A Critique of The American Law Institute's Draft Restatement of the Corporate Objective

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The American Law Institute (ALI) is currently working on a Restatement of the Law of Corporate Governance (Restatement). At the ALI's May 2022 annual meeting, the membership approved, inter alia, § 2.01, which purports to restate the objective of the corporation. Section 2.01 differentiates between what the drafters refer to as common law jurisdictions and stakeholder jurisdictions. The latter are those states that have adopted a constituency statute (a.k.a. a non-shareholder constituency statute).

The drafters assert that, in common law jurisdictions, the corporate objective is to "enhance the economic value of the corporation, within the boundaries of the law . . . for the benefit of the corporation's shareholders . . . ." In doing so, the corporation is allowed to consider the impact of its actions on various stakeholders, provided doing so redounds to the benefit of shareholders.

In stakeholder jurisdictions, the corporation's objective is to "enhance the economic value of the corporation, within the boundaries of the law . . . for the benefit of the corporation's shareholders and/or, to the extent permitted by state law, for the benefit of employees, suppliers, customers, communities, or any other constituencies."

In both sets of jurisdictions, the drafters assert that the corporation "may devote a reasonable amount of resources to public-welfare, humanitarian, educational, and philanthropic purposes, whether or not doing so enhances the economic value of the corporation."

This article is intentionally agnostic on the underlying normative issue of whether corporations should focus exclusively on shareholder interests or should also consider stakeholder interests. Instead, it offers a critique of § 2.01 and offers suggestions so as to clarify important open questions and better align § 2.01 with current law.

Aspects of § 2.01 addressed herein include: Do corporations have objectives? What is the corporate objective? Are tradeoffs allowed? Is opting out allowed? Should § 2.01 mandate obedience to the law? Does § 2.01 embrace Caremark*? How does § 2.01 apply in takeovers? What rules govern corporate charitable activities? Why did the drafters ignore the special problems of multinationals?*

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I. INTRODUCTION 2
II. THE NEW § 2.01 VERSUS THE OLD 4
III. DO CORPORATIONS HAVE OBJECTIVES? 10
IV. THE SUBSTANTIVE LAW OF CORPORATE PURPOSE 15
A. The Nature of the Objective 15
B. Are Tradeoffs Allowed? 18
1. The Restatement's Ambiguity 18
2. The Law in Common Law Jurisdictions 20
3. The Law in Stakeholder Jurisdictions 22
4. Summation 25
C. Is Opting Out Allowed? 28
D. Obedience to the Law 31
E. *Caremark* is Coming 37
F. Stakeholders and Takeovers 41
G. Charitable Activities 46
H. The Special Problems of Multinationals 51
V. CONCLUSION 51

I. INTRODUCTION

In 1978, the American Law Institute (ALI) authorized a project originally intended to result in a restatement of corporate law.[1] The project proved controversial from the outset[2] and is still regarded as one of the most controversial projects ever attempted by the ALI.[3] One respected commentator went even further, calling the project "the most controversial event in the history of

[1] *See* PRINCIPLES OF CORP. GOVERNANCE AND STRUCTURE: RESTATEMENT AND RECOMMENDATIONS viii (AM. L. INST. Tent. Draft No. 1, 1982).

[2] *See* Shyamkrishna Balganesh & Peter S. Menell, *Restatements of Statutory Law: The Curious Case of the Restatement of Copyright*, 44 COLUM. J.L. & ARTS 285, 314 (2021) ("While the project began as a Restatement initiative, it soon attracted criticism for being overtly reformative, a premise that it did not hide."); Joel Seligman, *A Sheep in Wolf's Clothing: The American Law Institute Principles of Corporate Governance Project*, 55 GEO. WASH. L. REV. 325, 351 (1987) ("The Business Roundtable virulently objected . . . to calling the Corporate Governance project a Restatement . . . [.]"); Robert B. Thompson, *Preemption and Federalism in Corporate Governance: Protecting Shareholder Rights to Vote, Sell, and Sue*, 62 L. & CONTEMP. PROBS. 215, 223 (Summer 1999) (noting that the project was "vigorously criticized as making overregulatory suggestions for state corporate law").

[3] *See* Balganesh & Menell, *supra* note 2 at 314 ("The Principles project was an innovation that the ALI introduced in 1984 when one of its very controversial efforts, the Corporate Governance Project, was met with significant resistance during its early days."); Douglas M. Branson, *Too Many Bells? Too Many Whistles? Corporate Governance in the Post-Enron, Post-Worldcom Era,* 58 S.C. L. REV. 65, 113 n.97 (2006) (noting that the project "proved very controversial").

American corporate law."[4] Perhaps because of the controversy surrounding the project, it has had little influence on judicial development of corporate law.[5]

Despite this dubious precedent, the ALI has returned to the corporate governance field with a proposed Restatement of the Law of Corporate Governance ("Restatement").[6] At the ALI's 2022 annual meeting, the membership considered Tentative Draft No. 1, which contained provisions defining various terms, discussing the duties of care and loyalty, and stating the social purpose of the corporation.[7] Except for one of the duty of loyalty provisions, the membership approved the draft.[8]

A key provision of the new restatement is § 2.01, which addresses the objective of the corporation.[9] By tackling this topic, the ALI reenters one of the most fervent debates in recent years. Although corporate social responsibility and stakeholder theory have long been among the most controversial issues in corporate law, the debate has flared significantly over the last few years.[10]

As finally approved in 1993, the Principles of Corporate Governance: Analysis and Recommendations ("Principles") included a provision on the "Objective and Conduct of the Corporation."[11]

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4 William J. Carney, *The ALI's Corporate Governance Project: The Death of Property Rights?*, 61 GEO. WASH. L. REV. 898, 898 (1993).

5 To be sure, there are those who claim to the contrary. *See, e.g.*, Einer Elhauge, *Sacrificing Corporate Profits in the Public Interest*, 80 N.Y.U. L. REV. 733, 738 (2005) (describing the Principles as "influential"); Steven A. Ramirez, *Fear and Social Capitalism: The Law and Macroeconomics of Investor Confidence,* 42 WASHBURN L.J. 31, 66 n.214 (2002) (describing the Principles as "very influential"). A detailed empirical analysis, however, found that "[c]ourts cite only a few sections of the Principles, the controversial provisions do not appear to be cited more often or more favorably than more traditional restatement-style provisions, and citations to the Principles have declined over time." Minor Myers, *Measuring the Influence of the* ALI's *Principles of Corporate Governance on Corporate Law* 1 (July 13, 2011) (unpublished preliminary draft), https://perma.cc/ZN5E-KQEJ.

6 *Restatement of the Law, Corporate Governance*, AM. L. INST., https://perma.cc/L5MF-PLET (last visited June 7, 2022).

7 *Id.*

8 *Id.* I have elsewhere argued that a restatement of corporate law is unnecessary given the dominance of Delaware law in this field. Stephen M. Bainbridge, *Do We Need a Restatement of the Law of Corporate Governance?*, 78 BUS. LAW. (forthcoming 2023), https://perma.cc/FTH6-JEXK.

9 RESTATEMENT OF THE L. OF CORP. GOVERNANCE § 2.01 (AM. L. INST., Tent. Draft No. 1, 2022) [hereinafter cited as RESTATEMENT].

10 *See* Benjamin T. Seymour, *Corporate Purpose and the Separation of Powers,* 36 BYU J. PUB. L. 113, 145 (2021) ("Corporate purpose, though a canonical subject of scholarly debate, has recently reemerged as the most contentious issue in corporate law."); Gregory H. Shill & Matthew L. Strand, *Diversity, ESG, and Latent Board Power,* 46 DEL. J. CORP. L. 255, 323 (2022) (noting the "renewed debates over corporate purpose").

11 PRINCIPLES OF CORP. GOVERNANCE: ANALYSIS AND RECOMMENDATIONS § 2.01 (AM. L. INST. 1994) [hereinafter cited as PRINCIPLES].

Although Section 2.01 of the Principles was relatively uncontroversial,[12] it proved even less influential than is typical of the Principles. It has been cited in only five decisions: as a *see also* citation in Justice Stevens's partial dissent in *Citizens United*;[13] in a concurrence in the Tenth Circuit's *Hobby Lobby* decision;[14] in a federal district court opinion, which was reversed on other grounds;[15] and two intermediate Massachusetts appellate court decisions.[16]

Assuming the Restatement is ultimately approved and the new version of § 2.01 ends up in the final draft in its current form, will it prove any more influential than did the Principles' version? Should it? Part I of this Comment sets the stage for the analysis by comparing the Restatement version of § 2.01 to that of the Principles. Part II asks whether it makes sense to refer to the corporation as having an objective. Part III assesses whether the new version of § 2.01 restates current law or tries to make new law. It also offers suggestions for improving the section so as to more accurately align with current law.[17]

II. THE NEW § 2.01 VERSUS THE OLD

Principles § 2.01 provided that:

> (a) Subject to the provisions of Subsection (b) and § 6.02 . . . , a corporation . . . should have as its objective the conduct of business activities with a view to enhancing corporate profit and shareholder gain.
> (b) Even if corporate profit and shareholder gain are not thereby enhanced, the corporation, in the conduct of its business:
>
> > (1) Is obliged, to the same extent as a natural person, to act within the boundaries set by law;

[12] Kathryn N. Fine, *The Corporate Governance Debate and the ALI Proposals: Reform or Restatement?*, 40 VAND. L. REV. 693, 700–01 (1987) ("Many scholars and practitioners consider section 2.01 to be one of the least controversial provisions in the ALI Principles.").

[13] Citizens United v. Fed. Election Comm'n, 558 U.S. 310, 470 (2010) (Stevens, J., dissenting in part).

[14] Hobby Lobby Stores, Inc. v. Sebelius, 723 F.3d 1114, 1147 (10th Cir. 2013) (Hartz, J., concurring), *aff'd sub nom*. Burwell v. Hobby Lobby Stores, Inc., 573 U.S. 682 (2014).

[15] Jordan v. Jewel Food Stores, Inc., 851 F. Supp. 2d 1102, 1111 (N.D. Ill. 2012), *rev'd*, 743 F.3d 509 (7th Cir. 2014).

[16] Crowley v. Commc'ns For Hosps., Inc., 573 N.E.2d 996, 1001 n..11 (Mass. App. 1991); Evans v. Multicon Constr. Corp., 574 N.E.2d 395, 399 (Mass. App. 1991).

[17] This article is deliberately agnostic on the underlying normative questions. I address the policy debate at length in my forthcoming book, STEPHEN M. BAINBRIDGE, THE PROFIT MOTIVE: IN DEFENSE OF SHAREHOLDER VALUE MAXIMIZATION (forthcoming 2023).

> (2) May take into account ethical considerations that are reasonably regarded as appropriate to the responsible conduct of business; and
> (3) May devote a reasonable amount of resources to public welfare, humanitarian, educational, and philanthropic purposes.[18]

Cross-referenced § 6.02 dealt with target board efforts to block unsolicited takeover bids.[19]

Restatement § 2.01 provides that:

> a) The objective of a corporation is to enhance the economic value of the corporation, within the boundaries of the law;
>
> 1) in common-law jurisdictions: for the benefit of the corporation's shareholders. In doing so, a corporation may consider:
>
> a) the interests of the corporation's employees;
> b) the desirability of fostering the corporation's business relationships with suppliers, customers, and others;
> c) the impact of the corporation's operations on the community and the environment; and
> d) ethical considerations related to the responsible conduct of business;
>
> 2) in stakeholder jurisdictions: for the benefit of the corporation's shareholders and/or, to the extent permitted by state law, for the benefit of employees, suppliers, customers, communities, or any other constituencies.
>
> b) A corporation, in the conduct of its business, may devote a reasonable amount of resources to public-welfare, humanitarian, educational, and philanthropic purposes, whether or not doing so enhances the economic value of the corporation.[20]

The first difference to be noted between the two is the absence in the Restatement version of a cross-reference to board duties in takeovers. The comments, however, suggest that the drafters will deal with those duties separately.[21] In Part IV below, I return to

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18 PRINCIPLES § 2.01.

19 *Id.* § 6.02.

20 RESTATEMENT § 2.01.

21 RESTATEMENT § 2.01 cmt. a (noting that § 2.01 "sets a backdrop for the other, more specific provisions of the Restatement," including restating the duties of directors in control transactions and tender offers in forthcoming Chapter 6). For an overview of

this issue to critique the Principles' approach and offer some suggestions for the Restatement.

Turning to substantive differences between the two, Principles § 2.01(b) obliged the corporation to obey the law and allowed it to consider appropriate ethical concerns[22] and to engage in philanthropic activities, in all cases, even if doing so did not promote shareholder value or corporate profit.[23] In contrast, in Restatement § 2.01, engaging in charitable activities—defined broadly as "public-welfare, humanitarian, educational, and philanthropic purposes"—is the only action expressly permitted "whether or not doing so enhances the economic value of the corporation."[24] This framing by the Restatement's drafters led Professor Eric Orts to object that:

> Allowing only an "economic objective" forces out any ethical or environmental consideration that does not technically qualify as a long-term economic rationalization. The Restatement's § 2.01 departs from the recognition in the Principles that ethical considerations may conflict with the economic objective, and that directors and officers may nevertheless follow their consciences in these situations. Even Milton Friedman, a famous (or infamous) champion of the economic objective in business corporations, conceded that profit-seeking must "conform[] to the basic rules of the society, both those embodied in law and those embodied in ethical custom." To employ an updated example, doing the right thing with respect to the climate emergency may require a particular firm (such as a big oil company) to sacrifice some profits even as calculated over the long term. The Restatement's § 2.01 seems instead to require big oil companies to maximize their long-term profits even it means burning our planet beyond all recognition. It seems also to require a corporation adopting an anti-racist personnel policy to justify it with an

PRINCIPLES § 6.02 and a comparison of that section to Delaware law, see STEPHEN M. BAINBRIDGE, MERGERS AND ACQUISITIONS 448–49 (4th ed. 2021).

22 Principles Chief Reporter Melvin Eisenberg explained that, "[b]ecause corporate officials deal with other people's money, they may properly take ethical principles into account only where those principles are generally recognized as relevant to the conduct of business." Melvin A. Eisenberg, *The Objective and Conduct of the Corporation and Corporate Structure*, *in* ALI-ABA COURSE OF STUDY: ABA'S PRINCIPLES OF CORPORATE GOVERNANCE, C973 ALI-ABA 1, 8 (1994). Eisenberg further explained that the relevant principles depended on the natnure of the business, offering newspapers as an example of a business to which "special policy considerations may attach." *Id.*

23 PRINCIPLES § 2.01(b).

24 RESTATEMENT § 2.01.

> economic or "business case" rationale rather than an appeal to an ethics of mutual respect and equal treatment.[25]

It seems unlikely, however, that the drafters intended thereby to effect any substantive change vis-à-vis the Principles. Comment e to Restatement § 2.01, for example, states that "corporations may take into account their effects on the environment, as well as the social impact of their operations."[26] Comment e also states that "the economic objective does not imply that the corporation must extract the last penny of profit out of every transaction in which it is involved."[27] Illustration 6 states that it would be licit for a corporation to adopt a mission statement committing the company "to creating a sustainable, low-carbon future, advancing equality and diversity, and fostering employee success."[28] Illustrations 27 and 28 both involve hypothetical oil companies that voluntarily reduce oil production claiming that doing so will both save the planet and be profitable in the long term.[29] In both, the drafters conclude that § 2.01 is not violated.[30] Given that the business judgment rule almost certainly would protect an informed decision by the board that the reduction would produce sustainable, long-term profits,[31] Professor Orts' concern seems misplaced.

A much more important difference is that the Restatement expressly splits out what it calls "stakeholder jurisdictions" from what it calls "common-law jurisdictions."[32] Since Pennsylvania adopted the first constituency statute in 1983,[33] more than thirty additional states have adopted constituency statutes (a.k.a. non-shareholder constituency statutes or stakeholder statutes).[34] Although the details vary somewhat, the statutes generally

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25 Eric W. Orts, *The ALI's Restatement of the Corporate Objective Is Flawed*, THE CLS BLUE SKY BLOG (June 6, 2022) (citation omitted), https://perma.cc/Q582-GEHJ.

