Apr. 12, 2012, 1:40 PM), *archived at* http://perma.cc/9YAK-JUD8.

223. Saki Knafo, *1 in 3 Black Males Will Go to Prison in Their Lifetime, Report Warns*, HUFF. POST (Oct. 4, 2013, 3:24 PM), *archived at* http://perma.cc/TN6-H56J.

224. THE SENTENCING PROJECT, REPORT OF THE SENTENCING PROJECT TO THE UNITED NATIONS HUMAN RIGHTS COMMITTEE REGARDING RACIAL DISPARITIES IN THE UNITED STATES CRIMINAL JUSTICE SYSTEM 1 (2013), *available at* http://sentencingproject.org/doc/publications/rd_ICCPR%20Race%20and%20Justice%20Shadow%20Report.pdf ("If current trends continue, one of every three black American males born today can expect to go to prison in his lifetime, as can one of every six Latino males—compared to one of every seventeen white males.").

are often privately operated.[225] Essentially, mass incarceration operates to create a new caste system of deeply disempowered minorities in the U.S.[226]

Public corporations profit from America's incarceration folly,[227] and it is natural for these firms to lobby lawmakers and make campaign contributions to further their economic interests.[228] Large private for-profit prison corporations spend dozens of millions of dollars annually to lobby for draconian sentencing penalties for crimes.[229] They also lobby lawmakers to hunt for "new" crimes that will result in incarceration.[230] For private prison profiteers, the name of the game is head count.[231] Their goal is to increase the number of heads that hit mattresses each night in their private carceral facilities.[232] In this way, it appears that private prison

225. William Selway & Margaret Newkirk, *Congress Mandates Jail Beds for 34,000 Immigrants as Private Prisons Profit*, BLOOMBERG (Sept. 23, 2013, 11:01 PM), *archived at* http://perma.cc/C3NM-TJJK.

226. MICHELLE ALEXANDER, THE NEW JIM CROW 4 (2010) ("Quite belatedly, I came to see that mass incarceration in the United States had, in fact, emerged as a stunningly comprehensive and well-disguised system of racialized social control that functions in a manner strikingly similar to Jim Crow.").

227. *See* Joe Weisenthal, *This Investor Presentation for a Private Prison Is One of the Creepiest Presentations We've Ever Seen*, BUS. INSIDER (Mar. 12, 2012, 1:06 PM), *archived at* http://perma.cc/E8PS-CDEP.

228. PAUL ASHTON & AMANDA PETTERUTI, JUSTICE POLICY INST., GAMING THE SYSTEM: HOW THE POLITICAL STRATEGIES OF PRIVATE PRISON COMPANIES PROMOTE INEFFECTIVE INCARCERATION POLICIES 22 (2011), *available at* http://www.justicepolicy.org/uploads/justicepolicy/documents/gaming_the_system.pdf (explaining that private prison companies like CCA, GEO Group, and Cornell Corrections have hired thirty lobbyists, in Florida alone, to promote their prison interests). Further, CCA has given over $900,000 annually to federal candidates since 2003, and the prison companies have given more than $16 million to state and federal legislators since 2000—evidence that states are some of the private prison companies' most important clients. *Id.* at 22, 24. *See also* Lee Hall, *Nomads Under the Tent of Blue: Migrants Fuel the U.S. Prison Industry*, 6 RUTGERS RACE & L. REV. 265, 308 (2004) (explaining how private prison lobbyists exercise influence); Clifford J. Levy, *Prison Company Faces Fine on Gaps in Lobbying Records*, N.Y. TIMES, Feb. 6, 2003, at B5.

229. Cassandre Monique Davilmar, Note, *We Tried to Make Them Offer Rehab, but They Said, "No, No, No!": Incentivizing Private Prison Reform Through the Private Prisoner Rehabilitation Credit*, 89 N.Y.U. L. REV. 267, 282 n.79 (2014) ("Private prison companies have aggressively promoted public policies that tend to increase revenues for private prisons.").

230. *See* AM. CIVIL LIBERTIES UNION, BANKING ON BONDAGE: PRIVATE PRISONS AND MASS INCARCERATION 38 (2011), *available at* http://www.aclu.org/files/assets/bankingonbondage_20111102.pdf; Laura Sullivan, *Prison Economics Help Drive Ariz. Immigration Law*, NPR (Oct. 28, 2010), http://www.npr.org/templates/story/story.php?storyId=130833741 (describing how CCA hired lobbyists to influence the Arizona legislature to pass a new law to increase prison populations).

231. *See* Davilmar, *supra* note 229, at 282 (noting that short term cost reductions lead to higher recidivism and a greater prison population for private exploitation); ASHTON & PETTERUTI, *supra* note 228, at 9–12 (describing how private prison corporations promote policies that lead to greater numbers of prisoners incarcerated which leads to larger profits for the corporation and its shareholders).

232. Davilmar, *supra* note 229, at 282 ("For society to benefit from private prisons, it must demand more than a short-term, convenient solution to the prison problem. Otherwise, if prison

corporations are perversely incentivized to increase human suffering in the name of profit maximization and greed.[233]

Disturbingly, the private prison corporation manufactures nothing, provides no genuinely valuable service, and simply acts as a conduit to transfer taxpayer funds from government coffers into the hands of shareholders and corporate executives.[234] Private prison companies exist primarily through government contracts that call upon them to warehouse city, state, and federal prisoners.[235] They siphon off taxpayer funds without manufacturing or providing anything truly useful.[236] Private prison executives sell their services to governments and municipalities by promising more efficiently run prisons and lower costs, but recent studies indicate that private prisons are run less efficiently, less safely, and less cost-effectively than are government-run prisons.[237] Moreover, private

corporations are allowed to focus solely on short-term cost-reduction, their long-term revenue stream will continue to increase to the detriment of society.").

233. *See* andré douglas pond cummings, *Private Prison Profiteering*, CONCURRING OPINIONS (Feb. 22, 2012), *archived at* http://perma.cc/J7WX-MMN3 (describing the lobbying efforts of private prison for-profit business leaders to increase prison populations in order to increase shareholder profits).

234. As Senator Robert F. Kennedy emphasized, in a 1968 speech at the University of Kansas, not all economic activity enhances social welfare:

> Gross National Product counts air pollution and cigarette advertising, and ambulances to clear our highways of carnage. It counts special locks for our doors and the jails for the people who break them. It counts the destruction of the redwood and the loss of our natural wonder in chaotic sprawl. It counts napalm and counts nuclear warheads and armored cars for the police to fight the riots in our cities. It counts Whitman's rifle and Speck's knife, and the television programs which glorify violence in order to sell toys to our children. Yet the gross national product does not allow for the health of our children, the quality of their education or the joy of their play. It does not include the beauty of our poetry or the strength of our marriages, the intelligence of our public debate or the integrity of our public officials. It measures neither our wit nor our courage, neither our wisdom nor our learning, neither our compassion nor our devotion to our country, it measures everything in short, except that which makes life worthwhile. And it can tell us everything about America except why we are proud that we are Americans.

