The Neoclassical View of Corporate Fiduciary Duty Law

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Traditionally, corporate fiduciary duties are said to run to the corporation itself. But what does this mean? Something, this Article argues, that is quite different from what both shareholder and stakeholder value maximization proponents think. Specifically, the argument is that corporate fiduciary duties are owed not to any flesh-and-blood stakeholder, including current shareholders, but rather to a hypothetical permanent investor whose holding period is forever. Like any statement of corporate purpose, this "permanent equity maximization norm" is rooted in an underlying model of the corporation. In this case, the underlying model must be one that sees the corporation as a vehicle uniquely designed for long-term capital allocation and therefore emphasizes the corporation's perpetual existence as the most important attribute for understanding its nature.

This interpretation of corporate fiduciary duties—what this Article calls the "neoclassical view"—does a better job than alternatives in explaining various puzzling features of corporate law, including the apparently conflicting focus on shareholder value maximization on the one hand and the reluctance, on the other, to hold corporate fiduciaries who engage in insider trading liable for common law fraud. It also explains the allocation of decision rights in the corporation, including why decision-making power is located in the board but also why shareholders have the right to bring derivative lawsuits and vote on certain matters. Under this view, the shareholder franchise is less about giving voice to shareholders and more about providing a tool the board can use at its choosing to generate information to help it in the difficult task of long-term capital allocation.

Perhaps the most important implication stemming from this neoclassical view of corporate fiduciary duty law is that, although a corporation deals in contracts, the corporation itself is not a creature of contract, and corporate law is not necessarily contractarian as a fundamental matter. Rather, the corporation represents a policy decision to create an entity designed for extreme long-term capital allocation without sacrificing a liquid securities market. More generally, this analysis demonstrates that the concern over "short-termism" in the corporation is not simply a passing fancy but rather is deeply embedded in fiduciary duty law and lies at the core of what a corporation is.

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INTRODUCTION

Corporate directors and officers have a duty to act loyally and with the care of a reasonably prudent person.[1] But loyalty to whom and reasonable care with respect to what? It is almost an article of faith in corporate law to answer this question by saying

[1] *See, e.g.*, JAMES D. COX & THOMAS LEE HAZEN, TREATISE ON THE LAW OF CORPORATIONS § 10.1 (3d ed. 2020).

that directors and officers owe fiduciary duties to the shareholders.[2] This mantra is repeated nearly every day in classrooms,[3] boardrooms[4] and courtrooms[5] across the country. Every once in a while, some stickler might point out that that's not "technically" right and that fiduciary duties are actually owed to the corporation itself.[6] But that line of inquiry is typically stamped out quickly enough to prevent it from developing into full blown heresy, usually by chalking it up to an older, outmoded way of thinking about fiduciary duties.[7]

Nevertheless, some residual anxiety about this "technicality" usually persists and might even manage to flare up every once in a while. This anxiety is likely to rear its head, for example, at the end of a lawsuit finding that the board violated its fiduciary duties, when the monetary remedy curiously bypasses the shareholders altogether and instead goes directly to the corporate treasury.[8] Or it might recur in deciphering the meaning of the

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2 *See* R. FRANKLIN BALOTTI & JESSE A. FINKELSTEIN, DELAWARE LAW OF CORPORATIONS & BUSINESS ORGANIZATIONS § 4.16 (John Mark Zeberkiewicz & Blake Rohrbacher eds., 4th ed. 2022) ("Directors owe a duty of loyalty to the corporation, and this duty is a companion obligation to the duty of care. These duties are based on the fact that the directors are duty-bound to the true owners of the corporation, the stockholders.").

3 *See, e.g.*, WILLIAM T. ALLEN & REINIER KRAAKMAN, COMMENTARIES AND CASES ON THE LAW OF BUSINESS ORGANIZATION 284 (5th ed. 2016) ("That director loyalty to the 'corporation' is, ultimately, loyalty to equity investors is an important theme of U.S. corporate law.").

4 *See, e.g.*, *Director Fiduciary Duties: Additional Risks in Times of Financial Distress*, CHOATE (May 26, 2020), https://perma.cc/BN4J-NE94 ("So long as a corporation remains solvent, [the fiduciary duties of care and loyalty] are to be exercised for the benefit of the common equity holders of the corporation.").

5 *See, e.g.*, eBay Domestic Holdings, Inc. v. Newmark, 16 A.3d 1, 26 (Del. Ch. 2010) ("All directors of Delaware corporations are fiduciaries of the corporations' stockholders.").

6 *See, e.g.*, Deborah A. DeMott, *The Figure in the Landscape: A Comparative Sketch of Directors' Self-Interested Transactions*, 62 L. & CONTEMP. PROBS. 243, 244 (1999) (explaining how in both the United States and the United Kingdom, "corporation law is grounded in a necessary formalism that treats the corporation itself as a distinct legal entity," which means that directors "owe duties to the corporation itself"); E. Norman Veasey & Christine T. Di Guglielmo, *How Many Masters Can a Director Serve? A Look at the Tensions Facing Constituency Directors*, 63 BUS. LAW. 761, 764 n.8 (2008); ALLEN & KRAAKMAN, *supra* note 3, at 284 ("To whom do directors owe loyalty? The short answer is that they owe their duty to the corporation as a legal entity.").

7 *See, e.g.*, COX & HAZEN, *supra* note 1, § 14:16 ("Some early decisions and even an occasional recent decision treat this [corporate fiduciary] duty as running only to the corporation, not to its shareholders. Most recent decisions and some statutes, however, affirm that this duty is owed to the corporation's shareholders as well as to the corporation itself.").

8 *See, e.g.*, Tooley v. Donaldson, Lufkin & Jenrette, Inc., 845 A.2d 1031, 1036 (Del. 2004) (explaining that while shareholders are the ones that bring derivative lawsuits, the recovery from the suit goes to the corporation).

well-established holding that insider trading doesn't constitute fraudulent nondisclosure at common law because corporate insiders don't owe duties directly to shareholders;[9] or when figuring out why shareholder voting rights are so limited and so easily manipulated by the board;[10] and so on.

This Article takes these anxieties seriously by reconsidering with a fresh eye what it means for fiduciary duties to be owed to the corporation itself, what I call "the classical formulation" of corporate fiduciary duties. Despite claims to the contrary,[11] this classical formulation is not an outmoded way of talking about corporate fiduciary duties. Something like it is endorsed by the Model Business Corporation Act.[12] The Delaware Supreme Court has also said something similar on occasion.[13] And it even appears in perhaps the most common formulation of corporate fiduciary duties,[14] also popular among Delaware courts,[15] that such duties are owed to "the corporation and its stockholders."[16]

This Article asks what this classical formulation might mean. The answer it provides is not the typical one.[17] Typically, the

9 *See, e.g.*, Goodwin v. Agassiz, 186 N.E. 659, 660 (Mass. 1933).

10 *See infra* notes 89–95 and accompanying text.

11 *See, e.g.*, COX & HAZEN, *supra* note 1, § 14:16.

12 *See* MODEL BUS. CORP. ACT § 8.30(a) (AM. BAR ASS'N 2017) ("Each member of the board of directors, when discharging the duties of a director, shall act . . . in a manner the director reasonably believes to be in the best interests of the corporation.").

13 *See* Guth v. Loft, 5 A.2d 503, 510 (Del. 1939) ("A public policy, existing through the years, and derived from a profound knowledge of human characteristics and motives, has established a rule that demands of a corporate officer or director . . . to protect the interests of the corporation committed to his charge."); *see also* Schoon v. Smith, 953 A.2d 196, 206 (Del. 2008) (citing *Guth* as the source of the Delaware Supreme Court's exposition of the duty of loyalty).

14 *See, e.g.*, Johnston v. Livingston Nursing Home, Inc., 211 So.2d 151, 156 (Ala. 1968); Master Recs., Inc. v. Backman, 652 P.2d 1017, 1020 (Ariz. 1982) (en banc); Mothershead v. Douglas, 221 S.W.2d 424, 426 (Ark. 1949); Pacelli Bros. Transp., Inc. v. Pacelli, 456 A.2d 325, 329 (Conn. 1983); Holi-Rest, Inc. v. Treloar, 217 N.W.2d 517, 525 (Iowa 1974); Babineaux v. Judiciary Comm'n, 341 So.2d 396, 400 (La. 1977); Axford v. W. Syndicate Inv. Co., 170 N.W. 587, 590 (Minn. 1919); Fought v. Morris, 543 So.2d 167, 171 (Miss. 1989); Anderson v. Clemens Mobile Homes, Inc., 333 N.W.2d 900, 904 (Neb. 1983); Dunagan v. Bushey, 263 S.W.2d 148, 152 (Tex. 1953).

15 *See, e.g.*, Dohmen v. Goodman, 234 A.3d 1161, 1168 (Del. 2020); *Schoon*, 953 A.2d at 206; *Guth*, 5 A.2d at 510; Alessi v. Beracha, 849 A.2d 939, 950 (Del. Ch. 2004); Frank v. Elgamal, 2014 WL 957550, at *20 (Del. Ch. Mar. 10, 2014); *In re* MONY Grp., Inc. S'holder Litig., 853 A.2d 661, 676 (Del. Ch. 2004).

16 *Dohmen*, 234 A.3d at 1168.

17 One interesting, although perhaps less typical, interpretation of the classical formulation is that it is inherently ambiguous. *See* Andrew S. Gold, *Theories of the Firm and Judicial Uncertainty*, 35 SEATTLE U. L. REV. 1087, 1096–1106 (2012); Christopher M. Bruner, *The Enduring Ambivalence of Corporate Law*, 59 ALA. L. REV. 1385, 1424–27

classical formulation is interpreted as giving rise to either a shareholder or stakeholder value maximization norm.[18] In other words, fiduciary duties run to the shareholders, or stakeholders, with the goal of maximizing value to them. While both these answers teach something important about corporate fiduciary duties, neither is exactly right.

That fiduciary duties run to individual shareholders doesn't really account for why the classical formulation says that duties are owed to the corporation.[19] And when one pulls back the curtain on the type of model of the corporation that underwrites the shareholder value maximization norm—models that view the corporation as solving some problem, whether it be agency costs,[20] incomplete contracting[21] or centralized decision-making[22]—those models don't do a particularly good job of explaining why shareholders have such little say in the corporation.[23]

The stakeholder value maximization norm has the opposite problem. To be sure, it does a better job explaining why the classical formulation says that fiduciary duties are owed to the corporation itself: if nothing else, the corporation is a collection of stakeholders, and so it is not crazy to think that duties owed to the corporation means that they are owed to all of the stakeholders.[24] But the model of the corporation that lies behind the stakeholder maximization norm—that the corporation is a solution to the problem of allocating surplus created by firm-specific investments[25]—can't really explain why shareholders have as much of a say as they do.[26]

(2008). Although the thesis is provocative, I think there is a way to square the circle, as this Article argues.

18 *Compare, e.g.*, Stephen M. Bainbridge, *In Defense of the Shareholder Wealth Maximization Norm: A Reply to Professor Green*, 50 WASH. & LEE L. REV. 1423, 1423–25 (1993), *with* E. Merrick Dodd, Jr., *For Whom Are Corporate Managers Trustees?*, 45 HARV. L. REV. 1145, 1148 (1932).

19 *See infra* notes 123–30 and accompanying text.

20 *See, e.g.*, Thomas S. Ulen, *The Coasean Firm in Law and Economics*, 18 J. CORP. L. 301, 312–16 (1993).

21 *See, e.g.*, *id.* at 316–17.

22 *See* Stephen M. Bainbridge, *Director Primacy: The Means and Ends of Corporate Governance*, 97 NW. U. L. REV. 547, 603–04 (2003) [hereinafter Bainbridge, *Director Primacy*].

23 *See infra* notes 123–52 and accompanying text.

24 *See infra* notes 96–103 and accompanying text.

25 *See* Margaret M. Blair & Lynn A. Stout, *A Team Production Theory of Corporate Law*, 85 VA. L. REV. 247, 275–86 (1999).

26 *See infra* notes 96–127 and accompanying text.

This Article argues that the classical formulation of corporate fiduciary duties means something else entirely. By saying that fiduciary duties run to the corporation, the classical formulation is not drawing attention to the many stakeholders that make up the corporation but rather to a different feature of the corporation: its perpetual existence. And the one thing that is a necessary feature of that perpetual entity is the equity capital itself. Thus, when the classical formulation says that fiduciary duties are owed to the corporation, it means that it's owed to the equity capital. But that isn't the same thing as fiduciary duties being owed to the individual shareholders who, in a publicly traded corporation, might come and go over time.

This "permanent equity maximization norm" can explain things the shareholder or stakeholder value maximization norms simply cannot: for example, how cases like *Dodge v. Ford*,[27] holding that directors must maximize the value to shareholders, can coexist with cases like *Goodwin v. Agassiz*,[28] which holds that insider trading does not constitute fraudulent nondisclosure at common law because fiduciary duties don't run to individual shareholders.

Moreover, the model of the corporation that underlies the permanent equity maximization norm, what I call the "perpetual entity model" of the corporation, can explain why corporate decision-making power is allocated to boards: they are less likely than the shareholders to engage in short-term thinking.[29] But it also explains why shareholders aren't completely cut out of the decision-making process altogether. Under this model, the corporation is a vehicle for extremely long-term capital allocation, in fact longer-term than anything that could be expected of the typical public company shareholder. Thus, while the current shareholders' views on a given matter, for example a merger, are not completely irrelevant to the board's extremely long-term planning, they are also not unimpeachable and should probably be approached with a healthy bit of skepticism. For this reason, the corporate voting system under this model looks less like an ironclad way of making group decisions and more like an optional tool

27 170 N.W. 668 (Mich. 1919).

28 186 N.E. 659 (Mass. 1933).

29 Justin Fox & Jay W. Lorsch, *What Good Are Shareholders?*, HARV. BUS. REV., July–Aug. 2012, at 57 (finding that managers and boards are more committed to long-term goals than shareholders).

for gathering information that may or may not be helpful to the real decision-maker, which is the board.

Situating corporate fiduciary duties within a narrative emphasizing the corporation's permanent capital highlights what, in my view, most differentiates the corporation from alternative entities, including the limited liability company (LLC) and the partnership. It also differentiates the corporation from the business trust, which some have argued quite persuasively,[30] is the most obvious substitute for the corporate form, at least historically. Thus, this account explains why the corporation evolved to predominate over these alternatives.

Moreover, under the perpetual entity model of the corporation, corporate law does not simply facilitate contracting between relatively short-term-focused shareholders and boards. Rather, it calls on boards to do something more—to transcend the short-term interests of shareholders, and sometimes to even resist them defiantly, in order to invest for the extremely long term with all of the private and public benefits (and, yes, costs) that such a long-term focus entails. Thus, the corporation under this view is not a creature of contract. Rather, it reflects an explicit policy decision that long-term thinking as to capital allocation is privately and socially valuable and needs to be encouraged. This of course does not mean that such thinking is costless. It most certainly is not, as recent scholarship has reminded us.[31] But at least with many types of businesses, this policy decision suggests, the benefits outweigh those costs. Ultimately, this Article seeks to demonstrate how deeply embedded a long-term capital allocation outlook is in the structure of corporate fiduciary duties; how this outlook distinguishes the corporation from other business entities; and how it is essential to understanding how corporations are governed and the shape of corporate law itself.

This Article is organized as follows. Part I provides background on corporate fiduciary duty law. It introduces the classical formulation of corporate fiduciary duties, which maintains that such duties run to the corporation. It also lays out the various data that any interpretation of this classical formulation must explain to be convincing. Part II lays out my interpretation of the

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30 *See* John Morley, *The Common Law Corporation: The Power of the Trust in Anglo-American Business History*, 116 COLUM. L. REV. 2145, 2166–96 (2016).

31 *See, e.g.*, Jesse M. Fried, *The Uneasy Case for Favoring Long-Term Shareholders*, 124 YALE L.J. 1554, 1592–98, 1607–15 (2015). *See also generally* Michal Barzuza & Eric Talley, *Long-Term Bias*, 2020 COLUM. BUS. L. REV. 104, 135–73.

classical formulation—what I call the "neoclassical view" of corporate fiduciary duties in recognition that it is a "new" take on the classical formulation. Under this neoclassical view, corporate fiduciary duties are oriented not toward any particular shareholder but toward the permanent equity in general. It also elaborates on the theory of the corporation that underlies this neoclassical view of corporate fiduciary duties, a theory that emphasizes the corporation's perpetual existence as its most important and distinctive feature. Part III discusses the implications of the neoclassical view and speculates about why a business entity that encourages extremely long-term thinking might be valuable as a public policy matter, despite well-documented costs.

I. BACKGROUND ON CORPORATE FIDUCIARY DUTY LAW

A. The Data for Interpreting the Classical Formulation of Corporate Fiduciary Duties

The purpose of this Article is to figure out the meaning of what I'm calling the classical formulation of corporate fiduciary duties. In other words, what does this formulation mean when it says that fiduciary duties run to the corporation itself?[32] To answer that question requires us to develop an interpretation that fits a whole host of data.

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32 *See, e.g.*, Storetrax.com, Inc. v. Gurland, 895 A.2d 355, 358–59 (Md. Ct. Spec. App. 2006); Int'l Bhd. of Elec. Workers Loc. No. 129 Benefit Fund v. Tucci, 70 N.E.3d 918, 926 (Mass. 2017) ("[T]he general rule of Massachusetts corporate law is that a director of a Massachusetts corporation owes a fiduciary duty to the corporation itself, and not its shareholders."); Limmer v. Medallion Grp., Inc., 428 N.Y.S.2d 961, 963 (N.Y. App. Div. 1980) (characterizing the directors' duty of loyalty as running to the corporation); Ritchie v. Rupe, 443 S.W.3d 856, 868 (Tex. 2014) ("Directors, or those acting as directors, owe a fiduciary duty to the corporation."); *see also* RESTATEMENT (SECOND) OF AGENCY § 14C cmt. a (AM. L. INST. 1958) (highlighting that directors owe duties "to the corporation itself rather than to the shareholders individually or collectively"); Blair & Stout, *supra* note 25, at 293 (observing that "case law makes clear that directors owe their fiduciary duties primarily *to the corporation itself*" (emphasis in original)); Robert C. Clark, *Agency Costs Versus Fiduciary Duties*, *in* PRINCIPALS AND AGENTS: THE STRUCTURE OF BUSINESS 55, 56 (John W. Pratt & Richard J. Zeckhauser eds., 1985) (describing officers as agents of the corporation itself); John C. Coates, IV, *Measuring the Domain of Mediating Hierarchy: How Contestable Are U.S. Public Corporations?*, 24 J. CORP. L. 837, 839 n.9 (1999) (referring to the "doctrinal tradition that directors owe fiduciary duties to the corporation (and not directly to the shareholders)"); Deborah A. DeMott, *Beyond Metaphor: An Analysis of Fiduciary Obligation*, 1988 DUKE L.J. 879, 917 ("Conventionally, one assumes that the corporation itself is owed fiduciary obligations by many persons, including its directors, officers, and controlling shareholders.").

1. The classical formulation of corporate fiduciary duties and related case law.

The first data point that needs to be explained before arriving at what might be called "the neoclassical view" of corporate fiduciary duties is this language about the ends of corporate law. Now, sometimes commentators try to dismiss this classical formulation, suggesting that it's limited to very old opinions or the like.[33] But that's simply not true. It is very much alive today, albeit appearing in slightly different versions in different places. For example, the Model Business Corporation Act says that directors need to manage "in the best interests of the corporation."[34] The Delaware courts have at times said something similar. For example, in what it has identified as the origin of its exposition on the duty of loyalty,[35] the Delaware Supreme Court has said that fiduciary duties require the corporate officer or director "to protect the interests of the corporation."[36] A more common version of the formulation under Delaware law is that directors owe fiduciary duties "to the corporation and its stockholders."[37] The question of course is what it might mean to owe fiduciary duties to the corporation itself, or, alternatively, to the corporation and the stockholders. That's the first data point that must be explained in developing the neoclassical view of corporate fiduciary duties.

