

***The Modern Corporation and Private Property* and the Evolving Norms of Corporate Governance**

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Abstract

The Financial Crisis Inquiry Commission – which was appointed by the U.S. Government to investigate the recent financial crisis – issued its Report on January 27, 2011. Among the many causes identified by the Commission, one was the failure of corporate governance and risk management at many leading financial institutions. This was the second time in a single decade that corporate governance issues had come to occupy the media limelight. The first time was the in the early years of the twenty-first century when the corporate crises at some high-profile public companies had led to a severe loss of confidence in the securities markets. For these among a host of other reasons, corporate governance has become a burgeoning field of study among scholars of law, economics, finance, management, and other cognate disciplines. The book *The Modern Corporation and Private Property*, by Adolf Berle and Gardiner Means, first published in 1932, continues to be a foundational work for the study of corporate law and governance. One striking feature of the book is the richness of its insights and their significance which still inspire debate and analysis among corporate law scholars almost eight decades after its initial publication. This essay provides a short explanation of the context in which *The Modern Corporation and Private Property* was written along with a brief note of some of the major developments in corporate law and governance. The essay also provides an overview of the prominent themes that continue to be debated and discussed among corporate law and governance scholars. This essay makes the claim that one underappreciated aspect of *The Modern Corporation and Private Property* is its recognition of corporate law as being akin to constitutional law for a new economic age. The evolving norms of corporate governance and their adaptation to the exigencies of the times reveal a pattern that sits well with the thesis of living constitutionalism.

We are well underway toward recognition that property used in production must conform to conceptions of civilization worked out through civilized processes of American constitutional government. Few American enterprises, and no large corporations, can take the view that their plants, tools and organizations are their own, and that they can do what they please with their own. There is increasing recognition of the fact that collective operations, and those predominantly conducted by large corporations, are like operations carried on by the state itself.¹

Adolf Berle and Gardiner Means

The Modern Corporation and Private Property

Preface to the Revised Edition

I. Introduction:

Corporate governance has been a burgeoning field of study in recent years among legal, management, financial, and other academics, and also among those involved in the nuts-and-bolts of dealing with its practical issues as managers, practicing lawyers, accountants, and other cognate professionals.²

A prominent recent instance of the public attention that corporate governance has received is contained in the Report of the Financial Crisis Inquiry Commission which was issued on January 27, 2011³ The Commission was appointed by the United States Government in 2009 to investigate the causes of the financial and economic crisis in the United States that began in December 2007. It was the worst such crisis since the 1930s and has had severe worldwide repercussions. Among the many causes identified by the Commission, one of the important findings was that “dramatic failure of corporate governance and risk management at many systemically important

¹ Adolf A. Berle and Gardiner C. Means, *The Modern Corporation and Private Property*, Preface at xxvi, (Revised edition, Harcourt, Brace & World, Inc. 1968). (First edition, 1932).

² For an overview of current issues relating to corporate governance, see Lucian A. Bebchuk and Michael S. Weisbach, *The State of Corporate Governance Research*, Review of Financial Studies, Vol. 23, No.3, at 939-961.

³ *The Financial Crisis Inquiry Report: Final Report of the National Commission on the Causes of the Financial and Economic Crisis in the United States* (U.S. Government Printing Office). Available at <http://www.gpo.gov/fdsys/pkg/GPO-FCIC/pdf/GPO-FCIC.pdf>.

financial institutions were a key cause of this crisis.”⁴ Earlier, the need for corporate governance reform had already been anticipated by the “say on pay” and “proxy access” provisions of the Dodd-Frank Wall Street Reform and Consumer Protection Act which was signed into law on July 21, 2010, and had been enacted in response to the financial and economic crisis.⁵

This was the second time in a single decade that corporate governance had come to occupy the media limelight. The first time was in the early years of the decade when the egregious corporate scandals at high-profile public companies such as Enron, Tyco, Worldcom, and others led to a collapse in their share prices and to a crisis of confidence in the securities markets. The U.S. Congress had responded to that situation by enacting the Sarbanes-Oxley Act of 2002⁶ which imposed stringent compliance requirements upon U.S. companies. The Act has been criticized by some on the grounds that the complexity of the regulatory mechanism it has put in place and the compliance requirements that it has imposed disadvantage American corporations vis-à-vis foreign competitors. Others have praised the Act for having restored public confidence in the accuracy of the information contained in corporate financial statements and in the securities markets.

In any event, the Sarbanes-Oxley Act continues to provoke comment and discussion, as the financial crisis of 2007 to 2010 and the provisions of the Dodd-Frank Act are likely to do over the coming years. Thereby, corporate governance is almost certainly going to remain a prominent topic of public discourse in the years ahead.

It is no surprise then, that Adolf Berle and Gardiner Means’s co-authored classic, *The Modern Corporation and Private Property*⁷ (hereafter *The Modern Corporation*) has been the subject of so much contemporary legal scholarship. Although first published

⁴ *Id.* at xviii. The dissenting statement of three of the ten members effectively concurs on this point although the words “corporate governance” are not expressly used. See *id.* at 427 to 429.

⁵ See generally: J.W.Verret, *Defending Against Shareholder Proxy Access: Delaware’s Future Reviewing Company Defenses in the Era of Dodd-Frank*, George Mason Law & Economics Research Paper No. 10-37. Available at SSRN:<http://ssrn.com/abstract=1655482>.

⁶ Pub.L. 107-204, 117 Stat. 745, available at <http://www.gpo.gov/fdys/pkg/PLAW-107pub1204/content-detail.html>.