Senator Robert F. Kennedy, Speech at the University of Kansas (Mar. 18, 1968), http://www.jfklibrary.org/Research/Research-Aids/Ready-Reference/RFK-Speeches/Remarks-of-Robert-F-Kennedy-at-the-University-of-Kansas-March-18-1968.aspx. Though prisons add to gross domestic product, they may substract from the general welfare of the nation.

235. RAMIREZ, *supra* note 2, at 21 ("Excessive prison expenditures may enhance short-term growth, but only at the cost of any reasonable measure of aggregate social happiness-a society that imprisons many of its citizens suffers from either an abnormally high concentration of dangerously violent people (unlikely) or an out-of-whack criminal justice system.").

236. *See* Robert J. Gordon, *Two Centuries of Economic Growth: Europe Chasing the American Frontier* 13 (Nat'l Bureau of Econ. Research, Working Paper No. 10662, 2004), *available at* http://www.nber.org/papers/w10662 (arguing that excessive prison expenditures in U.S. masks (in part) inferior U.S. productivity relative to Europe).

237. CORRECTIONAL INST. INSPECTION COMM. REP. ON THE INSPECTION AND EVALUATION OF THE LAKE ERIE CORRECTIONAL INSTITUTION, Jan. 22–23, 2013, *available at* http://big.assets.

prisons have failed to lower recidivism rates.[238] So, at its core, the private prison company simply exists as a transfer mechanism of taxpayer funds from average U.S. taxpayers to private prison shareholders and company executives.

More nefariously, private prison corporations also profit from prison labor, essentially engaging in a program of modern day indentured servitude.[239] Increasingly, private prison executives enter into contracts with a variety of companies that use prison labor at deep discounts to manufacture or develop their products. With companies able to pay prisoners significantly less than minimum wage, private prisons profit on the backs of those confined in their facilities, while the companies that contract for prison labor are able to place a "made in America" tag on their products and pay significantly less than minimum wage.[240] In both Georgia and Wisconsin, prisoners are paid nothing for their labor.[241] They are modern day slaves, exploited by the private prison regime. Corporations that have profited from prison labor since the inception of the private prison corporation include big-name companies like Starbucks, McDonalds, IBM, Victoria's Secret and many others.[242]

The for-profit private prison corporation profits by increasing the number of American citizens that are incarcerated while simultaneously exploiting their labor—perverse behavior that the law currently incentivizes.[243] To increase profits, corporate leadership of private prison companies must hope for, even work for, an increase in the number of men and women put behind bars in the United States. This work is handsomely rewarded as 2011 reports indicate that the two largest private prison

---

huffingtonpost.com/lakeeriereport.pdf; John Burnett, *Miss. Prison Operator out; Facility Called a 'Cesspool'*, NPR (Apr. 24, 2012), http://www.npr.org/2012/04/24/151276620/firm-leaves-miss-after-its-prison-is-called-cesspool; David M. Reutter, *Florida Provides Lesson in How Not to Privatize State Prisons*, PRISON LEGAL NEWS (Feb. 15, 2012), https://www.prisonlegalnews.org/news/2012/feb/15/florida-provides-lesson-in-how-not-to-privatize-state-prisons/.

238. Davilmar, *supra* note 229, at 276–77.

239. Patrice Fulcher, *Emancipate the FLSA: Transform the Harsh Economic Reality of Working Inmates*, ___ ST. JOHN'S J. C.R. & ECON. DEV. ___ (forthcoming 2014) (manuscript at 4) (on file with authors).

240. *Id.* at 14–15

241. *See id.* at 20 n.110 (citing Rhonda Cook, *Inmates Use Technology to Organize State Prison Protest*, ATLANTA JOURNAL-CONSTITUTION (Dec. 13, 2010, 3:48 PM), http://www.ajc.com/news/news/local/inmates-use-technology-to-organize-state-prison-pr/nQnsN/).

242. *See id.* at 32–33.

243. *See* Vicky Pelaez, *The Prison Industry in the United States: Big Business or a New Form of Slavery?*, GLOBAL RES. (Mar. 31, 2014), http://www.globalresearch.ca/the-prison-industry-in-the-united-states-big-business-or-a-new-form-of-slavery/8289.

companies, Corrections Corporation of America ("CCA") and the GEO Group together earned more than $2.9 billion in profits in 2010.[244]

It is important to understand how private prison corporations work for an increase in the number of persons incarcerated in the United States. The CEO, with no supervision and with boards that fail to hold him accountable, lobbies state and federal legislatures to increase prison construction and increase the flow of clients—prisoners—into the prison system. To accomplish this, the CEO has unfettered use of corporate funds at his disposal to hire lobbyists and political consultants for electioneering and politicking.[245]

The role of the corporation is to facilitate the flow of capital to innovative and entrepreneurial activities, not to create rent seeking from the destruction of human capital.[246] If casebooks included some discussion of privatization in general, and the new business of for-profit incarceration in particular, students would have the opportunity to think about the role of the corporation and the kinds of services that are best committed to public supervision.

B. The Privatization of Public Schools

For-profit companies that manage and operate primary and secondary public schools provide another example of the social impact of the corporate sector that all Business Associations casebooks overlook. In the early 1990s, educators looked to business leaders to help resolve the problem of failing public schools.[247] Business leaders proposed a market-

---

244. ASHTON & PETTERUTI, *supra* note 228, at 2.

245. *See* cummings, *supra* note 219, at 434–42.

246. One natural point for such discussion could be the *ultra vires* doctrine. Casebooks recognize that this doctrine has its roots in the traditionally narrow scope of permissible activities granted to corporations. EISENBERG & COX, *supra* note 7, at 249. But they typically fail to try to articulate any modern theory defining the proper role for the public corporation, or to discuss the possibility that corporations are not ideal for the wholesale displacement of government. Another point where such a discussion could occur is with respect to the power of the corporation to make charitable contributions, which at one time was considered *ultra vires*. *Id.* at 261–67. Instead, texts seem to assume there is no longer any theoretical limit to corporatization despite traditional skepticism and apprehension of corporatization. *See supra* note 216. *See also* CHOPER ET AL., *supra* note 7, at 19–29, 39–41, 65–69.