Next, the neoclassical view of corporate fiduciary duties must also make sense of the case law that purports to shed light on the classical formulation. That case law includes at least two different, yet important strands. First, there is a body of case law that assumes the purpose of corporate law is to maximize value for the shareholders and that fiduciary duties are therefore oriented toward this end. The most famous example is surely *Dodge v. Ford*, where the Dodge brothers, as minority shareholders, sued Ford Motor Co. President Henry Ford for breach of his fiduciary duties on the grounds that Ford's operational decisions were allegedly geared toward benefiting corporate constituencies other than shareholders, including consumers and employees.[38] The Michigan Supreme Court adopted a seemingly full-throated defense of the notion that fiduciary duties run to the shareholders:

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33 *See, e.g.*, COX & HAZEN, *supra* note 1, § 14:16.
34 MODEL BUS. CORP. ACT § 8.30(a)(ii) (AM. BAR ASS'N 2017).
35 *See* Schoon v. Smith, 953 A.2d 196, 206 (Del. 2008).
36 Guth v. Loft, 5 A.2d 503, 510 (Del. 1939).
37 *See* Dohmen v. Goodman, 234 A.3d 1161, 1168 (Del. 2020).
38 *See Dodge*, 170 N.W. at 671.

> A business corporation is organized and carried on primarily for the profit of the stockholders. The powers of the directors are to be employed for that end. The discretion of directors is to be exercised in the choice of means to attain that end, and does not extend to a change in the end itself, to the reduction of profits, or to the nondistribution of profits among stockholders in order to devote them to other purposes.[39]

To be sure, not everyone agrees with this reading of *Dodge*—that it endorsed a shareholder value maximization norm.[40] Some dismiss the opinion as a legal relic that was effectively overturned in the mid-twentieth century with a series of cases that arguably authorized directors to sacrifice shareholder concerns for the public interest.[41] However, these cases[42] seem to be less about overthrowing the *Dodge* case's emphasis on shareholder value as the proper end of corporate law and more about (i) clarifying that it is the long term, not short term, that matters when it comes to evaluating board decision-making and (ii) articulating a strong version of the business judgment rule to allow the unimpeded pursuit of such long-term thinking.[43]

Others argue that even if the *Dodge* opinion is still good law, the court didn't actually enforce the shareholder value maximization norm it articulated because it refused to grant the Dodge brothers' request that the court enjoin Ford from using profits to build a factory rather than paying them out in the form of a dividend.[44] While this is true, it overlooks the fact that the *Dodge*

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39 *Id.* at 684.

40 *See, e.g.*, Blair & Stout, *supra* note 25, at 301–03; Lynn A. Stout, *Why We Should Stop Teaching* Dodge v. Ford, 3 VA. L. & BUS. REV. 163, 164–68 (2008); Einer Elhauge, *Sacrificing Corporate Profits in the Public Interest*, 80 N.Y.U. L. REV. 733, 772–75 (2005).

41 *See* Blair & Stout, *supra* note 25, at 302–03.

42 *Id.* at 303 nn.140–43.

43 In defense of their view that *Dodge* is simply obsolete, Professors Margaret Blair and Lynn Stout argued that it is unreasonable to interpret these cases as clarifying the long-term nature of the shareholder value maximization norm rather than overturning that norm altogether. They contended that the cases in question would, for example, "uphold[ ] a board's discretion to reject a takeover bid at a substantial premium in order to protect the interests of the firm's employees or the community." Blair & Stout, *supra* note 25, at 304. Yet, they asked, "[h]ow can rejecting a premium offer benefit the long-run interests of the present pool of shareholders if—as modern financial theory holds—today's lower market price reflects the best possible estimate of those shareholders' future returns under current management?" *Id.* This is a good question, but, as should become clear in Part II, the neoclassical view of corporate fiduciary duties has what I think is an even better answer: the job of the board is to be so long-term-oriented that it is sometimes necessary to disagree with the market consensus.

44 *See, e.g.*, Elhauge, *supra* note 40, at 773–74.

court did affirm the lower court's injunction requiring Ford to pay the Dodge brothers the special dividend.[45] Thus, it's not as if the court didn't do anything to enforce its view of a shareholder-oriented fiduciary duty. More generally, this type of objection seems to overlook the importance of norms, even underenforced ones, in corporate law.[46] And finally, recent Delaware opinions have come pretty close to reinforcing not just the shareholder-oriented purpose of corporate fiduciary duty law but that reading of *Dodge* itself.[47] For these reasons, I think that *Dodge*, and its progeny, really does endorse some type of shareholder value maximization norm and must be accounted for in any attempt to define the neoclassical view of corporate fiduciary duties.

The second strand of case law the neoclassical view must explain assumes that fiduciary duties do not run to *individual* shareholders. This precedent consists largely of cases that reject the notion that corporate fiduciaries commit fraud against shareholders by engaging in insider trading over impersonal exchanges.[48] Consider, for example, *Goodwin v. Agassiz*, by far the most famous case of its kind. There, the plaintiffs sold Cliff Mining Co. stock to executives of the company who, at the time of the transaction, possessed material nonpublic information about the possible existence of copper deposits on property owned by the company, information the insiders failed to disclose.[49] The shareholder-plaintiffs argued that, as corporate fiduciaries, the insid-

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45 *See Dodge*, 170 N.W. at 685.

46 *See generally* Edward B. Rock & Michael L. Wachter, *Islands of Conscious Power: Law, Norms, and the Self-Governing Corporation*, 149 U. PA. L. REV. 1619 (2001).

47 *See, e.g.*, eBay Domestic Holdings, Inc. v. Newmark, 16 A.3d 1, 33 & n.105 (Del. Ch. 2010) (citing Jonathan R. Macey, *A Close Read of an Excellent Commentary on* Dodge v. Ford, 3 VA. L. & BUS. REV. 177, 179 (2008)) (articulating a shareholder wealth maximization norm, and citing Professor Jonathan Macey's article for the proposition that board actions must have "some plausible connection to a rational business purpose that ultimately benefits stockholders in some way" and that "the benefit to other constituencies cannot be at the stockholders' expense"); *In re* Citigroup Inc. S'holder Derivative Litig., 964 A.2d 106, 139 (Del. Ch. 2009) (opining on the directors' and managers' duty to "maximize shareholder value"); Agranoff v. Miller, 734 A.2d 1066, 1073 (Del. Ch. 1999) (commenting on the directors' "fiduciary duties in order to maximize shareholder value"); BTZ, Inc. v. Nat'l Intergroup, Inc., 1993 WL 133211, at *1 (Del. Ch. Apr. 7, 1993) (citing the complaint's allegation that directors' fiduciary duties require them to "maximize shareholder value").

48 Bawden v. Taylor, 98 N.E. 941, 942 (Ill. 1912); *Goodwin*, 186 N.E. at 660; Walsh v. Goulden, 90 N.W. 406, 410 (Mich. 1902); Crowell v. Jackson, 23 A. 426, 427 (N.J. 1891); O'Neile v. Ternes, 73 P. 692, 696–97 (Wash. 1903).

49 *See Goodwin*, 186 N.E. at 659.

ers to whom they sold their stock had a duty to disclose that information to avoid committing fraudulent nondisclosure, a form of common law fraud.[50]

The court disagreed, but not because it didn't recognize the tort of fraudulent nondisclosure.[51] Rather, it disagreed because it didn't think that corporate fiduciaries owe duties to the individual shareholders, and therefore there simply was no fraud in the case: "The directors of a commercial corporation stand in a relation of trust to the corporation and are bound to exercise the strictest good faith in respect to its property and business," the court said.[52] But, it continued, "[t]he contention that directors also occupy the position of trustee toward individual stockholders in the corporation is plainly contrary to repeated decisions of this court and cannot be supported."[53] And as if that wasn't enough, the court added that "[t]he principle thus established is supported by an imposing weight of authority in other jurisdictions."[54]

The reference to the weight of authority in other jurisdictions was certainly correct, but it wasn't exactly the whole story. In fact, there were instances where courts were willing to hold that insider trading was actionable under the common law but only where the insider and the shareholder were involved in face-to-face transactions.[55] And even then, most jurisdictions were only willing to go that far if there were other special circumstances weighing in favor of finding the insider liable.[56] Importantly, even in these cases, courts do not appear to have been saying that corporate fiduciary duties somehow run to individual shareholders. Rather, the reasoning appears to have been that in light of the personal nature of the transaction, and other special facts, if ap-

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[50] *See id.* at 660.

[51] RESTATEMENT (SECOND) OF TORTS § 551 (AM. L. INST. 1977).

[52] *Goodwin*, 186 N.E. at 660.

[53] *Id.*

[54] *Id.*

[55] *See, e.g.*, Barbara A. Ash, *State Regulation of Insider Trading—A Timely Resurgence?*, 49 OHIO ST. L.J. 393, 399–400 (1988) (discussing how some courts departed from the "no duty to disclose" rule in the case of face-to-face transactions).

[56] *See* Stephen M. Bainbridge, *Incorporating State Law Fiduciary Duties into the Federal Insider Trading Prohibition*, 52 WASH. & LEE L. REV. 1189, 1219–21 (1995) (discussing the early twentieth century case law on insider trading and how the so-called "special facts" rule was more prevalent than the "duty to disclose" rule but how, in any case, both rules only applied to face-to-face transactions).

plicable, fairness principles weighed in favor of finding the insiders guilty of fraud.[57] In fact, the *Goodwin* court itself seemed to suggest as much, acknowledging that "parties may stand in such relation to each other that an equitable responsibility arises to communicate facts."[58] It is notable that the court thought the disclosure responsibility, when it did apply, sounded in equity rather than in fiduciary principles.[59]

The point is that these two strands of case law both interpret the classical formulation, but they also seem to be in tension if not outright conflict. On the one hand, *Dodge* and related cases seem to suggest that fiduciary duties are oriented toward the maximization of shareholder value. On the other hand, *Goodwin* and the "weight of authority"[60] seem to suggest that fiduciary duties emphatically do not run to individual shareholders. So, any attempt to interpret the classical formulation of corporate fiduciary duties requires one to make sense of the language of the formulation as well as this apparently conflicting case law.

2. How the model of the corporation underlying a given interpretation of the classical formulation explains corporate law's allocation of decision rights.

There's one more thing to take into account in interpreting the classical formulation. Any interpretation of the ends of corporate law is associated with a particular model or view of the corporation which itself points toward the appropriate means of accomplishing those ends. For example, one might imagine a model of the corporation where the only important stakeholders are employees and entirely passive creditors who want no involvement in the firm other than financing it. Maybe in the thought world of this model, the only type of financing that exists is debt, and firms are entirely egalitarian, eschewing all forms of hierarchy. So, the employees contract for the funds provided by the creditors who insist that the firm be managed not to maximize value creation but merely to ensure solvency. That's the end of corporate law

57 *See, e.g.*, Lawrence E. Mitchell, *The Jurisprudence of the Misappropriation Theory and the New Insider Trading Legislation: From Fairness to Efficiency and Back*, 52 ALBANY L. REV. 775, 790 n.64 (1988) (containing authorities commenting on how the courts' findings of fraud in this line of cases were not premised on a finding of a fiduciary relationship between the insider and shareholder).

58 *Goodwin*, 186 N.E. at 661.

59 *See id.*

60 *Id.* at 660.

under that model. But because of the creditors' passive nature, the employees, not the creditors, are the decision-makers. That is the means of accomplishing the ends.

Admittedly, that would be a strange model of the corporation. But the point is that it's difficult to talk about ends or purposes of the corporation without also talking about the means of achieving those ends, all of which are embedded within some model of the corporation.[61] For this reason, it will be necessary to analyze how well a given view of the ends of corporate law fits the entity-based focus of the classical formulation's language as well as the case law interpreting that formulation. But we will also need to consider how the model of the corporation underlying that particular view of corporate law's purpose explains the allocation of decision rights within the corporation, or in other words the means of carrying out the given purpose.

There are four different corporate law models that need to be considered, each with its own implications for the means and ends of corporate law.

a) Principal-agent model. The principal-agent model conceives of the corporation as a means of solving an agency cost problem arising from the sale of the company to outside shareholders.[62] When an entrepreneur does this, the outside shareholders expect there to be agency costs, which is to say the costs associated with the fact that a hired hand lacks the incentives to do the job the way the principal would do it.[63] Thus, the principal adopts costly mechanisms in an effort to close this incentive gap.[64] When the entrepreneur sells the company to outsiders, those outsiders expect the management to shirk its duties or pursue a quixotic agenda of self-aggrandizement or otherwise fail to do what the outside shareholders would do if they were in charge.[65] Consequently, the shareholders bid down the price of these securities, causing management to internalize these costs.[66] In an effort to avoid these internalized costs, management implements various

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[61] Professor Stephen Bainbridge was the first to make this distinction between the means and ends of corporate law. *See generally* Bainbridge, *Director Primacy*, *supra* note 22.

[62] *See* Ulen, *supra* note 20, at 312–16; William W. Bratton, Jr., *The "Nexus of Contracts" Corporation: A Critical Appraisal*, 74 CORNELL L. REV. 407, 417–18 (1989).

[63] *See* Blair & Stout, *supra* note 25, at 258–59; Bratton, *supra* note 62, at 417–18.

[64] *See* Bratton, *supra* note 62, at 418.

[65] *See id.*

[66] *See id.*

constraints, like fiduciary duties and independent directors.[67] In the principal-agent model of the corporation, the principals are the shareholders, and the agent is the board or management. Therefore, the end of corporate law under this model is to maximize the value of the principals' (i.e., the shareholders') assets.

b) Property rights model. The property rights model also embraces a shareholder value maximization norm, but this result is reached in a different way from that of the principal-agent model.[68] Like the principal-agent model of the firm, the property rights theory takes for granted that intrafirm activity involves contracting,[69] but it focuses on a different problem than the problem of agency costs. For property rights theorists, many intrafirm contracts are "incomplete."[70] They don't specify every contingency that might arise under the contract, and therefore parties must come up with ways to decide what happens when the explicit terms of the contract run out.[71] The solution, according to these theorists, is to assign to one of the contracting parties control rights over whatever property happens to be the subject of the incomplete contract.[72] That way, there is a clear decision rule to apply in the event of a contractual gap. And those property rights are assigned to shareholders. Like the principal-agent model, the purpose of corporate law under the property rights model is to maximize shareholder value—in this case, the value of the shareholders' property rights.

c) Team production model. Like the principal-agent and property rights models, the team production model also views the corporation as a response to the shortcomings of contracting.[73] But unlike those models, the team production model does not result in the view that corporate law's ultimate purpose is to maximize shareholder value.[74] The team production model views the corporation as a mechanism for facilitating cooperative economic

67 *See id.*

68 *See* Ulen, *supra* note 20, at 316–17.

69 *Id.* at 316.

70 *See* Blair & Stout, *supra* note 25, at 259–60.

71 *See id.*

72 *See id.* at 260.

73 *See id.* at 275 (describing the public corporation "as a 'nexus of firm-specific investments,' in which several different groups contribute unique and essential resources to the corporate enterprise, and who each find it difficult to protect their contribution through explicit contracts"); *id.* at 283 (noting "that a mediating hierarchy can be an efficient response to problems of contracting over team production").

74 *See* Blair & Stout, *supra* note 25, at 287–89.

activity requiring firm-specific investments, which is to say investments in the business that can't be used elsewhere.[75]

For example, let's say that each team member has to develop different parts of a web-based platform that will have no application outside of that particular application. If they agree in advance to share the profits from the business according to some formula, there's the incentive for one or both of them to shirk. Solving it instead by making one of the team members the principal through control rights, which is essentially the principal-agent or property rights solution discussed previously, might not be agreeable to the noncontrolling team member who will fear that the controlling member won't exercise her rights to share the surplus. And finally, leaving the division of the surplus up to a negotiation after the fact will only serve to diminish that surplus as it goes to lawyers and other advisors. That leaves the solution of delegating the decision to a third party, an outsider who "makes no firm-specific investment herself. She is, however, given control over the team's assets, as well as the right to allocate output among team members and to fire individual team members or even break up the team."[76] Thus, under this view, the firm is a solution to this general team production problem.

Under the team production model, the board is said to be a "mediating hierarch[ ]."[77] It is a "hierarch" because decision-making authority is centralized within the board.[78] But it is a "mediating" one because it is meant to bring about a fair resolution to the conflicting claims of the various stakeholders.[79] Thus, the team production model views the corporation as combining a centralized decision-maker, the board, with a stakeholder value maximization norm.

d) Director primacy model. Another model that shares the centralized decision-making feature of the team production model is the director primacy model associated with Professor Stephen Bainbridge.[80] Despite this similarity, the director primacy model almost inverts the team production model. Instead of the team hiring the board, as in the team production model, in Bainbridge's

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75 *See id.* at 253.

76 *See id.* at 274.

77 *See id.* at 280–81.

78 *See id.* at 271, 280–81.

79 *See* Blair & Stout, *supra* note 25, at 280–81.

80 *See* Bainbridge, *Director Primacy*, *supra* note 22, at 599–600.

model, it is the board that effectively hires the team.[81] The resulting contractual negotiation also plays out differently. In the team production model, the board ends up being the central decision maker because the various team members decide that's the best (or perhaps the only) way to solve the holdout problem associated with firm-specific investments—allow for a neutral third party, a so-called mediating hierarch, to decide on how to allocate the surplus created by the team.[82] The director primacy model also results in the board wielding decision-making power, but for a different reason: as a way of capturing the cost efficiencies of centralized decision-making.[83] Additionally, whereas in the team production model, the board is to allocate the surplus created by the team among the various team members and therefore adopts a stakeholder value maximization norm, the director primacy model results in a shareholder value maximization norm.[84] This is because in the contractual negotiation among the various stakeholders, Bainbridge assumes that the nonshareholder stakeholders benefit from the shareholder wealth maximization norm more than the other stakeholders.[85] Thus, the director primacy model combines a centralized decision-maker, the board, with a shareholder value maximization norm.

A summary of where these models come out on the means and ends of corporate law is set forth in Table 1:

81 *See id.* at 559–60.

82 *See* Blair & Stout, *supra* note 25, at 271–76.

83 *See* Bainbridge, *Director Primacy*, *supra* note 22, at 557–59.

84 *See id.* at 563, 577–83.

85 *See id.* at 579.

TABLE 1

<table>
<tr><th>Ends of corporate governance</th><th></th><th>Model of the corporation</th><th></th><th>Means of corporate governance</th></tr>
<tr><td>1. Stake-holder value maximization</td><td>Is generated by the . . .</td><td>1. Team Production Model</td><td>Which allocates decision rights to . . .</td><td>The board</td></tr>
<tr><td rowspan="3">2. Share-holder value maximization</td><td rowspan="3">Is generated by the . . .</td><td>2(a). Principal-Agent Model</td><td rowspan="3">Which allocates decision rights to . . .</td><td>The shareholders</td></tr>
<tr><td>2(b). Property Rights Model</td><td>The shareholders</td></tr>
<tr><td>2(c). Director Primacy Model</td><td>The board</td></tr>
</table>

To recap, when we interpret the classical formulation, we are interpreting a statement about the ends of corporate law—whether corporate law should be oriented toward maximizing the value of shareholders, stakeholders, or some other constituency. But those ends presuppose some particular model of the corporation, which itself has implications about the way corporate law should look, particularly as to its means. In other words, when we decide on a particular end of corporate law, we are also by necessity choosing a model (or a group of possible models) of the corporation, and we need to evaluate how well those models explain the means of corporate law.