⁷ Adolf A. Berle and Gardiner C. Means, *The Modern Corporation and Private Property*, *supra* note 1.

in 1932, *The Modern Corporation* remains the foundational work for the study of corporate law and governance. The book continues to be analyzed and debated almost eight decades after its initial publication. Cases in point are two recent symposium issues of the *Seattle University Law Review* intended to mark the founding of the “Adolf A. Berle, Jr. Center on Corporation, Law and Society” at that University which showcase some outstanding contemporary legal scholarship on Berle and Means’s classic work.⁸ This is in addition to a wide array of other scholarship on the subject.

This essay has been prompted by a recent re-reading of *Modern Corporation* and some of the erudite scholarship on the book and its purport. One striking feature of the book is the richness of its insights and their continuing relevance. One prominent feature of the scholarship is the wide array of conflicting interpretations that *Modern Corporation* has been subjected to and the diverse theses that the book has been adduced in support of. This essay makes the claim that this multiplicity of theses and interpretations are capable of being reconciled when viewed in the light of Berle and Means’s assertion which runs as a subtext through the entire book—and is set out most succinctly in the final paragraph—that the law of corporations is akin to constitutional law for a new economic age. Proponents of living constitutionalism would have no difficulty in squaring the diversity of scholarly exegeses with Berle and Means’s claim.

After the present introduction, this essay has been organized as follows: Part II delineates the areas that are subsumed under the rubric of corporate governance; Part III explains in a brief outline form the context in which *The Modern Corporation* was written and published; Part IV presents an overview of the contents of the book and its principal theses; Part V describes some of the major developments relating to corporate law and corporate governance; Part VI sets out the principal claim of this essay that the continuously evolving norms of corporate law and governance in the United States are in conformity with the subtext of *The Modern Corporation* which likens the law of corporations to constitutional law for a new age. The essay ends with a brief conclusion.

⁸ See 33 *Seattle University Law Review* (2010), and 34 *Seattle University Law Review* (2011).

II. The Mechanism of Corporate Governance:

Apart from business corporations, the two principal forms of business organization are sole proprietorships and partnerships. The term “corporation” is principally used in the United States, whereas the term “company” is more commonly used in the United Kingdom and the countries in the British Commonwealth.

Corporate governance encompasses the totality of the system designed to shape and control corporations. In various ways, issues relating to corporate governance have been present ever since the inception of the corporate form. As far back as 1776, in his magnum opus *The Wealth of Nations*,⁹ Adam Smith had recognized a problem relating to corporate governance, the solution to which continues to remain elusive. The problem that Adam Smith identified was: When professional managers are entrusted with the task of managing money which is not their own, in the nature of things they would not bring to the task the same level of vigilance and industry that they would if it were their own.

In modern times, corporate governance issues arise mainly in connection with publicly traded corporations.¹⁰ The major concern remains the need to regulate the behavior of managers in ways that would lead them to act in the best interest of the shareholders, or the stakeholders, rather than in their own.

The term “coporate governance” collectively refers to mandatory rules and laws as also developing doctrines and norms designed to control corporations. Following is a brief outline of the various internal and external mechanisms that together form the subject matter of corporate governance.¹¹

A. Shareholders: The shareholders of the corporation are an important part of the corporate governance system to the extent that they can influence the direction of the corporation. In the past, dispersed individual investors formed the bulk of the share

⁹ Adam Smith, *An Inquiry Into the Nature and Causes of the Wealth of Nations* 606-607 (Penn State Press ed. 2005) (1776).

¹⁰ There were about 16,000 publicly traded corporations in the United States in 2002. SEC, Framework for Enhancing the Quality of Financial Information, 67 Fed. Reg.44,999 (July 5, 2002).

¹¹ For a fairly comprehensive recent explanation of the contours of corporate governance, see Arthur R. Pinto, *An Overview of United States Corporate Governance in Publicly Traded Corporations* (October 22, 2009). Brooklyn Law School, Legal Studies Paper no. 172. Available at SSRN: <http://ssrn.com/abstract=1492735>. This section draws upon this overview.

ownership and they could have very little say in the running of the corporation. In recent years, the large numbers of institutional shareholders are in a better position to influence the direction of the corporation. Through their political vote, shareholders can also influence the shaping of corporate laws.

B. Law: The law governing corporations consists of the federal law enacted by the U.S. Congress, the state law enacted by the legislature in each state, and the common law as embodied in the judgments of the state and federal judiciary.

Among federal laws, the Securities Act of 1933 and the Securities and Exchange Act of 1934 which, inter alia, established the Securities and Exchange Commission are the most important. More recently, the Sarbanes-Oxley and Dodd-Frank legislation are also significant.

Delaware state law, because of its business-friendly nature among other reasons, has come to occupy the pre-eminent position among laws governing corporations.

C. Internal corporate structure: The internal corporate structure refers to the rules governing the power arrangements among the principal constituents, that is, the board of directors, the management, and the shareholders. There is always a need for a delicate balance between shareholder rights and the need for management to have the freedom to promote in all legal and legitimate ways the business interest of the corporation. These rules relate to shareholder voting, proxy voting, independent directors, and other cognate issues.

III. The Context of *The Modern Corporation and Private Property*:

To understand the context in which *The Modern Corporation* was first published, it would be useful to briefly review the evolution of the corporate form in the United States.¹²

In pre-Independence America, there were three types of corporations – public, private, and commercial¹³ and their number was insignificant. In the early years of the American Republic, corporations were those that were granted charters by the government, and these were widely understood as being privileges granted at the

¹² For a very good survey of this historical development, see: P.M. Vasudev, *Corporate Law and its Efficiency: A Review of History*, 50 American Journal of Legal History, 237-283 (2010). Available at SSRN: <http://ssrn.com/abstract:1537985>.