247. GARY MIRON & CHARISSE GULOSINO, NAT'L EDUC. POLICY CTR., PROFILES OF FOR-PROFIT AND NONPROFIT EDUCATION MANAGEMENT ORGANIZATIONS 1 (Kevin Welner et al. eds., 14th ed. 2013), *available at* http://nepc.colorado.edu/publication/EMO-profiles-11-12. *See also* Vaughan Byrnes, *Getting a Feel for the Market: The Use of Privatized School Management in Philadelphia*, 115 AM. J. EDUC. 437, 437 (2009) ("[T]he plights facing the U.S. public education system have drawn much attention and have been widely documented. This attention has focused predominantly on the growing dropout crisis in U.S. high schools . . . [and] the widening achievement gap within U.S. public schools between minority and low-income students and their more advantaged counterparts . . . .").

based approach to school reform, and this helped to inspire the emergence of education management organizations ("EMOs").[248] The authors of a report published by the National Education Policy Center define an EMO "as a private organization or firm that manages public schools, including district and charter public schools."[249] The authors define for-profit EMOs as "businesses that seek to return a profit to the owners or the stockholders who invest in them."[250] They note that "[h]istorically, only a small portion of EMOs have been nonprofits."[251]

One company, Education Alternatives, Inc., was highly visible in the 1990s during the early years of school privatization. Education Alternatives began its foray into the education business by contracting with school boards in Dade County, Florida; Baltimore, Maryland; and Hartford, Connecticut.[252] The company operated and managed several public schools, but eventually, all of these contracts were cancelled.[253] Soon after the contracts were cancelled, in light of the difficulties experienced by Education Alternatives, an article exploring the future of for-profit investment in education suggested that school boards be more careful when considering future privatization possibilities.[254] The journalists cautioned school officials to inquire about a for-profit company's experience in education, the cost to prepare a contract, and the costs of overseeing and appraising a company's performance.[255]

Eventually, Education Alternatives changed its name to The Tesseract Group, Inc. As The Tesseract Group, the company owned and operated several proprietary private schools and rendered management and consulting services to public and private schools. But the company's difficulties continued. In 2000, The Tesseract Group filed for Chapter 11 bankruptcy.[256]

In spite of The Tesseract Group's failure, and the subsequent criticism of school privatization, for-profit corporations continue in the business of educating children. Some for-profit EMOs organize as corporations, others

248. MIRON & GULOSINO, *supra* note 247, at 1.
249. *Id.* at 2.
250. *Id.*
251. *Id.* at 2–3.
252. *See* The Tesseract Group, Inc., Ann. Rep. (Form 10-K), 4–5 (Sept. 28, 1998).
253. *Id.*
254. *See* Deb Riechmann & John Gittelsohn, *School Ventures on Hold?*, ORANGE CNTY. REGISTER, Feb. 2, 1996, at A12.
255. *Id*.
256. *School Firm Files for Banruptcy* [sic] *Protection*, PHOENIX BUS. J. (Oct. 9, 2000, 1:51 PM), www.bizjournals.com/phoenix/stories/2000/10/09/daily7.html.

as limited liability companies.[257] In 2012, for-profit EMOs operated in 35 U.S. states.[258] "Each year since 2001–2002 the average enrollment for [for-profit] EMO-managed schools has increased."[259] In the 2009–2010 academic year, 365,000 students attended schools managed by for-profit EMOs.[260] In 2011–2012, 462,926 students attended schools managed by for-profit EMOs,[261] representing a significant increase in the number of students who depend on for-profit businesses for their education.[262] The size and number of for-profit EMOs have slowly but steadily increased.[263] "In 2011–2012, the total number of schools operated by large for-profit EMOs was 840, up from 808 in 2010–2011, an increase of 37 schools."[264]

For-profit EMOs may manage or operate traditional district public schools or charter schools. EMOs that manage district public schools do so under a contract with local school districts.[265] EMOs that manage charter schools do so pursuant to a contract with the charter holder to manage the school on the charter holder's behalf.[266] "Charter holders may include academic institutions, nonprofit foundations, and groups of parents, teachers, or both."[267] There are states, however, like New York that do not allow charter schools to hire for-profit EMOs to manage them.[268]

There is much disagreement about whether privatizing public schools improves education. Those who support for-profit EMOs embrace the spirit of entrepreneurship and market-based competition as a way to more efficiently attain educational goals.[269] Their position applies to for-profits that manage charter schools as well as for-profits that manage district

---

257. *See* MIRON & GULOSINO, *supra* note 247, at 23–29.

258. *Id.* at i.

259. *Id.* at 12.

260. *Id.* at iv.

261. *Id.*

262. *Id.* at 18 ("There are some interesting differences between schools operated by for-profit and nonprofit EMOs. For-profit schools are more concentrated at the primary level than are nonprofit schools. Across all categories, we find that for-profit schools have much larger enrollments per school.").

263. *Id.* at 5 ("Since the first *Profiles* report in 1999, the number of for-profit EMOs has increased to 97 from 33. The number of states in which EMOs operate has grown to 35 from 16."). For-profit EMOs may operate charter schools or traditional district schools, but the charter schools they manage have tended to be significantly larger than charter schools that are not run by for-profits. John F. Witte, *Is It Privatization or Educational Choice that Matters? Comments on "Market- Versus Mission-Oriented Charter Schools"*, 85 SOC. SCI. Q. 1052, 1053 (2004).

264. MIRON & GULOSINO, *supra* note 247, at 8.

265. Alex Molnar & David R. Garcia, *The Expanding Role of Privatization in Education: Implications for Teacher Education and Development*, TEACHER EDUC. Q., Spring 2007, at 11, 13.

266. *Id.*

267. *Id.*

268. *See* S. B. A.11310, 2010 Assemb., Reg Sess. (N.Y. 2010).

269. *See* MIRON & GULOSINO, *supra* note 247, at 1.

schools. Proponents argue that public schools will have to improve dramatically in order to compete with charter schools.[270] According to this market-based analysis, public schools that do not improve will not survive because they cannot compete with the superior-functioning charter schools.[271] With respect to district schools managed by for-profits, privatization proponents believe them to be far more efficiently and effectively managed than district schools that are operated by government or nonprofit entities.[272] The enhanced efficiency and effectiveness, according to privatization proponents, are attributable to an EMO's profit motive. The companies will profit, shareholders or investors will benefit, and future contracts will be available, only if the EMOs manage schools efficiently.[273] Privatization advocates argue that schools managed by for-profit companies will educate students more efficiently because businesses are not laden with the bureaucratic layers that impede innovation within government and nonprofit organizations.[274] Private companies, they argue, are better run and more effectively use the resources they have.[275] Many of these same arguments are used to justify prison privatization.

Opponents of public education privatization also focus on the profit motive. Opponents are concerned that "already limited school resources" will be "redirected for service fees, profits, or both."[276] EMO managers must economize, perhaps at student expense, in order to yield a profit for shareholders at some point. Economizing to maximize profits, even if it compromises student interests, is required under the prevailing

---

270. *Id.* at 2.