When I say "means of corporate law," I'm really talking about how decision rights are allocated within the corporation. There are two important considerations in connection with that inquiry. The first is derivative lawsuits, and the second is shareholder voting rights. When directors or officers violate their fiduciary duties, it is typically the corporation's claim, not the shareholders', to bring.[86] The shareholders might be allowed to bring the lawsuit

[86] *See* Tooley v. Donaldson, Lufkin & Jenrette, Inc., 845 A.2d 1031, 1035 (Del. 2004). There are of course direct lawsuits as well, where shareholders bring the lawsuit in their

because the board can't be trusted to make an objective decision whether to bring the suit or not.[87] But even in the case of such derivative lawsuits, the recovery goes to the corporation, not the shareholders or any other stakeholder for that matter.[88]

At the same time, however, shareholders do have important decision rights. As a default, they are entitled to vote on director elections.[89] They are also entitled to vote on fundamental transactions, although the rules are a little more complex. Whether shareholders are entitled to voting rights depends on whether they are shareholders of the acquiring or acquired corporation in an acquisition (either of assets or stock) or the surviving or disappearing corporation in a merger. In a stock sale, the selling stockholders would obviously get to choose whether to sell, but the shareholders of the acquiring firm would not have a vote on the transaction.[90] In an asset sale involving the sale of substantially all of the assets of a corporation, the shareholders of the selling firm would have a vote, but not the shareholders of the acquiring firm.[91] In a merger, the shareholders of the disappearing firm have a right to vote.[92] But the shareholders of the acquiring firm don't, unless it amends its certificate or issues more than 20% of the outstanding shares in connection with the merger.[93]

However, even then, the surviving corporation could avoid the merger vote in several ways. It could restructure the deal as an asset sale or stock purchase. Or it could continue with the merger structure but pay cash (or a mixed stock-cash consideration

own capacity. These are typically limited to situations where shareholders are seeking injunctive relief for having been denied some right personal to them, such as voting rights.

87 This is the reason for the demand requirement in corporate law and the related doctrine of demand futility. J. MARK RAMSEYER, BUSINESS ORGANIZATIONS 90–93 (2012).

88 *See Tooley*, 845 A.2d at 1036.

89 DEL. CODE. ANN. tit. 8, § 216 (2021); MODEL BUS. CORP. ACT § 7.28 (AM. BAR ASS'N 2017).

90 *See, e.g.*, Lou R. Kling, Eileen T. Nugent & Brandon A. Van Dyke, NEGOTIATED ACQUISITIONS OF COMPANIES, SUBSIDIARIES AND DIVISIONS § 2.03[1] (2022).

91 *See id.* § 2.03[3].

92 *See id.* § 2.03[2].

93 *See id.*

but with a lower proportion of stock to fall under the 20% threshold),[94] or it could have the disappearing firm merge into a subsidiary.[95] Thus, while the stockholders of the selling or disappearing firm in a merger have a vote, the shareholders of the acquiring firm, or surviving firm in a merger, may not, depending on how the board decides to structure the deal.

The various models associated with a given end of corporate law must explain these additional data points.

94 For example, such a strategy was famously pursued in the merger of Time and Warner, which led to the famous case regarding Delaware's treatment of fiduciary duties in fundamental transactions. *See generally* Paramount Commc'ns, Inc. v. Time, Inc., 571 A.2d 1140 (Del. 1989).

95 *See* Kling et al., *supra* note 90, § 2.03[3]. To be clear, the merger with a subsidiary of the surviving firm would only avoid triggering voting rights if such rights were triggered because of an amended certificate, not because of stock issuance of more than 20% of the outstanding shares. *See* DEL. CODE. ANN. tit. 8, § 216 (2021).

B. Interpreting the Data

The task at hand is to evaluate all of the data discussed above, including the classical formulation and related case law. It also consists of evaluating how well the model underlying a given interpretation of the classical formulation explains corporate law's allocation of decision rights. This task is summarized in Table 2 below:

TABLE 2

<table>
<tr><th>How well does the . . .</th><th>Explain . . .</th></tr>
<tr><td rowspan="2">1. Interpretation of the classical formulation
(i.e., the statement of the ends of corporate law)</td><td>1(a). The language of the classical formulation</td></tr>
<tr><td>1(b). Case law interpreting the classical formulation
(e.g., Goodwin v. Agassiz)</td></tr>
</table>

And

How well does the . . .	*Explain . . .*
2. Model underlying the interpretation of the classical formulation	2. The allocation of decision rights in the corporation (e.g., derivative lawsuits and shareholder voting rights)

So, first—what does the language of the classical formulation itself mean? Broadly speaking, there are two different interpretations that have been advanced: that it implies a stakeholder value maximization norm and that it implies a shareholder value maximization norm. Then there are various models of the corporation associated with each of these interpretations: the team production model, which is associated with the stakeholder value maximization interpretation, and the principal-agent, property rights, and director primacy models, all of which are associated with the shareholder maximization interpretation. As illustrated in Table 3, the question is how well these interpretations fit the language and case law of the classical formulation and how the associated models fit with the actual allocation of decision rights. We'll consider each of these two interpretations in turn.

TABLE 3

End	*Fit with language of classical formulation and case law*	*Model*	*Fit with actual allocation of decision rights*
1. Stakeholder value maximization norm	?	1(a). Team Production Model	?
2. Shareholder value maximization norm	?	2(a). Principal-Agent Model	?
	?	2(b). Property Rights Model	?
	?	2(c). Director Primacy Model	?

1. Stakeholder value maximization norm.

We'll start with the stakeholder value maximization interpretation because it's probably the more obvious of the two. After all, a corporation consists of many different stakeholders—suppliers, employees, customers, and so on. And therefore, when the classical formulation of corporate fiduciary duties says that such duties are owed to the corporate entity itself, it seems reasonable to conclude this means that such duties are owed to all those stakeholders of the corporation. In other words, on its face, the classical formulation seems to imply a stakeholder value maximization norm.

At the same time, it's hard to make sense of this view in light of cases that seem to adopt what appears to be a shareholder value maximization norm. For example, if the classical formulation of corporate fiduciary duties boils down to a stakeholder value maximization norm, then what is one to make of a case like *Dodge v. Ford*, where the court seems to adopt a very strong shareholder value maximization norm?[96] One might argue that this doesn't really matter at the end of the day because typically corporate law also applies a strong business judgment rule,[97] even

[96] *See supra* notes 38–47 and accompanying text.

[97] *See, e.g.*, Shlensky v. Wrigley, 237 N.E.2d 776, 778–79 (Ill. App. Ct. 1968).

if the court didn't do so in *Dodge*.[98] But at the very least this means that the shareholder value maximization norm in cases like *Dodge* and its progeny are underenforced because of the accompanying strong version of the business judgment rule. Yet, underenforced or unenforced norms are thought nevertheless to exert a significant influence, at least in corporate law.[99] Thus, even with the strong deference to boards that the business judgment rule requires, the *Dodge* shareholder value maximization norm still persists. For this reason, I don't think the stakeholder maximization interpretation of the classical formulation can make sense of cases like *Dodge*.

It does a better job, however, accounting for other cases interpreting the ends of corporate law, including, for example, the case law rejecting claims of insider trading as common law fraud. Recall that in *Goodwin v. Agassiz*, the Massachusetts high court held that corporate insiders do not owe any duties of disclosure to individual stockholders when purchasing stock over impersonal exchanges because fiduciary duties aren't owed to shareholders individually.[100] This is consistent with a stakeholder value maximization interpretation of the classical formulation. If duties are owed to stakeholders collectively, then it's not clear why a shareholder would have a claim to recover for fraud when the insider fails to disclose material nonpublic information prior to trading.

Perhaps one could argue under a stakeholder value maximization norm that there should be a claim here in *Goodwin*; it just isn't the shareholders' to recover, at least not exclusively. In that case, perhaps one would expect courts to allow a derivative claim for the corporation to recover for the insider trading. Courts don't do this with respect to claims of insider trading as common law fraud. But they do allow it for claims of insider trading as a breach

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98 For example, Professor Einer Elhauge has made a similar argument in an influential article adopting a stakeholder value maximization norm. *See* Elhauge, *supra* note 40, at 738 (emphasis added):

> Corporate managers have never had an *enforceable* legal duty to maximize corporate profits. Rather, they have always had some legal discretion (implicit or explicit) to sacrifice corporate profits in the public interest. Indeed, as I show below, the implicit version of this discretion could not be eliminated without destroying the business judgment rule that is the bedrock of corporate law.

99 *See generally* Rock & Wachter, *supra* note 46.

100 *See Goodwin*, 186 N.E. at 660.

of the duty of loyalty.[101] These are so-called *Brophy* actions, named after *Brophy v. Cities Service Co.*,[102] and they aren't uncommon.[103]

For these reasons, I think it's reasonable to say that the stakeholder maximization norm does a fairly good, if imperfect, job explaining the classical formulation of fiduciary duties as well as relevant case law that sheds light on the ends of corporate law. But as already discussed, norms about the ends of corporate law, whether stakeholder or shareholder value maximization norms, don't exist in a theoretical vacuum—they presuppose some model of the corporation. The model of the corporation most closely associated with the stakeholder value maximization norm is the team production model discussed above.[104] So, if one adopts a stakeholder maximization interpretation of the classical formulation, the team production model essentially comes along with it. Yet, the team production model yields mixed results when it comes to explaining the allocation of decision rights in the corporation (or what I'm calling the means of corporate law).

First, consider derivative lawsuits. True, the team production model explains why in derivative actions, any monetary recovery goes to the corporation rather than the shareholders who are bringing the lawsuit. If fiduciary duties run to all stakeholders, then a breach of those duties imposes a cost on the stakeholders collectively, and so any monetary remedy should go to the corporation. With that said, however, that model has a more difficult time explaining why, in certain circumstances, courts will require the remedy in a derivative lawsuit to be paid to the shareholders. For example, in *Perlman v. Feldmann*,[105] the court required that the remedy be paid directly to the shareholder-plaintiffs, not the corporation, because it did not want to enrich the new controlling shareholder, who had breached the duty of loyalty.[106] But if fiduciary duties run to the stakeholders collectively, then the court should have made some effort to ensure that the remedy went to

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[101] *See* Brophy v. Cities Serv. Co., 70 A.2d 5, 8 (Del. Ch. 1949); Kahn v. Kolberg Kravis Roberts & Co., 23 A.3d 831, 838 (Del. 2011) ("This Court has cited *Brophy* approvingly when discussing how the duty of loyalty governs the misuse of confidential corporate information by fiduciaries.").

[102] 70 A.2d 5 (Del. Ch. 1949).

[103] For example, according to Westlaw, there are more than one thousand cases citing *Brophy*.

[104] *See supra* notes 74–79 and accompanying text.

[105] 219 F.2d 173 (2d Cir. 1955).

[106] *See id.* at 177–78.

the various stakeholders to the exclusion of the new controlling shareholder.

Second, consider shareholder voting rights more generally. On the one hand, the team production model explains why the board is in charge of managing the corporation—there needs to be a mediating hierarch to resolve the conflicting claims of the various stakeholders who have made firm-specific investments in the business.[107] But it has a more difficult time explaining why the shareholders have a say at all, let alone with respect to the issues—director elections and fundamental transactions—on which they are entitled to vote.[108] After all, in the team production model, the purpose of the mediating hierarch is to avoid having any of the actual claimants who have made firm-specific investments involved in the decision how to allocate the resulting surplus.[109]

Professors Margaret Blair and Lynn Stout have two different responses to this, one about how the law works in practice and one about the law on the books, neither of which I think is entirely satisfactory. As for how corporate law works in practice, Blair and Stout point out several obstacles preventing shareholders in the typical publicly held firm from exercising any meaningful control in the corporation.[110] With respect to director elections, a combination of rational apathy and legal rules that stack the deck in favor of management's nominees make the outcome of director elections in most cases a fait accompli.[111] And as for fundamental transactions, most corporate law statutes establish voting rights regarding such transactions in such a way that boards can usually avoid a vote simply by restructuring the deal.[112] Thus, while shareholders might appear on the books to have considerable say regarding important corporate decisions, in practice, that's not at all the case.

Nevertheless, it would seem that an adequate theory of the corporation needs to explain not just how the law works in practice but also how it appears on the books. In other words, why does corporate law, at least in theory, give shareholders so much apparent control? Blair and Stout have argued that it is for one of

107 *See supra* notes 74–79 and accompanying text.
108 *See supra* notes 74–79 and accompanying text.
109 *See* Blair & Stout, *supra* note 25, at 271.
110 *See id.* at 310–12.
111 *See id.* at 310–11.
112 *See id.* at 311–12.

two reasons: Shareholders might get voting rights simply because they are the best representatives of all stakeholder interests, at least with respect to questions of director elections and fundamental transactions.[113] Alternatively, they have argued, maybe shareholders are given voting rights as compensation for vulnerabilities that other stakeholders lack, including, for example, greater collective action problems, less access to information, and fewer opportunities to directly contract with management, at least as a relative matter.[114]

These are certainly plausible explanations, but I ultimately don't find them compelling because they are fundamentally at odds with each other. On the one hand, according to Blair and Stout, there are important reasons why shareholders have voting rights.[115] But on the other hand, in practice, shareholder voting rights don't really matter.[116] It would be much more compelling if the team production theory could explain why both things are true: why the law gives shareholder voting rights and also why these don't add up to much in practice. Relatedly, Blair and Stout's explanation of why shareholders are given voting rights might explain voting rights for director elections.[117] But it doesn't really explain voting rights for fundamental transactions, and in particular the peculiar feature that boards can fairly easily avoid triggering these rights simply by restructuring the transaction.[118] If shareholder voting rights are so important, either as instrumental rights that serve the interests of all the stakeholders[119] or as compensation for shareholders' unique vulnerabilities, then it is odd they would be designed to be so easily avoidable.

To summarize, the stakeholder value maximization norm does a fairly good job of explaining the classical formulation of

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113 *See id.* at 313. The idea here is in part primarily that shareholders will vote for the purpose of maximizing share price, which Blair and Stout have said "can benefit not just shareholders but other stakeholders in the firm as well, at least when directors can pursue this goal by retaining and reinvesting corporate earnings rather than paying them out as dividends to shareholders." Blair & Stout, *supra* note 25, at 313. Of course, if this is true, it's not entirely clear why Blair and Stout aren't in favor of a shareholder maximization norm. Presumably, it's because, as they go on to make clear, share value isn't a "perfect proxy" of "the total value of rents being generated by the corporation." *See id.* at 314.

114 *See id.*

115 *See id.* at 312–14.

116 *See id.* at 310–12.

117 *See* Blair & Stout, *supra* note 25, at 310–12.

118 *See supra* notes 89–95 and accompanying text.

119 In other words, shareholders are, for practical reasons, viewed as representatives of other stakeholders.

corporate fiduciary duty law. Even if it has a difficult time accounting for case law articulating a strong shareholder maximization norm, it offers an explanation of why corporate fiduciary duties are said to run to the entity itself.[120] It further explains other case law addressing the ends of corporate law, including derivative lawsuits and the jurisprudence rejecting insider trading as a species of common law fraud on shareholders.[121] However, the stakeholder value maximization norm, like all such norms about the ends of corporate law, is embedded within a broader theory of the corporation. And the team production model, which is the most prominent theory of the corporation underwriting the stakeholder value maximization norm, has a relatively difficult time explaining certain features of corporate law, including why the shareholders are given voting rights on fundamental transactions that the board can easily evade simply by restructuring the transaction.[122]

2. The shareholder value maximization norm.

The second interpretation of the classical formulation of corporate fiduciary duties is that it is focused not on maximizing stakeholder but shareholder value.[123] This is a less obvious interpretation for the straightforward reason that it is difficult to see how saying that corporate fiduciary duties run to the corporate entity could possibly be interpreted to mean that they actually run to the shareholders. After all, a corporation consists of a number of different stakeholders—shareholders, yes, but also employ-

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120 *See supra* notes 95–96 and accompanying text.

121 *See supra* notes 99–103 and accompanying text.

122 *See supra* notes 104–12 and accompanying text.

123 The classic articulation of a shareholder value maximization norm is by the Nobel Prize–winning economist, Milton Friedman. *See* Milton Friedman, *A Friedman Doctrine—The Social Responsibility of Business Is to Increase Its Profits*, N.Y. TIMES (Sept. 13, 1970), https://perma.cc/SL5P-J98J. By the end of the twentieth century, it was safe to say that shareholder value maximization was the dominant view of the purpose of corporate law. *See* LYNN STOUT, THE SHAREHOLDER VALUE MYTH 4 (2012). Nevertheless, this consensus masks considerable variety of opinion about how best to carry out that corporate purpose. *Compare, e.g.*, Bainbridge, *Director Primacy*, *supra* note 22, at 563 ("[D]irector primacy accepts shareholder wealth maximization as the proper corporate decisionmaking norm, but rejects the notion that shareholders are entitled to either direct or indirect decisionmaking control."), *with* Lucian Arye Bebchuk, *The Case for Increasing Shareholder Power*, 118 HARV. L. REV. 833, 908 (2005) ("[M]aking shareholder intervention possible would operate to reduce agency costs between management and its shareholders and to enhance shareholder value.").

ees, creditors, suppliers, vendors, and customers. The word "corporation" seems like a plausible way of referring to all those different stakeholders. By contrast, if by "corporation" one really just means "shareholders," then why not just say so? For this reason, commentators who favor a shareholder value maximization norm tend to reject or ignore the classical formulation entirely.[124]

An alternative approach might be to point to the modern version of the formulation, notably adopted by Delaware courts, among others, that fiduciary duties run to the "corporation and shareholders."[125] The challenge to such a position is explaining why we don't say that fiduciary duties run to shareholders "full stop" rather than incorporating the idea that they run to the corporation in addition. I suppose one response might be that shareholders are the sole beneficiaries of fiduciary duties during normal times with creditors stepping into their shoes when in the zone of insolvency.[126] Such an explanation would at least give some meaning to the formulation that fiduciary duties run to the "corporation and to shareholders"—they usually run to the shareholders except in the extraordinary case of insolvency when they run to creditors. However, the Delaware Supreme Court has all but foreclosed that interpretation in an opinion that at the same time reemphasizes the classical formulation.[127]

As for case law addressing the ends of corporate law, the shareholder value maximization norm tends, not surprisingly, to yield explanatory power that is the mirror image of that of the stakeholder value maximization norm. Unlike the stakeholder value maximization norm,[128] the shareholder value maximization norm can explain cases like *Dodge v. Ford* and others that say that boards have a duty to maximize shareholder value.[129] But

124 *See, e.g.*, Stephen M. Bainbridge, *Much Ado About Little? Directors' Fiduciary Duties in the Vicinity of Insolvency*, 1 J. BUS. & TECH. L. 335, 353 (2007) ("[T]he board of directors is the nexus of a set of contracts with various constituencies that the law collectively treats as a legal fiction called the corporation. As such, it simply makes no sense to think of the board of directors as owing fiduciary duties to the corporate entity."). Indeed, Bainbridge seems to believe that the formulation is only useful as a rule of thumb for distinguishing between derivative and direct lawsuits. *See id.* at 353.

125 *See supra* note 15.

126 *See, e.g.*, Credit Lyonnais Bank Nederland, N.V. v. Pathe Commc'ns Corp., 1991 WL 277613, at *34 & n.55 (Del. Ch. Dec. 30, 1991).

127 *See* N. Am. Cath. Educ. Programming Found., Inc. v. Gheewalla, 930 A.2d 92, 99–101 (Del. 2007) (holding that "directors owe their fiduciary obligations to the corporation and its shareholders" and that "[w]hen a solvent corporation is navigating in the zone of insolvency, the focus for Delaware directors does not change").

128 *See supra* notes 96–99 and accompanying text.

129 *See supra* notes 38–47 and accompanying text.

whereas the stakeholder value maximization norm can explain the case law rejecting insider trading as a form of common law fraud on shareholders,[130] the shareholder value maximization norm makes such cases look mysterious at best. After all, if corporate fiduciary duties run to shareholders, as the shareholder value maximization norm presupposes, then why wouldn't a corporate fiduciary's failure to disclose material nonpublic information regarding a transaction with shareholders constitute fraudulent nondisclosure? In sum, the shareholder value maximization norm probably has a harder time explaining the classical formulation of corporate fiduciary duties than the stakeholder value maximization norm. It can't really offer a compelling reading of the formulation itself, and it doesn't do any better than the stakeholder value maximization norm in explaining this case law that addresses the ends of corporate law.