26 RESTATEMENT § 2.01 cmt. e.

27 *Id.*

28 *Id.* § 2.01 cmt. e, illus. 6.

29 *Id.* § 2.01 cmt. h, illus. 27–28.

30 *Id.*

31 *See id.* § 4.02 (setting out the business judgment rule's requirements and explaining that, unless plaintiff proves they were not met, a court shall defer to the judgment of the directors or officers).

32 The Restatement drafters not infrequently use "traditional" interchangeably with "common law." *See, e.g.*, RESTATEMENT § 2.01 Reporters' Note 3 (referring to "courts in traditional jurisdictions").

33 D. Gordon Smith, *The Shareholder Primacy Norm*, 23 J. CORP. L. 277, 289 (1998).

34 BAINBRIDGE, *supra* note 21, at 449–52; *see also* Amanda Wise, *Corporate Law and the Business Roundtable: Adding to the Debate on Shareholder Primacy vs. Stakeholder Theory*, 49 CAP. U.L. REV. 499, 516 (2021).

authorize directors to consider various factors other than shareholder value maximization when making corporate decisions.[35] Massachusetts' statute is typical:

> (a) A director shall discharge his duties as a director, including his duties as a member of a committee: . . . (3) in a manner the director reasonably believes to be in the best interests of the corporation. In determining what the director reasonably believes to be in the best interests of the corporation, a director may consider the interests of the corporation's employees, suppliers, creditors and customers, the economy of the state, the region and the nation, community and societal considerations, and the long-term and short-term interests of the corporation and its shareholders, including the possibility that these interests may be best served by the continued independence of the corporation.[36]

The Principles' drafters did not address these statutes, instead relegating them to the Reporter's Notes, where the drafters opined that "it is clear that such statutes can be interpreted so as to be consistent with § 2.01."[37]

In the Restatement, constituency statutes are promoted to the black letter law. Oddly, however, the black letter text of § 2.01(a)(2) suggests that in states with a constituency statute it is only licit for directors to consider the interests of various constituencies.[38] As even a cursory reading of the Massachusetts statute suggests, however, the name constituency statutes is somewhat of a misnomer. Massachusetts allows directors to consider such factors as the economy of the state or nation and "societal considerations," for example, neither of which fit within a conventional definition of constituency.[39] Thirteen other states have similar provisions.[40]

In contrast, § 2.01(a)(1) explicitly contemplates that directors of corporations in common law jurisdictions may go beyond the interests of the corporation's constituencies to consider

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[35] For a detailed breakdown of what factors the individual statutes allow directors to consider, see BAINBRIDGE, *supra* note 21, at 449–52.

[36] MASS. GEN. LAWS ch. 156D, § 8.30(a).

[37] PRINCIPLES § 2.01, Reporter's Note 8.

[38] RESTATEMENT § 2.01(a)(2).

[39] *See, e.g.*, *Constituency*, MERRIAM-WEBSTER'S COLLEGIATE DICTIONARY (11th ed. 2020) (defining constituency, inter alia, as "the people involved in or served by an organization (as a business or institution)").

[40] *See* BAINBRIDGE, *supra* note 21, at 449–52 nn. 243–70 (specifying what factors the various statutes allow directors to consider).

environmental and ethical concerns.[41] This difference led Professor Orts to complain that Restatement § 2.01 "misinterprets the legal import of corporate constituency statutes in a manner that unduly narrows the discretion of corporate directors and managers."[42]

> For example, "the environment" and "ethical considerations" are explicitly included as allowable decision-making factors in common-law jurisdictions but omitted in stakeholder jurisdictions (§ 2.01(a)). Surely corporate decisionmakers in stakeholder jurisdictions may also take account of environmental and ethical considerations even if they are not specified as stakeholder interests.[43]

I disagree with Professor Orts' criticism of the Restatement drafters' reading of the constituency statutes. The factors most commonly authorized for director consideration by the statutes are the long-term interests of the corporation, firm profitability, growth prospects, employees, customers, suppliers, creditors, and communities.[44] No state explicitly lists the environment as a factor directors are authorized to consider.[45] Only 10 states authorize directors to consider "any other appropriate factors,"[46] which may implicitly authorize consideration of environmental concerns. In this regard, the Restatement drafters correctly interpreted the plain text of constituency statutes. Whether a court might take a broader view of the factors directors may consider in a stakeholder jurisdiction is uncertain, as there is almost no caselaw interpreting the statutes.[47]

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41 RESTATEMENT § 2.01(a)(1)(c)–(d).

42 Orts, *supra* note 25.

43 *Id.*

44 *See* BAINBRIDGE, *supra* note 21, at 449–52 tbl. 10-1 (listing the factors directors may consider on a state-by-state basis).

45 *See* Alexandra Leavy, *Necessity Is the Mother of Invention: A Renewed Call to Engage the SEC on Social Disclosure*, 2014 COLUM. BUS. L. REV. 463, 494 (2014) ("Many constituency statutes . . . do not allow consideration of environmental concerns."); Steven J. Haymore, Note, *Public(ly Oriented) Companies: B Corporations and the Delaware Stakeholder Provision Dilemma*, 64 VAND. L. REV. 1311, 1341 (2011) (asserting that "current constituency statutes omit any protection for directors who base decisions on consideration for the environment"); *see also* BAINBRIDGE, *supra* note 21 at 449–52 nn. 242–70 (specifying the other factors the statutes permit directors to consider, none of which include the environment).

46 *See* BAINBRIDGE, *supra* note 21, at 449–52 tbl. 1 (specifying whether state statutes permit consideration of "any other appropriate factors").

47 *See* Julian Velasco, *The Fundamental Rights of the Shareholder*, 40 U.C. DAVIS L. REV. 407, 464 (2006) ("Cases involving constituency statutes have been few and far between, and they rarely, if ever, hinge upon such provisions.").

III. Do Corporations Have Objectives?

Edward, First Baron Thurlow, reportedly asked: "Did you ever expect a corporation to have a conscience, when it has no soul to be damned, and no body to be kicked?"[48] To say that a corporation has an objective is thus a form of the reification fallacy.[49] To be sure, this is a pervasive error,[50] and for good reason:

> Reification, like the use of metaphor, can be useful. Indeed, it would be difficult to communicate effectively without it. Depending on its uses, however, reification can also be a barrier to effective analysis. It may be conceptually useful, for example, to depict corporations as paying taxes, but we delude ourselves and risk error if we do not appreciate that the burden of taxes is borne by individuals.[51]

It thus makes communication easier to say that the corporation has an objective, as for example when we speak of the "corporate purpose debate," but clarity of analysis obliges us to look at the objectives of people—not those of legal fictions.

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[48] John C. Coffee, Jr., "*No Soul to Damn: No Body to Kick": An Unscandalized Inquiry into the Problem of Corporate Punishment*, 79 MICH. L. REV. 386, 386 (1981). Other commentators assert that Thurlow actually said that "[c]orporations have neither bodies to be punished, nor souls to be condemned; they therefore do as they like." *See* Gilbert Geis & Joseph F. C. Dimento, *Empirical Evidence and the Legal Doctrine of Corporate Criminal Liability*, 29 AM. J. CRIM. L. 341, 342 n.3 (2002) (citing an 1814 source).

[49] "The lay definition of reification is simply to treat something which is in fact contingent and socially constructed as though it were natural, inevitable, necessary. It means to 'thingify.'" Norman W. Spaulding III, *Totemism Transcended?: The Ambivalent Aspirations of Richard Posner's Jurisprudence*, 26 SETON HALL L. REV. 1810, 1844 (1996). "[I]n reification we do not simply make a kind of private error about the true nature of what we are talking about; we participate in an unconscious conspiracy with others whereby everyone knows of the fallacy, and yet denies that the fallacy exists." Peter Gabel, *Reification in Legal Reasoning*, *in* 3 RSCH. IN L. AND SOCIO. 25, 26 (Steven Spitzer ed., 1980).

[50] *See* G. Mitu Gulati, William A. Klein, & Eric M. Zolt, *Connected Contracts*, 47 UCLA L. REV. 887, 890 (2000) ("The corporation is generally reified and often anthropomorphized.").

[51] *Id.* Looking at people rather than entities is also more correct from a theoretical perspective, as least for those who take "a contractarian view of the corporation[,]" as it allows one "to avoid reification of the corporation by viewing it as a nexus of contracts." D.A. Jeremy Telman, *The Business Judgment Rule, Disclosure, and Executive Compensation*, 81 TUL. L. REV. 829, 855 (2007). Some commentators contend it is more accurate to say a corporation has a nexus of contracts than to say the corporation is a nexus of contracts. *See, e.g.,* Stephen M. Bainbridge, *The Board of Directors as Nexus of Contracts*, 88 IOWA L. REV. 1, 17 (2002) ("After all, to say that the firm is a nexus is to imply the existence of a core or kernel capable of contracting. But kernels do not contract—people do."). Nevertheless, these commentators agree that reification needs to be avoided to ensure analytical clarity. *See id.* (arguing that "it does us no good to avoid reifying the firm by reifying the nexus at the center of the firm").

The Restatement nevertheless embraces the reification fallacy by stating that § 2.01 sets forth the objective of the corporation and does not "impose any obligations or liabilities on corporate officials."[52] But what then is the purpose of § 2.01? Oddly, the drafters' answer to that question focuses on people rather than entities:

> [B]y stating an objective, the law informs the individuals involved in running a corporation, e.g., directors and officers, what the corporation's ultimate objective is, and is not. As such, a corporation's objective is the beginning (but only the beginning) of an answer to a new director's reasonable question: "What are we trying to accomplish here?"[53]

A better answer to the director's question might be "you have a fiduciary duty to work with your fellow board members to maximize shareholder value." After all, telling someone who asks "why am I here" that the entity has an objective is not directly responsive. As a point of comparison, consider a newly hired law professor who asks what she is to do. Telling her that the law school's mission is to educate the next generation and advance human knowledge is far less helpful than telling her that her duty is to show up at 9 a.m. on Mondays, Wednesdays, and Thursdays to teach Securities Regulation in Room 1457.

The drafters further explain that § 2.01 is intended to set "a backdrop for the other, more specific provisions of the Restatement."[54] The drafters' reference here is to forthcoming provisions

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[52] RESTATEMENT § 2.01 cmt. a.

[53] *Id.* The illustrations to § 2.01 likewise focus on entities rather than the actual decision makers (i.e., people). Illustration 1, for example, proffers the following hypothetical:

> Corporation A is a publicly held corporation with annual earnings in the $20–30 million range. A has entered into a contract that is unenforceable against it under the Statute of Frauds. Performance of the contract will involve a loss of $700,000. Corporation A nevertheless performs the contract because the relevant corporate decisionmaker made a judgment, in a manner that meets the standards of § 4.02, that the loss is likely to be exceeded by long-run profits from preserving confidence in A's willingness to honor its commitments. Corporation A's action does not involve a departure from the economic objective stated in § 2.01 in either type of jurisdiction.

Id., § 2.01 cmt. e, illus. 1 (cross reference omitted). In fact, of course, *A* did not enter into a contract. Rather, an agent endowed with actual authority entered into the contract on behalf of the legal fiction known as Corporation *A*. The corporation did not perform the contract. Rather, as the drafters recognize, a decision-maker endowed with authority to make such decisions decided that the contract should be performed and delegated authority to agents to do so. Would it not thus be more sensible to ask whether the decision-maker complied with the relevant decision-making norm?

[54] *Id.*, § 2.01 cmt. a.

that will set out the fiduciary "standards of conduct for corporate officials and govern liability for conduct that falls below those standards."[55] If the point is to specify a baseline for specific provisions dealing with the duties of officers and directors, however, why not phrase the baseline in terms of those duties rather than as an objective of the entity?

The problem is highlighted by illustrations 5 and 8. The former involves a finance company that voluntarily adopts a program of devoting 5 percent of its loans to "inner-city projects that do not meet its normal risk standards" in the belief that the long-term health of urban areas will redound to the company's long-term economic benefit. According to the drafters, the action satisfies § 2.01.[56] In the latter, the drafters tweak the hypothetical by increasing the amount to 40 percent of the company's loan portfolio, by increasing the short-term losses thereby suffered from $3 million to $24 million, by having the relevant corporate decision-maker fail to identify any countervailing benefits, and by asserting that there are no countervailing benefits.[57] As to common law jurisdictions, the drafters assert that the company has departed "from the principles stated in § 2.01."[58] But so what? If there are no consequences to the corporation, who cares? Is not the real question whether the business judgment rule would prevent a court from reviewing the merits of the decision and thereby insulate the relevant decision-makers from any potential liability for a breach of their duty of care?[59]

In fact, the law § 2.01 purports to restate expressly focuses on questions of fiduciary obligation and business judgment. Both the common law and constituency statutes focus on the obligations of people—specifically, the directors of corporations—rather than those of entities. Granted, *Dodge v. Ford Motor Co.*[60] explains that a "corporation is organized and carried on primarily

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[55] *Id.*

[56] *Id.*, § 2.01 cmt. e, illus. 5.

[57] *Id.*, § 2.01 cmt. e, illus. 8.

[58] *Id.*

[59] Note that if the business judgment rule applies, the tweaks introduced in illustration 8 will not affect the outcome. As the Delaware Supreme Court explained in *Brehm v. Eisner*, 746 A.2d 244, 264 (Del. 2000), the concept of "substantive due care" "is foreign to the business judgment rule. Courts do not measure, weigh or quantify directors' judgments. We do not even decide if they are reasonable in this context." Similarly, in *Shlensky v. Wrigley*, 237 N.E.2d 776, 780 (Ill. App. 1st Dist. 1968), the court explained that where the business judgment rule applies deciding whether "the decision of the directors was a correct one . . . is beyond [a court's] jurisdiction and ability."

[60] 170 N.W. 668 (Mich. 1919).

for the profit of the stockholders,"[61] but the Michigan Supreme Court immediately linked that principle to the duties of directors. Instead of expounding on the objective of the corporation, the court focused on directors' powers and the scope of their discretion.[62] Similarly, in *eBay Domestic Holdings, Inc. v. Newmark*,[63] the Delaware Chancery Court discussed the nature of a for-profit corporation but focused on the consequent duties of the directors.[64] Likewise, constituency statutes typically do not state a corporate objective, but rather amend the adopting state's "existing statutory statement of the director's duty of due care."[65]

All of this may seem pedantic and/or scholastic, but it matters. By reifying the corporation, the Principles and the Restatement ignore the basic point that the corporation can only accomplish its objectives by acting through agents. In turn, § 2.01—both the old and new—ignores the basic fact that those agents may have a conflict of interest. Suppose the corporation must decide between two possible courses of action, one of which will benefit the shareholders at the expense of the stakeholders and one of which would not benefit the shareholders but would qualify as a "public-welfare, humanitarian, educational, or philanthropic" action that § 2.01 allows to be undertaken even if there is no evidence that it will benefit the shareholders. Of course, the corporation—being a mere legal fiction—will not make that decision. Instead, directors or officers will make it. Suppose the first course of action will benefit the decision-maker, while the second would not. At the very least, the decision maker will be tempted to choose the first alternative and justify it by reference to the benefits to shareholders. Conversely, if the second alternative favors the decision-maker's self-interest, the decision maker will be tempted to opt for it and justify that decision on humanitarian grounds. Section 2.01 gives decision-makers "wide discretion" to make such choices.[66]

It may be the rare case in which managers use that discretion to benefit themselves financially at the expense of shareholders and/or stakeholders, but it seems likely that managers often use their discretion to generate psychic benefits by directing corporate resources to pet charities and other personal preferences. As

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61 *Id.* at 684.

62 *Id.*

63 16 A.3d 1 (Del. Ch. 2010).

64 *See id.* at 34 ("Having chosen a for-profit corporate form, the craigslist directors are bound by the fiduciary duties and standards that accompany that form.").