¹³ See: Joseph Stancliffe Davis, *Essays on the Earlier History of American Corporations* (Harvard University Press, 1917).

discretion of the legislature. For various cultural and historical reasons, there was a widespread wariness of this aspect of corporations. A total number of 335 corporations were chartered in the United States in the two decades from 1781 to 1800.¹⁴ There was, during this period, a deep understanding of the positives and the negatives of the corporate form.¹⁵

A truly revolutionary change was initiated during Andrew Jackson's presidency from 1829 to 1837.¹⁶ To counter the hostility toward discretion and privilege, calls for reform led to a democratization of the corporate form in the shape of enactment of laws granting a general right of incorporation to anyone who wished to do so. Beginning with New York in 1846 laws relating to general incorporation had been enacted in 36 states by 1902.¹⁷ The right to incorporate now became a general right available to anyone subject to compliance with certain minimum mandatory rules expressly provided in the statute. The enactment of general incorporation laws did not by itself end the system of granting corporate privileges under charters. The two systems remained simultaneously in effect.

The economic expansion during the Industrial Revolution of the 19th century, the surge in business activity, and the rise of dynamic business leaders such as John Rockefeller and others led to changes in corporate law after 1880. Corporate law was seen as a hindrance rather than as a facilitator of economic growth. This led to the formation of the legal device known as "trusts." A trust was a legal stratagem intended to circumvent state laws prohibiting a corporation from holding extra-territorial property, or stock of another company. These trusts were viewed with concern because of the market power that they exercised.¹⁸ New Jersey was the first state to enact a statute that permitted one corporation to hold shares in another corporation. It had already been held by the U.S. Supreme Court that a corporation chartered in one state could do business in any other state.¹⁹ Thus, this law greatly facilitated business expansion and economic growth. It also served as an incentive for

¹⁴ *Id.*, at 26.

¹⁵ See Stuart Banner, *Anglo-American Securities Regulation: Political and Cultural Roots, 1690-1860*, at 210 (Cambridge University Press, 1998).

¹⁶ P.M. Vasudev, *supra note* 12, at 19 (SSRN).

¹⁷ *Id.* at 20.

¹⁸ See generally: Maury Klein, *The Genesis of Industrial America, 1870-1920* (Cambridge University Press, 2007).

¹⁹ *Bank of August v. Earle*, 38 U.S. (13 Pet.) 519.

corporations to make New Jersey the preferred state of incorporation, leading in turn to a competition among states to provide corporations with an environment congenial for conducting business. One such state was Delaware which enacted general incorporation laws in 1899.

At the start of the twentieth century, mergers of small-scale manufacturing firms led to the creation of huge enterprises that gained a pre-eminent market position and retained it for decades.²⁰ Along with the growth of the giant corporations, came a steep rise in the number of individual stockholders in publicly traded corporations with a particularly dramatic rise taking place in the 1920s.²¹ The end of the twenties decade saw the arrival of the Great Depression, amidst which *The Modern Corporation* was first published.

IV. *The Modern Corporation* and Its Themes:

Berle and Means began to work on *The Modern Corporation and Private Property*, in 1927. At that time, Adolf Berle was a professor of corporate law at Columbia Law School, while Gardiner C. Means was a graduate student of economics at Columbia University. He had earlier been a graduate student at Harvard University. Reflecting the specialized fields of study of its authors, the book examines the evolution of big business from legal and economic perspectives. *The Modern Corporation* was first published in 1932. The book is best known for two themes. The first is the separation of ownership and control in the modern corporation. The second is a somewhat ambiguous stance on whether a corporation should be run principally in the interest of its shareholders or its stakeholders.

The Modern Corporation traces the evolution of corporations and notes the extent to which a small number of huge corporations had come to accumulate an enormous concentration of economic power. Due to the extent of their size, stock ownership had become increasingly dispersed. This dispersal had led to an inability on the part of the shareholders to effectively engage in directing the affairs of the corporation. As Berle and Means noted:

²⁰ Naomi Lamoreaux, *The Great Merger Movement in American Business, 1895-1904* (Cambridge University Press, 1985).

²¹ See generally: Lawrence E. Mitchell, *The Speculation Economy: How Finance Triumphed over Industry* (Berrett-Koehler Publishers, Inc., 2007).

In place of actual physical properties over which the owner could exercise direction and for which he was responsible, the owner now holds a piece of paper representing a set of rights and expectations with respect to an enterprise. But over the enterprise and over the physical property – the instruments of production – in which he has an interest, the owner has little control.²²

As the actual owner of the property ceded control over it, the control vested in the board of directors or of management. Shareholders increasingly came to think of their stock as investments which bore dividend payouts and had a market value. This led to further management autonomy and increasing unaccountability, which in turn raised serious social and economic issues.

According to the conventional logic of the profit motive, economic profit should go to the person who is in actual control so as to motivate him to work more efficiently and more effectively. On the other hand, traditional notions of property dictated that economic profit should go to the shareholders in their capacity as the rightful owners. However, in light of the separation of ownership and control, the prevailing ideas of profits and property no longer applied. The new situation had catapulted the interest of society at large over that of either management or the shareholders.

Following is an exploration of the principal themes of The Modern Corporation.

A. The Separation of Ownership and Control:

It is generally believed that Berle and Means were the first scholars to identify the issue of the separation of ownership and control in the modern corporation. In an illuminating article, Harwell Wells has pointed out that there were other illustrious scholars who paved the way for Berle and Means although they had interpreted the situation differently.²³ In Wells's telling, the great achievement of Berle and Means was in highlighting the issue within the framework of the growth in the American economy and in explaining what the consequences of the separation entailed for society at large.