As for evaluating the means of achieving those ends of corporate law, like before, it is necessary to analyze the underlying theory of the corporation that underwrites the shareholder value maximization norm. As illustrated in Table 1, there are three of these: the principal-agent theory, the property theory, and the director primacy theory.

a) Principal-agent and property theories of the corporation. Both the principal-agent and property theories of the corporation locate the corporation's locus of decision-making power with the shareholders.[131] And under the property theory, it is the shareholders who are allocated the control rights over the corporation's assets to solve for the problem of incomplete contracts.[132] Unlike the team production model, these theories have the ability to explain why the shareholders have the right to vote on director elections and fundamental transactions.[133] Their problem isn't in explaining why shareholders have a say in corporate affairs but why they don't have more of one. As a legal matter, the board is not the agent of shareholders.[134] Nor is it accurate to say that share-

130 *See supra* notes 99–103 and accompanying text.

131 *See supra* notes 62–72 and accompanying text.

132 *See supra* notes 68–72 and accompanying text.

133 *See supra* notes 104–14 and accompanying text.

134 *See, e.g.*, Lyman P.Q. Johnson & David Millon, *Recalling Why Corporate Officers Are Fiduciaries*, 46 WM. & MARY L. REV. 1597, 1605 & n.25 (2005) (calling it a "universally accepted" assertion that neither the board nor the individual directors are agents of the shareholders).

holders have meaningful control rights over the corporation's assets.[135] If it were otherwise, then there would be no derivative lawsuits, and the board, if there were one, would not be shielded by various doctrines like demand futility and the business judgment rule. Thus, these models of the corporation don't do a great job explaining the means of corporate law.

b) Director primacy model of the corporation. The director primacy model also underwrites a shareholder value maximization norm, and that model does a better job explaining why shareholders don't have more of a say in corporate decision-making. Like those who apply the principal-agent model to the corporation, Bainbridge is a contractarian who believes that shareholders effectively negotiate (if not in reality, then at least hypothetically) to require the board to maximize shareholder profit.[136] But unlike those who subscribe to the principal-agent or property rights view of the corporation, Bainbridge also thinks that such a negotiation results in awarding the board substantial discretion in determining how to go about that profit maximization task because of the benefits associated with such centralized decision-making.[137]

I think it is fair to wonder about these assumptions. While there are certainly benefits to centralized decision-making, those benefits usually arise for one of two reasons: first, because decentralized decision-makers cannot be trusted to make the efficient decision[138] or second, because the transaction costs associated with establishing a system for aggregating their preferences are relatively high.[139] Yet, it's not clear why either of these things is true within Bainbridge's model. After all, Bainbridge assumes that the median shareholder is long-term-focused and thus could at least theoretically be entrusted with the decision-making

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[135] *See, e.g.*, Stephen M. Bainbridge, *Executive Compensation: Who Decides?*, 83 TEX. L. REV. 1615, 1649 (2005) (reviewing LUCIAN BEBCHUK & JESSE FRIED, PAY WITHOUT PERFORMANCE: THE UNFULFILLED PROMISE OF EXECUTIVE COMPENSATION (2004)) (characterizing the "existing regime" as one of "limited shareholder control rights").

[136] *See* Bainbridge, *Director Primacy*, *supra* note 22, at 557–59.

[137] *See id.* at 554–59.

[138] *See* Thomas W. Malone, *Is Empowerment Just a Fad? Control, Decision Making, and IT*, 38 SLOAN MGMT. REV. 23, 27 (1997) ("An obvious advantage of centralized decision making is that, with more information, people can often make better decisions."). In other words, the decentralized decision-making mechanism is thought to have less collective expertise.

[139] This is the famous collective action problem. *See generally* MANCUR OLSON, THE LOGIC OF COLLECTIVE ACTION (1971).

task.[140] And the corporate voting system already exists as a cost-effective system for aggregating shareholder preferences, thereby reducing the obvious costs of collective action. Why then should the board be in the driver's seat?[141] One answer might be that the shareholder voting mechanism is simply not the same thing as the market because shareholders are rationally apathetic as to participating in the franchise but not so in the case of the market.[142] However, shareholder "rational apathy"[143] is surely in part a function of the current allocation of decision-making rights in the corporation, which gives shareholders so little say. Give them more rights, and they become less apathetic.

All of this suggests that Bainbridge's vision of the corporation might fall short. But putting that to one side, Bainbridge's director primacy model at least has the advantage over these other shareholder-oriented models in making the board the locus of decision-making in the corporation and rejecting the erroneous notion that shareholders are either the principal or the owners of the corporation's assets. This is a promising move, even though in Bainbridge's model it's not exactly clear why the economics of centralized versus decentralized decision-making favor placing the board in that role.

But even if we take that calculus as a given, Bainbridge's model still has a problem—it doesn't explain the allocation of decision rights at anything other than a quite high level of generality. Perhaps the cost-effectiveness of centralized decision-making explains why shareholders don't have a say on every issue. But what determines why they have a say at all or on what issues in particular? And furthermore, why give the shareholders voting rights but then, at least in the case of fundamental transactions, allow the board to avoid triggering those rights by restructuring the transaction?

The director primacy model's deficiency in this respect resembles that of the team production model. The difference is that

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140 If he didn't make this assumption, then he couldn't be confident that a hypothetical bargain (i.e., a contractual approach) would result in the efficient rule.

141 To put it another way, if you accept all of modern financial theory—and in particular the fact that shareholders on the whole are so good at aggregating and analyzing available information that the market price is the best estimate of the value of a given corporate strategy—then there has to be a reason (other than lack of consensus or divergent interests) why the shareholders shouldn't be in the driver's seat. Yet, what is that reason within his model?

142 *See* Bainbridge, *Director Primacy*, *supra* note 22, at 558.

143 *Id.* at 571.

Bainbridge might have a response. He might respond by arguing that the contractarian nature of the firm that underlies his model countenances a body of corporate law full of default rules, and the optionality[144] of voting requirements is simply a type of default rule.[145] To be sure, there is some sense in such an argument—but only at a fairly high level of generality. It doesn't, for example, explain why shareholders of selling firms in acquisitions or disappearing firms in mergers almost always have voting rights, but shareholders on the other side of these transactions generally don't.[146] Furthermore, there seems to be some equivocation when it comes to the definition of default rules here. When Bainbridge talks of default rules within his contractarian-based model, he's talking about rules that apply by default unless the board and shareholders decide on some other arrangement through some type of real or hypothetical negotiation.[147] And yet, if the voting rules applicable to fundamental transactions are a type of default rule, they're a very different type indeed, one where the board can unilaterally decide whether the default should apply or not. There might be an explanation for such a rule, but if so, Bainbridge's model doesn't exactly provide it.

To summarize then, the shareholder value maximization norm has a difficult time explaining the classical formulation of corporate fiduciary duties without ignoring entirely the formulation's focus on the corporate entity.[148] In this respect, it is inferior to the stakeholder value maximization norm. And it does no better than the stakeholder value maximization norm in explaining the case law addressing the ends of corporate law.[149] As for theories of the corporation that underlie the shareholder value maximization norm, the director primacy theory does the best in explaining the allocation of decision rights in the corporation.[150] But the principal argument motivating that view—the cost-effectiveness of centralized decision-making—loses much of its force when

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144 By "optionality," I mean the fact that corporate voting rights can be sidestepped through alternative deal structuring.

145 *See, e.g.*, Henry N. Butler & Larry E. Ribstein, *Opting Out of Fiduciary Duties: A Response to the Anti-Contractarians*, 65 WASH. L. REV. 1, 10–11 (1990).

146 *See infra* notes 236–38 and accompanying text (explaining that under the neoclassical view, and the accompanying perpetual entity model of the corporation, shareholders generally have voting rights whenever the long-term decision-making structure of the firm is poised to undergo a change).

147 *See* Bainbridge, *Director Primacy*, *supra* note 22, at 577–78.

148 *See supra* notes 123–27 and accompanying text.

149 *See supra* notes 128–30 and accompanying text.

150 *See supra* notes 136–43 and accompanying text.

evaluated in light of the underlying assumptions.[151] And even then, it can't explain shareholder voting rights at an appropriate level of specificity. Table 3 summarizes the analysis.

TABLE 3[152]

End	*Fit with language of classical formulation and case law*	*Model*	*Fit with actual allocation of decision rights*
1. Stakeholder value maximization norm	Mixed	1. Team Production Model	Mixed
2. Shareholder value maximization norm	Poor	2(a). Principal-Agent Model	Poor
		2(b). Property Rights Model	Poor
		2(c). Director Primacy Model	Mixed

As Table 3 indicates, the stakeholder value maximization norm does better than the shareholder value maximization norm in explaining the language of the classical formulation and the various case law interpreting that formulation. But it's not perfect, since it can't really explain strong shareholder value maximization cases like *Dodge v. Ford*. For this reason, Table 3 indicates that the stakeholder value maximization norm's fit here is "mixed" while the shareholder value maximization norm's is "poor." With respect to the various models of the corporation that underwrite these interpretations of the classical formulation, the team production model and the director primacy models have the best fit, but again, the results aren't perfect. Neither model does a particularly good job explaining why shareholders have the rights that they do, and the director primacy model's attempt to characterize shareholder voting rights as yet another default rule doesn't really explain why the default rule is a unilateral one in favor of the board. (In other words, the board alone gets to decide

[151] *See supra* notes 143–47 and accompanying text.

[152] The qualifiers in Tables 3 and 4—"mixed," "poor," and so on—should be understood as indicating a relative, not absolute, ranking system.

whether the relevant voting rights apply depending on how it decides to structure the transaction.) In other words, none of the prevailing interpretations of the classical formulation are particularly compelling accounts. What we need is a different interpretation, and perhaps a different model of the corporation, both of which I set forth in Part II below.

II. THE NEOCLASSICAL VIEW OF CORPORATE FIDUCIARY DUTIES

In this Part, I argue for a different articulation of the ends of corporate law, and for a different theory of the corporation, that I believe better fits all of this data. I call this the "neoclassical view" of corporate fiduciary duties. The neoclassical view conceives of corporate fiduciary duties as owed not to any flesh-and-blood stakeholder, including current shareholders, but rather to a hypothetical permanent equity investor whose holding period is forever. Under the neoclassical view, the corporation is a vehicle for encouraging extreme long-term thinking about capital allocation. This type of thinking might be reflected in market prices, but it often won't be. For this reason, the neoclassical view contemplates a highly robust role for the board of directors, which must have the authority to make decisions that at times will trade off current for future shareholder wealth.

This view of corporate fiduciary duties differs from the alternatives considered in Part I in its focus on (i) shareholder wealth maximization, (ii) the future beyond the current market investing horizon, (iii) the robust role it contemplates for the board, or a combination of these considerations. The neoclassical view bears the closest resemblance to the director primacy model of the corporation, and indeed it might be characterized as articulating a type of director primacy. But the neoclassical view differs from current versions of director primacy in its insistence that the corporation cannot be a creature of contract because of the extreme long-term orientation that requires the board to look beyond the concerns of any current group of shareholders.

Let's first consider what the neoclassical view says about the proper ends of corporate fiduciary duties.

A. The Permanent Equity Value Maximization Norm

Instead of a shareholder or stakeholder value maximization norm, the neoclassical view of corporate fiduciary duties embraces what I call a "permanent equity value maximization norm."[153] Notice this means that fiduciary duties are oriented toward maximizing the value of the equity capital. But it is important to be very clear at the outset that this isn't the same thing as a shareholder value maximization norm because it's not focused on any particular shareholder. Rather, it is an equity value maximization norm that is so long-term-focused that it looks beyond the holding period of any current, or really any, shareholder. One might also refer to it as a hypothetical permanent shareholder value maximization norm because it maximizes profits for the permanent shareholder, who doesn't actually exist in reality. Perhaps the most complete statement in the case law of this interpretation of the classical formulation is this:

> [T]he fiduciary relationship requires that the directors act prudently, loyally, and in good faith to maximize the value of the corporation over the long-term for the benefit of the providers of presumptively permanent equity capital, as warranted for an entity with a presumptively perpetual life in which the residual claimants have locked in their investment.[154]

For the permanent equity value maximization norm to meet our criteria of what should count as a good interpretation of the classical formulation of corporate fiduciary duties, it must first and foremost make sense of the language of the classical formulation, which says that fiduciary duties are owed to the corporate entity itself. What does it mean for fiduciary duties to be trained on the corporate entity? In Part I, we said that the reference to the corporate entity in the classical formulation might be a reference to the many different stakeholders of the corporation, which is why a stakeholder maximization norm is a plausible take on that formulation.[155] But the reference to the corporate entity might instead be a reference to some other feature of the corporation, for example, its perpetual nature. In that case, the classical formulation might be telling us that fiduciary duties are to be

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153 By "permanent equity," I mean the same thing that commentators mean by "capital "lock-in"—the fact that corporate shareholders do not have redemption rights that would allow them to pull their money out of the corporation whenever they feel like it. *See generally, e.g.*, Margaret M. Blair, *Locking In Capital: What Corporate Law Achieved for Business Organizers in the Nineteenth Century*, 51 UCLA L. REV. 387 (2003) [hereinafter Blair, *Locking In*].

154 Frederick Hsu Living Tr. v. ODN Holding Corp., 2017 WL 1437308, at *18 (Del. Ch. Apr. 14, 2017).

155 *See supra* notes 90–91 and accompanying text.

trained on something permanent within the corporation, and the only permanent thing about a corporation is its equity capital.[156] The equity capital is in fact one of the only things that a corporation is required to identify in the certificate of incorporation, in addition to its name, address, and statement of purpose.[157] As a theoretical matter, one could imagine a corporation without creditors, employees, or suppliers.[158] But a corporation can't exist without locked-in equity capital.

Of course, where there is equity capital, there are also shareholders. But the problem with identifying the classical formulation with a shareholder value maximization norm is that any particular shareholder is not actually permanent. To be sure, in closely held corporations, a shareholder might hold for an entire lifetime. But that's still not the same thing as permanent equity. And in publicly held corporations, where shareholders come and go, the average holding period is much less.[159] Indeed, in most publicly traded companies, even a holding period of a single year would likely be considered long-term.[160] Thus, the permanent equity value maximization norm requires corporate fiduciaries to act with care and loyalty in maximizing the value of the equity capital over the extremely long term, beyond the holding period of any current shareholder.

Not only is this reading of the classical formulation consistent with the idea of duties running to the corporate entity itself (because duties are fixed on the corporation's permanent existence as embodied in its equity), but it is also consistent with the modern version of that formulation, popular in Delaware, where duties run to the corporation, and to shareholders.[161] In that modern take on the classical formulation, the reference to the corporation again suggests training fiduciary duties on something permanent within the corporation.[162] But this time, the formulation fills in a

156 This is what Vice Chancellor Travis Laster meant, I think, when he said: "A Delaware corporation, by default, has a perpetual existence. Equity capital, by default, is permanent capital." *In re* Trados Inc. S'holder Litig., 73 A.3d 17, 37 (Del. Ch. 2013) (citation omitted).

157 *See* DEL. CODE ANN. tit. 8, § 102(a)(4) (2021); MODEL BUS. CORP. ACT § 2.02(a)(2) (AM. BAR ASS'N 2017).

158 Think of a company that just receives checks from some runoff business where all funds are automatically deposited as dividends in the shareholders' bank account.

159 Saikat Chatterjee & Thyagaraju Adinarayan, *Buy, Sell, Repeat! No Room for "Hold" in Whipsawing Markets*, REUTERS (Aug. 3, 2020), https://perma.cc/2KHV-NS75.

160 *See id.*

161 *See supra* note 15 and accompanying text.

162 *See supra* notes 26–27 and accompanying text.

few inferential gaps by telling us that that something must be connected in some way to shareholders. The only possible candidate is the equity capital.

Thus, the permanent equity value maximization norm helps make sense of the language of the classical formulation of fiduciary duties and in particular its reference to the corporate entity. However, it also does something that neither the stakeholder nor shareholder maximization norms can do, which is reconcile the seemingly conflicting case law interpreting the classical formulation. Cases like *Dodge v. Ford*, which endorse a shareholder value maximization norm,[163] all of a sudden make sense because the permanent equity value maximization norm is a type of extremely long-term, shareholder-focused orientation, with the difference being that it has abstracted away any current shareholder's attributes or time horizon.

The permanent equity value maximization norm also accounts for the case law rejecting insider trading as common law fraud on particular shareholders. Cases like *Goodwin v. Agassiz* are premised on the notion that insiders do not owe fiduciary duties directly to shareholders, at least not without some additional "special facts"[164] that might create a personal relationship of trust and confidence.[165] Consequently, an insider's failure to disclose material information to the shareholder on the other side of the trade can't constitute fraudulent nondisclosure because the insider lacked any duty to disclose.[166] As discussed above, this makes absolutely no sense under a shareholder value maximization norm, where fiduciary duties run to the individual

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163 *See supra* notes 38–47 and accompanying text.

164 *See* Barbara A. Ash, *State Regulation of Insider Trading—A Timely Resurgence?*, 49 OHIO ST. L.J. 393, 399–400 (1988):

> [L]ong before even the promulgation of rule 10b-5, the majority rule [providing that insiders have no duty to disclose when trading with shareholders] had been effectively rendered a minority position by two developments. First, a substantial number of states adopted the "special facts" doctrine, first articulated by the Supreme Court in 1909 in the landmark case of *Strong v. Repide*[, 213 U.S. 419 (1909)]. Under that approach, officers and directors have had an affirmative duty to disclose nonpublic information when, in a face-to-face transaction, special circumstances or special facts render nondisclosure unconscionable. Second, several jurisdictions went so far as to require disclosure of nonpublic information to shareholders in all face-to-face transactions irrespective of any special facts or circumstances.

165 *See Goodwin*, 186 N.E. at 660.

166 *See id.*

shareholders themselves.[167] But it makes perfect sense under the permanent equity value maximization norm, under which duties don't run to any particular shareholder.

For these reasons, the permanent equity value maximization norm is a better interpretation of the classical formulation than the shareholder or stakeholder value maximization norms. But as with those statements of corporate law's ends, the permanent equity value maximization norm doesn't exist in a vacuum but rather is embedded within some model of the corporation. What is that model exactly, and is it consistent with the way corporate law allocates decision rights?

B. The Perpetual Entity Model of the Corporation

The model underlying the permanent equity value maximization norm might be referred to as the "perpetual entity model," and it's a model of the corporation that emphasizes the corporation's permanent equity capital (by way of the corporation's perpetual existence and capital lock-in) and transferability of shares.[168] Recall that the models of the corporation reviewed in Part I all had something to do with solving a problem incidental to joint ownership, whether it was agency costs in the case of the principal-agent model,[169] incomplete contracting in the property rights model,[170] the balance between accountability and control in the director primacy model,[171] or the allocation of surplus value in the face of firm-specific investments in the case of the team production model.[172] The problem at the heart of the perpetual entity model is the following: how (i) to foster an extremely long-term capital allocation outlook while (ii) allowing for the type of transferability of shares that gives rise to liquid securities markets. The answer provided by the corporate form is that condition (i) is

167 *See supra* note 130 and accompanying text.

168 Because corporate shareholders lack redemption rights, their capital is committed for the corporation's existence, which itself is not subject to an expiration date due to its perpetual nature. *See, e.g.*, Margaret M. Blair, *Reforming Corporate Governance: What History Can Teach Us*, 1 BERKELEY BUS. L.J. 1, 13–15, 26–28 (2004) [hereinafter Blair, *Corporate Governance*] (describing the corporation's unique features as perpetuity of existence, transferability of shares, and capital lock-in for a potentially indefinite period of time); Blair, *Locking In*, *supra* note 153, at 387–88 (highlighting capital lock-in as an essential feature of the corporate form).