65 BAINBRIDGE, *supra* note 21, at 449.

66 Fine, *supra* note 12, at 701.

Jonathan Macey explained, Principles § 2.01 thus gave the ALI's imprimatur to a regime that would increase rather than decrease agency costs:

> Although corporate philanthropy often serves corporate and shareholder interests, when corporate philanthropy does not serve shareholder interests, it is indefensible to allow management to use shareholders' money to pursue their own private view of the good. If managers of public corporations, who generally are not considered undercompensated by any measure, wish to aid some humanitarian, educational, or philanthropic cause, they should do so with their own, and not their shareholders', resources. From the ALI's perspective, of course, these provisions benefit society by increasing the flow of funds to worthy causes. But from a business perspective—particularly that of investors—the ALI's provisions simply empower corporate management to divert corporate resources for private interests that they are able to describe as philanthropic.[67]

Larry Ribstein similarly observed that the Principles, which he derisively referred to as the ALI "code," posited "that the managers of all corporations must be free to act in a 'socially responsible' way whether or not the shareholders want their resources to be used in this way."[68] Ribstein and other critics thus complained that the Principles failed to provide for adequate shareholder oversight of the process by which philanthropic activities are chosen and failed to provide any mechanism for allowing shareholders to voice their preferences as to where such activities should be directed.[69]

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[67] Jonathan R. Macey, *The Transformation of the American Law Institute*, 61 GEO. WASH. L. REV. 1212, 1219 (1993).

[68] Larry E. Ribstein, *The Mandatory Nature of the ALI Code*, 61 GEO. WASH. L. REV. 984, 1001 (1993).

[69] Michael Bradley, Cindy A. Schipani, Anant K. Sundaram, & James P. Walsh, *The Purposes and Accountability of the Corporation in Contemporary Society: Corporate Governance at a Crossroads*, 62 L. & CONTEMP. PROBS. 9, 49 (Summer 1999). In contrast, I have argued that:

> Board discretion over issues like charitable giving is the inescapable side-effect of separating ownership and control. If there are good reasons for maintaining that separation, and there are, the board's discretionary authority must be preserved. . . . [H]olding directors accountable for their use of that discretionary authority inevitably limits that discretion.

STEPHEN M. BAINBRIDGE, CORPORATION LAW AND ECONOMICS 437–38 (2002). For a more elaborate defense of the proposition that corporate law does and should generally defer to board decisions, which situates that defense in my board-centric director primacy model, see *id.* at 195–208.

Ribstein contended that case law did not permit directors and managers to indulge themselves in this way.[70] Instead, by focusing on the decision maker's fiduciary duties, and forbidding them from adopting "a corporate policy that specifically, clearly, and admittedly seeks *not* to maximize the economic value of a for-profit Delaware corporation for the benefit of its stockholders,"[71] the case law helps prevent corporate social responsibility from being used to camouflage self-interested decisions. The Restatement should do likewise.

In sum, the shareholder value maximization norm and the so-called law of corporate purpose properly "ha[ve] been read into the fiduciary duties of loyalty and care and their progeny."[72] As such, it is inaccurate and unhelpful to frame the question as one of corporate objective rather than one of fiduciary obligation.[73] The drafters should reframe and repurpose § 2.01 accordingly.

IV. THE SUBSTANTIVE LAW OF CORPORATE PURPOSE

A. The Nature of the Objective

The Principles defined the corporate objective as enhancing "corporate profit and shareholder gain."[74] One immediately apparent difficulty with that definition was that corporate profit and shareholder gain are not necessarily synonymous.[75] This is

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[70] *See* Ribstein, *supra* note 68 at 1002 (arguing that "there is prominent case law, most notably *Dodge v. Ford Motor Co.*, that restricts directors' power to act in ways that do not benefit the shareholders directly").

[71] eBay Domestic Holdings, Inc. v. Newmark, 16 A.3d 1, 34 (Del. Ch. 2010).

[72] Kyle Westaway & Dirk Sampselle, *The Benefit Corporation: An Economic Analysis with Recommendations to Courts, Boards, and Legislatures*, in NEW YORK BENEFIT CORPORATIONS AT FIVE YEARS OLD: A LOOK BACK AND A PEEK INTO THE FUTURE (2016), Westlaw 20160929P NYCBAR 35.

[73] Haskell Murray has aptly summarized my position: "Bainbridge does not 'think it's useful to ask the question of "what purpose does the law mandate the corporation pursue?"' Instead, Bainbridge argues 'it is far more preferable to operationalize this discussion as a question of the fiduciary duties of corporate officers and directors than as a corporate purpose.'" J. Haskell Murray, *Choose Your Own Master: Social Enterprise, Certifications, and Benefit Corporation Statutes*, 2 AM. U. BUS. L. REV. 1, 8 n.26 (2012).

[74] PRINCIPLES § 2.01(a).

[75] As Henry Hu explained:

> [T]he financial well-being of the corporation is distinct from the well-being of the shareholder in the publicly held corporation. Specifically, a diversified shareholder would not want the managers of a publicly held corporation to act in a way intended to ensure the well-being of the corporation. If managers were to focus on the total risk of an investment project instead of the nondiversifiable risk, for instance, they might enhance the health of the firm, but they would probably not maximize the share price. Shareholders, regardless of their

not a mere quibble. Consider, for example, a 1980s-style leveraged buyout. Such a transaction typically will adversely impact economic returns to stakeholders,[76] while producing substantial shareholder gains.[77] The drafters were aware of this problem, as the commentary to § 2.01 in Tentative Draft Number 2 of the Principles acknowledged "[p]ossible tensions" between corporate profit and shareholder gain.[78] Curiously, however, the commentary to § 2.01, as it was finally adopted, simply elided that difficulty by suggesting that the stated corporate objective "may be thought of as a broad injunction to enhance economic returns . . . ."[79]

In this regard, the Principles were inconsistent with longstanding corporate law. As long ago as 1905, for example, a New Jersey court explained that "[t]he success of a great business or manufacturing corporation is measured by what the stockholders get, and not by mere accumulation of assets."[80] The court therefore held that the directors could only retain profits and expand the firm so long as doing so did not lead to the "practical starvation of the stockholders."[81]

The drafters of the Restatement wisely avoided this problem by opting for a single maxim: namely, enhancement of "the economic value of the corporation, within the bounds of the law . . . for the benefit of the shareholders," while allowing the corporation in the course of doing so to consider the specified four sets of non-shareholder interests.[82] Setting aside the question of whether directors may make tradeoffs between shareholder interests and

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> individual risk preferences, generally would want managers instead to focus primarily on nondiversifiable risk in evaluating corporate investment opportunities.

Henry T.C. Hu, *Risk, Time, and Fiduciary Principles in Corporate Investment*, 38 UCLA L. REV. 277, 299–300 (1990) (footnote omitted).

76 *See* Marcel Kahan & Michael Klausner, *Antitakeover Provisions in Bonds: Bondholder Protection or Management Entrenchment?*, 40 UCLA L. REV. 931, 933 n.2 (1993) (stating that, "as a result of mergers, acquisitions or leveraged buyouts" between 1984 and 1988, the bonds of 183 companies "lost value").

77 Bernard Black & Joseph A. Grundfest, *Shareholder Gains from Takeovers and Restructurings Between 1981 and 1986: $162 Billion Is a Lot of Money*, J. APPLIED CORP. FIN., Spring 1988, at 5 (estimating that gains to shareholders from takeovers between 1981 and 1985 were $162 billion).

78 *See* Donald E. Schwartz, *Defining the Corporate Objective: Section 2.01 of the ALI's Principles*, 52 GEO. WASH. L. REV. 511, 527 (1984) (quoting Principles of Corp. Governance: Analysis and Recommendations § 2.01 (Am. L. Inst., Tent. Draft No. 2, 1984)).

79 PRINCIPLES § 2.01 cmt. f.

80 Raynolds v. Diamond Mills Paper Co., 60 A. 941, 948 (N.J. Ch. 1905).

81 *Id.* at 945.

82 RESTATEMENT § 2.01(a). The language quoted in the text restates what the drafters believe to be the law in common law states. *Id.*

one or more of the four sets of non-shareholder interests,[83] this accurately restates current law, which consistently defines the corporate objective[84] as being the maximization of the long-term benefit of the shareholders.[85] Indeed, the Restatement's formulation seems to be a slight tweak of Chancellor William Chandler's *eBay* decision, which held that Delaware requires directors "to maximize the economic value of a for-profit Delaware corporation for the benefit of its stockholders."[86]

The drafters also tracked current law by confirming that corporations have substantial discretion to select the time frame and means by which the economic value will be enhanced.[87] There is no obligation for directors to maximize short-term gain at the expense of sustainable long-term gain.[88] Instead of squeezing every last penny out of a transaction or venture, management is entitled to take appropriate ethical considerations into account and is obliged to act within the bounds of the law.[89]

Finally, the drafters also tracked current law by ducking the question of how to measure the corporation's economic value and, accordingly, how to determine whether that value has been enhanced. Does one look to the company's market capitalization, book value, enterprise value, discounted future cash flows, Tobins' Q, or some other metric? Both courts and commentators

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83 *See infra* Part B.

84 In light of the discussion in Part III *supra*, I use the term "corporate objective" hereinafter solely for the sake of semantic convenience and for coherence with the phrasing of the Restatement.

85 *See, e.g.,* Dodge v. Ford Motor Co., 170 N.W. 668, 684 (Mich. 1919) (holding that that business corporations are "organized and carried on primarily for the profit of the stockholders"); Malone v. Brincat, 722 A.2d 5, 9 (Del. 1998) (holding that that directors have a "legal responsibility to manage the business of a corporation for the benefit of its shareholder owners"); Katz v. Oak Industries Inc., 508 A.2d 873, 879 (Del. Ch. 1986) (holding that that directors have obligation "to attempt, within the law, to maximize the long-run interests of the corporation's stockholders"); TW ServicesServs., Inc. v. SWT Acquisition Corp., 1989 WL 20290, at *7 (Del. Ch. Mar. 2, 1989) (Allen, J.) (stating that directors "owe a duty to shareholders as a class to manage the corporation within the law, with due care and in a way intended to maximize the long run interests of shareholders").

86 eBay Domestic Holdings, Inc. v. Newmark, 16 A.3d 1, 34 (Del. Ch. 2010).

87 As for current law, see Daniel J. H. Greenwood, *Discussing Corporate Misbehavior: The Conflicting Norms of Market, Agency, Profit and Loyalty,* 70 BROOK. L. REV. 1213, 1235 (2005) (stating that "courts generally do not require anything resembling a strong version of short-term profit-maximization"); Darian M. Ibrahim, *A Return to Descartes: Property, Profit, and the Corporate Ownership of Animals*, 70 L. & CONTEMP. PROBS. 89, 105 (2007) (stating that "even if the law mandates that corporate managers pursue the sole end of profit maximization, it does not require that profits be maximized in the short term").

88 *See* RESTATEMENT § 2.01 cmt. e (explaining that the "economic objective does not mean that the directors or officers must maximize shareholder value in the short term").

89 *Id.*

have generally avoided offering precise answers to that question.[90] Consistent with the general policy of deference to unconflicted board decisions,[91] however, the drafters might usefully observe that such enhancement can take a variety of forms, including dividends, stock repurchases, and takeover premia.

B. Are Tradeoffs Allowed?

A key unanswered question is whether § 2.01's authorization for the corporation to consider stakeholder interests allows the corporation to make tradeoffs between shareholder and stakeholder interests. In other words, after considering stakeholder interests, could the corporation make a decision that enhances the value of the corporation—whatever that means—by transferring wealth from shareholders to stakeholders? Alternatively, could directors make a decision that provides modest benefits to shareholders while providing substantially greater benefits to the stakeholders?

1. The Restatement's Ambiguity

Prominent takeover lawyer Martin Lipton has advanced what he calls a "New Paradigm" for understanding corporate law, under which it is proper for a board to balance "total shareholder return and earnings targets . . . against a more holistic understanding of firm value."[92] Indeed, Lipton asserts that "directors have the ability, and in many instances *the obligation*, to use their reasoned business judgment to balance the interests of all

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90 *See* Eric Franklin Amarante, *What We Talk About When We Talk About Shareholder Wealth Maximization*, 19 TRANSACTIONS: TENN. J. BUS. L. 455, 459 (2017) (arguing that "each of the words in the phrase 'shareholder wealth maximization' lacks sufficient definition to provide any reasonable guidance"); Jill E. Fisch, *Measuring Efficiency in Corporate Law: The Role of Shareholder Primacy,* 31 J. CORP. L. 637, 639 (2006) (noting that although empirical studies of "the shareholder primacy norm . . . . [F]requently fail to define firm value explicitly, they incorporate the concept of shareholder primacy by evaluating legal rules in terms of their effect on measures of shareholder value such as stock price and Tobin's Q"); Joan MacLeod Heminway, *Shareholder Wealth Maximization as a Function of Statutes, Decisional Law, and Organic Documents*, 74 WASH. & LEE L. REV. 939, 970 (2017) (observing that, "although commentators on the shareholder wealth maximization norm most often talk about 'wealth' without definition, it is clear that many intend to refer to wealth in its simple, financial form").

91 *See* RESTATEMENT § 4.02 Reporters' Note 9 ("Cases have generally afforded deference to decisions in which a majority of the board acted in compliance with the business judgment rule.").

92 Martin Lipton, *Corporate Governance: The New Paradigm*, HARV. L. SCH. F. ON CORP. GOVERNANCE (Jan. 11, 2017), https://perma.cc/G2E9-V35B.

stakeholders."[93] In other words, Lipton believes it is licit for directors to make tradeoffs between the interests of shareholders and stakeholders and, presumably, at least in some cases to favor one set of interests at the expense of the other.

The Restatement's drafters take note of Lipton's argument and treat it with a curious degree of equivocation, perhaps reflecting Lipton's influence as an emeritus member of the ALI Council and an active member of the Restatement's board of advisers.[94] In the Reporters' notes, they quote an essay by Lipton, in which he opines that "[t]he purpose of a corporation is to conduct a lawful, ethical, profitable and sustainable business in order to ensure its success and grow its value over the long term" and that doing so requires consideration of stakeholder interests.[95] The Restatement drafters then observe that:

> This vision of a stakeholder-oriented corporate governance that leads to long-term value creation is consistent with the statement in the black letter in both traditional and stakeholder jurisdictions, although, under current law, not mandated by either. To the extent that there are serious tradeoffs between the interests of shareholders and other stakeholders, the choice to incorporate in a traditional jurisdiction or a "stakeholder" jurisdiction or as a "benefit corporation" will affect how much flexibility exists. If this movement continues to grow, it could result in changes in the law applicable to public corporations, large corporations, or even all corporations.[96]

There are several noteworthy points in this passage. First, notice that neither Lipton nor the Restatement drafters qualify their references to "value" with the limiting phrase "for the benefit of the shareholders." Second, the drafters observe that the degree of flexibility available to make tradeoffs depends on where one has chosen to incorporate. Third, the drafters suggest that Lipton's vision is not yet but might become the law.[97]

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93 Martin Lipton, *Directors have a duty to look beyond their shareholders*, FIN. TIMES (Sept. 17, 2019) (emphasis supplied), https://perma.cc/E63M-9FMN.

94 *See* RESTATEMENT at v (listing advisers).

95 RESTATEMENT § 2.01 Reporters' Note 4 (quoting Martin Lipton, et. al., *On the Purpose of the Corporation*, HARV L. SCH. F. ON CORP. GOVERNANCE (May 27, 2020), https://perma.cc/6HQ9-WKXK).

96 *Id.*

97 The Restatement elsewhere asserts that in both common law and stakeholder jurisdictions "boards of directors have substantial discretion to balance the interests of all stakeholders," RESTATEMENT § 2.01 cmt. a, which also fails to provide a definitive answer.