271. *Id.*

272. *Id.* ("A for-profit company contracted to manage district public schools, it is reasoned, will have incentives (making a profit in the short term and retaining a profitable contract in the long term) to seek efficiencies and improve student outcomes and achievement. The competition, in this context, takes place not among schools or districts themselves, but among current or potential managers of schools.").

273. *Id. See also* Molnar & Garcia, *supra* note 265, at 11 ("Advocates of market approaches to education reform contend that creating a market in educational services will foster competition among providers and thus spur delivery of better services at the same or lower cost than providing them through traditional public schools.").

274. Byrnes, *supra* note 247, at 438.

275. *Id.* The position of privatization proponents "stem from the very fundamentals of traditional capitalist economic doctrine, going back to the core of Adam Smith and *The Wealth of Nations*." *Id.* Indeed, "[t]he basic ideas of removing government interference in the field of education and allowing the natural free market forces such as competition to provide the public consumer with the best possible education services are in a sense traditionally American, finding support from the preeminent American economist of the twentieth century, Milton Friedman." *Id.*

276. MIRON & GULOSINO, *supra* note 247, at 1.

interpretation of corporate law.[277] If a company cuts corners to the detriment of students in order to increase profits, parents will be displeased and students may be harmed, but shareholders will be delighted. When a for-profit EMO cuts corners to maximize profits, it is doing what is expected under corporate law, even if the company is not doing what is best for the students. In order to be profitable, EMOs may "slash . . . per-pupil spending . . . [and] 'economize' by increasing class sizes, cutting back drastically on special education and eliminating 'non-essential' teachers of art, music and other specialized subjects."[278] Similar questions arise when for-profit companies operate prisons. "Does a private corporation skimp on food, cut corners on health care, reduce rehabilitation activities, or pay its guards less in an effort to squeeze more profit out of a prison contract?"[279] Emerging evidence suggests that private prisons do in fact take these very measures in order to squeeze a profit margin out of its prison contracts.[280]

Opponents of public school privatization are also concerned about the problems inherent in "creating another layer of administration."[281] They disagree with privatization proponents who claim that for-profit businesses reduce bureaucracy and operate more efficiently.[282] Opponents of school privatization are concerned that the business and governance of for-profit education companies are not sufficiently transparent.[283] This concern

---

277. *Cf.* Dodge v. Ford Motor Co., 170 N.W. 668, 684 (Mich. 1919). While *Dodge* is frequently cited to support the notion of shareholder primacy, some commentators believe that the case does not compel corporate managerial decision making that always requires the subordination of non-shareholder interests to those of shareholders, as long as the decision that benefits non-shareholders has some connection to corporate profitability. *See, e.g.*, William H. Simon, *What Difference Does It Make Whether Corporate Managers Have Public Responsibilities?*, 50 WASH. & LEE L. REV. 1697, 1698–99 (1993); Michael E. DeBow & Dwight R. Lee, *New Directions in Corporate Law: Shareholders, Nonshareholders and Corporate Law: Communitarianism and Resource Allocation*, 18 DEL. J. CORP. L. 393, 398 (1993) ("It has been the dominant American conception of the corporation for many years that a corporation's primary goal is, and should be, the maximization of shareholder welfare."); David Millon, *Communitarians, Contractarians, and the Crisis in Corporate Law*, 50 WASH. & LEE L. REV. 1373, 1374 (1993) ("[S]hareholder primacy has served as corporate law's governing norm for much of this century.").

278. Beth Wade, *The Business of Educating*, AM. CITY & CNTY., Jan. 1995, at 24, 27 (quoting the President of the National Education Association, Keith Geiger).

279. Lemov, *supra* note 212, at 45. *See also* Francis Wilkinson, *Taking Prisons Private*, AM. LAW., Nov. 1988, at 101; Cheryl L. Wade, *For-Profit Corporations That Perform Public Functions: Politics, Profit, and Poverty*, 51 RUTGERS L. REV. 323 (1999) (citing Ira P. Robbins, *Debate Over Private Prisons Begs Ethical Questions*, MANHATTAN LAW., Dec. 11, 1989, at 13) (stating that prison privatization "raises major policy, legal and moral questions").

280. *See supra* note 237.

281. MIRON & GULOSINO, *supra* note 247, at 1.

282. *Id.*

283. *Id.*

seems justified by the low response rate of for-profit EMOs to requests for basic structure and governance information from the National Education Policy Center.[284] The Center compiles information about the profiles of both for-profit and nonprofit companies that manage or operate public schools. Seventy-six percent of large for-profit EMOs did not respond to the Center's request for information.[285] Seventy-six percent of medium for-profit EMOs failed to respond, and ninety-three percent of small for-profit EMOs ignored the Center's requests for information.[286]

Both proponents and opponents of school privatization present convincing arguments. And attempts to establish empirically the benefits or disadvantages of school privatization are inconclusive. "Where empirical studies have been done on different privatization models, the research has been quite mixed, with positive results for privatization in some cases and negative results in others."[287] One recent empirical study compared public schools to traditional private schools and found that public schools are the best providers of educational services.[288] Where one stands in the debate about privatization is not critically important. Critical, however, is the fact that the debate about the role of the corporation in public functions is not described in any of the leading Business Associations casebooks.[289]

For-profit corporations that assume public functions, such as educating children, or imprisoning individuals, are uniquely important. The businesses in which they engage have profound effects not only on the students and prisoners they purport to serve, but also on society in general. The entire nation relies on the adequate provision of the services these companies render.

---

284. *Id.* at 239.

285. *Id.*

286. *Id. See also* Molnar & Garcia, *supra* note 265, at 19 ("The governance structures of for-profit companies are often obscured from public view. Therefore, much of what the public knows about the governance of for-profit firms comes from anecdotal accounts.").

287. Byrnes, *supra* note 247, at 440.

288. CHRISTOPHER A. LUBIENSKI & SARAH THEULE LUBIENSKI, THE PUBLIC SCHOOL ADVANTAGE: WHY PUBLIC SCHOOLS OUTPERFORM PRIVATE SCHOOLS 129–31 (2013) (finding that, after accounting for socioeconomic status, race, and other demographic differences among students, public school math achievement equaled or outstripped math achievement at every type of private school in grades 4 and 8); DIANE RAVITCH, REIGN OF ERROR: THE HOAX OF THE PRIVATIZATION MOVEMENT AND THE DANGER TO AMERICA'S PUBLIC SCHOOLS 1–10 (2013) ("[T]he transfer of public funds to private management and the creation of thousands of deregulated, unsupervised, and unaccountable schools have opened the public coffers to profiteering, fraud, and exploitation by large and small entrepreneurs.").