169 *See supra* notes 62–67 and accompanying text.

170 *See supra* notes 68–72 and accompanying text.

171 *See supra* notes 80–85 and accompanying text.

172 *See supra* notes 74–78 and accompanying text.

satisfied by an entity that has locked-in perpetual capital to which fiduciary duties are trained, and condition (ii) is satisfied by transferable shares with limited liability.

1. The benefits of the perpetual entity model of the corporation.

As Professor Andrew Schwartz has explained, the corporation's perpetual existence and capital lock-in allows for capital allocation with an extremely long-term outlook, what he calls "immortal investing."[173] The permanent equity value maximization norm is, I propose, what operationalizes such immortal investing in the corporate context. The primary benefit of such an expansive corporate investment horizon is a greater economic pie, not just for shareholders but for others as well—suppliers, employees, and so on—who are in a position to capture that value. The extremely long-term outlook confers advantages on investors, allowing them to find opportunities to invest at rates of return that compound over long periods of time. What advantages exactly?

First, an extremely long-term investing outlook entails a completely different view of risk than shorter-term strategies.[174] For most of the investing world, risk is synonymous with volatility, which is to say the zigs and zags of market prices.[175] In fact, so entrenched is this concept that modern finance incorporates this volatility-as-risk definition in its model for pricing securities.[176] Yet, for the extremely long-term investor, such price movements are completely irrelevant.[177] For such investors, risk refers to the likelihood of permanent capital loss, and short-term price swings are as unimportant to long-term investment success as a twenty-four-hour stomach bug is to a marathon runner's overall

173 Andrew A. Schwartz, *The Perpetual Corporation*, 80 GEO. WASH. L. REV. 764, 783 (2012). In relying on Schwartz's helpful account of the benefits of the corporation's perpetual nature, this Section aims to explain how that perpetual nature makes possible the neoclassical understanding of corporate fiduciary duties.

174 *Id.* at 785–86.

175 *Id.* at 792–94.

176 *See, e.g.*, Jeffrey N. Gordon & Lewis A. Kornhauser, *Efficient Markets, Costly Information, and Securities Research*, 60 N.Y.U. L. REV. 761, 779 n.45 (1985).

177 *See, e.g.*, Letter from Warren E. Buffett, Chairman of the Bd., Berkshire Hathaway Inc., to S'holders of Berkshire Hathaway Inc. (Mar. 1, 1994) [hereinafter Berkshire Hathaway 1994] (available at https://perma.cc/95GH-PFCE); Schwartz, *supra* note 173, at 794 ("An immortal investor has all the time in the world to wait for an investment to bear fruit, which allows it to invest in ultra-volatile investments.").

fitness level.[178] What the extremely long-term investor is concerned about is whether over time the business is getting better, deepening its durable competitive advantage and reinvesting profits at high returns on capital or, failing that, returning excess cash to shareholders.[179] Market swings are simply irrelevant.

Another thing that distinguishes the extremely long-term investor from the rest of the market is her discount rate, which is to say her opportunity cost of making an investment or the return she needs to justify a given investment.[180] The extremely long-term investor has a relatively lower discount rate than other investors for the simple reason that she, by definition, values the future more than the next person.[181] This lower discount rate translates into a larger potential investment opportunity set than shorter-term investors. These factors combine to put extremely long-term investors in a position where they can create enormous economic value. At the same time, the strategies of extremely long-term investors can look foolish to investors with a shorter-term outlook.

A good example of this is Amazon. From its very inception, Amazon's founder, Jeff Bezos, made clear that the "everything store"[182] would take an unusually long-term outlook to capital allocation.[183] Nevertheless, for years, shareholders complained that the company appeared to operate like a charity for consumers.[184]

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178 *See, e.g.*, Schwartz, *supra* note 173, at 794.

179 *See, e.g.*, Letter from Warren E. Buffett, Chairman of the Bd., Berkshire Hathaway Inc., to S'holders of Berkshire Hathaway Inc. 7 (Feb. 2008) (emphasis in original) (available at https://perma.cc/QFT2-GNH9):

> Long-term competitive advantage in a stable industry is what we seek in a business. If that comes with rapid organic growth, great. But even without organic growth, such a business is rewarding. We will simply take the lush earnings of the business and use them to buy similar businesses elsewhere. There's no rule that you have to invest money where you've earned it. Indeed, it's often a mistake to do so: Truly great businesses, earning huge returns on tangible assets, *can't* for any extended period reinvest a large portion of their earnings internally at high rates of return.

180 *See* Schwartz, *supra* note 173, at 786–91.

181 *See id.*

182 *See* BRAD STONE, THE EVERYTHING STORE: JEFF BEZOS AND THE AGE OF AMAZON 24 (2013).

183 *See* Letter from Jeffrey P. Bezos, Founder & Chief Exec. Officer of Amazon.com, Inc., to S'holders of Amazon.com, Inc. 1 (1997) (available at https://perma.cc/83XT-8ZE9) ("We believe that a fundamental measure of our success will be the shareholder value we create over the *long term*." (emphasis in the original)).

184 Matthew Yglesias, *Amazon Profits Fall 45 Percent, Still the Most Amazing Company in the World*, SLATE (Jan. 29, 2013), https://perma.cc/PFE7-XRPY:

The company was benefiting from enormous economies of scale, meaning that its average costs went down, and average profits rose, with the increase of the quantity of products sold. But the company was taking those increased profits and reinvesting them back into the business with the specific goal of improving the customer experience.[185] The result was an increase in revenue as more and more consumers flocked to a business that was almost maniacally focused on the consumer.[186] And yet, the reinvestment of profits meant higher costs in terms of research and development and other income statement line items, decreasing margins and profits.[187] In other words, to pretty much everyone except Jeff Bezos and a select few unusually long-term investors, it seemed that Amazon was sacrificing shareholder profits for the benefit of consumers.[188] What Amazon was actually doing was growing its customer base until it enjoyed an enormous revenue stream that it could turn into profits simply by cutting back on reinvestment once it dominated e-commerce. This is exactly what happened, and enormous value was created for both investors and consumers.[189] Nor is Amazon an anomaly. Similar stories could be told

> Amazon kept up its streak of being awesome this afternoon by announcing a 45 percent year-on-year decline in profits measuring Q4 2012 against Q4 2011. Not because sales went down, mind you. They're up. Revenue is up. The company's razor-thin profit margins just got even thinner, and in total the company lost $39 million in 2012. The company's shares are down a bit today, but the company's stock is taking a much less catastrophic plunge . . . . That's because Amazon, as best I can tell, is a charitable organization being run by elements of the investment community for the benefit of consumers. The shareholders put up the equity, and instead of owning a claim on a steady stream of fat profits, they get a claim of a mighty engine of consumer surplus. Amazon sells things to people at prices that seem impossible because it actually is impossible to make money that way. And the competitive pressure of needing to square off against Amazon cuts profit margins at other companies, thus benefiting people who don't even buy anything from Amazon.

185 *See* Josh Tarasoff & John McCormack, *How to Create Value Without Earnings: The Case of Amazon*, 25 J. APPLIED CORP. FIN. 39, 41 (2013).

186 *See Annual Net Sales Revenue of Amazon from 2004 to 2022*, STATISTA (Feb. 14, 2023), https://perma.cc/8A4W-86JN; *see also About Amazon*, AMAZON, https://perma.cc/E9KS-RTXL (describing Amazon's mission "to be Earth's most customer-centric company" (quotation marks omitted)).

187 *See* Tarasoff & McCormack, *supra* note 185, at 40.

188 *See* Yglesias, *supra* note 184; *see also*, Tarasoff & McCormack, *supra* note 185, at 40 ("We believe that Amazon has done a superb job of building shareholder wealth by acting single-mindedly to maximize long-run 'free cash flow' per share. It has done so through aggressive reinvestment of cash flow at high rates of return on invested capital.").

189 *See* Tarasoff & McCormack, *supra* note 185, at 40.

about other extremely long-term focused companies: Ford in its heyday, Berkshire Hathaway, Costco, and so on.[190]

In sum, there are potentially significant benefits associated with extremely long-term investing. The long-term investor's different approach to risk and discount rates means that there is a greater set of investment opportunities available to the long-term, as compared to the short-term, investor. There is also built-in leverage in the form of deferred taxes.[191] If I can realize a compounded annualized return of 15% for ten years in two alternative investments, but the first option allows me to stay invested for the entire duration while the second option requires many short-term investments, along with the accompanying realization of taxable income, the first option will end up producing a considerably larger after-tax return than the second option.[192] Combine all of these advantages with a long-term holding period, and you end up with an investment whose return compounds for a very long time, leading to a relatively greater economic pie.

But a Buffett or Bezos, the type who is simply hardwired for extremely long-term thinking, might only come along once in a generation. How can such long-term thinking be encouraged in lesser mortals? One approach might be to force shareholders to adopt such thinking and then legally require corporate fiduciaries to maximize shareholder value. In other words, one could prevent shareholders from ever selling and then train fiduciary duties on those shareholders. That's more or less what the partnership form does: it places limitations on the transferability of partnership interests, locking in partners,[193] and then creates fiduciary

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190 That's not to say that these examples are free of controversy. That's certainly not the case with Amazon anyway. There are legitimate criticisms that one might level at how the company treats its employees or how its brand of take-no-prisoners competition has harmed mom-and-pop stores and their local communities. But these types of criticisms are not uniquely a function of Amazon's extremely long-term outlook.

191 *See, e.g.*, Berkshire Hathaway 1994, *supra* note 177, at 8 ("[T]ax-paying investors will realize a far, far greater sum from a single investment that compounds internally at a given rate than from a succession of investments compounding at the same rate.").

192 *See How to Invest Tax-Efficiently*, FIDELITY (Feb. 2023), https://perma.cc/7FZL-WLBN ("Securities held for more than 12 months before being sold are taxed as long-term gains or losses with a top federal rate of 23.8%, versus 40.8% for short-term gains . . . . Being conscious of holding periods is a simple way to avoid paying higher tax rates.").

193 *See* REVISED UNIF. P'SHIP ACT §§ 102(23), 503(a)(3) (NAT'L CONF. OF COMM'RS ON UNIF. STATE L. 1997) (establishing as a default rule that while a partner's economic rights are freely transferable, its governance rights are not); Neema Amini, *Transfer Restrictions in LLC and Partnership Agreements*, AMINI & CONANT (June 22, 2022), https://perma.cc/WY8D-GXND (listing transfer restrictions that partnership agreements frequently layer over that default rule).

duties that run to the individual partners rather than the entity.[194] But that approach has at least two significant drawbacks. First, there is no guarantee that the individual partners are long-term focused, especially considering that partnerships are, by default, "at will," and therefore fiduciary duties that are trained on individual partners won't necessarily result in such extreme long-term investing.[195] Second, and perhaps even more importantly, that approach doesn't lead to liquid securities markets[196] and the significant economic benefits associated with such markets.[197]

What about modifying the partnership form to at least facilitate such liquid securities markets? It turns out that accomplishing such a feat is more complicated than it first appears. In particular, such a move would require more than simply the transferability of partnership interests, which partners can mutually agree to under the current way partnership works.[198] After all, partners are individually liable for the debts of the partnership,[199] and so the identity of a given partner, their risk profile, and their financial makeup, become incredibly important to the other partners who are liable for that partner's decisions.[200] Therefore, it is unlikely that a rational partnership would ever decide to create a situation where partnership interests are traded in a truly liquid market without concern for who is buying and selling. Such a move would require limited liability. But while limited liability would foster a liquid securities market, it's

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194 This is at least true of the older common law view that a partnership "was not a legal person in addition to the natural persons who were the partners." A. Ladru Jensen, *Is a Partnership Under the Uniform Partnership Act an Aggregate or an Entity?*, 16 VAND. L. REV. 377, 377 (1963).

195 *See* REVISED UNIF. P'SHIP ACT §§ 102(13), 801(1) (NAT'L CONF. OF COMM'RS ON UNIF. STATE L. 1997) (defining "partnership at will" as any partnership where the partners haven't explicitly agreed to remain partners until some specified time, and providing that a dissolution occurs whenever a partner has given notice of his "express will" to withdraw as a partner).

196 The antitransferability rules of partnership reduce liquidity because they prevent investors from freely buying and selling partnership interests.

197 *See* Marcel Kahan, *Securities Laws and the Social Costs of "Inaccurate" Stock Prices*, 41 DUKE L.J. 977, 1019–20 (1992).

198 *See* REVISED UNIF. P'SHIP ACT § 503(a)(3) (NAT'L CONF. OF COMM'RS UNIF. STATE L. 1997) (establishing that while a partner's economic rights are freely transferable, its governance rights are not).

199 *See id.* § 306(a).

200 *Cf.* Schwartz, *supra* note 173, at 769–70 (describing limited liability as essential to the public corporation because it assures investors that they will not be liable for the corporation's debts and "renders the identity and wealth of shareholders irrelevant").

not going to result in extreme long-term investing if fiduciary duties run to those shareholders who are trading in and out of the company's shares. Such a situation couldn't really be expected to cause Amazon, in the absence of a Jeff Bezos, to ignore the criticisms of its long-term strategy by current shareholders. Rather, fiduciary duties need to be trained on something permanent, which is the corporate entity itself and in particular the permanent equity capital.

2. The meaning behind the "extreme long term."

The neoclassical view of fiduciary duties, and the related perpetual entity model, then depict the corporation as an entity that is uniquely designed for extreme long-term capital allocation because fiduciary duties are directed at something that is extremely long-term—the locked-in equity of a permanent entity. Whether this makes sense depends on what we mean by the "extreme long term." It also depends on assumptions made about current shareholders and the market itself. After all, if a critical mass of shareholders could be categorized as adopting an extremely long-term investment horizon, which would then be reflected in market prices, we could accomplish our goal of creating an extremely long-term vehicle simply by orienting fiduciary duties toward current shareholders and the maximization of market price. Unfortunately, however, this won't work.

Market prices reflect investors' forecasts of a corporation's future performance. But how far into the future? At least for some companies, it could be as much as a decade.[201] But what I mean in this Article by the "extreme long term" is a period of time that is longer, and possibly much longer, than that. There are structural reasons why the market is subject to a limited investment horizon. Most investors invest in the stock market indirectly through investment funds.[202] Such funds report to their investors on a quarterly and annual basis and face redemptions if investments don't "work out" over a time period measured in months or years,

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[201] *See* ALFRED RAPPAPORT & MICHAEL J. MAUBOUSSIN, EXPECTATIONS INVESTING: READING STOCK PRICES FOR BETTER RETURNS 10 (2001) (explaining that we know markets take the long view because "most companies need over ten years of value-creating cash flows to justify their stock price" and expected dividends over the next five years explain only a relatively small percentage of the current stock price).

[202] *See* Hal S. Scott, Opinion, *Capital Market Regulation Needs an Overhaul*, WALL ST. J. (Apr. 20, 2011), https://www.wsj.com/articles/SB10001424052748704529204576256761539125534.

not decades.[203] What happens if a fund manager finds a long-term investment that he knows will produce a significant annualized return when compounded over the life of the investment, but the returns will be "lumpy," meaning in any given year, they might be minimal if not negative? The answer is that he might pass on the investment if he thinks that his investors won't stick with him through the lumpiness to see the investment through the end.[204]

But even where investment management is not delegated—for example, where an investment fund might be primarily owned by the employees themselves—sophisticated investors tend to be trained to adopt a particular methodology that favors the appearance of precision, which doesn't mesh well with extreme long-term investing.[205] Think again of the Amazon example. Jeff Bezos talks about how he knew lowering prices at Amazon would create a virtuous cycle—his famous flywheel—that would result in increased cash flow in the extreme long run.[206] But he had no idea how much of an increase, and in the short run at least earnings would likely go down.[207] In other words, Bezos couldn't say that by year twelve of the investment, earnings would be 25% greater than the current year. But he could say they would be meaningfully higher.

Yet, the bread and butter of business school valuation classes and Wall Street analyst desks is the discounted cash flow (DCF) model, which requires one to estimate a company's cash flows over a five- to fifteen-year period and then discount those income streams by some appropriate discount rate.[208] It is difficult enough to take that approach to an investment horizon that

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203 *See* Houman B. Shadab, *Hedge Fund Governance*, 19 STAN. J.L. BUS. & FIN. 141, 145 (2013) (emphasis in original):

> [H]edge fund governance is [ ]uniquely *responsive* in the sense that to obtain and retain investor capital, hedge fund managers must be highly responsive to the preferences of equity investors (the limited partners). This responsiveness arises from a fundamental dynamic of hedge fund governance—the propensity of investors to "pull the plug" and cash out of a fund if they are dissatisfied.

204 There's a similar argument made about why there might be too little arbitrage in markets. *See* Andrei Shleifer & Robert W. Vishny, *The Limits of Arbitrage*, 52 J. FIN. 35, 47 (1997).

205 *See supra* notes 183–87.

206 Ben Thompson, *The Relentless Jeff Bezos*, STRATECHERY (Feb. 3, 2021), https://perma.cc/KZ97-Z87T.

207 James B. Stewart, *Amazon Says Long Term and Means It*, N.Y. TIMES (Dec. 16, 2011), https://www.nytimes.com/2011/12/17/business/at-amazon-jeff-bezos-talks-long-term-and-means-it.html.

208 *See* TIM KOLLER, MARC GOEDHART & DAVID WESSELS, VALUATION: MEASURING AND MANAGING THE VALUE OF COMPANIES 177–91 (7th ed. 2020).

reaches ten years out, which is why most DCF's probably stop at year four or five.[209] For anything beyond that, such an approach is a nonstarter. One solution would be to simply not think much about what happens beyond year ten, which is what analysts tend to do by including in the model some "terminal value" representing the value of the company in year ten or whatever the ending year of the model happens to be.[210] But this is just a way of not thinking about what happens to the business or investment beyond that point, and not surprisingly financial models are notoriously sensitive to the amount of this terminal value.[211]

These structural factors—the risk of redemptions at institutional investors and the illusion of precision in valuation models—make for a market with a relatively short-term investment horizon, or at least one that falls far short of the extreme long term in the sense of this Article. They also cause investors to focus on certain types of questions to the exclusion of others. For example, in a passage rumored to have been written by famed investor and then–Marathon employee Nick Sleep, Marathon Asset Management has described a scenario where Colgate Palmolive undertook a significant, very long-term advertising investment in support of a new toothpaste:

> By advertising heavily, the firm hoped to change the buying habits of a generation of shoppers who would subconsciously think of Colgate as they approached the toothpaste section of a supermarket, and when they got there, would find a product which was new, superior and, because of advertising spend, trusted.[212]

Colgate's strategy proved enormously successful, leading to a twenty-five-fold stock price increase over two decades.[213] And yet,

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209 *See* MICHAEL J. MAUBOUSSIN, LEGG MASON CAP. MGMT., COMMON ERRORS IN DCF MODELS 3 (2006).

210 *See id.* at 2.

211 Another approach would be to adopt a different methodology altogether. For example, according to one shareholder letter, Berkshire Hathaway founder Warren Buffett appears to try to understand a company at a sufficiently deep level that he is confident of its competitive advantage and growth prospects. He then waits to buy it until he is sure it is trading at a discount to fair value, whatever that happens to be. *See, e.g.*, Berkshire Hathaway 1994, *supra* note 177. For Buffett, this lack of precision is a feature of his methodology, not a bug. *See id.* ("It is better to be approximately right than precisely wrong."). To quote Seth Klarman, another famous, and famously long-term, investor, "[a]ny attempt to value businesses with precision will yield values that are precisely inaccurate." SETH A. KLARMAN, MARGIN OF SAFETY 118 (1991).