Some prominent intellectual forebears of Berle and Means were Louis Brandeis,

²² Berle and Means, *supra note 1*, at 64.

²³ Harwell Wells, *The Birth of Corporate Governance*, 33 *Seattle University Law Review* 1247 (2010). This section draws upon the article by Harwell Wells.

who later became a Justice of the U.S. Supreme Court, influential journalist Walter Lippmann, economist Thorstein Veblen, and William Z. Ripley.

Brandeis expressed his concern in 1914.²⁴ In his view, the dispersion of share ownership and the resulting inability of shareholders to partake in the management of the corporation led to their dependence on bankers to evaluate the worth of their securities resulting in a shift of power into the hands of bankers.

Walter Lippmann recognized the separation of ownership and control in 1913 in his book *Drift and Mastery*.²⁵ However, he did not consider it a problem for society but as something beneficial. In his view, since the salaried manager would have no selfish interest at stake in the profit of the corporation, he would be more inclined to think of the effect of his decisions on society at large.

Thorstein Veblen first observed the separation of ownership and control in his 1904 book, *Theory of the Business Enterprise*.²⁶ However, he noted its consequences in the light of his understanding of corporate finance of that period. He saw it as a problem between managers who owned preferred stock and had a prior claim on the corporeal assets of the firm, as opposed to the ordinary shareholders.

Another major book which highlighted the separation of ownership and control was *Main Street and Wall Street* by William Z. Ripley.²⁷ Adolf Berle noted Ripley's contribution in the introduction to *The Modern Corporation*.²⁸ Ripley had observed that "[t]he prime fact confronting us as a nation is the progressive diffusion of ownership on the one hand and the ever-increasing concentration of managerial power on the other."²⁹

However, it was the publication of *The Modern Corporation* in 1932 which truly catapulted the issue of the separation of ownership and control into public consciousness. The book's strengths flowed from its use of copious empirical and statistical data and elaborate factual and conceptual arguments. One particularly striking new move was the mooted of "control" as a concept apart from ownership

²⁴ Louis Brandeis, *Other People's Money and How the Bankers Use It* (F. A. Stokes, 1914).

²⁵ Walter Lippmann, *Drift and Mastery* (Prentice-Hall 1961) (1914).

²⁶ Thorstein Veblen, *The Theory of Business Enterprise* (The New American Library 1904).

²⁷ William Z. Ripley, *Main Street and Wall Street* (Little, Brown, and Company, 1927).

²⁸ Berle and Means, *supra* note 1, at xlii.

²⁹ Ripley, *supra* note 27, at 131.

and management. This “control,” according to Berle and Means vested with those who were in a position to appoint the board of directors, and thereby influence the direction of the corporation.

The concern about the separation of ownership and control was the “agency cost” that would potentially follow in its wake.

B. For Whose Benefit Is the Corporation To Be Run?

Flowing from the primary theme about the separation of ownership and control there emerged a consequential theme: For whose benefit is the corporation to be run?

This theme had already been anticipated in a debate between Adolf Berle and Merrick Dodd of Harvard Law School in the pages of the Harvard Law Review.³⁰ Adolf Berle took up the position that “all powers granted to a corporation or to the management of a corporation, or to any group within the corporation...[are] at all times exercisable only for the ratable benefit of all the shareholders as their interest appears.”³¹ Merrick Dodd, on the other hand, took the position that the purpose of a business corporation was not merely to make a profit for the shareholders but also to serve the interests of society. Berle and Dodd are widely believed to be the respective forerunners of what have come to be called “shareholder primacy” and “corporate social responsibility.” However, as William Bratton and Michael Wachter have pointed out, this is an oversimplified characterization of their positions.³² Both Berle and Dodd had more nuanced views about the purpose of a corporation and both refined their positions over the years as the context changed.

It is equally unclear what position Berle and Means advocated in *The Modern Corporation*. Once again, as William Bratton and Michael Wachter have pointed out, Books II and III of *Modern Corporation* take the stand that managers must function as trustees of shareholders whereas Books I and IV urge that the managers attend to

³⁰ Adolf A. Berle, *Corporate Powers as Powers in Trust*, 44 Harvard Law Review 1049 (1931), E. Merrick Dodd, *For Whom Are Corporate Managers Trustees?* 45 Harvard Law Review 1145 (1932).

³¹ Adolf Berle, *id.*, at 1049.

³² William W. Bratton and Michael L. Wachter, *Shareholder Primacy's Corporatist Origins: Adolf Berle and "The Modern Corporation,"* 34 Journal of Corporation Law 99 (2008).

the larger question of the welfare of society.³³ Bratton and Wachter have argued that the book was written over a long period of gestation, and those years were politically, economically, and socially tumultuous years. Berle's views were context-specific and were modified with the changing times.

In any event, it was another signal achievement of *The Modern Corporation* that questions relating to the true purpose of the corporation were propelled to the forefront of public discourse. Debate on this question remains unabated. Berle himself had refined his position in later years, and leaned toward a manager-oriented model that supported giving wide discretion to managers in the running of the corporation in the belief that professional managers would act as fiduciaries for the social good.

Corporate social responsibility is also the subject of a recurring debate that has persisted since the publication of *The Modern Corporation*. The case for greater corporate social responsibility waxes and wanes in lockstep with the changing economic, political, and social context.³⁴

In recent years, due to the corporate failures of the first decade of the twenty-first century, special emphasis has been placed upon director independence under the provisions of the Sarbanes-Oxley Act of 2002, and the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010. The underlying theory is that more rigorous oversight by the Board of Directors will deter management from using corporate resources for self-aggrandizement.