If by all of this the drafters mean to adopt Lipton's position that directors can make tradeoffs between shareholder value and stakeholder impact—accepting a reduction in shareholder value so as to preserve or enhance stakeholder welfare—the Restatement represents a departure from existing law.[98] To be sure, the comments to § 2.01 somewhat clarify the drafters' position, by stating that:

> When decisions involve tradeoffs among stakeholders, the differences between the models become more important and can affect outcome. While under the traditional approach, consideration of nonshareholder interests must be "rationally related" to shareholder benefits, in a "may" or "shall" jurisdiction, consideration of nonshareholder interests sometimes will not only be permissible without regard to shareholder benefit but may be mandatory.[99]

Yet, as we shall see, neither statement is entirely accurate.[100]

2. The Law in Common Law Jurisdictions

The Restatement drafters opine that common law jurisdictions require that any "consideration of nonshareholder interests must be 'rationally related' to shareholder benefits."[101] It is true that *Revlon* so held.[102] As the Chancery Court later explained in *eBay*, where the business judgment rule applies, Delaware courts "will not question rational judgments about how promoting non-stockholder interests . . . ultimately promote stockholder value."[103] In this context, the term "rational"

> is to be equated with conceivable or imaginable and means only that the court will not even look at the board's judgment if there is any possibility that it was actuated by a legitimate business reason. It clearly does not mean, and cannot legitimately be cited for the proposition, that individual directors

98 *See infra* notes 101–124 and accompanying text (discussing current law).

99 RESTATEMENT § 2.01 cmt. a.

100 *See infra* notes 101–124 and accompanying text (discussing current law).

101 RESTATEMENT § 2.01 cmt. a.

102 Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc., 506 A.2d 173, 182 (Del. 1986) ("A board may have regard for various constituencies in discharging its responsibilities, provided there are rationally related benefits accruing to the stockholders.").

103 *See* eBay Domestic Holdings, Inc. v. Newmark, 16 A.3d 1, 33 (Del. Ch. 2010).

> must have, and be prepared to put forth, proof of rational reasons for their decisions.[104]

As former Delaware Chancellor Allen explained, "such limited substantive review as the [business judgment] rule contemplates (i.e., is the judgment under review 'egregious' or 'irrational' or 'so beyond reason,' etc.) really is a way of inferring bad faith."[105] Accordingly, a judicial inquiry into the rationality of a board decision is properly understood to be a proxy for an inquiry into whether the decision was tainted by self-interest.[106]

The fact that the business judgment rule will generally protect rational director decisions, as so defined, however, does not mean that directors have license to make tradeoffs between shareholder and stakeholder interests. In the famous *Dodge v. Ford Motor Company* decision, for example, the Michigan Supreme Court held that although it was permissible for a corporation to make "an incidental humanitarian expenditure . . . for the benefit of the employés, like the building of a hospital for their use and the employment of agencies for the betterment of their condition," the directors must bear in mind that the "corporation is organized and carried on primarily for the profit of the stockholders."[107] Accordingly, while directors have discretion as to "the choice of means to attain" the objective of shareholder value maximization, they have no discretion to change that objective.[108] Because the directors thus may not choose to devote corporate profits "to other purposes,"[109] *Dodge* does not allow directors to make decisions that benefit stakeholders at the expense of shareholders.[110]

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104 Michael P. Dooley, *Two Models of Corporate Governance*, 47 BUS. LAW. 461, 478 n.58 (1992).

105 In re RJR Nabisco, Inc. S'holders Litig., 1989 WL 7036, at *13 n.13 (Del. Ch. Jan. 31, 1989).

106 *See* Parnes v. Bally Entertainment Corp., 722 A.2d 1243, 1246 (Del. 1999) (quoting In re J. P. Stevens & Co., 542 A.2d 770, 780–81 (Del. Ch. 1988)) ("The presumptive validity of a business judgment is rebutted in those rare cases where the decision under attack is 'so far beyond the bounds of reasonable judgment that it seems essentially inexplicable on any ground other than bad faith.'").

107 170 N.W. 668, 684 (Mich. 1919).

108 *Id.*

109 *Id.*

110 *See* Dirks v. SEC, 463 U.S. 646, 674675–76 (1983) (Blackmun, J., dissenting) ("Henry Ford's philanthropic motives did not permit him to set Ford Motor Company dividend policies to benefit the public at expense of shareholders"); Murphy v. Inman, No. 161454, 2022 WL 1020127, at *7 (Mich. Apr. 5, 2022) (quoting Thompson v. Walker, 234 N.W. 144, 147 (1931)) (holding that because "a corporation is carried on primarily for the profit of its shareholders, . . . the 'essence' of directors' fiduciary duties is to 'produce to each stockholder the best possible return for his [or her] investment'").

As we have seen, Delaware law likewise permits directors in certain circumstances to consider stakeholder interests, so long as they rationally relate to shareholder gain.[111] As that qualifier suggests, Delaware law does not allow directors to make tradeoffs that benefit stakeholders at the expense of shareholders. In *In re Trados, Inc. Sholder Litigation,* for example, Vice Chancellor Travis Laster held that "the standard of conduct for directors requires that they strive in good faith and on an informed basis to maximize the value of the corporation for the benefit of its residual claimants, the ultimate beneficiaries of the firm's value, not for the benefit of its contractual claimants."[112] *Trados* plausibly can be read as also suggesting that shareholders must be the primary beneficiary of corporate decisions.

3. The Law in Stakeholder Jurisdictions

Turning to the drafters' treatment of stakeholder jurisdictions, the drafters assert that "consideration of nonshareholder interests sometimes will not only be permissible without regard to shareholder benefit but may be mandatory" in "a 'may' or 'shall' jurisdiction."[113] It is not clear whether consideration of such interests contemplates making tradeoffs between them. As currently drafted, however, the blackletter text of § 2.01 asserts that the corporation's objective is to enhance the corporation's economic value "for the benefit of the corporation's shareholders and/or, to the extent permitted by state law, for the benefit of employees, suppliers, customers, communities, or any other constituencies."[114] The dual conjunction—"and/or"—appears to suggest that directors are allowed in stakeholder jurisdictions to make tradeoffs between shareholders and stakeholders, possibly including benefiting stakeholders at the expense of the shareholders.

Analysis should begin by clarifying the distinction between what the drafters call may and shall jurisdictions. The drafters appear to use those terms to distinguish between constituency statutes ("may") and public benefit corporation (PBC) statutes

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111 *See supra* text accompanying note 102 (discussing the *Revlon* decision).

112 In re Trados, Inc. Shareholder Litig., 73 A.3d 17, 40–41 (Del. Ch. 2013). Although we are concerned herein with U.S. law, it is interesting to note a 19th century United Kingdom case, *Hutton v. West Cork Ry. Co.*, (1883) 23 Ch. D. 654, 673, in which Lord Justice Bowen stated that the law "does not say that there are to be no cakes and ale, but there are to be no cakes and ale except such as are required for the benefit of the company."

113 RESTATEMENT § 2.01 cmt. b.

114 *Id.*, § 2.01(a)(2).

("shall").[115] The apparent conflation of these rather different statutes into the single stakeholder jurisdiction category is a source of potential confusion, especially because the drafters recognize that PBC statutes are so new and have generated so little law that trying to incorporate them into the blackletter law was undesirable.[116] The drafters therefore should carve out PBCs and treat them entirely separately from constituency statutes throughout not only the blackletter law but also the commentary and reporters' notes.

Under PBC statutes, it is true that directors must consider the impact of their decisions on the corporation's chosen public interest.[117] In doing so, it seems likely that they will be allowed—if not affirmatively required—to make tradeoffs between shareholder wealth and the chosen public benefit. As a quartet of distinguished Delaware commentators note with respect to Delaware's PBC statute, "it seems nearly impossible for a court to second-guess director judgment about a tradeoff between stockholder pecuniary gain and accomplishment of the PBC's stated public benefit."[118]

As to constituency statutes, however, former Delaware Chief Justice Leo Strine observes that:

> Although a majority of U.S. states have enacted constituency statutes, which enable directors to consider the best interests of other corporate constituencies when conducting a sales

[115] *See id.*, § 2.01 cmt. b ("Unlike the permissive (may) model reflected in constituency statutes, benefit corporations are more prescriptive (shall) . . . ."). Since 2010, roughly 40 states have adopted statutes authorizing businesses to be organized as PBCs. Sandra Feldman, *Georgia and Alabama enact benefit corporation laws*, WOLTERS KLUWER (2021), https://perma.cc/S2N6-3C4Q. Although the details vary somewhat from state to state, PBC statutes generally are intended to provide a limited liability entity through which for-profit businesses may lawfully depart from the shareholder value maximization rule. *See* Michael B. Dorff, *Why Public Benefit Corporations?*, 42 DEL. J. CORP. L. 77, 89 (2017) (quoting Professor Larry Hammermesh to the effect that "the primary purpose of passing the PBC statute was to provide another option to businesses that wanted it"). Indeed, in general, unlike companies incorporated under traditional business corporation statutes, those incorporated under a PBC statute are not just allowed but are required to deviate from the shareholder wealth maximization norm. Directors of a PBC thus must balance shareholder profit, stakeholder interests, and the company's stated public benefit. Alicia E. Plerhoples, *Delaware Public Benefit Corporations 90 Days Out: Who's Opting in?*, 14 U.C. DAVIS BUS. L.J. 247, 248 (2014).

[116] RESTATEMENT § 2.01 cmt. b.

[117] *See* Deborah J. Walker, *Please Welcome the Minnesota Public Benefit Corporation,* 11 U. ST. THOMAS L.J. 151, 152 (2013) (stating that "directors must consider the public benefits before making a decision").

[118] Frederick H. Alexander, Lawrence A. Hamermesh, Frank R. Martin, and Norman M. Monhait, *M&A Under Delaware's Public Benefit Corporation Statute: A Hypothetical Tour,* 4 HARV. BUS. L. REV. 255, 271 (2014).

> process or deciding whether to accept a takeover offer, these statutes only permit—and do not require—directors to take such interests into account. As a result, constituency statutes give little real power to other corporate constituencies at the expense of the stockholders.[119]

In addition to being merely permissive, although constituency statutes allow directors to consider interests of non-shareholder constituencies, the statutes do not expressly authorize directors to harm shareholder interests in order to benefit stakeholders.[120]

This interpretation is confirmed by a North Carolina court's discussion of the context in which the constituency statutes arose, which explained that:

> Illinois, for example, adopted a statute that specifically authorized directors to consider the interests of corporate constituents other than shareholders when responding to a hostile takeover. In doing so, Illinois statutorily adjusted the balance of power between shareholders and other corporate constituents by giving additional power to directors that *Revlon* had arguably taken away. It did so not to advance the power of directors, but to permit directors to assert the interests of other corporate constituents in the heat of the takeover battle. It did not eliminate shareholder rights; it arguably put a little more tension in the elasticity on the side of the directors so that they could consider "corporate value" as including values important to society.[121]

In other words, we can understand the constituency statutes as being a narrow rejection of *Revlon*'s rule that shareholder value is the sole licit metric for director decision-making once a sale of control process has begun,[122] which was intended as a tweak rather than a fundamental change in corporate law. Accordingly, the constituency statutes could plausibly be interpreted as preserving a requirement that director actions taken after considering stakeholder interests must still be rationally related to

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[119] Leo E. Strine, Jr., *The Soviet Constitution Problem in Comparative Corporate Law: Testing the Proposition that European Corporate Law is More Stockholder Focused than U.S. Corporate Law*, 89 S. CAL. L. REV. 1239, 1250 n.20 (2016).

[120] *See* Comm. on Corp. Laws, *Other Constituencies Statutes: Potential for Confusion*, 45 BUS. LAW. 2253, 2265–66 (1990) (discussing how to interpret constituency statutes).

[121] First Union Corp. v. SunTrust Banks, Inc., No. 01-CVS-10075, 2001 WL 1885686, at *5 (N.C. Super. Ct. Aug. 10, 2001).

[122] On the *Revlon* duties of directors in connection with a sale of control process, *see infra* Part F.

shareholder interests.[123] As such, the most pro-stakeholder capitalism spin one can put on the statutes is that they "are mere tie-breakers, allowing managers to take the interests of non-shareholder constituencies into account when doing so does not harm shareholders in any demonstrable way."[124]

4. Summation

It is certainly true that many business decisions are potentially win-win scenarios, such that the proverbial rising tide usually does lift all boats.[125] This is true even of decisions that in the short run seem to favor stakeholders at the expense of shareholders. Providing health benefits for employees may increase expenses and reduce profits in the short term, for example, but often leads to greater productivity in the long term.[126] Accordingly, as noted above, *Dodge v. Ford Motor Company* confirmed that it would be appropriate for a board of directors to approve "an incidental humanitarian expenditure of corporate funds for the benefit of the employés, like the building of a hospital for their use and the employment of agencies for the betterment of their condition."[127] Such an expenditure typically would be protected by the business judgment rule.[128]

But this does not mean that managers can explicitly benefit stakeholders at the expense of shareholders.[129] To the contrary, "the position that board actions that ignore shareholder wealth maximization in favor of the promotion of third-party stakeholder

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[123] *See* Comm. on Corp. Laws, *supra* note 120, at 2266 (discussing import of statutory references to the "best interests of the corporation").

[124] Jonathan R. Macey, *A Close Read of an Excellent Commentary on* Dodge v. Ford, 3 VA. L. & BUS. REV. 177, 179 (2008).

[125] *See* Lisa M. Fairfax, *Making the Corporation Safe for Shareholder Democracy*, 69 OHIO ST. L.J. 53, 96 (2008) (arguing that "the vast majority of stakeholders have interests that collide with shareholders").

[126] *See* Larry S. Boress, *An Extreme Makeover for the Employer's House of Health Benefits,* 32 J. LEGAL MED. 51, 55 (2011) (reporting survey data finding "that there is a link between an employee's health and their productivity, with 84% of employers believing health benefits are a necessary cost of doing business and 85% viewing health benefits as an investment in human capital with a measurable outcome").

[127] Dodge v. Ford Motor Co., 170 N.W. 668, 684 (Mich. 1919).

[128] *See* Fisch, *supra* note 90, at 652 ("The business judgment rule provides a corporation's officers and directors with broad discretion to consider the interests of other stakeholders."); J. Haskell Murray, *Adopting Stakeholder Advisory Boards*, 54 AM. BUS. L.J. 61, 66 (2017) ("The business judgment rule protects, but does not require, director consideration of peripheral stakeholders in most circumstances.").

[129] *See* Kent Greenfield, *Proposition: Saving the World with Corporate Law*, 57 EMORY L.J. 948, 961 (2008) ("If they honestly declare that they are acting to benefit other stakeholders at the expense of shareholders, then the business judgment rule will not protect the managers.").

interests are a proper corporate goal is a fringe, aspirational position, rather than a reflection of what the law and weight of scholarship articulate."[130] Tradeoffs thus are impermissible.

The late Larry Ribstein contended that the Principles "arguably went beyond prior law in clearly permitting managerial decisions that do not enhance corporate or shareholders' interests."[131] It would be helpful if the drafters clarified whether they agree with that interpretation of the Principles and, if so, whether they mean to adopt it. If they do intend to adopt that interpretation, they should also acknowledge that they are proposing a change in the law—in both common law and stakeholder jurisdictions—rather than restating it.

Of course, this entire discussion is something of an artificial construct. "Corporations are engines of profit making, and they seek profit at every opportunity," even when they are run by those who purportedly prioritize their social values.[132] To cite but a single—albeit high profile—example, the Wall Street Journal reported on August 29, 2020, that one day after "Salesforce.com Inc. posted record quarterly sales, the business-software company notified its 54,000-person workforce that 1,000 would lose their jobs later this year."[133] As John Stoll opined in the Journal, Salesforce CEO and Business Roundtable 2019 statement signatory Marc "Benioff called the company's strong earnings a 'victory for stakeholder capitalism.'"[134] Benioff claimed to have done "a great job" for both shareholders and stakeholders.[135] One might reasonably ask, however, as Stoll did, "how does the billionaire founder justify this claim when shortly after that interview Salesforce

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[130] Marc A. Greendorfer, *Discrimination as a Business Policy: The Misuse and Abuse of Corporate Social Responsibility Programs*, 8 AM. U. BUS. L. REV. 307, 342 (2020).