289. *See supra* note 246. This is, of course, an outcome dictated by the paltry discussions about any limits on corporatization or any discussion challenging the role of the corporation at all in contemporary society.

The business conducted by for-profit prisons and EMOs has great ontological significance. These companies have assumed the most vital government functions. The quality of a child's life, whether she fails or succeeds, may depend on how well an EMO performs. There are potentially dangerous consequences to the general public when a for-profit company fails to consider adequately the interests of prisoners. For-profit companies that manage prisons profoundly impact the lives of those they incarcerate, and these companies determine their chances of success in the future. The work that for-profit prisons and EMOs do "can be the starting point, the fountainhead, of a life worth living."[290]

For-profit prisons and EMOs "engage in businesses where human beings are the source of shareholder profit. When private companies manage prisons [and] public schools . . . the inmates [and] students they purport to serve become human commodities that are more like the widgets manufactured by more typical corporations than they are like the constituencies of traditional companies."[291] In this context, students and inmates depend on for-profit companies for their critical existential needs. The companies depend on the students and inmates for shareholder profits.[292]

The history of the corporation includes a robust discussion of its proper role under law.[293] Traditionally, corporations were required to specify their purposes and could not act *ultra vires* these purposes.[294] The general-purpose corporation is a relatively recent innovation dating only to the late 19th century.[295] The enhanced political power of the corporation to redefine "lawful" business and the encroachment of the public firm upon traditionally public functions calls for a re-ignition of that debate.

Instead, none of this discussion appears in any of the major modern/contemporary corporations and business organizations textbooks.[296] No existing textbook mentions privatization of historically

290. Wade, *supra* note 279, at 340.

291. *Id.* at 325.

292. *Id.* at 330.

293. Even as recently as 1971, scholars suggested that corporate activities and powers be limited. LATTIN, *supra* note 32, at 170–79, 201–05.

294. *Id.* at 201–38.

295. *Id.* at 176.

296. Texts focus on such archaic issues as the power of the corporation to make charitable contributions rather than the proper role of the corporation (notwithstanding chapter titles to the contrary). *See* EISENBERG & COX, *supra* note 7, at 251–68 (discussing the objective and conduct of the corporation); KLEIN ET AL., *supra* note 7, at 251–67 (section entitled "The Role and Purposes of the Corporation"). Others give even more limited coverage on the power and role of corporations. *See* CHOPER ET AL., *supra* note 7, at 64–68; O'KELLEY & THOMPSON, *supra* note 7, at 156–58, 684–86.

public functions. Also ignored is the possibility that privatization is potentially motivated by perverse incentives. Nor is there an opportunity for law students to explore whether these companies establish or implement social policy that is not in accordance with democratic principles as reflected in the Constitution, but in accordance with highly non-democratic corporate governance law.

VI. TOO BIG TO FAIL AND THE TWILIGHT OF CAPITALISM

Yet another undemocratic outcome is the emergence of public firms that are Too Big to Fail ("TBTF"). TBTF is the idea that the government and taxpayers must expend taxpayer money to support certain financial institutions and large public corporations when they suffer financial difficulties.[297] This public support is required, the argument goes, because the corporations are big and interconnected, and national and global economies would be destroyed if they failed.[298] The concept of TBTF is only briefly mentioned in leading corporate law textbooks today.[299] Discussion of the massive government bailouts of TBTF public firms and the corporate governance practices that led them to near financial collapse is nearly invisible in the business law texts most adopted in law school classrooms across the country.[300]

During the Great Financial Crisis of 2007–2009 the U.S. government bailed out large public corporations of all stripes ranging from massive investment banks[301] and the world's largest insurance company[302] to bank

297. During the crisis of 2008–2009 a total of 942 firms received government support from the Troubled Asset Relief Program ("TARP") bailouts alone. These firms included banks, mortgage firms, insurance companies, investment funds, other financial companies and auto companies. *Bailout Recipients*, PROPUBLICA, http://projects.propublica.org/bailout/list (last visited July 24, 2014).

298. The website of the NASDAQ stock market provides the following definition of TBTF:

> Government practices that protect large banking organizations from the normal discipline of the marketplace because of concerns that such institutions are so important to markets and their positions so intertwined with those of other banks that their failure would be unacceptably disruptive, financially and economically.

Financial Glossary: Too Big to Fail, NASDAQ, http://www.nasdaq.com/investing/glossary/t/too-big-too-fail (last visited June 30, 2014).

299. The primary bailout in terms of both federal expenditures and political attention was the TARP, created under the Emergency Economic Stabilization Act of 2008, Pub. Law No. 110-343, 122 Stat. 3765, 3788, 3790. The Federal Reserve ("Fed") made massive emergency loans under section 13(3) of the Federal Reserve Act. *See* 12 U.S.C. § 343(3) (2012). The FDIC used the bank deposit insurance fund to back-up government guarantees of bank asset values and to guarantee bank debt under the so-called systemic risk exception to its otherwise limited statutory authority. *See* 12 U.S.C. § 1823(c) (2012).

300. *See* CHOPER ET AL., *supra* note 7, at 1169.

301. *See, e.g.*, Gretchen Morgenson, *Rescue Me: A Fed Bailout Crosses a Line*, N.Y. TIMES, Mar. 16, 2008, at BU1 (detailing Fed bailout of Bear Stearns). Ultimately, the Fed actually subsidized the

holding companies[303] and automobile manufacturers.[304] The government's ad hoc approach to using taxpayer funds to bail out massive public firms whose leadership had failed left the most seasoned economists befuddled.[305] The only common element to these ad hoc bailouts was the inept but politically powerful management of the public corporations that accepted government bailout funds.[306] Today, the megabanks cast an even larger shadow over our economy than before the crisis.[307]

Perhaps nothing illustrated the political power of the modern corporation in action more than the astounding U.S. government bailouts of the megabanks starting in 2008.[308] William Poole, Former President of the Federal Reserve Bank of St. Louis, called the bailouts an "affront" to capitalism and our democracy.[309] The government was so indulgent of senior corporate executives during the bailout era that one Nobel-winning economist termed the bailouts "ersatz capitalism" meaning "the privatizing

merger of Bear Stearns with JPMorgan Chase, which effectively made JP Morgan Chase even bigger. Press Release, Fed. Reserve Bank of N.Y., Statement on Financing Arrangement of JPMorgan Chase's Acquisition of Bear Stearns (Mar. 24, 2008), *archived at* http://perma.cc/96GH-Y3P7.

302. *A Nuclear Winter?*, THE ECONOMIST, Sept. 20, 2008, at 88.