212 CAPITAL RETURNS 56 (Edward Chancellor ed., 2016).

213 *Id.* at 57.

as Marathon pointed out, "Colgate presentations do not mention the company's advertising spend . . . . 'Most people don't think it is important,' confessed the firm's investor relations spokeswoman."[214] Marathon confided that it was the only one "to have sought and gained a meeting with Colgate's director of advertising and marketing," the person in charge of this extremely long-term investment.[215] It's worth emphasizing that the market participants who didn't think such information was important—most investors other than Sleep and his fund—were absolutely right. It really didn't matter for an investment horizon of less than a decade, which is the typical horizon for the market. It's just that Marathon was looking at a more distant horizon.

So, current shareholders and the market are not necessarily focused on the extreme long term, and yet there are potentially both significant private and public benefits from a corporation adopting such an investment time horizon, as already discussed. If current shareholders and the market more generally are not focused on the extreme long term, and assuming that there are reasons to encourage extremely long-term corporate capital allocation, how does one encourage boards and management to adopt such a focus? The answer is you create an entity with a perpetual, locked-in capital and then train fiduciary duties on the permanent equity of that business. That's the neoclassical view of corporate fiduciary duties.

3. Alternatives to the corporation as a perpetual entity.

One obvious question that this perpetual entity model of the corporation raises is whether the corporation is really unique in this sense of fostering an extremely long-term outlook while also facilitating a liquid securities market. Couldn't alternative, noncorporate forms that predated the rise of the corporation emerge to meet these conditions? It's already been suggested why the answer is "no" with respect to the partnership form.[216] Partnerships are, by default, "at will" associations that can be dissolved at any time by any change in the relationship among partners.[217] To be sure, the partners could agree to impose a particular term on the partnership. But that still doesn't solve the problem

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[214] *Id.*

[215] *Id.*

[216] *See supra* notes 193–200 and accompanying text.

[217] *See* REVISED UNIF. P'SHIP ACT §§ 102(13), 801(1) (NAT'L CONF. OF COMM'RS UNIF. STATE L. 1997).

of nontransferable shares and illiquid securities markets. By default, partners can't transfer their ownership interests without getting the approval of the other partners. That can be changed, of course, to allow for free transferability. But it isn't clear in partnership law that fiduciary duties run to the entity as opposed to individual partners. At least, it wasn't clear that was the case until after the rise of the corporation,[218] and thus the partnership form would have even then lacked the long-term focus that the neoclassical view confers on the corporation. And even if it had been made clear prior to the rise of the corporation that something like the neoclassical view of corporate fiduciary duties also applied to partnership, without limited liability, which the partnership form lacks,[219] there can't really be a liquid securities market in partnership interests.

So, the partnership isn't much of a substitute for the corporation as a perpetual entity with fiduciary duties trained on the permanent equity. A much more likely candidate for a corporate alternative is the business trust, which predated the corporate form. In an important article, Professor John Morley has made the case that the business trust actually contained all of the attributes that are traditionally associated with the corporation: limited liability, entity shielding, tradeable shares, and legal personhood.[220] Thus, Morley argues, there must be some reason other than these why the corporate form was preferred over the business trust.[221]

The reason might have to do with perpetual existence and the neoclassical view of corporation fiduciary duties. As for perpetual existence, it's certainly true that early business trusts weren't

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218 There are two views of partnership, the aggregation and the entity views. *See* Jenson, *supra* note 194, at 377–81. Under the older aggregation view, fiduciary duties ran to individual partners. *See id.* at 377 (explaining that "a partnership was not a legal person in addition to the natural persons who were the partners"). Under the more modern entity view, fiduciary duties in partnership seem to track the classical formulation of corporate fiduciary duty law in that courts tend to say they run to the partnership and the partners. *See* REVISED UNIF. P'SHIP ACT § 409(a) ("A partner owes to the partnership and the other partners the duties of loyalty and care."); Wallace *ex rel.* Cencom Cable Income Partners II, Inc. v. Wood, 752 A.2d 1175, 1180 (Del. Ch. 1999) ("Unquestionably, the general partner of a limited partnership owes direct fiduciary duties to the partnership and to its limited partners.").

219 *See* Blair, *Corporate Governance*, *supra* note 168, at 20.

220 *See* Morley, *supra* note 30, at 2166–96.

221 *See id.* at 2148.

subject to the rule against perpetuities.[222] Nevertheless, they almost certainly didn't have perpetual existence because of common law rules limiting the duration of an indestructible trust to a life in being plus twenty-one years.[223] Admittedly, such a rule would still have allowed a business trust to last for a very long time, perhaps one hundred years, but it wasn't perpetual. For example, Colgate-Palmolive[224] or DuPont,[225] among many other very long-lived companies, simply could not have existed as business trusts because of these limitations on duration.

Additionally, the classical formulation of corporate fiduciary duties, as is the case with partnerships, lacks an analog when it comes to business trusts. In other words, in that context, the trustees' fiduciary duties are owed directly to the beneficiaries, not to the entity itself.[226] And therefore, even if a business trust were to endure for the maximum time of a life in being plus twenty-one years, the trustee's time horizon might be much shorter, depending on the time horizon of the particular trust beneficiaries.

Thus, this account of corporate fiduciary duties does identify a difference between corporations and business trusts, which is to say, a fiduciary structure that is built around permanent equity. I've argued that the purpose of this difference is to create a vehicle that is uniquely designed for extreme long-term profit maximization. Whether it does in fact accomplish this goal is a different matter entirely and one that I don't address here. Nevertheless, this difference between business trusts and the corporation might contain the bare bones of an argument for why the corporation came to win out over the alternatives.[227]

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222 *See* Horace E. Whiteside, *Restrictions on the Duration of Business Trusts*, 9 CORNELL L.Q. 422, 432 (1923).

223 *See id.* at 428.

224 *Our History*, COLGATE-PALMOLIVE (2023), https://perma.cc/CXU9-HF6W.

225 *Our History*, DUPONT (2023), https://perma.cc/2FB8-6Q66.

226 The reason for this is that, as a general matter, like the partnership form, the business trust at common law was not considered to be an entity separate from the trustees or beneficiaries. *See* Sheldon A. Jones, Laura M. Moret & James M. Storey, *The Massachusetts Business Trust and Registered Investment Companies*, 13 DEL. J. CORP. L. 421, 430–31 (1988) (discussing how in Massachusetts, the business trust was only treated as a separate legal entity for certain narrow purposes); Morley, *supra* note 30, at 2154. Whether a business trust was treated as a separate legal entity may have depended on the degree to which the trust beneficiaries exercised control over the trustees. *See* E. Merrick Dodd, Jr., *Dogma and Practice in the Law of Associations*, 42 HARV. L. REV. 977, 987–88 (1929).

227 To flesh out that explanation, one would need to explain why that difference might be valuable not only to society, as I've argued above, see *supra* Part II.B.1, but also to those making the decision as to choice of entity. One possibility is that entrepreneurs in the late

4. How the perpetual entity model of the corporation explains the allocation of corporate decision rights.

As already discussed, the permanent equity value maximization norm does a better job than the stakeholder and shareholder value maximization norms in explaining the language of the classical formulation of corporate fiduciary duties.[228] It also is superior in explaining the seemingly conflicting case law interpreting that classical formulation.[229] The question is whether the model that underwrites that permanent equity value maximization norm, the perpetual entity model discussed above, can explain the allocation of decision rights in the corporation.

Recall that the other models of the corporation, reviewed in Part I, produced mixed results in this regard.[230] The principal-agent and property rights models have a difficult time explaining why the board exists in the first place and why shareholders have such limited roles.[231] For example, both models can't really explain the fact that the shareholders are limited to bringing certain fiduciary duty claims on behalf of the corporation rather than themselves, the fact that their voting rights are limited to so few decisions, and even then, why those rights are so easily avoidable by the board.

The director primacy and team production models do a better job explaining why the board has such an important role in the corporation: in the case of the director primacy model, because of the benefits of centralized decision-making,[232] and in the case of the team production model, because the board is the mediating hierarch charged with allocating surplus value created in the face of team members' firm-specific investments.[233] But the team production model has a difficult time explaining derivative lawsuits—the issue isn't so much why derivative lawsuits exist but

nineteenth and early twentieth centuries, many of whom were recent immigrants from Great Britain, were particularly preoccupied with creating the type of intergenerational wealth characteristic of their native countries, and so chose the proper entity form for achieving that goal. It's possible that those decisions, combined with a certain path dependency, resulted in the dominance of the corporate form, at least until the invention of the LLC in the late 1970s.

228 *See supra* notes 156–60160 and accompanying text.

229 *See supra* notes 161–67 and accompanying text.

230 *See supra* tbl.3.

231 *See supra* notes 124–28 and accompanying text.

232 *See supra* notes 80–85 and accompanying text.

233 *See id.*

why exactly it is shareholders who are entitled to bring them.[234] And both models have a difficult time explaining why shareholders have voting rights at all and why those voting rights look the way they do.[235]

The perpetual entity model does a better job on all fronts. Like the director primacy and team production models, and in contrast to the principal-agent and property models, the perpetual entity model explains why decision-making authority is located with the board: its job is to maximize the value of the hypothetical permanent shareholder, and there is no stakeholder, including the current shareholders, who has such an extreme long-term outlook. Like the director primacy model, but unlike the team production model, the perpetual entity model also can explain derivative lawsuits: fiduciary duties don't run to individual shareholders, but if there's reason to believe that the board can't make an objective litigation decision, someone else must take up the case, and the interests of the current shareholders are probably more closely related to that of the hypothetical permanent shareholder than any other stakeholder. But any recovery should go to the corporation for redeployment according to the extreme long-term outlook.

Furthermore, unlike both the director primacy and team production models, only the perpetual entity model can explain why shareholders have the limited voting rights they do. The board's task to engage in extremely long-term investing is notoriously difficult, and they need all the help they can get. Although the current shareholders might not be extremely long-term-focused, their opinions on a given transaction aren't entirely irrelevant to the task of maximizing the value of the permanent equity capital (or the hypothetical permanent shareholder), and there might be situations where the board could benefit from those opinions.[236] However, in the end, by virtue of their duties owed to the permanent equity capital, it is the board and the board alone who is

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[234] *See supra* notes 104–06 and accompanying text.

[235] *See supra* notes 107–09, 143–52 and accompanying text.

[236] Note that I don't read Bainbridge's director primacy model as allowing for such an explanation since his reason for placing the board at the center of the corporation's decision-making structure is that shareholders can't be relied on to make corporate decisions (due to a combination of informational asymmetries, divergent interests, and rational apathy). By contrast, the neoclassical view of corporate fiduciary duties, and the accompanying perpetual entity model, adopts a much more positive view of shareholder decision-making. It just thinks that shareholders are not generally aligned with an extremely long-term outlook.

capable of making these long-term decisions. Consequently, the board should be able to seek the current shareholders' opinion when they want to or not. Under the perpetual entity model, therefore, the board's ability to avoid triggering shareholder voting rights on fundamental transactions is a feature, not a bug. These voting rights are essentially an optional information-producing mechanism as far as the board is concerned.

Of course, there will be situations, perhaps often, where the board will decide on a particular deal structure not because it's interested in taking a straw poll of shareholders but for other reasons, including tax and regulatory reasons.[237] Even in those cases, the neoclassical view, and the accompanying perpetual entity model, can explain why voting rights look the way they do. Generally, voting rights apply where the transaction at issue will materially alter the long-term decision-making structure of the business. So, the shareholders of a company that is being merged out of existence, or whose assets are all being acquired, have a vote because those businesses will, post-transaction, be governed by a different group of people subject to different rules and conditions.[238]

This is the same reason, incidentally, why shareholders also vote on director elections. Someone has to elect the directors, and the shareholders are certainly more likely to get that decision right, being current beneficiaries of the value of the permanent equity, than other stakeholders whose relationship with the permanent equity is more attenuated. Under the perpetual entity model, if that decision-making structure is going to be changed for whatever reasons—whether through an annual election or a fundamental transaction—there needs to be a vote. Thus, the perpetual entity model establishes a continuity between the reason for voting rights on director elections and fundamental transactions.

This analysis is summarized in Table 4:

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[237] *See* 1 MARTIN D. GINSBURG, JACK S. LEVIN & DONALD E. ROCAP, MERGERS, ACQUISITIONS, AND BUYOUTS: A TRANSACTIONAL ANALYSIS OF THE GOVERNING TAX, LEGAL, AND ACCOUNTING CONSIDERATIONS ¶ 104 (2023).

[238] This constitutes an additional, or possibly an alternative, justification for voting rights for significant transactions compared to the traditional one, which is focused on the "final period problem," which is to say the idea that the built-in, disciplining threat of retaliation against cheaters in a repeated transaction disappears in a situation where the transaction is the final one in a series, thereby increasing the risk that cheating will occur.

TABLE 4

<table>
<tr><th>End</th><th>Fit with language of classical formulation and case law</th><th>Model</th><th>Fit with actual allocation of decision rights</th></tr>
<tr><td>1. Stakeholder value maximization norm</td><td>Mixed</td><td>1. Team Production Model</td><td>Mixed</td></tr>
<tr><td rowspan="3">2. Shareholder value maximization norm</td><td rowspan="3">Poor</td><td>2(a). Principal-Agent Model</td><td>Poor</td></tr>
<tr><td>2(b). Property Rights Model</td><td>Poor</td></tr>
<tr><td>2(c) Director Primacy Model</td><td>Mixed</td></tr>
<tr><td>3. Permanent equity value maximization norm</td><td>Good</td><td>3. Perpetual Entity Model</td><td>Good</td></tr>
</table>

III. IMPLICATIONS, OBJECTIONS, AND SPECULATIONS

The analysis in Part II gives rise to implications, objections, and speculations, all of which are discussed below:

A. Implications

1. Information-producing nature of shareholder franchise.

Most scholars assume that, as in the political context, the shareholder voting mechanism is a tool for group decision-making.[239] This assumption is entirely reasonable if one adopts a principal-agent, or property rights, view of the corporation, both of

[239] *See, e.g.*, Marcel Kahan & Edward Rock, *The Hanging Chads of Corporate Voting*, 96 GEO. L.J. 1227, 1230 (2008) (analogizing corporate voting to U.S. political elections); Frank H. Easterbrook & Daniel R. Fischel, *Voting in Corporate Law*, 26 J.L. & ECON. 395, 401–02 (1983) (explaining that the purpose of corporate voting is to allow shareholders to make decisions that fill in the gaps that inevitably arise from the corporation's nexus of contracts). To be clear, shareholder voting does function as a decision-making mechanism with respect to director elections but, I would argue, not with respect to fundamental transactions.

which put the shareholder in the driver's seat either as the principal or owner of the corporation's assets.

Under the neoclassical view of corporate fiduciary duties, however, the shareholder franchise has a different purpose. It doesn't exist as a decision-making mechanism. Because the neoclassical view takes a longer-term outlook on capital allocation than the current shareholders or even the market, under the neoclassical view, the current shareholders shouldn't be deciding how the long-term equity capital gets invested. At the same time, the extremely long-term orientation of fiduciary duties under the neoclassical view creates an enormously challenging task for the board. And the current shareholders' opinion is certainly not irrelevant, and might be an important input, for carrying out that task. For these reasons, under the neoclassical view, the shareholder franchise serves as a mechanism for generating information for the benefit of the board and at its election.

If the board of, say, a peanut butter company is contemplating purchasing the assets of a jelly company, and the current peanut butter shareholders are opposed because of a shortsighted obsession with an anti-jelly fad diet, then the peanut butter board can structure the deal as an asset purchase and bypass the shareholders altogether. If, by contrast, the current shareholders don't suffer from any obvious fleeting pathology (other than simply being more shortsighted in general than the board), and the board has some genuine reservations about the investment, the board can structure the deal as a merger and go through the shareholder voting process to solicit the shareholders' opinion on the matter.

In other words, the neoclassical view of corporate fiduciary duties can explain both why the shareholder franchise exists (to solicit the shareholders' opinion on important matters) and why it is so easy for the board to avoid triggering voting rights (because corporate fiduciary duties require a longer-term outlook than that held by current shareholders). It's true that alternative theories of the corporation—for example, the director primacy or team production model—might similarly view the shareholders as something other than decision-makers in the corporation. But neither of these theories produces a compelling account of the purpose of the shareholder franchise. The director primacy model purports to explain why boards can avoid triggering voting rights so easily (because under that theory, default rules are preeminent), but it can't really explain why the franchise exists in the first place. If the calculus of the allocation of decision rights favors a centralized decision-maker in the form of the board, why take the pains of creating a system that seems to depart from that? Similarly mysterious is the treatment of the shareholder franchise under the team production model—if the board is the mediating hierarch tasked with mediating among the conflicting claims, then why give the shareholders decision rights? The neoclassical view of corporate fiduciary duties provides answers to these questions.

2. The anticontractarian nature of corporate law.

An equally important implication that arises from the neoclassical view of corporate fiduciary duty law is that the corporation itself is not fundamentally a creature of contract, and corporate law is not necessarily contractarian.[240] If, as the neoclassical view counsels, the corporation is an entity designed to foster extremely long-term capital allocation, longer term than the market or any current shareholder, then it's probably not contractarian.

This conclusion follows from the insight that a permanent equity value maximization norm—which, as I've argued, is the best way of understanding the ends of corporate fiduciary duty law—is unlikely to result from a hypothetical contractual bargain between the board and a group of shareholders, none of which will actually hold their equity in perpetuity. To be sure, just because no actual holders of equity in perpetuity are present at the bargaining table doesn't mean that those long-term interests aren't represented in the negotiation. But exactly who represents them? It is only reasonable to assume that the interests of the theoretically permanent equity holder will not always align perfectly with

[240] *See* Grant M. Hayden & Matthew T. Bodie, *The Uncorporation and the Unraveling of "Nexus of Contracts" Theory*, 109 MICH. L. REV. 1127, 1129 (2011) ("The nexus of contracts theory, generally attributed to Jensen and Meckling's *Theory of the Firm*, holds that the firm—and by extension the corporation—is merely a central hub for a series of contractual relationships."); Michael Klausner, *The Contractarian Theory of Corporate Law: A Generation Later*, 31 J. CORP. L. 779, 780 n.4 (2006) (describing Judge Frank Easterbrook and Professor Daniel Fischel as "the primary expositors of the contractarian theory"). Over the years, the theory has attracted a number of adherents. *See, e.g.*, Lewis A. Kornhauser, *The Nexus of Contracts Approach to Corporations: A Comment on Easterbrook and Fischel*, 89 COLUM. L. REV. 1449, 1449 (1989) ("Critics and advocates agree that a revolution, under the banner 'nexus of contracts,' has in the last decade swept the legal theory of the corporation."); Ulen, *supra* note 20, at 303 ("[T]he nexus-of-contracts view of the modern corporation and the principal-agent explanation of some important aspects of the firm . . . have had profound implications for some of the most important issues of corporation law.").

those of the actual current shareholder. And although board members might prefer, all else equal, an arrangement that gives them more decision-making authority, like the neoclassical view of fiduciary duties clearly does, there are ways of achieving such ends that do not require the board to agree to the Herculean task implicit in the extreme long-term outlook demanded by the neoclassical view.[241] For example, how about fiduciary duties requiring the maximizing of "current shareholder profits"[242] combined with a robust business judgment rule? That is, after all, how corporate contractarians typically interpret corporate fiduciary duties and thus think of the result of the hypothetical contractual bargain.[243] I agree with them on this likely result, if one assumes that the board's objective function is to maximize profits according to the market's investing horizon. That would presumably align with the interests of current shareholders, since as a group they, after all, adopt the market's investing horizon.

[241] I suppose one might respond by arguing that a board doesn't actually give up any discretion in agreeing to take an extreme long-term outlook with respect to shareholder value maximization if there is at the same time a robust version of the business judgment rule in place. But I'm assuming throughout this discussion that even a law that lacks the threat of sanctions has some effect on director behavior. And thus, even if a robust version of the business judgment rule prevents courts from second-guessing, let alone sanctioning, a board for failing to maximize its objective function (whether short-term profits, long-term equity value, and so on), the law is nevertheless internalized in some sense by the directors and acts as a constraint on behavior. I don't think this is an unusual assumption to make in corporate law, because without it, it is difficult to explain the business judgment rule. And even though it's an assumption that's not always made explicitly by corporate law scholars, something like it has been elaborated on before. *See generally* Edward B. Rock, *Saints and Sinners: How Does Delaware Corporate Law Work?*, 44 UCLA L. REV. 1009 (1997).