[131] Larry E. Ribstein, *Accountability and Responsibility in Corporate Governance*, 81 NOTRE DAME L. REV. 1431, 1469 (2006). *See also* James D. Cox, *The ALI, Institutionalization, and Disclosure: The Quest for the Outside Director's Spine*, 61 GEO. WASH. L. REV. 1233, 1243 (1993) (explaining that the ALI debates on the Principles indicate that the Principles were not intended to "require necessarily that board action advancing an interest of the corporation also advance the shareholders' interests").

[132] Karthik Ramanna, *Friedman at 50: Is It Still the Social Responsibility of Business to Increase Profits?*, 62(3) CAL. MGMT. REV. 28, 30 (2020); for a discussion of the values held by today's corporate leaders, and the political valence of those views, *see* Stefan J. Padfield, *Does Stakeholder Capitalism Have A (Viewpoint) Diversity Problem?*, 13 U. PUERTO RICO BUS. L.J. 1, 7–10 (2022) (discussing different explanations for the turn among business leaders toward socially-motivated decision-making, including a divergence in social values between business and political elites and the rest of society).

[133] Patrick Thomas, Sarah Chaney, and Chip Cutter, *New Covid-19 Layoffs Make Job Reductions Permanent,* WALL ST. J. (Aug. 28, 2020), https://perma.cc/8LJT-XGKQ.

[134] John D. Stoll, *How's the CEO 'Stakeholder Pledge' Working Out? Depends Who You Ask*, WALL ST. J. (Aug. 28, 2020), https://perma.cc/LQB3-GHGP.

[135] *Id.*

notified staff of plans for around 1,000 layoffs? This despite Mr. Benioff's no-layoff pledge in March on Twitter and the challenge to other CEOs to follow his lead."[136]

Over the years, we have seen many such examples. Consider such common decisions as downsizing and offshoring. These decisions almost always are intended for the benefit of shareholders. The impact on employees and communities in which the companies did business are commonly given short shrift.[137] It seems unlikely that a Restatement would work a fundamental change in director and management decision-making.

After all, it is not just the law of corporate purpose that aligns director and manager incentives with shareholder interests. Managers are chosen by directors, who are chosen by shareholders. As I have previously observed: "Because only shareholders are entitled to elect directors, for example, boards of public corporations are insulated from pressure by nonshareholder corporate constituencies, such as employees or creditors."[138]

Corporate directors and officers owe fiduciary duties to both the shareholders and the corporate entity.[139] The former set of duties is enforced through direct lawsuits, typically brought as a class action representing all affected shareholders.[140] The latter set is enforced through derivative lawsuits, which are brought on behalf of the company for redress of an injury done to the company. Only shareholders have standing to bring a derivative proceeding. Employees and other stakeholders lack standing to sue derivatively, except for the limited case of an insolvent corporation, in which case creditors—but only creditors—may bring a derivative proceeding. "Consequently, . . . nonshareholder

136 *Id.*

137 Don Mayer, *The Law and Ethics of CEO Social Activism*, 23 J.L. BUS. & ETHICS 21, 28 (2017) ("In short, offending employees and other stakeholders is, at times, an inevitable feature of doing business, especially in a globalized economy.").

138 *See* Stephen M. Bainbridge, *The Board of Directors as Nexus of Contracts,* 88 IOWA L. REV. 1, 8 (2002).

139 *See* Strougo v. Bassini, 282 F.3d 162, 173 (2d Cir. 2002) ("Maryland courts have clearly established the proposition that directors and officers owe fiduciary duties to both the corporation and the shareholders."); Cargill, Inc. v. JWH Special Circumstance LLC, 959 A.2d 1096, 1115 n.75 (Del. Ch. 2008) (opining that "in the corporate context, both officers and directors of a corporation owe fiduciary duties to the company and its shareholders"); Adelman v. Conotti Corp., 213 S.E.2d 774, 779 (Va. 1975) (holding that both the officers and the directors of a corporation owe fiduciary duties to the corporation and its shareholders).

140 *See, e.g.,* Shenker v. Laureate Educ., Inc., 983 A.2d 408, 424 (Md. 2009) (holding that "a shareholder may bring a direct action, either individually or as a representative of a class, against alleged corporate wrongdoers when the shareholder suffers the harm directly or a duty is owed directly to the shareholder").

constituents of the corporation have no effective method for holding directors accountable . . . ."[141]

Lastly, about 60% of CEO pay is directly linked to how well the company's stock's performs.[142] At smaller companies, 75% of the average CEO's pay comes in the form of stock options, restricted stock grants, and performance-based cash bonuses.[143] Only a relatively small number of companies factor ESG metrics into executive pay and then only in rather limited ways.[144] The bottom line is that "executive pay arrangements, and their evaluation by shareholders and proxy advisors, provide executives with incentives not to ever sacrifice shareholder value to provide benefits to stakeholders."[145] The bulk of these arrangements are not dependent on the law § 2.01 purports to restate.

C. Is Opting Out Allowed?

Whether corporate law is comprised mainly of mandatory or default rules is a longstanding debate.[146] The law governing corporate purpose is no exception. Some commentators argue that a corporation can opt out of the shareholder value maximization principle in the articles of incorporation.[147] Others contend that the shareholder value maximization principle is a mandatory rule out of which a corporation may not opt.[148]

The Restatement's blackletter text is silent on this issue. In comment a, the Restatement's drafters state that § 2.01 specifies "the default goal" and thereby "rules out some alternative goals and thus informs the analysis of what it means to act in good faith."[149] Although not stated in the context of whether

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141 *See* Eric J. Gouvin, *Resolving the Subsidiary Director's Dilemma*, 47 HASTINGS L.J. 287, 303–04 (1996).

142 Lucian A. Bebchuk & Roberto Tallarita, *The Illusory Promise of Stakeholder Governance*, 106 CORNELL L. REV. 91, 151 (2020).

143 *Id.*

144 *Id.*

145 *Id.* at 152–53.

146 *See* Brett H. McDonnell, *Sticky Defaults and Altering Rules in Corporate Law*, 60 SMU L. REV. 383, 386 (2007) (noting "the debate over mandatory versus default rules" and "how default rules should be set").

147 *See, e.g.*, Heminway, *supra* note 90, at 957 (arguing that "a charter provision that is inconsistent with the shareholder wealth maximization norm should be valid"); Macey, *supra* note 124, at 179 (arguing that "because the corporation is a contract-based form of business organization, maximizing shareholder gain is only a default rule").

148 *See, e.g.*, Stefan J. Padfield, *The Role of Corporate Personality Theory in Opting Out of Shareholder Wealth Maximization*, 19 TRANSACTIONS: TENN. J. BUS. L. 415, 439 (2017) (observing that "Chancellor Chandler's comments in the *eBay* decision suggest that" efforts to opt out of shareholder value maximization may be unavailing).

149 RESTATEMENT § 2.01 cmt. a.

corporations can opt out of § 2.01, this comment plausibly could be read as suggesting that § 2.01 is a default rule rather than a mandatory one.

Illustration 6 to § 2.01 also plausibly can be read as suggesting that the section states a default rule out of which corporations may opt:

> Corporation X is a large and very successful publicly held software company. The corporate decisionmaker has made a judgment, in a manner that meets the standards of § 4.02, that its success (financial and otherwise) comes from being a purpose-driven organization. In furthering that purpose, X has committed to and implements throughout the organization a "mission statement" that articulates the company's core values and says:
>
>> We believe the business of business is improving the state of the world for all of our stakeholders, including our stockholders, customers, employees, community, environment, and society. We are committed to creating a sustainable, low-carbon future, advancing equality and diversity, and fostering employee success. We try to integrate social good into everything we do. All of these goals align with our long-term growth strategy and financial and operational priorities.[150]

The drafters assert without explanation that "X's action does not involve a departure from the economic objective stated in § 2.01 in either type of jurisdiction."[151] Suppose Corporation X faced a zero-sum decision in which it must decide between the interests of shareholders and stakeholders. The decision unavoidably will leave one set of constituents better off and the other worse off. Does the mission statement allow X to opt for the choice that benefits stakeholders at the expense of shareholders? Does it matter whether the mission statement is incorporated into the company's articles of incorporation?

Instead of answering those questions in either the blackletter or the comments, the drafters left them to the Reporters' Notes. The pertinent note opines that a corporation's organizers can opt out of the common law shareholder value maximization rule by forming a nonprofit corporation, incorporating as a PBC in a state where that is an option, or incorporating in a state with a

[150] *Id.* § 2.01 cmt. e, illus. 6.
[151] *Id.*

constituency statute.[152] As for a firm incorporated under a state's general business corporation act, in a state lacking a constituency statute, however, the Reporters' Note states that § 2.01 does not speak to whether that firm can opt out of the shareholder-primacy objective.[153] The drafters duck that issue on grounds that there is no law to restate, observing that it is unclear under current law "whether a firm may opt out of shareholder primacy by original charter provision or by charter amendment."[154]

In 1992, I argued that:

> [S]tate law arguably does not permit corporate organic documents to redefine the directors' fiduciary duties. In general, a charter amendment may not derogate from common law rules if doing so conflicts with some settled public policy. In light of the well-settled shareholder wealth maximization policy, nonmonetary factors charter amendments therefore appear vulnerable.[155]

Today, I believe that the widespread adoption of PBC statutes has strengthened the argument that firms formed under a general corporation law may not opt out of the shareholder value principle.[156]

After all, if shareholder value maximization were not the law, PBCs would be unnecessary. Boards of business corporations would be free to pursue public benefits without violating their fiduciary duties. The perceived need for PBC statutes thus suggests that boards are not free to do so absent the statute. The drafters of the California PBC statute presumably had such an argument in mind when they included the following qualification in the statute: "The existence of a provision of this part shall not

152 RESTATEMENT § 2.01 Reporters' Note 8.

153 *See id.* ("Section 2.01 does not address the question of when a corporation organized under a business-corporation law may restrict the general profit-making objective by a shareholders' agreement or charter provision.").

154 *Id.* In contrast, the Principles' drafters contended that "there is little doubt that such limitations would normally be permissible if agreed to by all the shareholders," whether in the articles of incorporation or a shareholder agreement. PRINCIPLES § 2.01 Reporters' Note 6.

155 Stephen M. Bainbridge, *Interpreting Nonshareholder Constituency Statutes*, 19 PEPP. L. REV. 971, 985 (1992).

156 *See* David G. Yosifon, *Opting Out of Shareholder Primacy: Is the Public Benefit Corporation Trivial?*, 41 DEL. J. CORP. L. 461, 486 (2017) (noting that widespread adoption of PBC statutes "may actually have reduced flexibility, making it more difficult to form socially conscious enterprises, and restricting the ability of existing shareholder primacy firms to adopt charter terms committing themselves to greater social responsibility"). The Restatement's drafters take the position that "the extent to which [PBCs] will influence the interpretation of other provisions is unclear." RESTATEMENT § 2.01 Reporters' Note 8.

of itself create any implication that a contrary or different rule of law is or would be applicable to a business corporation that is not a benefit corporation."[157]

D. Obedience to the Law

Principles § 2.01 asserted that a corporation has an obligation to obey the law, even if doing so reduces profits and shareholder value.[158] Restatement § 2.01 likewise obliges a corporation "to act within the boundaries set by law," although that obligation is not explicitly linked to a command to do so even if profits would be sacrificed.[159] Do these provisions restate the law? Professor Cynthia Williams asserted (approvingly) that the Principles imposed "a new, specifically corporate law obligation on the corporation to obey the law, whether profits are enhanced thereby or not."[160] Whether or not there was a specific obligation for corporations to obey the law when the Principles were promulgated,[161] Delaware law has moved strongly in that direction in recent years.[162] Curiously, however, the Reporters' Notes do not address the relevant case law.

Although the Restatement accurately restates Delaware law, it perpetuates bad policy.[163] Suppose a major city adopted an anti-congestion law that significantly increased traffic fines for double parking, in hopes that doing so will improve traffic flow. In this city, however, most buildings lack parking garages and loading docks. Street parking spaces are almost always full. As a result, delivery drivers frequently double-park while making deliveries

157 CAL. CORP. CODE § 14600(b) (2012).

158 PRINCIPLES § 2.01(b)(1).

159 RESTATEMENT § 2.01 cmt. f.

160 Cynthia A. Williams, *Corporate Compliance with the Law in the Era of Efficiency*, 76 N.C. L. REV. 1265, 1281 (1998).

161 Such a duty was perhaps implied in *TW Services, Inc. v. SWT Acquisition Corp.*, CIV.A. Nos. 10427, 10298, 1989 WL 20290, at *7 (Del. Ch. Mar. 2, 1989), which held that "directors may be said to owe a duty to shareholders as a class to manage the corporation within the law . . . ."

162 *See, e.g.*, *In re* Massey Energy Co., C.A. No. 5430-VCS, 2011 WL 2176479, at *20 (Del. Ch. May 31, 2011) (holding that "a fiduciary of a Delaware corporation cannot be loyal to a Delaware corporation by knowingly causing it to seek profit by violating the law"); Metro Commc'n Corp. BVI v. Advanced Mobilecomm Techs. Inc., 854 A.2d 121, 131 (Del. Ch. 2004) ("Under Delaware law, a fiduciary may not choose to manage an entity in an illegal fashion, even if the fiduciary believes that the illegal activity will result in profits for the entity."); Guttman v. Huang, 823 A.2d 492, 506 n.34 (Del. Ch. 2003) (holding that "one cannot act loyally as a corporate director by causing the corporation to violate the positive laws it is obliged to obey.").

163 *See generally* BAINBRIDGE, *supra* note 69, at 272–74 (arguing that an unqualified duty of obedience is overbroad).

to offices and apartments. Upon passage of the new law, a major delivery company's board of directors met to discuss how the company should respond. The board was advised by legal counsel and experts in logistics and traffic management. The board was advised that compliance with the law would significantly slow deliveries, as drivers circle the block looking for parking and, once they find parking, have further to walk to reach the targeted building. Complying with the law will thus require hiring more drivers and buying more delivery trucks, which the board is informed will not only be very expensive but will also increase the company's carbon footprint. The board was very concerned by the latter point, because the company is under considerable pressure from activist shareholders and environmentalists to reduce its carbon output. The board is told that it would be cheaper and greener to instruct the company's drivers to continue double-parking even though they will be breaking the law. In my longstanding view, "it is hardly clear that liability should follow."[164]

This is an issue as to which the Principles' and the Restatement's reification of the corporation poses especially pronounced difficulties. I assume that all would agree that the hypothetical delivery corporation ought to pay the resulting fines. But does it follow that there should be corporate governance consequences? If so, because § 2.01 is toothless, those consequences presumably would be effected through the fiduciary duties of the board of directors.[165] Yet, the hypothetical board engaged in a rational and well-informed cost-benefit analysis motivated by a desire to enhance shareholder value and simultaneously reduce climate change. Allowing shareholders to sue such a board would mostly benefit lawyers.[166] Accordingly, as I have observed elsewhere:

> The point is not that corporations should be allowed to break the law. They should not. If a corporation breaks the law, criminal sanctions should follow for the entity and/or the responsible individuals. The point is only that fiduciary obligation and the duty to act lawfully make a bad fit. If the question is one of reconciling authority and accountability, it is

[164] *Id.* at 272.

[165] *See supra* notes 52–73 and accompanying text (discussing how the principle announced in § 2.01 will be operationalized).

[166] *See* Roberta Romano, *The Shareholder Suit: Litigation Without Foundation?*, 7 J.L. ECON. & ORG. 55, 84 (1991) (explaining that, in most shareholder derivative lawsuits, it is the plaintiffs' counsel who benefits rather than the shareholders, who typically receive only "minimal compensation").