303. For example, in early 2009 the government announced a massive bailout of Bank of America. Press Release, U.S. Dep't of the Treas., Federal Reserve and the FDIC Provide Assistance to Bank of America (Jan. 16, 2009), *archived at* http://perma.cc/3HDQ-6S85. The government did not replace senior management at Bank of America nor reduce their compensation rights. *See id.* This followed a similar bailout at Citigroup. Press Release, U.S. Dep't of Treas., Joint Statement by Treasury, Federal Reserve and the FDIC on Citigroup (Nov. 23, 2008), *archived at* http://perma.cc/KC56-VK3A. Again, the government did not replace senior management nor negotiate any reduction in their compensation. *See id.*

304. *See* Jonathan G. Katz, *Who Benefited from the Bailout?*, 95 MINN. L. REV. 1568, 1592–93 (2011) (exploring differences between auto bailouts and financial institution bailouts).

305. *See* Anna Jacobson Schwartz, Op-Ed., *Man Without a Plan*, N.Y. TIMES, July 26, 2009, at WK12 ("The market was thus bewildered when the Fed rescued certain firms and not others. Mr. Bernanke should have explained the principles behind these decisions. The market could not understand why the Fed rescued Bear Stearns and then permitted Lehman Brothers to die.").

306. *What Were They Smoking?*, FORTUNE, Nov. 26, 2007, at 66. *See also* Paul Krugman, Op-Ed., *Banks Gone Wild*, N.Y. TIMES, Nov. 23, 2007, at A37 ("The point is that the subprime crisis and the credit crunch are, in an important sense, the result of our failure to effectively reform corporate governance after the last set of scandals.").

307. *See* Harvey Rosenblum, *Choosing the Road to Prosperity: Why We Must End Too Big to Fail—Now*, *in* FED. RESERVE BANK OF DALL., 2011 ANNUAL REPORT 2, 6 exhibit 2 (2012).

308. Mehrsa Baradaran, *Banking and the Social Contract*, 89 NOTRE DAME L. REV. 1283, 1285 (2014) ("[The megabanks] make up less than one percent of the banks in the country, but control the majority of the country's banking assets and wield a disproportionate amount of political power."). Economist Simon Johnson states the reality well: "Do not deceive yourselves, the fact that Dodd-Frank places constraints on the ability of the Fed, the fact that it modifies the emergency powers, the fact that it changes other parts of the legal powers and authorities around the financial system does not mean that there cannot be and will not be another bailout." Simon Johnson, *Keynote Address: The Continuing Problem of "Too Big to Fail"*, 18 N.C. BANKING INST. 1, 8 (2013).

309. Heidi N. Moore, *Jumping Into the Regulatory Poole for Banks*, WALL ST. J., Apr. 3, 2009, *available at* http://blogs.wsj.com/deals/2009/04/03/jumping-into-the-regulatory-poole-for-banks/.

of gains and the socializing of losses."[310] Government inquiries conducted by oversight panels later concluded that the bailouts amounted to giveaways of taxpayer wealth to the megabanks and to their corporate leadership.[311] Why would government leaders consider no alternative other than to bail out the very corporations that brought the economy to the brink of disaster? Business law textbooks fail to discuss these issues, thereby failing to give law students an opportunity to consider an economic policy that posits that banks are so large and "important" to the economy that their collapse threatens the entire global marketplace.[312]

Even though many alternatives were available, the U.S. government attempted to resolve the financial crisis by choosing a bailout strategy most favorable to senior corporate managers at the firms most responsible for the crisis.[313] One prominent economist suggested forming new banks with the funds used to bailout the megabanks because the new banks could continue to lend based upon "pristine balance sheets" unencumbered by toxic assets.[314] Other alternatives included bankruptcy protection for the failed megabanks or even allowing megabank failure, letting the market work where the reckless and mismanaged firms could be absorbed by stronger and better-managed firms.[315] In truth, no alternative avenue was seriously considered by the government other than the full-scale bailout of Wall Street banks and firms that effectively redistributed losses from private firms to taxpayers.[316]

---

310. Joseph E. Stiglitz, Op-Ed., *Obama's Ersatz Capitalism*, N.Y. TIMES, Apr. 1, 2009, at A31 (arguing that privatizing gains and socializing losses amounts to "ersatz capitalism").

311. *See* CONG. OVERSIGHT PANEL, FEBRUARY OVERSIGHT REPORT: VALUING TREASURY'S ACQUISITIONS 4 (Feb. 6, 2009), *archived at* http://perma.cc/JUM7-NUF6 (presenting a valuation study of the ten largest TARP transactions and concluding that "[o]verall, in the ten transactions, for each $100 spent, the Treasury received assets worth approximately $66.").

312. *See* Andrew G. Haldane, Exec. Dir., Fin. Stability & Member of the Fin. Policy Comm., On Being the Right Size, Speech at the Institute of Economic Affairs' 22nd Annual Series 12–13 (Oct. 25, 2012), *archived at* http://perma.cc/SZ4N-PHA2 (stating that after adjusting for implicit subsidies banks over $100 billion do not outperform smaller banks).

313. Simon Johnson, *TARP: the Long Goodbye*, N.Y. TIMES (Sept. 30, 2010), *archived at* http://perma.cc/L9S6-CQA9 ("TARP was an essential piece of a necessary evil—that is, it saved the American financial system from collapse, but it was put in place in a way that was excessively favorable to the very bankers who had presided over the collapse. And this sets up exactly the wrong incentives as we head into the next credit cycle."); Carter Dougherty, *How Sweden Handled a Financial Crisis Without Burdening Taxpayers*, N.Y. TIMES, Sept. 23, 2008, at C9 (suggesting that the U.S. follow Sweden's more punitive approach to bailouts).

314. Paul Romer, Op-Ed., *Let's Start Brand New Banks*, WALL ST. J. (Feb. 6, 2009), http://online.wsj.com/news/articles/SB123388681675555343.

315. *See, e.g.*, Guillermo Rosas, *Bagehot or Bailout? An Analysis of Government Responses to Banking Crises*, 50 AM. J. POLI. SCI. 175, 181 tbl.3 (2006).