[242] When I say "current shareholder profits" here, this could include what most people think of as long-term profits, meaning the five- to ten-year time horizon of the market. I mean simply to distinguish this from the extreme long-term outlook that I think corporate fiduciary duties require, looking beyond the typical market time horizon.

[243] This is certainly the case for shareholder primacy advocates like Professor Lucian Bebchuk, who favor empowering shareholders without making a distinction between short- and long-term investing horizons. *See, e.g.*, Bebchuk, *supra* note 123, at 865. It is perhaps less clear what director primacy champions like Bainbridge think, however, the fact that he takes a contractarian view of the corporations suggests that he sees no difference between long-term and short-term shareholder interests. This view is also implicit in his position that directors have discretion in determining the time horizon across which they are maximizing shareholder profit. *See, e.g.*, Stephen M. Bainbridge, *Long-Term Bias and Director Primacy*, 2020 COLUM. BUS. L. REV. 801, 820 [hereinafter Bainbridge, *Long-Term Bias*] (citing approvingly a Delaware opinion that he characterizes as "acknowledg[ing] that management need not always focus on long-term projects"). I read the opinion that Bainbridge cites differently as not disavowing the board's obligation to think long-term but rather recognizing the possibility that seeming short-term actions, like declaring a dividend, might actually be the best course of action for the long term.

But that's not the result that we observe. Indeed, that's the central argument of this Article: that corporate fiduciary duties, properly understood, require the board to adopt an extreme long-term outlook that is sometimes longer than the market's investing horizon. And that is not the result that the contractarians predict for corporate fiduciary duties. But if that's so, then there must be some other explanation for the observed results, namely that they're not the product of a hypothetical bargain. They're simply not contractarian.

One might object to this line of argument by pointing out that much of corporate law consists of default rules, which seems contractarian. However, there's nothing inconsistent with a noncontractarian view of corporate law and the existence of contract-like default rules. In fact, we might expect to see default rules, despite the neoclassical view and the accompanying noncontractarian corporation, for at least two reasons. First, there might be rules that appear as default rules but are more accurately characterized as rules that give the board optionality. Shareholder voting rights are like this, at least as they pertain to fundamental transactions. Because these rights are so easily avoidable, some contractarians have characterized them as default rules,[244] but they're really not, because they're not structured to give both the board and the shareholders the ability to decide whether they apply. Rather, the decision whether to trigger shareholder voting rights is a decision that lies with the board and the board alone.

Second, there might be true default rules on issues where shareholder myopia on the question of capital allocation is not likely to pose a problem, for example, whether to allow for written consent[245] or a staggered board.[246] What this suggests is that contractarianism's normative project to make corporate law default rules across the board is misguided as it risks undermining the very purpose of the corporation.[247] So, for example, under the neoclassical view, it would be a very bad idea to allow shareholders

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[244] *See, e.g.*, Butler & Ribstein, *supra* note 145, at 10.

[245] DEL. CODE ANN. tit. 8 § 211(b) (2022).

[246] *Id.* § 141(d).

[247] *See* JONATHAN R. MACEY, CORPORATE GOVERNANCE: PROMISES KEPT, PROMISES BROKEN 22 (2008) ("[Under the nexus-of-contracts theory], business law, including corporate law, exists to economize on transaction costs by supplying sensible 'off-the-rack' rules that participants in a business can use to economize on the costs of contracting."); Stephen M. Bainbridge, *Community and Statism: A Conservative Contractarian Critique of Progressive Corporate Law Scholarship*, 82 CORNELL L. REV. 856, 860 (1997) (book review):

to contract around fiduciary duties,[248] as is the case in the LLC context.[249]

Undoubtedly, the conclusion that the corporation itself is not a creature of contract, more than any other feature of the neoclassical view, will get the most pushback from corporate scholars.[250] But not all. For example, Professor Robert Clark famously argued in favor of a regulatory model of corporate law, and the neoclassical view might be understood as a rearticulation of that model but grounded in the structure of fiduciary duties.[251] That of course won't satisfy the contractarians who rejected Clark's model. But even some contractarians have admitted cracks in their view of the corporation. This was true of the late Professor Larry Ribstein.[252] And even Stephen Bainbridge has suggested that his view of the corporation as a nexus of contracts is more "a metaphor rather than [ ] a positive account of economic reality."[253]

Nor is one likely to find significant opposition from the Delaware courts. As Vice Chancellor Travis Laster has said,

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> The nexus of contracts model has important implications for a range of corporate law topics, the most obvious of which is the debate over the proper role of mandatory legal rules. Contractarians contend that corporate law is generally comprised of default rules, from which shareholders are free to depart, rather than mandatory rules. As a normative matter, contractarians argue that this is just as it should be.

See Lucian Arye Bebchuk, *Foreword: The Debate on Contractual Freedom in Corporate Law*, 89 COLUM. L. REV. 1395, 1397 (1989) ("[Corporate law contractarians argue] that the contractual view of the corporation implies that the parties involved should be totally free to shape their contractual arrangements.").

248 *See, e.g.*, Macey, *supra* note 47, at 185 ("The goal of profit maximization for shareholders is the law, but it is only a default rule. If the shareholders and the other constituents of the corporate enterprise could agree on some other goal for the corporation, then the law clearly should not interfere."); Butler & Ribstein, *supra* note 145, at 28 ("An important aspect of the contract theory of the corporation, and one that is hotly disputed by the anti-contractarians, is that fiduciary duties are a term of the corporate contract and therefore consensual in nature.").

249 *See* Peter Molk, *How Do LLC Owners Contract Around Default Statutory Protections?*, 42 J. CORP. L. 503, 508–13 (2017).

250 Although, this statement is not true of everyone. *See, e.g.*, Rock & Wachter, *supra* note 46, at 1628–30 (discussing the limits of the view that the corporation is a "nexus of contracts").

251 *See, e.g.*, Ronald J. Gilson & Reinier Kraakman, *Clark's Treatise on Corporate Law: Filling Manning's Empty Towers*, 31 J. CORP. L. 599, 607 (2006).

252 LARRY E. RIBSTEIN, THE RISE OF THE UNCORPORATION 68–69 (2010).

253 Stephen M. Bainbridge, *Contractarianism in the Business Associations Classroom:* Kovacik v. Reed *and the Allocation of Capital Losses in Service Partnerships*, 34 GA. L. REV. 631, 644 (2000).

> notwithstanding scholarly approaches such as the widely embraced view of the corporation as a nexus of contracts . . . , the [Delaware General Corporation Law] rests on a concept of the corporation that is grounded in a sovereign exercise of state authority: the chartering of a "body corporate" that comes into existence on the date on which a certificate of incorporation becomes effective.[254]

It is true that Vice Chancellor Laster goes on to add that he finds the nexus-of-contracts theory a "helpful metaphor,"[255] but one might wonder how helpful that metaphor truly is. Under the neoclassical view, it's not particularly helpful, not just because it is inconsistent with how the corporation comes into being but because it obscures the thing that makes the corporation distinct—fiduciary duties oriented toward an outlook for capital allocation that exceeds that of the market or current shareholders. The corporation might be a nexus of contracts, but only once it exists and has purpose and definition, none of which involve contracting.[256] For this reason, the nexus-of-contracts metaphor might be helpful, but not as a way of understanding the nature of the corporation.

But once a corporation exists, then the nexus-of-contracts metaphor works fine. In other words, it bears emphasizing that even though the corporation is not contractarian, this doesn't mean that corporations don't deal in contracts. Indeed, most of what corporations do involves contracting. And those models of the firm that model the corporation as involving contracting still might apply to the corporation under the neoclassical view. The analogy might be made to contract law itself. For example, just because one can't contract around fraud doesn't mean that the agreement is somehow noncontractual.[257] Similarly, just because you can't contract around fiduciary duties, or limited liability, and so on doesn't mean that a corporation is not heavily contractual.

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[254] Juul Labs, Inc. v. Grove, 238 A.3d 904, 913 n.7 (Del. Ch. 2020).

[255] *Id.*

[256] Others have pointed out that the nexus-of-contracts theory really only explains corporations once they come into existence, not before. *See, e.g.*, Hayden & Bodie, *supra* note 240, at 1129 n.8 ("Thus, the nexus of contracts model in a sense assumes the existence of the corporation and then goes on to tackle a problem within the corporate model.").

[257] *See generally* Glenn D. West & W. Benton Lewis, Jr., *Contracting to Avoid Extra-Contractual Liability—Can Your Contractual Deal Ever Really Be the "Entire" Deal?*, 64 BUS. LAW. 999 (2009) (arguing that the traditional rules preventing parties from contractually eliminating fraud liability should be relaxed for sophisticated transaction partners).

But it's a mix of bottom-up contract rules and top-down policy decisions, just like in real contracts.

For this reason, it was wrong for early law and economics scholars to assume that the corporation and corporate law needs to be contractarian in order to follow those economists who wished to go beyond Ronald Coase's view of the firm to model intrafirm activity as largely contractual.[258] It is possible for the corporation itself to be an entity and for that entity to be awash in contracting. This is why I call the model of the corporation underlying the neoclassical view the perpetual *entity* model of the corporation. But this doesn't mean that contractual theories have no explanatory power in describing what corporations do.

3. LLCs are a different beast.

Another implication of the neoclassical view of corporate fiduciary duties is that the LLC is a completely different beast from the corporation. Under the neoclassical view of corporate fiduciary duties, and the accompanying perpetual entity model of the corporation, the corporation's extremely long-term outlook can only exist because the corporation is not contractarian. In other words, if an entity is contractarian, then it can't have this defining feature of the corporation. LLCs are maximally contractarian, because there, even the existence of fiduciary duties are up for negotiation.[259] For this reason, an LLC is a truly different entity. Importantly, this doesn't mean that an LLC's flexibility would allow it to mimic a corporation. Under the neoclassical view, the LLC could never effectively imitate the extremely long-term outlook of a corporation because such an outlook is inconsistent with the contractarian nature of the LLC. For this reason, the neoclassical view of the corporation looks askance at claims that the LLC is superior to the corporation or predictions that it will supplant the corporation.[260] To be sure, it might supplant the corporation, but if so, we would be replacing an entity that is uniquely oriented toward extremely long-term capital allocation with one that is not.

[258] For a useful history of these intellectual developments, see Ulen, *supra* note 20, at 304–21.

[259] *See* Paul M. Altman, Elisa Erlenbach Maas & Michael P. Maxwell, *Eliminating Fiduciary Duty Uncertainty: The Benefits of Effectively Modifying Fiduciary Duties in Delaware LLC Agreements*, AM. BAR ASS'N (Feb. 2013), https://perma.cc/6JEP-BS5T.

[260] *See, e.g.*, RIBSTEIN, *supra* note 252, at 193.

4. Meaning of the business judgment rule.

The neoclassical view of corporate fiduciary duties, and the accompanying perpetual entity model, also has important implications for understanding the business judgment rule. Under the neoclassical view, the business judgment rule operates to preserve the board's unique role as a decision-making body with a mandate for the extreme long term. As already discussed, the board is better equipped than current shareholders to carry out this task because, by definition, the extreme long term in this context exceeds the time horizon of current shareholders as well as the market itself.[261] The board is also better equipped at carrying out this task than courts, assuming of course that it acts in good faith, free of any conflicts that might compromise the all-important long-term capital allocation goal.

This view of the business judgment rule differs from alternative theories not so much in terms of how the rule operates to preserve the board's discretion but rather why it does so.[262] For example, the team production theory views the business judgment rule as necessary in order to preserve the board's ability to act as a mediating hierarch among conflicting stakeholder claims.[263] While this is a coherent defense of the business judgment rule, it has other problems, not least of which is the fact that a stakeholder norm conflicts with prominent case law to the contrary.[264]

Theories that underwrite a shareholder maximization reading of the classical formulation have a more difficult time, I think, offering a coherent explanation of the business judgment rule. This is particularly true of the agency and property rights theories, which view shareholders not only as the primary beneficiaries of the corporation's activities but also the locus of its decision-

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261 *See supra* notes 201–04 and accompanying text.

262 Agency and property theories of the corporation frankly have a difficult time explaining why the business judgment rule exists in the first place and would probably favor a weaker version of the rule than what is currently in place.

263 *See* Blair & Stout, *supra* note 25, at 300 ("The mediating hierarchy model we propose, however, suggests that the business judgment rule may serve an important economic function. In particular, the rule may help prevent coalition members (and especially shareholders) from using lawsuits as strategic devices to extract rents from the coalition.").

264 *See, e.g.*, Shlensky v. Wrigley, 237 N.E.2d 776, 779–80 (Ill. App. Ct. 1968).

making power.[265] Why a rule of deference to the board is necessary in this context typically goes unanswered.[266]

The director primacy theory, by contrast, has a different problem. It favors a strong version of the business judgment rule, consistent with its view that the locus of decision-making power is the board, not the shareholders, even though the shareholders are the primary beneficiaries of the board's decisions.[267] But it's not clear why this is so. Bainbridge has explained that the business judgment rule is necessary to protect the corporation's centralized decision-making mechanism, which he regards as the essential attribute of the corporation.[268] But again, why? It is not for institutional competence reasons—Bainbridge has been clear that courts step in all the time to answer complex, highly specialized questions touching on science, medicine, and the like.[269] It's not clear, in his view, why they couldn't do the same with respect to business questions.[270] No, Bainbridge thinks that the reason is simply centralized decision-making. He takes it as a given that the corporation just simply is, by definition, a thing with centralized decision-making, and to fail to have something like the business judgment rule would undermine this defining attribute.[271] That's certainly true, but it feels like an incomplete explanation. After all, why is centralized decision-making the defining attribute, particularly when it's not entirely clear why the benefits of centralized decision-making outweigh the costs in an entity where there is already in place a method for sharing information

265 *See supra* notes 62–72 and accompanying text.

266 *See, e.g.,* Blair & Stout, *supra* note 25, at 303 ("As these examples illustrate, modern corporate law does not adhere to the norm of shareholder primacy."); Bainbridge, *Director Primacy*, *supra* note 22, at 601 ("Blair and Stout correctly assert that the business judgment rule does not reflect a norm of shareholder primacy, but err in suggesting that the business judgment rule does not reflect a norm of shareholder wealth maximization.").

267 *See* Stephen M. Bainbridge, *The Business Judgment Rule as Abstention Doctrine*, 57 VAND. L. REV. 83, 127–29 (2004) [hereinafter Bainbridge, *The Business Judgment Rule*] (articulating the view that the business judgment rule, properly understood as an abstention doctrine, requires the court to refrain from any sort of review of the reasonableness of the board's judgment, provided that there is no evidence of self-dealing or bad faith).

268 *See* Bainbridge, *Director Primacy*, *supra* note 22, at 602–03.

269 *See* Bainbridge, *Business Judgment Rule*, *supra* note 267, at 119–20; WILLIAM A. KLEIN, J. MARK RAMSEYER & STEPHEN M. BAINBRIDGE, TEACHER'S MANUAL: BUSINESS ASSOCIATIONS 185 (10th ed. 2018).

270 *See* Bainbridge, *Business Judgment Rule*, *supra* note 267, at 119–20.

271 *See* Bainbridge, *Director Primacy*, *supra* note 22, at 602–03.

with and aggregating the preferences of the primary beneficiaries of that decision-making?[272]

The neoclassical view, and the accompanying perpetual entity model, offers in my view a more complete explanation: the business judgment rule is required to preserve the board's autonomy because the board's extremely long-term outlook, something that can be easily misunderstood by markets and current shareholders, is highly unlikely to benefit from heightened judicial review.[273]

5. The neoclassical view and takeover law.

The neoclassical view also sheds light on corporate takeover law. As already discussed, the neoclassical view endorses a robust business judgment rule, which shields board decision-making from judicial scrutiny unless there is evidence of a conflict of interest. Importantly, consistent with the neoclassical view's emphasis on fostering an extreme long-term outlook, not just any conflict will do to dislodge deferential business judgment review. The conflict must be one that plausibly interferes with the board's ability to decide in favor of the permanent equity.

Takeovers present a situation where there exists the nearly constant specter of conflicts that might interfere with the board's extreme long-term outlook. A board might decide to sell not because it is the best long-term strategy for the company but because the chairman wishes to retire.[274] Even if a sale is in the interest of the hypothetical permanent shareholder, a board might choose a less attractive merger partner, and a lower bid, simply because that potential suitor pledges to keep the board in place or

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[272] This is after all basically the argument used by scholars who wish to empower shareholders. *See, e.g.*, Bebchuk, *supra* note 123, at 880–84.

[273] A similar view of the business judgment rule has been expressed by Professors Kelli Alces Williams and Larry Ribstein. *See* Larry E. Ribstein & Kelli A. Alces, *Directors' Duties in Failing Firms*, 1 J. BUS. & TECH. L. 529, 536 (2007). They view the business judgment rule as granting "a lot of discretion to managers" out of the recognition "that courts are not business experts and therefore cannot easily determine whether a bad result was due to mismanagement." *Id.* at 533; *see also* Larry Ribstein, *The* Gheewalla *Case: The Delaware Supreme Court Clarifies Directors' Duties in Bankruptcy*, HARV. L. SCH. F. ON CORP. GOVERNANCE (June 6, 2007), https://perma.cc/3NP5-DDL3. The difference then between their view of the classical formulation and the one expressed herein is that in this Article, the classical formulation really does articulate a purpose for corporate law: supporting the board's task of long-term capital allocation.

[274] *Cf.* Smith v. Van Gorkom, 488 A.2d 858, 866, 874 (Del. 1985) (noting that the chairman who negotiated a sale was approaching mandatory retirement, and later refusing to apply the business judgment rule for several reasons).

provide lucrative consulting fees and other payoffs to key players in the negotiation.[275]

For these reasons, the neoclassical view could certainly accommodate a rule providing that heightened review applies to a sale decision unless there is evidence that the sale is the result of a long-term strategy. This would explain in broad brush strokes the doctrine from *Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc.*,[276] which holds that heightened scrutiny is triggered by certain types of sales decisions.[277] It would also explain exceptions to *Revlon*, like *Paramount Communications, Inc. v. Time, Inc.*,[278] where the court refused to apply *Revlon*'s heightened review to a long-planned merger between Time and Warner that was part of a long-term strategic plan.[279]

True, the neoclassical view might not provide an obvious explanation for cases like *Paramount Communications, Inc. v. QVC Network, Inc.*,[280] where *Revlon* was applied despite a long-term strategy because the planned merger involved a change of control.[281] On the other hand, a change of control, and the accompanying sale of the control premium, is something that should be of concern to the hypothetical permanent shareholder. Accordingly, perhaps the neoclassical view would recognize *Paramount v. QVC* as a legitimate "exception to the exception"—in other words, even where there is evidence of a long-term strategy, like the merger between Paramount and Viacom, heightened scrutiny might be appropriate if it appears that a control premium is being sold out from under long-term shareholders. Additionally, since the concern in all of these takeover cases is with conflicts between the board and the hypothetical permanent equity holder, judicial scrutiny should probably mirror other conflicts cases, where a vote by disinterested shareholders cleanses the conflict.[282] This of

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275 *Cf.* Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc., 506 A.2d 173, 184 (Del. 1986) (applying heightened scrutiny to a transaction where the board favored a "white knight" bidder in the form of billionaire Ted Forstmann, where that favoritism principally benefited the directors at the expense of the shareholders).

276 506 A.2d 173 (Del. 1986).

277 *See* Kling et al., *supra* note 90, § 4.04[3].

278 571 A.2d 1140 (Del. 1989).

279 *See id.* at 1150.

280 637 A.2d 34 (Del. 1994).