Despite a host of post-publication developments, such as a questioning of the premises of *The Modern Corporation* by those who argue for a conception of a corporation as a "nexus-of-contracts,"³⁵ Berle and Means's principal thesis continues to hold sway in scholarly debate. The book has been subjected to a host of conflicting interpretations that have varied with the ebb and flow of political, social, and economic events in the United States.

³³ William W. Bratton and Michael L. Wachter, *Tracking Berle's Footsteps: The Trail of the Modern Corporation's Last Chapter*, 33 *Seattle University Law Review* 849 (2010).

³⁴ For a comprehensive chronicle of the corporate social responsibility debate, see Harwell Wells, *The Cycles of Corporate Social Responsibility: An Historical Retrospective for the Twenty-First Century*, 51 *University of Kansas Law Review* 77 (2002).

³⁵ See Michael C. Jensen and William H. Meckling, *Theory of the Firm: Managerial Behavior, Agency Costs and Ownership Structure*, in Michael C. Jensen, *A Theory of the Firm: Governance, Residual Claims and Organizational Forms* (Harvard University Press, 2000).

V. Major Steps In the Development of Corporate Law:

Corporations have played an important role in the economic development of the United States, and in the shaping of cultural attitudes of its people. This is reflected in the development of the law relating to corporations in the United States.

The Supreme Court of the United States and other federal and state courts have played a role in the development of laws relating to corporations. Herewith is a brief recapitulation of a few of the major landmark decisions of the U.S. Supreme Court that have had major ramifications for the development of corporate law.³⁶ This account covers only a few of the high points and is not comprehensive.

The first major case was that of *McCulloch v. Maryland*,³⁷ which was decided by the United States Supreme Court in 1819. This case related, in part, to the power of the United States Congress to charter a bank although no such power was expressly granted in the U.S. Constitution. The Court held that Congress did have such a power and it flowed from the Necessary and Proper Clause in furtherance of effectuating the express powers granted to Congress under the taxing and spending clause. The power of Congress to enact laws relating to economic, monetary, and financial matters was thereby established.

In the same year, the U.S. Supreme Court ruled in the case of *Trustees of Dartmouth College v. Woodward*³⁸ that the corporate charter granted in 1769 by King George III to the trustees of Dartmouth College under which the College had been founded was tantamount to a contract and the act of the state legislature seeking to impair its provisions violated the Contract Clause set out in Article 1, section 10, Clause 1 of the

³⁶ See generally: Lydie Nadia Cabrera Pierre-Louis, *Corporate Law: A Historical Perspective of the Supreme Court's Corporate Law Decisions from the Nineteenth Century to the Present*, in *Encyclopedia of the Supreme Court of the United States*, Volume 1, at 443 to 451 (David S. Tanenhaus, Editor, Macmillan Reference USA, 2008).

³⁷ *McCulloch v. Maryland*, 17 U.S. 316 (1819). Writing the opinion of the Court, Chief Justice Marshall memorably wrote: "We must never forget that it is a Constitution we are expounding...intended to endure for ages to come, and consequently, to be adapted to the various crises of human affairs." *Id.*, 407,415. These words are often cited as presaging the idea of a "living constitution."

³⁸ *Trustees of Dartmouth College v. Woodward*, 17 U.S. (4 Wheat.) 518 (1819). In the Court's opinion, Chief Justice Marshall described a corporation as "an artificial being ...existing only in the contemplation of law." In the early years of the twentieth century, jurists gradually began to reconfigure this into an understanding that postulated the corporation as a "real entity."

U.S. Constitution.

In the 1877 case of *Munn v. Illinois*,³⁹ the U.S. Supreme Court upheld the right of a state to regulate the rates of grain elevators charged by a company as it was deemed to be a business being conducted in the public interest.

In furtherance of the aforesaid holding, the U.S. Supreme Court ruled in 1886 in the *Railroad Commission Cases*⁴⁰ that in spite of a charter contract granting railroad companies the right to fix reasonable charges, the state retained the right to determine what was reasonable in the absence of any express provision in the contract divesting the state of such right. Nevertheless, in a significant obiter dictum, the Court indicated that the ruling did not invest the state with the right to take any action that would amount to a taking without due process of law.

This set the stage for the U.S. Supreme Court's famous decision in the 1886 case of *Santa Clara County v. Southern Pacific Railroad Company*.⁴¹ The Court's ruling in this case is conventionally understood to mean that the equal protection clause of the Fourteenth Amendment to the U.S. Constitution applied to corporations, too.⁴²

³⁹ *Munn v. Illinois*, 94 U.S.113 (1877).

⁴⁰ *Railroad Commission Cases*, 106 U.S. 307 (1886).

⁴¹ *Santa Clara County v. Southern Pacific Railroad Company*, 118 U.S. 394 (1886).

⁴² The headnote to the case in the U.S. Reports reads:

“The Court does not wish to hear argument on the question whether the provision in the Fourteenth Amendment to the Constitution, which forbids a State to deny to any person within its jurisdiction the equal protection of the laws, applies to these corporations. We are of the opinion that it does.”

Id. at 396. The actual text of the opinion of the Court, however, does not include this statement.

A corporation is not vested with the rights associated with citizenship, such as the right to vote. However, citizenship has not been considered to be an essential pre-requisite for the enjoyment of various rights enumerated in the Bill of Rights. In *First National Bank of Boston v. Bellotti*, 435 U.S. 765 (1978), the U.S. Supreme Court recognized a corporation's right to free speech under the First Amendment to the U.S. Constitution. This was later made subject to reasonable restrictions in *Austin v. Michigan Chamber of Commerce*, 494 U.S. 652 (1990). In various decisions, the U.S. Supreme Court has also recognized a corporation's constitutional rights under the First, Fourth, Fifth, Sixth, and Seventh Amendments to the U.S. Constitution. See Scott R. Bowman, *Corporate Citizenship* in *Encyclopedia of the American Constitution* at 688 (Second Edition, Edited by Leonard W. Levy and Kenneth L. Karst, Macmillan Reference, 2000).