316. For alternatives not considered by the U.S. government, see *US Does Not Have Capitalism Now: Stiglitz*, CNBC (Jan. 19, 2010, 8:39 AM), *archived at* http://perma.cc/C24C-UNMG. *See*

The U.S. government provided $23 trillion in commitments to save Wall Street firms and other corporations between 2008 and 2009.[317] Yet, without precedent in either U.S. or global history, few senior executives lost their job or faced serious investigation as a result of these unprecedented bailouts.[318] The clear takeaway for senior corporate executives is that disincentives associated with failure and reckless leadership are now diluted.[319] Further, creditors will provide capital to these firms at a lower cost.[320] With no discipline from the credit markets, the firms will take more risk onto their balance sheets.[321] Ultimately, firms not backed by the government's implied bailout promise cannot compete. Only a fragmented financial sector without implied bailout guarantees would secure competition.[322] In short, these megafirm bailouts are antithetical to the meritocratic competition that should be central to capitalism.[323]

The bailouts of 2007–2009 stand without precedent. The government ultimately guaranteed all of the obligations of the megabanks, including compensation arrangements with senior managers.[324] The government did not attempt to negotiate for fair value in exchange for its mammoth commitment of taxpayer capital and bailout monies for shareholders,

---

generally Kenneth Ayotte & David A. Skeel, Jr., *Bankruptcy or Bailouts?*, 35 J. CORP. L. 469, 471 (2010) (comparing failure under bankruptcy law to "ad-hoc" rescues chosen by government in financial crisis and concluding that government's approach embedded perverse incentives).

317. Dawn Kopecki & Catherine Dodge, *U.S. Rescue May Reach $23.7 Trillion, Barofsky Says*, BLOOMBERG (July 20, 2009), *archived at* http://perma.cc/9SLD-V62U.

318. *See* EMMA COLEMAN JORDAN, CTR. FOR AM. PROGRESS, A FAIR DEAL FOR TAXPAYER INVESTMENTS 1 (2009), *archived at* http://perma.cc/7D4J-JZW6 ("92 percent of the management and directors of the top 17 recipients of TARP funds are still in office").

319. Rosenblum, *supra* note 307, at 19 ("In practice, these rescues have penalized equity holders while protecting bond holders and, to a lesser extent, bank managers. Disciplining the management of big banks, just as happens at smaller banks, would reassure a public angry with those whose reckless decisions necessitated government assistance.").

320. *See id.* at 4 ("Moral hazard reinforces complacency. Moral hazard describes the danger that protection against losses encourages riskier behavior. Government rescues of troubled financial institutions encourage banks and their creditors to take greater risks, knowing they'll reap the rewards if things turn out well, but will be shielded from losses if things sour.").

321. *See* Johnson, *supra* note 308, at 12 ("We just experienced the greatest financial crisis since the 1930s because incentives in the financial system encouraged people to take excessive risk, to have too little capital, too much leverage, and too much debt relative to thin cushions of equity.").

322. *See* Rosenblum, *supra* note 307, at 21 ("A financial system composed of more banks, numerous enough to ensure competition in funding businesses and households but none of them big enough to put the overall economy in jeopardy, will give the United States a better chance of navigating through future financial potholes and precipices.").

323. *See id.* at 4 ("When competition declines, incentives often turn perverse, and self-interest can turn malevolent. That's what happened in the years before the financial crisis.").

324. SIMON JOHNSON & JAMES KWAK, 13 BANKERS: THE WALL STREET TAKEOVER AND THE NEXT FINANCIAL MELTDOWN 11–13 (2010).

managers and unsecured creditors alike.[325] This irresponsible fiscal behavior on the part of the government corrodes the economic rule of law as ordinary citizens witness the unfair indulgences that are granted to the rich and powerful.[326]

The cost of bailing out TBTF institutions is not limited to actual government outlays of taxpayer funds—as massive as those were. The hidden and more injurious cost is that this totally non-punitive government backstop and fiscal irresponsibility invites excessive risk taking within the core of our economy—the financial sector.[327] The Great Financial Crisis exemplifies this excessive and reckless risk inspired by an implicit bailout guarantee.

Senior executives at major financial corporations contributed to causing the crisis by saddling their firms with unprecedented levels of risk and risky leverage.[328] The high-risk mortgages and debt assumed by these executives and firms led to immediate short-term profits and positive compensation gains for the executives at the cost of economic catastrophe for all others.[329] One commentator termed the debacle "one of the worst miscalculations in the annals of risk management."[330] Savvy business and finance experts recognized that this risk manipulation for profit resulted in part from deeply flawed compensation arrangements for senior executives.[331] TBTF exacerbates these perverse incentives in compensation arrangements by assuring that failure and recklessness go unsanctioned. Essentially, TBTF means that government insures failures

325. *Id.*

326. Rosenblum, *supra* note 307, at 4 ("[C]ompetition and the rule of law provide market discipline that keeps self-interest in check and steers it toward the social good of producing more of what consumers want at lower prices.").

327. Johnson, *supra* note 308, at 12 ("The cost of any financial crisis is not primarily in the emergency provision of capital liquidity by authorities that may or may not be paid back; the cost of financial crisis is the loss of jobs and the loss of growth.").

328. *E.g.*, Hill & McDonnell, *supra* note 152, at 859–60 ("The financial crisis helps make the case that boards should do more monitoring. Corporate behavior in the crisis yielded enormous negative externalities for the greater society. Corporations were able . . . [to] incentivize risky behavior that yields negative externalities, [so] it seems appropriate that boards do more to prevent the abuse of [limited liability].").

329. *See* Bebchuk et al., *supra* note 152, at 259–60 (finding that "the top executive teams of Bear Stearns and Lehman" derived billions in compensation, exceeding the value of the executives' stock holdings at the beginning of the period, such that "the bottom-line payoffs of these executives during 2000–2008 were not negative but rather decidedly positive.").

330. Shawn Tully, *Wall Street's Money Machine Breaks Down*, FORTUNE, Nov. 26, 2007, at 75.

331. Raghuram Rajan, *Bankers' Pay Is Deeply Flawed*, FIN. TIMES (Jan. 8, 2008, 4:21 PM), http://us.ft.com/ftgateway/superpage.ft?news_id=fto010920081142101282 ("[U]nless we fix incentives in the financial system we will get more risk than we bargain for. Unless bankers offer these better explanations, their enormous pay, which has been thought of as just reward for performance, will deservedly come under scrutiny.").

because there is simply no downside. Recklessness and short-termism are incentivized as corporate leadership is wholly insulated from both criminal sanction and economic injury.[332] A more anti-capitalistic approach is difficult to imagine.

The Dodd-Frank Act, despite being hailed as new and improved financial sector regulation, does not prohibit the government-sponsored bailouts implemented in 2008 and 2009. The Federal Reserve and the FDIC can now legally engage in subsidizing the failures that occurred in 2008–2009. While Dodd-Frank included some minor changes in containing the size of the megabanks and a new resolution authority, it is very unlikely that either can be actualized.[333] More importantly, and more economically dangerous, the megabanks are much larger today than ever before.[334] Therefore, in the future, Congress may face the same dire choices that came before it in the fall of 2008 when, on the eve of an election, it faced either a total meltdown of the financial sector or being forced to throw nearly $1 trillion in subsidized capital at the financial sector to rescue it from demise.[335]

Law students have no opportunity to consider TBTF and the suggestion that it should be neutralized. Casebooks should provide law students with an opportunity to explore whether megabanks should be broken-up in order to restore proper incentives for board members and senior executive officers on Wall Street and working in the financial sector.[336] One is hard-

332. RAMIREZ, *supra* note 2, at 173–79; *see also* Lynne L. Dallas, *Short-Termism, the Financial Crisis, and Corporate Governance*, 37 J. CORP. L. 265 (2012) (exploring why short-termism exists "with particular attention given to the financial crisis of 2007–09").