281 *See generally id.*

282 The theory for the cleansing of a conflict through a disinterested shareholder vote under the neoclassical view would be based on a second-best approach—ideally, we would require approval from the permanent shareholder, but failing that, approval by the current shareholders would be good enough.

course is the result that Delaware reached in *Corwin v. KKR Financial Holdings LLC*.[283]

However, the one area of Delaware takeover law that is probably not supported by the neoclassical view is the *Unocal* doctrine, originating from *Unocal Corp v. Mesa Petroleum Co.*[284] which applies heightened judicial scrutiny to a board's defense against an unsolicited tender offer.[285] Under the neoclassical view, defending against an actual or potential hostile takeover to preserve a long-term strategy (the *Unocal* scenario)[286] just doesn't present the same concerns as the decision to sell a company as a potential short-term solution to a takeover threat (the *Revlon* scenario).[287] In this sense, the *Unocal* doctrine's gradual evolution to its current form as a type of business judgment review, a phenomenon documented by various commentators,[288] would likely be viewed as a welcome development under the neoclassical view of corporate fiduciary duties.

B. Objections

1. What about agency costs?

One obvious objection to the neoclassical view of corporate fiduciary duties, as well as the accompanying perpetual entity model of the corporation, is that it ignores agency costs. For many, if not most corporate law scholars, minimizing agency costs is the primary purpose of corporate law.[289] Under the neoclassical view, and the perpetual entity theory, the purpose of corporate law is

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[283] 125 A.3d 304, 309 (Del. 2015); *see also Firefighters' Pension Sys. of City of Kan. City, Mo. Tr. v. Presidio, Inc.*, 251 A.3d 212, 254 (Del. Ch. 2021) (referring to "*Corwin* cleansing" as a "path[ ] for lowering the standard of review from enhanced scrutiny to the business judgment rule").

[284] 493 A.2d 946 (Del. 1985).

[285] *See id.* at 955.

[286] *See id.* at 955–56.

[287] *See Revlon*, 506 A.2d at 176–79.

[288] *See, e.g.*, James D. Cox & Randall S. Thomas, *Delaware's Retreat: Exploring Developing Fissures and Tectonic Shifts in Delaware Corporate Law*, 42 DEL. J. CORP. L. 323, 384 (2018) ("The Delaware Supreme Court's movement of *Unocal* in the direction of the traditional deferential business judgment rule."); Stephen M. Bainbridge, *Delaware Merges* Blasius *and* Unocal*: Commentary on* Coster v. UIP Cos., Inc., PROFESSORBAINBRIDGE.COM (July 2, 2023), https://perma.cc/8ZY8-SM93 ("Critics of *Unocal* have long complained that it is an essentially toothless standard.").

[289] *See* Blair & Stout, *supra* note 25, at 248 & n.1 (describing as a "recurring theme" in the literature the idea that "the central economic problem addressed by corporation law is reducing 'agency costs,'" and collecting sources in support of that proposition, despite a literature "too voluminous to cite in its entirety").

something quite different: one might say that it is to create and support a board that is oriented for the extreme long term. But that doesn't mean that the neoclassical view completely ignores agency costs. In particular, the neoclassical view, and the perpetual entity model, welcomes mechanisms to minimize agency costs between management and the board. These include monitoring activities, compensation practices, and various financial and legal controls.

With that said, however, it is certainly true that the neoclassical view, and the perpetual entity model, rejects mechanisms to align directors' and officers' interests with those of current shareholders. Under this model, those simply aren't agency costs because there's no agency relationship between the board and shareholders (or any other stakeholder for that matter).[290] Nor should the law, for instrumentalist reasons, pretend that there is such a relationship because aligning the board's interests with those of current shareholders will only undermine the board's extremely long-term outlook, which after all is at the heart of the neoclassical view of corporate fiduciary duties and at the root of the perpetual entity model of the corporation.

Thus, the fact that the neoclassical view ignores the agency costs between shareholders and the board is a legitimate objection—the neoclassical view does indeed ignore such costs. However, it's not ultimately a compelling one in my opinion. Under the neoclassical view, and the accompanying perpetual entity theory, the corporation is essentially a vehicle for extremely long-term capital allocation, and one consequence of this entity is the (necessary) occasional misalignment of incentives between the board and current shareholders. There are always trade-offs in life, and this particular trade-off highlights the importance of choice among business entities. If one wants an entity that is more short-term focused and aimed at minimizing the distance between the board or management on the one hand and shareholders on the other, the LLC is well designed for that purpose.[291] If one instead wants an entity oriented toward extremely long-term capital allocation, the corporation is the right choice for that purpose.

[290] This has always been the biggest knock against the agency cost view of the corporation—the board simply isn't an agent of the shareholders. *See* Clark, *supra* note 32, at 56–59.

[291] *See supra* Part III.A.3.

2. Equity-based compensation.

Another objection, related to the agency cost one, might be that the neoclassical view doesn't actually matter in reality because compensation practices favor an investment horizon that is much shorter than the hypothetical permanent shareholder's. And there is certainly some truth to such an objection. For example, in one well-known study, researchers found that on average, executive pay vests about 1.2 years after it is granted.[292] This is a short period of time, particularly in light of the same study's average CEO tenure of six years,[293] which itself is short relative to the perspective of the hypothetical permanent shareholder. It seems reasonable then to think that this relatively short compensation duration might matter more than the neoclassical view of corporate fiduciary duties in influencing corporate management's investment horizon. And there is some evidence supporting that conclusion.[294]

But that might be viewed as an objection that has less to do with the neoclassical view and more to do with current executive pay practices. It is perhaps for this reason, among others, that some companies that are famously and quite self-consciously oriented toward the extremely long term take a different approach with respect to executive compensation. The most extreme example is Berkshire Hathaway, where the compensation committee "has established a policy that neither the profitability of [the company] nor the market value of its stock are to be considered in the compensation of any executive officer."[295] Even more unusual, the compensation committee delegates to Warren Buffett, the founder, CEO, chairman of the board, and largest shareholder, to

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292 *See* Radhakrishnan Gopalan, Todd Milbourn, Fenghua Song & Anjan V. Thakor, *Duration of Executive Compensation*, 69 J. FIN. 2777, 2794 (2014). This figure is calculated "as the weighted average duration of the four components of pay (i.e., salary, bonus, restricted stock, and stock options)." *Id.* at 2785. Because pay duration is calculated relative to the year end, salary and bonus are viewed as having a vesting period of zero. *Id.* Thus, to calculate the duration of executive pay, the researchers are effectively discounting the vesting of an executive's restricted stock and option grants by the percentage that noncash compensation represents relative to total compensation.

293 *Id.* at 2781.

294 *See id.* at 2808 ("[F]irms that offer their CEOs longer-duration pay contracts are associated with lower accruals and more specifically, less positive (earnings-enhancing) accruals, which is consistent with the intuition that short-duration pay provides incentives for managers to emphasize short-term earnings.").

295 Berkshire Hathaway Inc., *Schedule 14A: Proxy Statement Pursuant to Section 14(a) of the Securities Exchange Act of 1934*, U.S. SECS. & EXCH. COMM'N (Apr. 30, 2022), https://www.sec.gov/Archives/edgar/data/1067983/000119312522073447/d208624ddef14a.htm.

determine the pay of top executives. At the very least, this allows Berkshire more leeway in focusing on true long-term performance. The company's proxy statement suggests as much. In explaining how the executive pay of those managers below that of the two vice chairmen and chief financial officer is established, the proxy says that "[m]any different incentive arrangements are utilized, with their terms dependent on such elements as the economic potential or capital intensity of the business."[296] Although it takes some reading of the tea leaves, this sounds as if executive compensation depends on how well the company's various businesses are managed for the long term.

Of course, not every company is Berkshire Hathaway, and not every chairman is Warren Buffett. Other long-term-oriented companies adopt equity-based compensation practices but with a much longer vesting period than the average company and without incentivizing management to maximize short-term profit. For example, Amazon explains in its proxy statement that it does not "tie cash or equity compensation to performance goals."[297] As it explains:

> [T]o have a culture that relentlessly pursues invention and is focused on building shareholder value, not just for the current year, but five, ten, or even twenty years from now, we must encourage experimentation and long-term thinking, which, by definition, means we do not know in advance what will work. We do not want employees to focus solely on short-term returns at the expense of long-term growth and innovation.
>
> We recognize that this is a different approach to executive compensation; however, it has worked for us. For example, in 1997, had we adopted performance measures appropriate for a bookseller, we may have inadvertently discouraged our employees from investing their time and energy in initiatives that later became AWS, Kindle, Alexa, and our robust third-party seller business.[298]

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[296] *Id.*

[297] Amazon.com, Inc., *Schedule 14A: Proxy Statement Pursuant to Section 14(a) of the Securities Exchange Act of 1934*, U.S. SECS. & EXCH. COMM'N (May 26, 2021), https://www.sec.gov/Archives/edgar/data/1018724/000110465921050333/tm2035374-1_def14a.htm [hereinafter Amazon Proxy Statement].

[298] *Id.*

In addition to rejecting performance goals, Amazon structures its executive compensation so that a greater proportion than average is noncash with a much greater than average vesting period. Specifically, in 2020, the average pay of Amazon's named executive officers was approximately $29 million, and a full 99.4% of that was noncash.[299] By comparison, on average, the noncash component of executive pay across publicly traded corporations is only 73%.[300] Moreover, the Amazon compensation vests over a period of six to seven years with an average of four years.[301] Because the bulk of Amazon's executive pay is noncash, its "compensation duration"—the average vesting discounted by the percentage of non-cash pay—is 3.6 years. That is three times the compensation duration of the average public company's named executive officers.[302]

In other words, while it is perfectly valid to criticize the relevance of the neoclassical view's extremely long-term outlook by pointing to the relatively short-term focused nature of pay practices, this might simply point toward the need to reform pay practices to bring them more in line with the neoclassical view of corporate fiduciary duties. To be sure, a full-blown analysis of such a reform project is beyond the scope of this Article. But the Berkshire Hathaway and Amazon models at least provide the outlines of two potential ways of going about doing this.[303] The Berkshire approach is to sidestep equity-based compensation altogether and to delegate the executive pay determination to a significant shareholder who is as close to the hypothetical permanent shareholder as possible. This will almost certainly be an option in only very rare cases. The more feasible approach will be that of Amazon: make noncash pay the lion's share of total compensation and then adopt a relatively long vesting schedule.

Another point worth making is to emphasize the difference between the board and management. One obstacle to taking the

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299 This is excluding Jeff Bezos, the former CEO whose policy as founder and largest shareholder of the company, was to accept only a de minimis salary relatively speaking. For example, in 2021, Bezos's total compensation was about $1.7 million. But that represents a salary of $81,840, no stock awards, and $1.6 million in costs of security protection. *See id.*

300 *See* Gopalan et al., *supra* note 292, at 2793.

301 *See* Amazon Proxy Statement, *supra* note 297, at 64–65.

302 The average CEO's compensation duration is 1.44 years. *See* Gopalan et al., *supra* note 292, at 2793.

303 For a thoughtful treatment of the challenges of using executive pay reform to address corporate short-termism, see generally David I. Walker, *The Challenge of Improving the Long-Term Focus of Executive Pay*, 51 B.C. L. REV. 435 (2010).

Amazon approach to compensation is that executives will invariably want more of a guaranteed salary than what that approach can promise. If this is the case, then perhaps the focus should turn to board compensation and the board's role in making long-term capital allocation decisions. Board members aren't typically reliant on their board position for their primary source of income. Additionally, their tenure on the board is typically materially longer than the average tenure of executive management.[304] Thus, perhaps it would make sense to compensate board members with equity-based compensation with very long vesting schedules, and encourage boards to be more involved in capital allocation decisions.

C. Speculations

We've already discussed some of the private and public benefits associated with a business entity oriented toward the extreme long term.[305] Such entities take a different view of risk and discount rates, giving rise to a larger universe of potential investment projects. Indeed, Amazon argues that without its extreme long-term outlook, it might not have ever pursued its third-party seller business or its cloud business, the latter of which, many think, is the most valuable part of the company.[306] And thinking hard about what needs to happen today to influence the world two decades from now holds the promise of significant public benefits as well.

But that doesn't mean there aren't also costs associated with such a long-term focused entity. For example, Professors Eric Talley and Michal Barzuza have argued that corporate management might be biased in favor of the long term in a way that is just as potentially destructive as a short-term bias, subject to the overconfidence bias believe that they are smarter or luckier than others and so the average results simply don't apply to them.[307]

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[304] *See* Matteo Tonello, *Corporate Board Practices in the Russell 3000 and S&P 500*, HARV. L. SCH. F. ON CORP. GOVERNANCE (Oct. 18, 2020), https://perma.cc/C3TT-D3VN (showing that the average tenure for directors of S&P 500 and Russell 3000 companies is about ten years). The average tenure of CEOs is about six years. *See* Gopalan et al., *supra* note 292, at 2781.

[305] *See supra* Part II.B.1.

[306] *See* Subrat Patnaik, *Amazon Cloud Unit on Course for $3 Trillion Value, Redburn Says*, BLOOMBERG (June 29, 2022), https://www.bloomberg.com/news/articles/2022-06-29/amazon-cloud-unit-on-course-for-3-trillion-value-redburn-says?leadSource=uverify%20wall.

[307] *See* Barzuza & Eric Talley, *supra* note 31, at 112.

Consequently, they end up making decisions that prefer long-term projects over a shorter-term alternative offering superior returns.[308]

In addition, Professor Jesse Fried has shown how, even in the absence of an overconfidence bias, a long-term outlook can actually result in certain types of value-destroying behavior.[309] For example, Fried showed how a firm focused on maximizing long-term shareholder value might choose to repurchase shares rather than pursue alternative investments that would actually deliver greater value to all—short-term, long-term, and future—shareholders.[310] He has shown how stock issuances can have a similar effect.[311]

What should we make of these arguments? The corporate form represents a policy decision to encourage long-term thinking despite its potential costs. Is this rational? We can only speculate, but I think so. There is no question that overconfidence can be a problem. But it's also true that what looks like overconfidence in retrospect might simply be a case of misperception.[312] Few investments are sure bets, and so there is always a possibility that the investment will not turn out as expected. Great care needs to be taken in sorting out true cases of overconfidence from those where the long-term investment was justified on an ex ante basis even though it appears in retrospect like a mistake.

Nevertheless, even if the phenomenon of overconfidence bias poses some type of problem, and it surely does, it's not clear that it's the same sort of problem as the short-term analog, which is reinforced by the structural issues favoring relatively short-term investing, as discussed earlier.[313] Furthermore, if we understand short-term in this context to mean anything less than the extreme long-term investment horizon focused on in this Article, the short-term bias is also encouraged by the relatively short-term nature of careers at the heights of corporate management.

As for Fried's arguments, a rational firm should only engage in repurchases if high-return internal investments are not particularly plentiful.[314] This will typically occur once a company has

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308 *See id.* at 140–47.

309 *See* Fried, *supra* note 31, at 1592–98, 1607–15.

310 *See id.* at 1592–98.

311 *See id.* at 1607–15.

312 *See* Bainbridge, *Long-Term Bias*, *supra* note 243, at 812–13.

313 *See supra* notes 208–15 and accompanying text.

314 BERKSHIRE HATHAWAY INC., 2021 ANNUAL REPORT 8–9 (2022) (explaining that repurchases make good sense for investors "as alternative paths become unattractive").

reached a relatively mature stage in its life cycle, after it's gone through a growth phase. Value-destroying repurchases during a firm's twilight years might simply represent the cost of encouraging the type of long-term planning necessary to generate the growth created during its adolescence. Additionally, it's not entirely clear that in a dynamic model, Fried's prediction is correct. After all, once a company carries out a value-destroying repurchase, the market should respond by bidding down the value of the stock, which obviously affects the long-term shareholder. Given this, it might turn out not to be optimal for a long-term shareholder-maximizing board to go through with the value-destroying repurchase. This argument applies with even greater force to value-destroying stock issuances, which of course, unlike repurchases, require substantial disclosure beforehand and therefore will elicit an immediate market response before the issuance is actually carried out.

Finally, as discussed before, the fact there are costs associated with a business entity, like the corporate form, that is oriented toward an extremely long-term investment horizon doesn't necessarily imply the need to alter the corporation to rein in these long-term tendencies. At the most, it implies that we should have choice, which we do in the form of the LLC. For those companies that for whatever reason tend to suffer more from long-term bias, they can choose the LLC form. Similarly, if Fried's point about repurchases and stock issuances are a real problem in practice, or if they are more of a problem with certain businesses than others, then one would expect that companies in those industries will also gravitate toward the LLC.[315]

More generally, the neoclassical view of corporate fiduciary duty law drives home the fact that the corporation is not simply a tool for enabling Coasean bargaining between shareholders and management but rather an institution reflecting an important policy decision on the part of legislators that extremely long-term capital allocation is a worthy economic goal. Although as Talley,

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[315] For example, let's say that a long-term capital allocation outlook is necessary to produce extreme growth during the first part of a particular company's life cycle, and that such growth offsets the risk of value-destroying repurchases that such a long-term outlook might encourage on the back end of the company's life cycle. Then, such a business would find it optimal to operate as a corporation. If, by contrast, you have a business like See's Candies, for example, that, although a great business, never benefited from a significant runway for growth, then an LLC might be the preferred route.

Barzuza, and Fried have shown, that policy decision is not costless,[316] it is nevertheless plausibly cost-justified.[317] In other words, Ribstein was right when he observed that the board of directors plays a "political[ly] legitimizing role" aimed at "help[ing] constrain corporations to act consistently with the objectives of lawmakers rather than solely those of investors."[318] But whereas he meant that as a deficiency in the corporate form, this Article suggests that it is actually a virtue.

CONCLUSION

Corporate fiduciary duties are said to run to the corporate entity. Yet, attempts to boil this classical formulation down to a simple shareholder or stakeholder maximization norm run up against formidable logical roadblocks: On the shareholder maximization side of the debate, why should "the corporate entity" be identified with shareholders? And what about well-established case law saying that fiduciary duties don't in fact run to individual shareholders? As for the stakeholder side of the ledger, what about cases like *Dodge v. Ford*, which, at the very least, seems to endorse a strong focus on maximizing equity value?

In this Article, I have argued that the classical formulation means that corporate fiduciary duties are aimed at maximizing the value of the permanent equity capital, abstracted away from any current shareholders, and therefore requires an extremely long-term outlook that may well exceed that of the market itself. This is what I call the neoclassical view of corporate fiduciary duties. It's a view of fiduciary duties that is underwritten by a model of the corporation that highlights the entity's perpetual existence as the most important attribute of the corporation.

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316 *See* Barzuza & Talley, *supra* note 31, at 136–47.

317 There are those, to be sure, who disagree. *See* Lucian A. Bebchuk, *The Myth That Insulating Boards Serves Long-Term Value*, 113 COLUM. L. REV. 1637, 1676, 1686 (2013). This Article responds to Bebchuk not by taking issue with his cost-benefit analysis nor by arguing that boards must be insulated. In fact, the neoclassical view might welcome board accountability as long as such accountability furthers the board's task of extreme long-term capital allocation. Rather, this Article argues that fiduciary duty law is structured in a way that assumes that board insulation from shareholders is necessary to further the policy goal of long-term wealth maximization. Bebchuk might accept that policy goal while at the same time rejecting the means of achieving it, but we should at least understand the truly revolutionary effect such a rejection would have on the structure of corporate fiduciary duties.

318 RIBSTEIN, *supra* note 252, at 68.

This view of fiduciary duties, and the accompanying model of the corporation, helps distinguish the corporation from alternative entity forms, including the LLC and the business trust. It also implies a more vital function for corporate law than exists under contractarian view of the firm: instead of creating default rules that save on transaction costs, corporate law principally has to do with creating the type of decision-making entity that can engage in the all-important, yet very difficult, task of extremely long-term capital allocation. Ultimately, it is the corporation's perpetual existence, and corporate fiduciary duties' focus on maximizing the equity of that perpetual entity, that is essential for understanding the nature of the corporation and the structure of corporate law.