> not self-evident that corporate law should hold directors accountable simply for deciding that the corporation's interests are served by violating a particular statute. After all, "[a] business corporation is organized and carried on primarily for the profit of the stockholders. The powers of the directors are to be employed for that end."[167]

Obviously, that argument does not extend to all corporate crimes:

> The criminal law long has distinguished between crimes that are *malum in se* and those that are merely *malum prohibitum*. The latter are acts that are criminal merely because they are prohibited by statute, not because they violate natural law. It is said that "misdemeanors such as jaywalking and running a stoplight are *mala prohibita*, as are most *securities-law* violations." Individuals routinely make cost-benefit analyses before deciding to comply with some malum prohibitum law, such as when deciding to violate the speed limit.[168]

The distinction between *malum in se* and *malum prohibitum* offenses thus seems an appropriate limiting principle.

The Restatement's drafters acknowledge that:

> Some maintain that a corporation's decision whether to adhere to a given legal rule may properly depend on a kind of cost–benefit analysis in which probable corporate gains are weighed against either probable social costs, measured by the dollar liability imposed for engaging in such conduct, or probable corporate losses, measured by potential dollar liability discounted for likelihood of detection.[169]

I long have been among the unnamed some who so maintain,[170] and it still strikes me as a perfectly reasonable position.[171] But the Restatement's drafters reject that view.[172]

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[167] BAINBRIDGE, *supra* note 69, at 273 (quoting Dodge v. Ford Motor Co., 170 N.W. 668, 684 (Mich.1919).

[168] *Id.* at 272 (footnote omitted) (quoting Black's Law Dictionary 401 (pocket ed. 1996) (emphasis supplied)).

[169] RESTATEMENT § 2.01 cmt. f.

[170] *See* BAINBRIDGE, *supra* note 69, at 272–73 ("Is it self-evident that directors of a corporation should be barred from engaging in similar cost-benefit analyses?").

[171] *See, e.g.*, Stephen M. Bainbridge, Star Lopez & Benjamin Oklan, *The Convergence of Good Faith and Oversight*, 55 UCLA L. REV. 559, 592 (2008) (posing the same question).

[172] *See* RESTATEMENT § 2.01 cmt. f ("Section 2.01 rejects this position."). In doing so, they track the Principles. *See* Principles § 2.01 cmt. g ("Section 2.01 does not adopt this position.").

First, the drafters argue that a cost-benefit analysis is out of place in this context because fines do not constitute a payment for the ability to break the law.[173] But this argument is self-evidently false. Have the Restatement's drafters never opted to risk a speeding ticket in order to reach a destination faster? In our heavily regulated business environment, in which it has been suggested that most people commit three felonies every day,[174] regulatory fines such as the one in my hypothetical are simply a cost of doing business.[175] Indeed, to continue the traffic analogy, sometimes regulatory fines are simply government revenue generators,[176] such as with speed traps.[177]

Second, the Restatement drafters invoke a "moral norm of obedience to law,"[178] but they immediately undercut the persuasive power of that claim by recognizing multiple exceptions to that norm. Among those exceptions are "necessity in extraordinary situations in which compliance would inflict substantial harm on third parties," "desuetude, i.e., disuse, when both social morality and relevant government authorities condone a departure from a legal rule," and breaking the law in order to generate a test case of the law's validity.[179]

Another exception the Restatement drafters recognize to the norm of obedience is a *de minimis* violation.[180] Presumably the drafters thus contemplate that *de minimis* violations do not

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[173] RESTATEMENT § 2.01 cmt. f (arguing that "dollar liability is not a 'price' that can properly be paid for the privilege of engaging in legally wrongful conduct").

[174] HARVEY A. SILVERGLATE, THREE FELONIES A DAY: HOW THE FEDS TARGET THE INNOCENT xxxvi (2011) ("[I]t is only a slight exaggeration to say that the average busy professional in this country wakes up in the morning, goes to work, comes home, takes care of personal and family obligations, and then goes to sleep, unaware that he or she likely committed several federal crimes that day.").

[175] *See* JOHN BRAITHWAITHE, CORPORATE CRIME IN THE PHARMACEUTICAL INDUSTRY 331 (1984) ("Fines as they currently operate are justifiably criticised as licence fees to break the law."); Daniel R. Fischel, *The Corporate Governance Movement*, 35 VAND. L. REV. 1259, 1271 (1982) ("A firm may also find it advantageous to violate a law deliberately and pay the penalty for the same reason that an individual in some cases may prefer to breach a contract and pay damages.").

[176] *See* Beth A. Colgan, *The Excessive Fines Clause: Challenging the Modern Debtors' Prison*, 65 UCLA L. REV. 2, 13 (2018) (noting "the risk that the government will abuse the prosecutorial power to take advantage of the revenue generating capacity of fines").

[177] *See* Wiggins v. State, 290 S.E.2d 427, 429 (Ga. 1982) (upholding a state statute as "rationally related to the legitimate governmental objective of preventing local law enforcement officers from using radar to operate local revenue producing 'speed traps'"); Michael L. Rich, *Should We Make Crime Impossible*?, 36 HARV. J.L. & PUB. POL'Y 795, 810 n.72 (2013) (noting that "speed traps and red-light cameras are frequently criticized for aiming to increase government revenue instead of enhancing public safety").

[178] RESTATEMENT § 2.01 cmt. f.

[179] *Id.*

[180] *Id.*

violate § 2.01, although that could be made clearer. In any case, isn't the exception for *de minimis* violations inconsistent with the principle that you cannot pay a fine for the privilege of breaking the law, albeit a sensible one? In addition, is the exception for *de minimis* violations inconsistent with the drafters' rejection of cost-benefit analysis? After all, doesn't deciding whether a violation is *de minimis* or not at least imply some degree of cost-benefit analysis? If so, there is no basis for limiting cost-benefit analysis to *de minimis* cases.[181]

For my purposes, however, the key exception acknowledged by the Restatement drafters is for "cases in which it is widely understood that liability is properly viewed as a price of noncompliance, such as parking tickets for overstaying a parking meter."[182] Does this solve the concern posed by my hypothetical? Not completely.

First, the drafters framed this point as an exception to the norm of obedience, rather than making it an express exception to the black letter law of § 2.01. Granted, the drafters probably intend it to function as such an exception. Stating so more explicitly and with greater clarity would be helpful, however.

Second, given that § 2.01 is not self-executing, it will need to be operationalized via the provisions on director and officer fiduciary duties.[183] The drafters thus must ensure that the *de minimis* and price of noncompliance exceptions are incorporated into those provisions. Otherwise, directors and officers could be held liable for conduct that does not violate § 2.01. Indeed, this example provides a compelling instance of the problems created by framing § 2.01 as a corporate objective rather than as part of the directors' and officers' fiduciary duties.

Third, the drafters do not specify by whom it must be "widely understood" that the fine in question is just a cost of doing business. Do they mean trial lawyers, corporate lawyers, businesspeople, or the general community? Given that § 2.01 is intended to provide an answer for a director who asks "what are we trying to accomplish here,"[184] one assumes that the business community is

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[181] By way of analogy, in a case involving interpretation of a federal environmental statute, the Supreme Court observed that if some cost-benefit analysis is permissible, there is "no statutory basis for limiting its use to situations where the benefits are *de minimis* rather than significantly disproportionate." Entergy Corp. v. Riverkeeper, Inc., 556 U.S. 208, 226 (2009).

[182] RESTATEMENT § 2.01 cmt. f.

[183] *See supra* notes 52–73 and accompanying text (discussing the relationship between § 2.01 and the Restatement's fiduciary duty provisions).

[184] *See supra* text accompanying note 53.

the relevant focus. If so, however, how are courts hearing cases involving fiduciary duties to which § 2.01 serves as a backstop to assess whether the regulation in question is widely understood by businesspeople to be a mere price? It seems inevitable that that question would lead to a battle of the experts at trial or, at the very least, raise the settlement value of such cases.

Finally, the Restatement's drafters provide no other guidance as to where to draw the dividing line between situations like "parking tickets for overstaying a parking meter" and cases in which the regulation in question should not be viewed as a cost of doing business. On which side of that line does the anti-congestion law in my hypothetical fall? By choosing such a trivial example, the drafters leave us uncertain.

Consider, for example, Illustration 11 to § 2.01:

> F Corporation is a publicly held corporation with annual earnings in the $30–50 million range. F hopes to be awarded a supply contract by P, a large, publicly held corporation. The anticipated profits on the contract are $50 million over a two-year period. A vice president of P has approached Brown, the relevant corporate decisionmaker of F, with the suggestion that if F pays the vice president $200,000, F will be awarded the contract. Brown knows such a payment would be illegal but correctly regards the risk of detection as being extremely small. After carefully weighing that risk and the consequences of detection, Brown causes F to pay the $200,000. F's action involves a departure from the principle stated in § 2.01.[185]

It has long been held that bribery is *malum in se* rather than *malum prohibitum*,[186] so the illustration does not resolve cases such as my traffic fine and anti-congestion law examples. The illustration also fails to grapple with the question of whether $200,000 is a *de minimis* violation. In particular, the framing of the illustration raises the unanswered question of whether the *de minimis* exception is to be determined on a relative or absolute basis. Is that question determined by comparing the $200,000 bribe to F's annual earnings or the incremental increase in earnings if F is awarded the contract? Would the outcome change if making such

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[185] RESTATEMENT § 2.01 cmt. f, illus. 11. Notice that this illustration provides another example of how the Restatement conflates the corporate objective and the acts of a decision-maker. *See supra* note 53 (discussing Illustration 1).

[186] *See, e.g.*, Bateman v. Robinson, 11 N.W. 736, 737 (Neb. 1882) (noting a 1778 case in which Lord Mansfield drew a "distinction between acts which are *mala in se*, such as bribery, and such as are prohibited by statute").

payments is a common practice in P's and F's industry at which the pertinent regulators routinely wink?

A better approach would be for the drafters to simply excise the obedience-to-law element from § 2.01.[187] The fiduciary duty provisions of the Restatement should be revised to recognize that a board decision—or one by a senior officer—that causes the corporation to break the law is not protected by the business judgment rule.[188] The Restatement then should require a court to evaluate whether the directors violated their duty of care, using a gross negligence standard.[189] If the court concludes that the directors did so, monetary liability should be subject to the "net loss rule, under which directors cannot be held monetarily liable if the overall gains to the corporation from the violation exceed the losses directly attributable thereto, such as fines or legal expenses."[190]

E. *Caremark* is Coming

Obedience to the law is essentially passive. In contrast, law compliance is proactive.[191] In the famous *Caremark* decision,

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[187] In making that suggestion, I am by no means abandoning my preferred outcome that § 2.01 be abandoned in its entirety and its principles worked into the fiduciary duty provisions of the Restatement. Instead, as with the suggestions in the following sections, I offer it on the assumption that my preferred alternative will not be accepted by the drafters.

[188] It is, of course, a longstanding principle that the business judgment rule does not protect corporate decision-makers who cause the corporation to act illegally. *See, e.g.*, Int'l Ins. Co. v. Johns, 874 F.2d 1447, 1461 (11th Cir. 1989) ("A court will not call upon a director to account for his action in the absence of a showing of abuse of discretion, fraud, bad faith, or illegality."). Whether the business judgment rule protects officers as well as directors has been the subject of considerable debate. The Restatement takes the position that the rule, as set out in § 4.02, "protects the business judgments of both directors and officers." RESTATEMENT § 4.02 cmt. j.

[189] *See* Harvey L. Pitt, *On the Precipice: A Reexamination of Directors' Fiduciary Duties in the Context of Hostile Acquisitions*, 15 DEL. J. CORP. L. 811, 830 n.71 (1990) ("While the standard of liability for a breach of the duty of care has been the subject of much debate, . . . Delaware has adopted a standard of 'gross negligence.'"). The Restatement's drafters distinguish between standards of aspirational conduct, standards of review by which courts evaluate director conduct, and standards of liability that determine if the director faces monetary liability. RESTATEMENT § 4.01 cmt. d (discussing the three standards). Section 4.01 deals solely with the first of the three. *Id.* It adopts a "simple negligence standard." *Id.* § 4.01 cmt. g. Section 4.02 sets forth both the standard of review and the standard of liability. *Id.* § 4.01 cmt. d. At least as to whether the directors were reasonably informed, § 4.02 adopts a gross negligence standard.

[190] Bainbridge, Lopez, & Oklan, *supra* note 171, at 592–93.

[191] COMM. OF SPONSORING ORGS., TREADWAY COMM'N, COMPLIANCE RISK MANAGEMENT: APPLYING THE COSO ERM FRAMEWORK 15 (2020) ("As compliance programs have matured, they have moved to a more integrative, proactive approach based not on a particular past crisis that the organization wishes to avoid repeating, but on the

Delaware Chancellor William T. Allen established the proposition that the corporation should proactively establish reasonable "information and reporting systems . . . concerning both the corporation's compliance with law and its business performance."[192]

As Chancellor Allen initially phrased the state corporate law oversight obligation, it arose out of the duty of care.[193] The business judgment rule typically did not apply to oversight cases, because the allegation typically involved a claim that directors had failed to act either by failing to establish a reasonable compliance system or, having established such a system, failed to monitor it.[194] In *Guttman v. Huang*,[195] however, then-Vice Chancellor Leo Strine treated *Caremark* claims as arising out of the duty of loyalty.[196] Strine's reinterpretation of *Caremark* was subsequently adopted by the Delaware Supreme Court in *Stone v. Ritter*.[197]

Comment f to Restatement Section 2.01 contemplates an oversight duty like that of *Caremark*.

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systematic assessment of the organization and its environment to identify current and future threats to compliance."); PRINCIPLES OF THE L., COMPLIANCE AND ENF'T FOR ORGS. § 4.10 (AM. L. INST., Tentative Draft No. 2, 2021) ("Organizations should anticipate possible weak links in their controls and address these links proactively.").

[192] *In re* Caremark Int'l Inc. Derivative Litig., 698 A.2d 959, 970 (Del. Ch. 1996).

[193] *See* H. Lowell Brown, *The Corporate Director's Compliance Oversight Responsibility in the Post* Caremark *Era*, 26 DEL. J. CORP. L. 1, 19–20 (2001) ("Chancellor Allen noted that the essence of the complaint was that the Caremark directors had breached their duty of care . . . ."); Martin Petrin, *Assessing Delaware's Oversight Jurisprudence: A Policy and Theory Perspective*, 5 VA. L. & BUS. REV. 433, 442 (2011) ("*Caremark* is clear in treating oversight as a care-based duty").

[194] *See* Renee M. Jones & Michelle Welsh, *Toward a Public Enforcement Model for Directors' Duty of Oversight*, 45 VAND. J. TRANSNAT'L L. 343, 357 (2012) ("Under *Caremark*, a board's failure to create a monitoring system would constitute a breach of the duty of care, and as an unconsidered failure to act, would not be protected by the business judgment rule."). In *Stone ex rel. AmSouth Bancorporation v. Ritter*, the Delaware Supreme Court explained that there were two basic types of *Caremark* claims: "(a) the directors utterly failed to implement any reporting or information system or controls; or (b) having implemented such a system or controls, consciously failed to monitor or oversee its operations thus disabling themselves from being informed of risks or problems requiring their attention." 911 A.2d 362, 370 (Del. 2006).

[195] 823 A.2d 492 (Del. Ch. 2003).

[196] *Id.* at 506.

[197] 911 A.2d . *See* Alan R. Palmiter, *Duty of Obedience: The Forgotten Duty*, 55 N.Y.L. SCH. L. REV. 457, 466 (2011) ("*Caremark* said compliance was a matter of care and *Stone v. Ritter* said it involved good faith, a subset of loyalty . . . ."). There has been considerable debate as to both the doctrinal and policy merits of *Guttman*'s and *Stone*'s characterization of the oversight duty as arising out of the duty of good faith, which in turn was subsumed by *Stone* into the duty of loyalty. *Compare* Stephen M. Bainbridge, Caremark *and Enterprise Risk Management*, 34 J. CORP. L. 967, 975–77 (2009) (criticizing *Guttman* and *Stone*), *and* Andrew D. Appleby & Matthew D. Montaigne, *Three's Company*: Stone v. Ritter *and the Improper Characterization of Good Faith in the Fiduciary Duty "Triad"*, 62 Ark. L. Rev. 431, 459–62 (2009) (same), *with* Robert T. Miller, *The Board's Duty to Monitor Risk After* Citigroup, 12 U. PA. J. BUS. L. 1153, 1161 (2010) (defending *Guttman* and *Stone*).