333. JOHNSON & KWAK, *supra* note 324, at 207.

334. As Professor Murdock notes:

> In 1970, the five largest banks held 17% of banking assets, the next ninety-five banks had 37% of assets, and the 12,500 smallest banks had 48% of assets. By 2010, the share of the five largest banks had increased to 52%, the share of the next ninety-five had dropped to 32%, and the share of the 5,700 smallest banks had plummeted to 16%.

Charles W. Murdock, *The Big Banks: Background, Deregulation, Financial Innovation, and "Too Big to Fail"*, 90 DENV. U. L. REV. 505, 541–42 (2012).

335. Rosenblum, *supra* note 307, at 20.

336. As the President of the Federal Reserve Bank of Dallas put it:

> The TBTF institutions that amplified and prolonged the recent financial crisis remain a hindrance to full economic recovery and to the very ideal of American capitalism. It is imperative that we end TBTF. In my view, downsizing the behemoths over time into institutions that can be prudently managed and regulated across borders is the appropriate policy response. Only then can the process of "creative destruction"—which America has perfected and practiced with such effectiveness that it led our country to unprecedented economic achievement—work its wonders in the financial sector, just as it does elsewhere in our economy. Only then will we have a financial system fit and proper for serving as the lubricant for an economy as dynamic as that of the United States.

Id. at 1.

pressed to find even a mention of TBTF in any of the mainstream corporations textbooks most adopted in U.S. law schools.

Further, while the Great Financial Crisis remains a fairly recent occurrence, none of the major corporate law textbooks takes a critical look at TBTF or the incentives it created as causes of the mortgage crisis.[337] None of the leading corporate law textbooks provides a meaningful exploration of the mortgage crisis at all.[338] With the newest edition of the *O'Kelley* text and the *Eisenberg* text published in 2014, the *Choper* text published in 2013, the *Klein* text in 2012, and the most recent edition of *Epstein* published in 2010, all had an opportunity to examine the causes of the market meltdown and facilitate a conversation regarding the failure of corporate law to protect against the crisis.[339] But each of the texts fails to engage in a critical examination of the financial crisis. It is difficult to imagine why, on the heels of the greatest market correction and crisis since the Great Depression, modern corporate law textbooks contain no examination of the causes of the crisis or the continuing economic danger of TBTF. The absence of any genuine analysis of the mortgage crisis, the subprime mortgage market collapse and the resultant bailout of TBTF megafirms deprives students of critical analyses and information. Students are exposed only to textbooks written by authors who seem to be apologists for a skewed capitalism that favors the elite and disfavors main street citizens. The business law professoriate is failing an entire generation of law graduates and lawyers.

VII. CONCLUSION

Corporate law textbooks fail to critically assess the entrenchment of white male privilege at the commanding heights of the economy, and the means by which this is perpetuated. Nor, do they critically assess the new political power of the corporation. They provide little perspective on the proper role of the corporation. The role of corporate governance in the Great Financial Crisis of 2008 also garners little to no attention. TBTF

337. O'KELLEY & THOMPSON, *supra* note 7, at 1175; CHOPER ET AL., *supra* note 7, at 1169; KLEIN ET AL., *supra* note 7, at 927; EPSTEIN ET AL., *supra* note 7, at 643. The issue will take on greater significance in the future as more firm managers seek the government backing implicit in TBTF status. *See* Cheyenne Hopkins & Robert Schmidt, *House Lawmakers Say 'Too Big to Fail' Panel Too Secretive*, INS. J. (July 16, 2014), *archived at* http://perma.cc/X6RQ-3RAJ (reporting that Prudential Financial, GE Finance and AIG have been deemed TBTF).

338. The *Epstein* text creditably explains the role of leverage and derivatives. EPSTEIN ET AL., *supra* note 7, at 311–12, 315–18.

339. *See* O'KELLEY & THOMPSON, *supra* note 7, at 7–8; KLEIN ET AL., *supra* note 7, at 911–19; *see also* EPSTEIN ET AL., *supra* note 7, at 638–41.

appears to be a taboo subject. These are core issues relating to corporate governance and the essential nature and purpose of the corporate form in our society.

Whether or not the casebook authors agree with more critical perspectives on such issues, we argue that shielding a new generation of leaders from such perspectives and important evidence cannot be justified. Nobel laureates in economics—like Joseph Stiglitz or Paul Krugman—assail corporate governance law from the point of view of agency costs and CEO power. The proof of the importance of this issue for future business leaders is manifest in recent lawmaking and regulatory activity in the wake of the financial crisis. Law students and future policymakers should be allowed to consider such evidence in thinking about corporate law.

When corporations reap profits from mass incarceration or privatization of schools, students should consider the role of the modern corporation. Traditionally, this topic formed an essential part of the education of tomorrow's leaders. Students today should be given the same opportunity to consider the monolithic demographic make-up of senior executive officers and directors at the nation's most powerful firms, particularly in an era of very high economic inequality. The basic corporations' class is the logical locus for such learning.

Essentially, this Article demonstrates that no author or publisher of a recent or longstanding leading corporate law textbook has addressed the increasing economic and political power wielded by those in control of the public firm, nor has any author confronted the legitimacy of this power shift from a policy perspective. The enhanced power of CEOs gets little or no mention, and changes in law and regulation that underlie this power shift are not identified or analyzed. One can read entire corporate law textbooks cover to cover and find little to no mention of TBTF, the role of the public corporation in the collapse of capitalism in 2008, the lack of diversity in the boardroom, the criminal immunity of some of those in control of key financial corporations, or the incentives corporations have to destroy the environment, foment war or imprison fellow citizens. This failure leads to a critical disservice visited upon aspiring lawyers and business leaders in our nation's law school classrooms.

If the power of the corporation is too awesome to speak of, if the control of CEOs cannot be discussed, and if fundamental values such as the environment, freedom and education, and the perverse incentives created by corporate governance law and regulation are not part of the discourse, then the modern public corporation will be a unique and costly threat to society instead of the indispensable prop to modern capitalism that it was created to be. This Article concludes that training tomorrow's leaders and corporate law experts in a more fulsome corporate law that includes a power perspective and that questions the proper role of the corporation in society ultimately paves the way for the full realization of the potential of the public corporation.