In the 1897 case of *Allgeyer v. Louisiana*,⁴³ the U.S. Supreme Court extended the meaning of the word “liberty” as used in the Due Process Clause of the Fourteenth Amendment to the U.S. Constitution to encompass not merely the sense of freedom from physical restraint but also freedom to do all lawful acts necessary in pursuance of a lawful calling. The entity in question in this case was a corporation. However, the question of corporate personhood was not at issue as the impugned statute expressly covered corporations along with persons and firms.

Another significant U.S. Supreme Court judgment was delivered in the 1938 case, *Erie Railroad Co. v. Tompkins*.⁴⁴ In this case, the Supreme Court held that in a diversity action, provided that the Constitution or acts of Congress did not govern, it was incumbent upon federal courts to apply not only statutory law but state common law as well. In subsequent cases, the Court limited the application of this principle to state substantive law and not to procedural law. However, this had significant ramifications for the development of corporate law inasmuch as it paved the way for the rise of Delaware state law in matters relating to corporate law and governance.

A recent case relating to corporate personhood has been the decision of the U.S. Supreme Court in the case of *Federal Communications Commission v. AT&T, Inc.*⁴⁵ decided on March 1, 2011, in which the Court denied corporations the right to “personal privacy” for the purpose of Exemption 7 (C) of the Freedom of Information Act.

After the Court’s judgment in *Erie Railroad v. Tompkins*, state law, particularly Delaware state law, has played a major role in the shaping of corporate law. More than half of all publicly traded corporations in the United States are incorporated in Delaware.

Federal securities laws have important implications for companies. Some of the most important of these laws were enacted during the thirties, during the Franklin Roosevelt presidency in response to the economic crisis engendered by the Great Depression. The most prominent of these are: the Securities Act of 1933, the Securities Exchange Act of 1934, the Public Utility Holding Company Act of 1935, the Trust Indenture Act of 1939, the Investment Company Act of 1940, and the Investment

⁴³ *Allgeyer v. Louisiana*, 165 U.S. 578 (1897).

⁴⁴ *Erie Railroad Co. v. Tompkins*, 304 U.S. 64 (1938).

⁴⁵ *Federal Communications Commission v. AT&T*, 562 U.S. _____ (2011) (Decided March 1, 2011).

Advisers Act of 1940.

It would also be useful to note the antitrust or competition laws that have been enacted over the years to curb the abuse of market power by giant corporations. In response to the accelerating rise of big business during the 1880s and 1890s, the Interstate Commerce Act of 1887 was enacted with a view to shift the regulatory power from the states to the federal government. The major antitrust laws that have followed are the Sherman Antitrust Act (1890), the Clayton Antitrust Act (1914), the Federal Trade Commission Act (1914), the Robinson-Patman Act (1936), and the Celler-Kefauver Act (1950). All these Acts have had significant impact on the market activities of corporations and each was enacted in response to a felt societal need.

VI. Corporate Law and Governance as Constitutional Law:

Amidst the plethora of theories and interpretations that the Modern Corporation has been subjected to, one underappreciated point has been the ringing peroration at the end of the final chapter of the book in which Berle and Dodd liken corporate law to constitutional law for a new age. The concluding lines of the final paragraph read:

The rise of the modern corporation has brought a concentration of economic power which can compete on equal terms with the modern state – economic power versus political power, each strong in its own field. The state seeks in some aspects to regulate the corporation, while the corporation, steadily becoming more powerful, makes every effort to avoid such regulation....The future may see the economic organism, now typified by the corporation, not only on an equal plane with the state, but possibly even superseding it as the dominant form of social organization. The law of corporations, accordingly, might well be considered as a potential constitutional law for the new economic state, while business practice is increasingly assuming the aspect of economic statesmanship.⁴⁶

Although it would be a stretch to say that the corporation or any other economic organism has in fact superseded the dominance of the state, Berle and Means's statement is replete with foresight and wisdom. The collapse of mega-corporations such as Enron and Worldcom in the early years of the twenty-first century had an

⁴⁶ Berle and Means, *supra* note 1, at 313.

impact on the lives of vast numbers of shareholders and stakeholders and upon society at large in the shape of shaken confidence in corporate probity and the trustworthiness of the financial markets. This was further aggravated by the worldwide financial crisis in the latter years of the decade, triggered at least in part by failures of corporate governance in major financial institutions such as Goldman Sachs, Lehman Brothers, and others, which impacted the lives of millions in the United States and consequently in other countries across the world. These events have once again highlighted in stark relief the overriding importance of laws and norms of corporate governance for the well-being – economic and otherwise – of the people of a nation. As the *Financial Crisis Inquiry Commission Report* has pointed out: “Businesses, large and small, have felt the sting of a deep recession. There is much anger about what has transpired, and justifiably so....The collateral damage of this crisis has been real people and real communities. The impacts of this crisis are likely to be felt for a generation.”⁴⁷

Given these facts, it would not be incorrect to say that though the state remains the dominant form of social organization, and although constitutional law in its conventional sense continues to retain its pre-eminent status as the paramount law of the state, the law of corporations, along with the corporate governance norms that it engenders is almost as far-reaching in its impact and consequences as constitutional law.