> Corporations operate in complex environments and face a multitude of overlapping rules and regulations. In such contexts, legal risks are pervasive. A corporation must manage its legal risks and, in doing so, should have an adequate compliance program.[198]

As with § 2.01 generally, because the obligation to have "an adequate compliance program" is phrased as a corporate obligation rather than as a duty of directors and officers, it is unclear how the drafters contemplate enforcement of this obligation. Presumably, they contemplate operationalizing this requirement via directors' duties of care or loyalty.[199]

I have elsewhere explained at length why *Caremark* was a mistake both doctrinally and from a policy perspective.[200] In my view, the Delaware Supreme Court correctly phrased the oversight obligation in *Graham v. Allis-Chalmers Manufacturing Co.*,[201] a case "Chancellor Allen essentially overruled" in *Caremark*.[202] Under *Graham*, directors had no duty "to install and operate a corporate system of espionage to ferret out wrongdoing which they have no reason to suspect exists."[203] Directors would only have liability if they "recklessly reposed confidence in an obviously untrustworthy employee" or had "ignored either willfully or through inattention obvious danger signs of employee wrongdoing."[204]

The Restatement drafters ought to revive *Graham*. There is a very "interesting analogy between *Graham* and the well-known aphorism 'every dog gets one bite.'"[205] At common law, a dog owner could only be held liable to someone the dog had bitten if the

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198 RESTATEMENT § 2.01 cmt. f.

199 *See* RESTATEMENT at xvii (noting that future drafts will address oversight). The Principles treated oversight as a duty of care issue. *Id.* § 4.01 cmt. a. It appears that the Restatement drafters, however, plan to follow *Guttman* and *Stone*. *See id.* § 4.01 cmt. b (explaining that "the duty of oversight has evolved to include components of both the duty of care and the duty of loyalty"). The fact that the drafters intend to address the oversight issue in § 5.04, *id.*, seems to confirm that assumption because Chapter 5 is entitled the duty of loyalty. *Id.* at 83.

200 *See* Stephen M. Bainbridge, *Don't Compound the* Caremark *Mistake by Extending it to ESG Oversight*, 77 BUS. LAW. 651, 655–61 (2022).

201 188 A.2d 125 (Del. 1963).

202 Charles M. Elson, *The Public REIT Legal Sourcebook*, 52 BUS. LAW. 1003, 1006 (1997) (book review).

203 *Graham*, 188 A.2d at 130.

204 *Id.*

205 Bainbridge, Lopez & Oklan, *supra* note 171, at 577. The following discussion draws on *id.* at 577–78.

owner was aware that the dog had vicious propensities.[206] In general, the rule required that either the dog previously have bitten someone (the proverbial first free bite) or the owner was otherwise on notice of the dog's vicious disposition.[207]

> The analogy to cases like *Graham* should be readily apparent. Just as a dog's master is not liable unless the master knew ex ante that the dog has a propensity to bite, directors are liable under *Graham* only if they are on notice that firm employees have a propensity for misconduct. Just as a prior bite puts a dog's master on such notice, prior criminal violations or breaches of fiduciary duty can put directors on notice. Just as masters have an affirmative duty to control dogs of an inherently vicious breed, moreover, directors will be held liable when they recklessly fail to monitor an obviously untrustworthy employee.[208]

The rationale behind the one-free-bite rule was that a rule imposing liability regardless of whether the owner was on notice of the dog's propensity to bite would require the owner to take costly precautions in the form of fencing, insurance, and other interventions.[209]

> As with the dog bite rule, there is a strong cost-benefit justification for *Graham*. Compliance programs are expensive. Programs with real teeth require substantial high-level commitment and review, frequent and meaningful communication to employees, serious monitoring and auditing, and appropriate discipline when violations are discovered. By

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[206] *See, e.g.*, Ferrara v. Marra, 823 A.2d 1134, 1137 (R.I. 2003) ("Under the common law a person could recover damages from a dog bite only if that person could prove that the owner was aware of the dog's dangerous propensities . . . ."); Harris v. Anderson County Sheriff's Off., 673 S.E.2d 423, 424–25 (S.C. 2009) ("The 'one free bite' rule imposed common law liability against a dog owner only when the owner knew or should have known of the dog's vicious propensities, that is, there was no liability for the first bite.").

[207] *See, e.g.*, Mascola v. Mascola, 401 A.2d 1114 (N.J. Super. Ct. App. Div. 1979) (holding that the keeper of a vicious dog may be liable at common law if he has knowledge of dog's vicious disposition); Pattermann v. Pattermann, 496 N.W.2d 613, 616 (Wis. Ct. App. 1992) (affirming directed verdict for defendant where plaintiff "produced no evidence at all that chows are a dangerous breed of dog or that [dog] had previously bitten someone").

[208] Bainbridge, Lopez & Oklan, *supra* note 171, at 578.

[209] *Cf.* Susan Rappaport et al., *Pit Bulls: Maryland's* Solesky *Case Changes Liability Standard*, 44 U. BALT. L.F. 60, 66–67 (2013) (explaining that a decision imposing strict liability on those who control the premises on which a pit bull is present caused "landlords, property management companies, and other business owners who have the right to control the presence of pit bulls on their property to incur additional expenses in the form of insurance or other costly interventions to ensure that they are protected from these new liabilities").

analogy to the one-bite rule, one thus would expect a firm to take such precautions only when the board of directors is on notice of a past violation.[210]

F. Stakeholders and Takeovers

Under Delaware law, the extent of judicial review of complaints alleging that the board departed from shareholder value maximization is highly dependent on context. As we saw above, where the business judgment rule applies, courts will defer to a board decision that meets a rather modest test of rationality.[211] In takeover situations, where the *Unocal* version of the enhanced scrutiny standard applies,[212] a board of directors "may have regard for various constituencies in discharging its responsibilities, provided there are rationally related benefits accruing to the stockholders."[213] If the board's *Revlon* duties have triggered,[214] "concern for non-stockholder interests is inappropriate . . . ."[215]

Principles § 2.01 was not intended to address board decisions relating to takeovers, but Patrick Ryan argued that it could be used to justify takeover defenses intended to protect stakeholder interests:

> Although Section 2.01 was not intended by the A.L.I. to apply directly to takeover defenses, it can be used to show how adopting a tin parachute would comport with the fundamental corporate objectives of enhancing corporate profit and shareholder gain. These objectives are met because corporate profitability would be preserved by using a tin parachute to encourage worker productivity during a bid's pendency and

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[210] Bainbridge, Lopez & Oklan, *supra* note 171, at 578.

[211] *See supra* notes 101–105 and accompanying text.

[212] The Delaware Chancery Court has explained that "[t]he *Unocal* standard of enhanced judicial scrutiny—not the business judgment rule—is the standard of review that applies to a board's defensive actions taken in response to a hostile takeover," and that "[t]his is how Delaware has always interpreted the Unocal standard." Air Prods. & Chems. v. Airgas, Inc., 16 A.3d 48, 94 (Del. Ch. 2011). Under *Unocal* as it has been interpreted by subsequent cases, "if the board of directors' defensive response is not draconian (preclusive or coercive) and is within a 'range of reasonableness,' a court must not substitute its judgment for the board's." Unitrin, Inc. v. Am. Gen. Corp., 651 A.2d 1361, 1388 (Del. 1995) (quoting Paramount Commc'ns Inc. v. QVC Network Inc., 637 A.2d 34, 37 (Del. 1994)).

[213] Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc., 506 A.2d 173, 182 (Del. 1986).

[214] For a discussion of the content of *Revlon* duties and what triggers application of those duties, *see* Stephen M. Bainbridge, *The Geography of* Revlon-*Land*, 81 FORDHAM L. REV. 3277 (2013). For an argument that *Revlon* applies to a wider set of cases, see Mohsen Manesh, *Defined by Dictum: The Geography of* Revlon-*Land in Cash and Mixed Consideration Transactions*, 59 VILL. L. REV. 1 (2014).

[215] *Revlon*, 506 A.2d at 182.

> to prevent the firm from falling into the hands of inefficient management. Moreover, the tin parachute as compensation for displaced workers probably would pass muster as "reasonably regarded as appropriate to the responsible conduct of business."[216]

Principles § 6.02 provided that "[i]n considering whether its action is a reasonable response to the offer . . . [t]he board may . . . have regard for interests or groups (other than shareholders) with respect to which the corporation has a legitimate concern."[217] The board could only do so, however, "if to do so would not significantly disfavor the long-term interests of shareholders."[218] Having said that, however, Principles Chief Reporter Melvin Eisenberg argued that:

> Whether the action of directors would "significantly" disfavor long-term interests of shareholders may, under appropriate circumstances, involve consideration by the directors of issues other than simply the impact of the directors' action on the price that shareholders would receive for their shares. For example, if a corporation's charter or a shareholder-adopted bylaw states a policy that the corporation's business will be conducted with a particular interest in maintaining a

[216] Patrick J. Ryan, *Corporate Directors and the "Social Costs" of Takeovers–Reflections on the Tin Parachute*, 64 TUL. L. REV. 3, 36 (1989) (quoting Principles, § 2.01). Ryan explains:

> Tin parachutes are installed voluntarily by a potential takeover target's board of directors, usually in advance of a takeover bid announcement. Essentially, a tin parachute plan requires that the successful raider pay lump sums to the corporation's employees who leave the target's employ during a fixed interval after a hostile takeover. The payment obligation applies whether the employee is discharged, laid off, or quits because wages or other compensation have been significantly reduced. The payment amounts are usually computed for each employee based on salary and time of service and can equal as much as two years' wages.

Id. at 10–12. Although tin parachutes benefit stakeholders by ameliorating "some of the harsh effects of the takeover process" on stakeholders such as employees and creditors, they can injure shareholders by deterring takeover bids. *Id.* at 12. Tin parachutes are thus a classic example of the conflict of interest that arises when directors are allowed to take stakeholder interests into consideration. The directors may have been motivated by a concern for employees or creditors, but they also may be motivated by a desire to preserve their own position. *See id.* at 53 (noting that a tin parachute is "an act that instinctively could be regarded as an example of corporate social responsibility in the abstract [but] might instead be just another example of managerial self-interest if widely undertaken"); *see generally* Unocal Corp. v. Mesa Petroleum Co., 493 A.2d 946, 954 (Del. 1985) (noting that takeover defenses present an "omnipresent specter that a board may be acting primarily in its own interests").

[217] PRINCIPLES § 6.02(b)(2).

[218] *Id.*

> clean environment, or ensuring the well-being of communities in which the corporation maintains its principal plants, within the limits of § 2.01, and persons who acquired shares after the initial adoption of the policy may be deemed to be on notice of these policies through the manner in which the corporation openly conducts its business or through adequate and ongoing mechanisms of disclosure, the directors would be entitled under § 6.02(b)(2) to view continued maintenance of such a policy as part of long-term interests of shareholders in determining whether their action significantly disfavored such interests.[219]

The extent to which the Principles restated corporate common law thus was uncertain.

Tentative Draft Number 1 of the Restatement does not include blackletter law provisions directly dealing with the *Unocal* and *Revlon* duties.[220] Instead, the drafters have tentatively reserved § 6.02 to deal with those situations, with those provisions to be proposed in future tentative drafts.[221] One of the illustrations in the comments to § 2.01, however, signals the direction in which the drafters will go.

Illustration 9 assumes a target corporation whose board of directors has decided to sell the corporation. Two offers have emerged. Bidder A offers $2.9 billion and has disclosed an intent to reduce headcount and outsource substantial operations. Bidder B offers a lower price ($2.7 billion) but plans to keep the workforce intact. The target board accepts the lower bid and seeks to lockup that deal with various defensive techniques.[222]

According to the drafters, in common law jurisdictions, the target board departed from the proper objective of the corporation "because the action cannot be justified as in the interests of the shareholders whose interest in [the target] will end after the sale."[223] In stakeholder jurisdictions, however, the drafters assert that there has been no such departure, because "[m]ost constituency statutes were adopted specifically to reject *Revlon* and to permit this decision."[224]

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219 Eisenberg, *supra* note 22, at 12.
220 *See* RESTATEMENT at xvii (listing provisions covered by Tentative Draft No. 1).
221 *See id.* at xx (setting out tentative table of contents for the entire Restatement).
222 *See id.* § 2.01 cmt. e, illus. 9.
223 *Id.*
224 *Id.*

The drafters cite *Revlon* as support for their interpretation of how common law jurisdictions would decide the case,[225] but it is not obvious that all common law jurisdictions follow *Revlon*. There are seventeen common law jurisdictions.[226] Alabama, Alaska, Arkansas, Colorado, Louisiana, Montana, New Hampshire, Oklahoma, South Carolina, and Washington have no case law on point. In addition to Delaware, courts in five states have followed *Revlon*. There is one reported opinion and one unreported decision in California, both decided by the Court of Appeals.[227] An unreported Kansas trial court decision followed *Revlon*, while recognizing that there was no authoritative Kansas appellate decision on point.[228] An unreported Michigan Supreme Court decision followed *Revlon*,[229] while an unreported Pennsylvania trial court opinion followed *Revlon* in a case governed by West Virginia law. The Pennsylvania court explained that it followed *Revlon* "[b]ecause West Virginia's Supreme Court looks to Delaware precedent, and . . . West Virginia lacks any anti-*Revlon* constituency statute . . . ."[230] On the other hand, the Virginia Supreme Court had held that "the *Revlon* test is not applicable in Virginia."[231] Although North Carolina lacks a constituency statute, an unpublished North Carolina superior court decision held that North Carolina's corporation statute nevertheless "expressly rejected the *Revlon* standard."[232] In sum, it seems fair to say that the law in common law jurisdictions may not be as settled as the drafters suggest.

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[225] *Id.*

[226] Alabama, Alaska, Arkansas, California, Colorado, Delaware, Kansas, Louisiana, Michigan, Montana, New Hampshire, North Carolina, Oklahoma, South Carolina, Virginia, Washington, West Virginia. This list is derived from the drafter's listings of the various sub-types of constituency statutes. RESTATEMENT § 2.01 Reporters' Note 5.

[227] Kirschner Brothers Oil, Inc. v. Natomas Co., 229 Cal. Rptr. 899, 907 (Cal. Ct. App. 1986); Cinotto v. Levine, 2D CIV. B242191, 2014 WL 4604750, at *9 (Cal. Ct. App. Sept. 16, 2014). The *Cinotto* decision is dubious as a precedent, because the court was applying Minnesota law and assumed Minnesota would follow *Revlon*. *Id.* Because Minnesota has a constituency statute, MINN. STAT. § 302A.251 subd. 5, however, a Minnesota court is unlikely to do so. *But see* Matthew D. Cain et al., *Does* Revlon *Matter? An Empirical and Theoretical Study*, 108 CAL. L. REV. 1683, 1692 n.29 (2020) (arguing that Minnesota is one of several states that has adopted *Revlon* despite having a constituency statute).

[228] *In re* Sprint Nextel Corp. S'holder Litig., No. 12-CV-8366, 2013 Kan. Dist. LEXIS 4, at *9 (Jan. 4, 2013).

[229] Murphy v. Inman, No. 161454, 2022 WL 1020127, at *7 (Mich. Apr. 5, 2022).

[230] *In re* Portec Rail Prods., CONSOLIDATED CIVIL ACTION G.D.10-3547, G.D.10-3562, G.D.10-3982, 2010 Pa. Dist. & Cnty. Dec. LEXIS 157, at *28 (C.P. Apr. 21, 2010).

[231] Willard *ex rel.* Moneta Bldg. Supply, Inc. v. Moneta Bldg. Supply, Inc., 515 S.E.2d 277, 284 (Va. 1999).

[232] Strougo v. N. State Bancorp, 15 CVS 14696, 2016 WL 615709, at *1 (N.C. Super. Feb. 16, 2016).