The Modern Corporation was first published in 1932, during the difficult period of the Great Depression. There have been many developments and modifications in the law of corporations and in the norms of corporate governance since then. There have been see-sawing changes in the common understanding of some key concepts. There have been fluctuations in the primacy accorded to shareholders, stakeholders, managers, and directors. There have been inflections and changes in the societal understanding of the extent to which corporations have responsibility vis-à-vis society at large. In the light of some seeming contradictions within the book and Berle’s other writings, there have been divergences in the views regarding what Berle and Means really stood for and sought to canvass. There are conflicting claims about the validity of the arguments set forth by Berle and Means. There have been some deft conceptual plays such as the nexus-of-contracts approach seeking to supplant the understanding of the separation of ownership and control.

⁴⁷ *The Financial Crisis Inquiry Commission Report*, *supra* note 3, at xv and xvi.

These protean changes and vicissitudes emphasize, rather than detract from, the prescience of Berle and Means's analogizing of the law of corporations to constitutional law. It is almost otiose to say that there are fundamental differences between constitutional law and the law of corporations. The most obvious of these is regarding the amendment procedure. The onerous procedural requirement set out in Article V of the U.S. Constitution is a major hurdle to surmount if any change is sought to be made in the provisions of the constitution. That is one of the major reasons why there have been only twenty-seven amendments to the U.S. Constitution over the space of over two centuries, the last one having been enacted on May 5, 1992.

For this reason, if there is any change of political or economic circumstances or of societal understanding that requires a constitutional provision to be viewed in a new light, it falls upon the courts to articulate anew the meaning of the constitutional provisions so as to reflect accurately the changing exigencies, mores, and expectations of the zeitgeist. Corporate law is not encumbered with comparable baggage.

Strong arguments have been made to support a broader view of the constitution beyond the text that was ratified at the Philadelphia Convention in 1789 and the twenty-seven subsequent amendments.⁴⁸ Proponents of a mode of interpretation termed as "living constitutionalism" believe that the meaning of the constitution cannot remain coagulated at what it was understood to mean at some particular moment in time such as its formal ratification, but that each generation should be called upon to mould its meaning to accord with the exigencies of its own era.⁴⁹ Pragmatism is the hallmark of the principle of "living constitutionalism."

In an article in the *Harvard Law Review*, eminent constitutional scholar Bruce Ackerman has distinguished between what he terms the "official canon" and the "operational canon."⁵⁰ He describes the official canon as consisting of the Constitutional document ratified in 1789 and the subsequent amendments, but the

⁴⁸ For example, Sanford Levinson has argued for an understanding of the term "constitution" to include fundamental documents such as the Declaration of Independence and the Gettysburg Address and, beyond that, aspects of the American experience that cannot be reduced to a text at all." Sanford Levinson, *Constitutional Faith* 185 (Princeton University Press, 1988).

⁴⁹ Jack Balkin's assertion that the constitution must embody the values and aspirations of the people fits in well with the idea of a living constitution. See: Original Meaning and Constitutional Redemption, *Constitutional Commentary*, Vol.24, 427, 461-466.

⁵⁰ Bruce Ackerman, *The Living Constitution*, 120 *Harvard Law Review* 1737.

operational canon as encompassing also “superprecedents” and landmark statutes. In answer to the question whether the Constitution is a machine or an organism, Ackerman states that both sides of the argument have an element of validity. Whereas the organicists support the common law method whereby “slowly, by half steps, the common law judge senses the changing patterns of social mores and keeps the law in tune with life,”⁵¹ the mechanists base their arguments on popular sovereignty. Bruce Ackerman concludes by stating that he favors an amalgam of both views “based on two organic developments – one in political consciousness, and the other in political institutions.”⁵²

On a similar note, former U.S. Supreme Court Justice David Souter has eloquently pointed out the contradictions inherent in the Constitution.⁵³ Stating that desirable values can sometimes conflict with each other, Justice Souter states:

The constitution is a pantheon of values, and a lot of hard cases are hard because the Constitution gives no simple rule of decision for the cases in which one of the values is truly at odds with another. Not even its most uncompromising and unconditional language can resolve the potential tension of one provision with another, tension the Constitution’s Framers left to be resolved another day; and another day after that, for our cases can give no answers that fit all conflicts, and no resolutions

⁵¹ *Id.*, at 1802..

⁵² *Id.*, at 1809. Woodrow Wilson had been an early propounder of the idea of a difference between viewing the Constitution as a machine or as an organism. Woodrow Wilson, *Constitutional Government in the United States* (Columbia University Press, 1908), cited in *Encyclopedia of the American Constitution* at 1633 (Second Edition, Edited by Leonard W. Levy and Kenneth L. Karst Macmillan Reference, 2000). So also, Justice Oliver Wendell Holmes Jr., had intimated a view of the Constitution as a living organism when he stated in *Missouri v. Holland*, that the words of the Constitution

...have called into life a being the development of which could not have been foreseen completely by the most gifted of its begetters. It was enough for them to realize or to hope that they had created an organism; ... The case before us must be considered in the light of our whole experience, and not merely in that of what was said a hundred years ago.

Missouri v. Holland, 252 U.S. 416 (1920).

⁵³ Justice David D. Souter, *Harvard University’s 359th Commencement Address*, 124 *Harvard Law Review* 429 (2007).

immune to rethinking when the significance of old facts may have changed in the changing world.⁵⁴

The Modern Corporation was first published a bare two years before a major articulation of the concept of living constitutionalism in a judicial pronouncement.⁵⁵ Its apparent contradictory stance on issues also accords with Justice Souter's observation about contradictory values.

Berle and Means were remarkably perspicacious and prescient in their understanding of corporations and their growth. Subsequent developments over the decades have only confirmed and reinforced their exposition of how pervasive the hold of corporations had become in the economic, social, and political lives of individuals as employees, customers, suppliers, business competitors and as members of communities. The laws, the doctrines, and the norms of corporate law and corporate governance have fluctuated and evolved and been refined over the decades in accordance with the growth and evolution of corporations and their impact on society and the consequent change in social mores.

The ubiquity of corporations in the present era and the seeming obviousness of their virtues and vices should not obscure the originality of the insights contained in *The Modern Corporation* and the book's effectiveness in propelling them into public consciousness. Eminent thinkers and scholars such as John Kenneth Galbraith, Peter

⁵⁴ *Id.* at 435.

⁵⁵ Chief Justice Hughes in *Home Building & Loan Ass'n v. Blaisdell*, 290 U.S. 398 (1934). Writing for the Court, Chief Justice Hughes stated:

It is no answer to say that this public need was not apprehended a century ago, or to insist that what the provision of the Constitution meant to the vision of that day it must mean to the vision of our time. If by the statement that what the Constitution meant at the time of its adoption it means today, it is intended to say that the great clauses of the Constitution must be confined to the interpretation which the framers, with the conditions and outlook of their time, would have placed them, the statement carries its own refutation.

(290 U.S. 398, at 422, 443).

Justice Brennan of the U.S. Supreme Court articulated a strong case for living constitutionalism in William J. Brennan, Jr., *The Constitution of the United States: Contemporary Ratification*, 27 South Texas Law Review 433 (1986).

Justice Holmes's famous dissenting judgment in *Lochner v. New York* 198 U.S. 45 (1905), also intimated a view of the constitution as a living document, albeit in the form of judicial deference to legislative experimentation.

Drucker, and others have been influenced in various ways by *The Modern Corporation*.⁵⁶

The evolution of norms of corporate law and governance over the years are in accordance with Bruce Ackerman's ideal of a living constitution that is shaped both by the adaptation of the law to accord with changing social mores, and as developing on the basis of popular sovereignty. The enactment of the Sarbanes-Oxley Act and the Dodd-Frank Act are prominent instances of both.

The growth of corporations in the United States and the expansion of their reach and power in consonance with the changing economic, political, and social landscape have shaped the development of the law governing corporations and the norms relating to corporate governance. The principles of corporate law and the norms of corporate governance reflect Justice Oliver Wendell Holmes's famous description of the nature of law in the opening paragraph of *The Common Law*. The passage reads:

The life of the law has not been logic: it has been experience. The felt necessities of the time, the prevalent moral and political theories, intuitions of public policy,...even the prejudices which judges share with their fellow-men, have had a good deal more to do than the syllogism in determining the rules by which men should be governed. The law embodies the story of a nation's development through many Centuries, and it cannot be dealt with as if it contained only the axioms and corollaries of a book of mathematics. ... We must alternately consult history and existing theories of legislation. But the most difficult labor will be to understand the combination of the two into new products at every stage.⁵⁷

Although written with reference to the common law, Holmes's lines could aptly be used to express the idea of the living constitution.

VII. Conclusion:

The Modern Corporation and Private Property is one of the remarkable achievements

⁵⁶ See for example: John Kenneth Galbraith, *The New Industrial State* (Princeton University Press, 2007) (1967), and Peter F. Drucker, *Management: Tasks, Responsibilities, Practices* (Harper & Row, 1973).

⁵⁷ Oliver Wendell Holmes Jr., *The Common Law* 1 (Mark D. Wolfe Howe editor, Harvard University Press, 1967) (1881).

in the history of legal and economic literature. The widespread influence of the book reveals itself in the prolific scholarly study that it continues to generate. One of the myriad prescient insights that the book contains is that due to the ubiquitous growth of corporations and their impact on the lives of individuals, corporate law had become akin to constitutional law for the new era. A study of the evolution of corporate law and the norms of corporate governance over the past century lends substance to this assertion.

The Modern Corporation and Private Property (近代株式会社と私有財産) とコーポレート・ガバナンスの進化する基準

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要 約

金融危機調査委員会—これは近年の金融危機を調べるために、アメリカ合衆国が設立したものであるが、2011年1月27日にその報告書を提出した。その委員会が原因としたものが多くある中で、多くのすぐれた金融機関における、コーポレート・ガバナンスの失敗と危機管理の失敗が挙げられた。コーポレート・ガバナンスの問題が、メディアからの注目を浴びたのは、この10年で2度目のことであった。最初は、21世紀の初頭、有名な株主会社が、証券市場においてひどく信頼を喪失した時に、企業が危機に陥った。多くの理由の中でも、コーポレート・ガバナンスは、法律や経済、金融、経営や他の同族分野の中でも急成長している分野の研究となっている。Adolf Berle と Gardiner Means の著作『*The Modern Corporation and Private Property* (近代株式会社と私有財産)』は、1932年に初版がでたが、企業法とガバナンスの研究の基礎であり続けている。この本のすばらしい特徴は、その洞察と意義の豊かさであり、そのため初版から約80年経た今でも企業法の学者の間で分析され、論議をかもしたものである。『*The Modern Corporation and Private Property* (近代株式会社と私有財産)』は、企業法とガバナンスの大きな発展の短い記録とともに書かれているが、その流れでこの論文では短い説明をしている。またこの論文は、卓越しているが故に、企業法とコーポレート・ガバナンスの研究者の間で議論を重ね続けているこのテーマについて、概観を呈示している。この論文で主張しているのは、『*The Modern Corporation and Private Property* (近代株式会社と私有財産)』の十分に評価されていない側面の一つは、新しい経済時代への憲法と同様に、企業法の認識ということである。コーポレート・ガバナンスの進化し続ける基準と、時代の緊急事態へそれを適用することにより、生きた憲法主義の論文にある、一つのパターンを明らかにするものである。