Conversely, the law in constituency statute jurisdictions also may not be as clear as the drafters suggest. As noted above, a California decision asserting that Minnesota would follow *Revlon* ignored the fact that Minnesota has a constituency statute.[233] This is not an uncommon error. A recent empirical study of *Revlon* cases points out that "roughly half of the states that have adopted *Revlon* into their law also have non-shareholder constituency statutes (Illinois, Maryland, Mississippi, Minnesota, and Missouri)."[234] There thus seems to be substantial confusion among courts as to what the law in constituency statute states actually mandates. The authors further suggest that, "[i]n spite of the apparent incongruity, such statutes may not be inconsistent with *Revlon* because all make the consideration of other constituency interests optional."[235] Of course, that suggestion stands in stark contrast to the standard assumption that the statutes were intended to reject *Revlon*,[236] thereby further highlighting the confusion as to the law's content in constituency statute states.

Turning from the content of *Revlon* duties to the question of when those duties apply, Reporters' Note 3 to Section 2.01 suggests that those duties trigger "when a corporation is sold for cash" and "all of the shareholders will be cashed out."[237] If the drafters intend thereby to suggest that *Revlon* is always triggered by a sale for cash, that claim is somewhat controversial. True, dictum in some Delaware Chancery Court decisions suggests that all cash sales and some mixed consideration sales trigger *Revlon*.[238] I have elsewhere argued that those decisions are inconsistent with controlling Delaware Supreme Court precedent.[239] In my view, the relevant Supreme Court precedents clearly indicate "that an acquisition by a publicly held corporation with no controlling shareholder that results in the combined corporate entity being owned by dispersed shareholders in the proverbial 'large, fluid, changeable and changing market' does not trigger Revlon whether the deal is structured as all stock, all cash, or somewhere in the middle. The form of consideration is simply irrelevant."[240] I have also argued that the Chancery Court dicta is inconsistent

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[233] *See supra* note 227.

[234] *See* Cain et al., *supra* note 227.

[235] *Id.*

[236] *See supra* notes 123–24 and accompanying text.

[237] RESTATEMENT § 2.01 Reporters' Note 3.

[238] *See* Manesh, *supra* note 214, at 13 (discussing Chancery court dicta suggesting that "a mixed consideration merger" triggers *Revlon* duties).

[239] Bainbridge, *supra* note 214, at 3331–33.

[240] *Id.*

with the policy concerns that motivated *Revlon*.[241] The Chancery Court dicta is premised on the notion that *Revlon* is concerned with "whether there will be a tomorrow for the shareholders," but *Revlon* in fact was mainly concerned with whether the structure of the transaction allows the market to redress any conflicts of interest on the part of the target directors.[242] As long as the acquirer is publicly held, the conflict of interest concerns are muted and "diversified shareholders will be indifferent as to the allocations of gains between the parties. In turn, those shareholders also will be indifferent as to the form of consideration."[243] It is that approach to *Revlon* duties that the drafters should restate.

G. Charitable Activities

As we have seen, Principles § 2.01 authorized the corporation to "devote a reasonable amount of resources to public welfare, humanitarian, educational, and philanthropic purposes," even if doing so did not redound to the benefit of the shareholders.[244] The pertinent comment explained that:

> It is now widely accepted that the corporation should at least consider the social impact of its activities, so as to be aware of the social costs those activities entail. By implication, the corporation should be permitted to take such costs into account, within reason. For example, the corporation may take into account, within reason, public-welfare concerns relevant to groups with whom the corporation has a legitimate concern, such as employees, customers, suppliers, and members of the communities within which the corporation operates. Furthermore, because of the central position of corporations in the economic structure, the cooperation of corporations in furthering established governmental policies is often critical to the success of such policies. Social policy also favors humane behavior by major social institutions. Finally, social policy favors the maintenance of diversity in educational and philanthropic activity, and this objective would be more difficult to achieve if corporations, which control a great share of national resources, were not allowed to devote a portion of these resources to those ends.[245]

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[241] *Id.* at 3333–35.
[242] *Id.* at 3334.
[243] *Id.* at 3335.
[244] PRINCIPLES § 2.01(b)(3).
[245] *Id.* § 2.01 cmt. i.

The comment further explained that the reasonableness limitation on such expenditures depended on the circumstances surrounding specific disbursements, including the size of the disbursement relative to the corporation's assets and earnings and the strength of the nexus between the donation and the corporation's lines of business.[246]

The Restatement takes essentially the same approach. Indeed, the Restatement commentary's explanation of the policy rationale for the blackletter law is cut and pasted from the corresponding section of the Principles as quoted above.[247] The discussion of the reasonableness limitation likewise closely tracks that of the Principles.[248]

There is much that is contestable in the Principles' and the Restatement's rationale for corporate philanthropy. In economic terms, a corporation that considers the "social impact of its activities" is evaluating whether those activities generate negative externalities and considering whether—and, if so, how—to internalize those costs.[249] Redressing the negative externalities of its conduct scarcely qualifies as a charitable, humanitarian, or philanthropic activity. As David Vogel observes, traditional models of corporate social responsibility that focused on philanthropic activities were largely unrelated to the business' core operations.[250]

Instead of addressing the negative externalities associated with the corporation's activities, much corporate philanthropy is aimed at rich people's charities, which have at best tangential relevance to the business even as a means of generating good will. In large part, "corporate charitable contributions have served as a medium through which corporate executives have competed for the fellowship and esteem of elite nonprofit leaders and other business executives."[251] Director and officer discretion to expend corporate resources on philanthropic activities thus will often be

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[246] *Id.*

[247] *Compare* RESTATEMENT § 2.01 cmt. g *with* PRINCIPLES § 2.01 cmt. i.

[248] *Compare* RESTATEMENT § 2.01 cmt. g *with* PRINCIPLES § 2.01 cmt. i.

[249] It is true that all "social impacts—good and bad alike—are externalities." Richard D. Cudahy, *Retail Wheeling: Is This Revolution Necessary?*, 15 ENERGY L.J. 351, 355 (1994). The Principles' and Restatement's drafters seem to assume that all externalities—or, at least those pertinent to § 2.01—are negative, as there is no reference to the possibility that a corporation's economic activities may confer positive social impacts without regard to charitable intentions.

[250] DAVID VOGEL, THE MARKET FOR VIRTUE: THE POTENTIAL AND LIMITS OF CORPORATE SOCIAL RESPONSIBILITY 17–24 (2005).

[251] Faith Stevelman Kahn, *Pandora's Box: Managerial Discretion and the Problem of Corporate Philanthropy*, 44 UCLA L. REV. 579, 616 (1997).

an added source of agency costs within the corporation.[252] One might reasonably doubt whether such activities deserve the imprimatur of the ALI.[253]

Second, a corporate response to "public-welfare concerns" relating to its various stakeholders is a radically different proposition from charitable and philanthropic activities aimed at society as a whole. As the Restatement's drafters acknowledge, much so-called corporate philanthropy is actually done for profit maximizing purposes.[254] Arguably, the law of corporate philanthropy should mandate a nexus between the business and the object of the corporation's charitable gifts. As the Michigan Supreme Court explained in *Dodge v. Ford Motor Company*, "[t]he difference between an incidental humanitarian expenditure of corporate funds for the benefit of the employés, like the building of a hospital for their use and the employment of agencies for the betterment of their condition, and a general purpose and plan to benefit mankind at the expense of others, is obvious."[255] There is a widely shared assumption that happy and healthy employees are more productive, for example, which redounds to the benefit of the shareholders.[256] Requiring such a nexus would lessen the risk that corporate philanthropic activities will focus on pet charities and management's personal causes.

Third, it is not self-evident that achieving "established governmental policies" is necessarily beneficial to society. Instead, government policies often are designed to benefit powerful interest groups rather than the population at large.[257] Even with

[252] *See* Bruce Seifert et al., *Having, Giving, and Getting: Slack Resources, Corporate Philanthropy, and Firm Financial Performance*, 43 BUS. & SOC'Y 135, 150 (2004) (finding that firms with higher agency costs, as indicated by slack resources, contribute more to charities); *see also* Lisa Atkinson & Joseph Galaskiewicz, *Stock Ownership and Company Contributions to Charity*, 33 ADMIN. SCI. Q. 82, 86 (1988) (finding that charitable contributions decrease as stock ownership becomes more concentrated).

[253] *See* William J. Carney, *The ALI'S Corporate Governance Project: The Death of Property Rights?*, 61 GEO. WASH. L. REV. 898, 920 (1993) (arguing that Principles § 2.01 "confirmed the erosion of shareholders' property rights to insist that agents act only within specified bounds").

[254] RESTATEMENT § 2.01 cmt. g.

[255] 170 N.W. 668, 684 (Mich. 1919).

[256] Alison A. Reuter, *Subtle but Pervasive: Discrimination Against Mothers and Pregnant Women in the Workplace*, 33 FORDHAM URB. L.J. 1369, 1407 (2006) ("[Some] employers have learned that family-friendly policies make employees happy, and that happy employees make productive employees.").

[257] *See* Note, *Labor Relations in the Public Service*, 75 HARV. L. REV. 391, 393 (1961) ("[G]overnment policies are normally the product of pressures exerted by special-interest groups."); Harry G. Hutchison, *Choice, Progressive Values, and Corporate Law: A Reply to Greenfield*, 35 Del. J. Corp. L. 437 (2010) ("Mounting evidence indicates that the mission

respect to government policies that are broadly in the public interest, moreover, it is not obvious that corporations should be enlisted in achieving government's goals. The corporation is an important intermediating institution between the government and the individual. As I have argued elsewhere:

> [T]he modern public corporation has become a powerful engine for focusing the efforts of individuals to maintain the requisite sphere of economic liberty. Those whose livelihood depends on corporate enterprise cannot be neutral about political systems. Only democratic capitalist societies permit voluntary formation of private corporations and maintain a sphere of economic liberty within which they may function. This gives those who value such enterprises a powerful incentive to resist both statism and socialism. Because tyranny is far more likely to come from the public sector than the private, those who for selfish reasons strive to maintain both a democratic capitalist society and, of particular relevance to the present argument, a substantial sphere of economic liberty therein, serve the public interest. As Michael Novak observes, private property and freedom of contract were "indispensable if private business corporations were to come into existence." In turn, the corporation gives "liberty economic substance over and against the state."[258]

Viewed from that perspective, the Restatement should not be slanted towards encouraging corporations to act as government's foot soldiers.

Fourth, Principles Chief Reporter Melvin Eisenberg's claim that the corporation "is a social as well as an economic institution"[259] is more in the nature of a platitude than a statement of law. According to a widely shared view developed by law and economics scholars, "the corporation is not a social institution, but rather a nexus of contracts."[260] In turn, "the nexus of contracts model emphasizes that firms are a form of private ordering."[261] By

of the modern state is to 'satisfy the private preferences of collusive interest groups.'") (quoting JOHN GRAY, POST-LIBERALISM: STUDIES IN POLITICAL THOUGHT at 12 (1996)).

[258] Stephen M. Bainbridge, *Community and Statism: A Conservative Contractarian Critique of Progressive Corporate Law Scholarship*, 82 CORNELL L. REV. 856, 898–99 (1997) (footnotes omitted) (quoting MICHAEL NOVAK, TOWARD A THEOLOGY OF THE CORPORATION 45 (2d ed. 1990)).

[259] Melvin Aron Eisenberg, *An Overview of the Principles of Corporate Governance*, 48 BUS. LAW. 1271, 1276 (1993).

[260] Peta Spender, *Guns and Greenmail: Fear and Loathing After* Gambotto, 22 MELB. U. L. REV. 96, 127 (1998). On nexus of contracts theory, see *supra* note 51.

[261] Usha Rodrigues, *Entity and Identity*, 60 EMORY L.J. 1257, 1273 (2011).

tracking Eisenberg's text in the Principles, the Restatement drafters thus embrace his error of conflating "a firm—a nexus of contracts voluntarily and lawfully entered into by individuals to maximize their joint welfare—and a public body serving the public interest."[262]

Finally, in most states, the issue of corporate charitable contributions is governed by statutes granting corporations the power to make charitable donations.[263] Given that the primary purpose of a Restatement is to restate the common law,[264] it is thus unclear why—other than perhaps for the sake of completeness—the Restatement addresses this issue. But if the Restatement is going to address the issue, it should engage the argument made by Harvard Law Professor Einer Elhauge that corporate charitable contribution statutes are evidence that state corporate law (importantly, including that of Delaware) suggests that directors have power to consider ESG factors in pursuit of stakeholder capitalism.[265] In fact, Professor Elhauge has it exactly backwards. As Leo Strine observed, "the reality is that case law interpreting the [Delaware] statute further proves the [shareholder value maximization] rule: when approving contested charitable gifts, Delaware courts have emphasized that the stockholders would ultimately benefit from the gift in the long run."[266]

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[262] Fischel, *supra* note 175, at 1285.

[263] *See, e.g.*, DEL. CODE ANN., tit. 8, § 122(9); MODEL BUS. CORP. ACT § 3.02(m). For a useful discussion of the evolution of these statutes, see Kahn, *supra* note 251, at 594–605.

[264] *See* RESTATEMENT at x ("The law of the Restatements is generally common law, the law developed and articulated by judges in the course of deciding specific cases.").

[265] Einer Elhauge, *Sacrificing Corporate Profits in the Public Interest*, 80 N.Y.U. L. REV. 733, 767 (2005).

[266] Leo E. Strine, Jr., *The Dangers of Denial: The Need for a Clear-Eyed Understanding of the Power and Accountability Structure Established by the Delaware General Corporation Law*, 50 WAKE FOREST L. REV. 761, 779 (2015). *See also* DAVID YOSIFON, CORPORATE FRICTION: HOW CORPORATE LAW IMPEDES AMERICAN PROGRESS AND WHAT TO DO ABOUT IT 83 (2018) (concluding that the statutory "power to make charitable donations . . . represents no real exception or deviation from the fundamental rule of shareholder primacy"); Greendorfer, *supra* note 130, at 322 n.60 (2020) (arguing that "a board that managed the corporation in a way that favored giving to local schools over producing returns for shareholders would most certainly run afoul of the applicable corporate law statute of its jurisdiction of incorporation"). Chief Reporter Eisenberg claimed in 1993 that these statutes "give indirect support to section 2.01(b)(2), because it would be anomalous to permit a corporation to donate money for the public welfare or for charitable purposes while prohibiting a corporation from considering ethical principles." Eisenberg, *supra* note 259, at 1277. It would not be anomalous, however, if one required that corporate charitable contributions benefit the corporation's shareholders.

H. The Special Problems of Multinationals

The Principles were criticized for failing to "specifically address issues of concern to multinational enterprises."[267] In particular, the drafters failed to address how multinational corporations should respond to situations in which countries in which they operate have inconsistent legal or ethical standards.[268] The Restatement's drafters have likewise failed to address such situations. In light of the considerable increase in globalization since the Principles were finalized in the early 1990s,[269] this is a curious omission.

V. CONCLUSION

Section 2.01 is fundamentally flawed. It makes no sense from a theoretical or practical perspective to speak of the corporate objective. Corporations are a legal fiction representing a nexus of explicit and implicit contracts. The principles set forth in § 2.01 thus should be incorporated into the Restatement's provisions on the fiduciary duties of directors and managers.

Whether § 2.01 remains in place or is incorporated into Chapters 5 and 6 of the Restatement, there are a number of tweaks that the drafters should incorporate to modify and clarify its various provisions. Clarifying whether opting out is allowed would be especially helpful. Most important, however, the drafters should clarify and confirm that in both common law and stakeholder jurisdictions directors may not under any circumstances benefit stakeholders at the expense of shareholders. This is demonstrably the law in common law jurisdictions and is the most plausible understanding of the constituency statutes.

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[267] Bradley et al., *supra* note 69, at 50.

[268] *Id.*

[269] *See generally* MANFRED B. STEGER & PAUL JAMES, GLOBALIZATION MATTERS: ENGAGING THE GLOBAL IN UNSETTLED TIMES (2019) (discussing globalization trends).