THE HYBRID APPROACH: BALANCING A CORPORATION'S ECONOMIC DESIRES AGAINST ITS SOCIAL RESPONSIBILITY

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ABSTRACT

The principle of shareholder wealth maximization maintains that the ultimate objective of a corporation is to maximize the net value of a business in order to yield higher shareholder gains. Accordingly, a corporation should be governed in a manner that best achieves this objective. On the other hand, corporate social responsibility takes the position that companies have an obligation to consider the social and environmental effects of their business practices. It comes without surprise that in a capitalist society shareholder wealth maximization steals the spotlight, leaving corporate social responsibility in its shadows.

Though shareholder wealth maximization is generally perceived as the "appropriate" operating goal, this paper tackles the question of which theory corporations should employ, ultimately presenting a distinctive view of corporate governance. This paper takes a traditional approach to answering this question, tracing the evolution of each theory and the role courts played in the development of corporate governance. It notes that though courts historically sided with the shareholder wealth maximization norm, modern case law evidenced the emerging importance of corporate social responsibility.

As argued here, the company scandals that pervaded the twenty-first century, specifically the 2010 British Petroleum Oil Spill, revealed a general distrust in the business model and serve to justify a reassessed notion of corporate governance. Rather than exclusively employing one management approach over the other, corporations should employ a *hybrid approach*. The *hybrid approach* to corporate governance recognizes that the two theories can co-exist, acting as a limit on the other; it encourages corporations to maximize equity, but only to the extent that such economic objectives do not post detriments to the environment and society as a whole.

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I. INTRODUCTION

In April 2016, Senator Bernie Sanders, Democratic candidate for President, sat down with the New York Daily News to discuss his views on corporate governance in America. In his interview, Sanders blamed large corporations—in particular, General Electric—for "destroying the moral fabric of America," candidly asserting "what corporate America has shown us in the last number of years" is that "the only thing that matters is their profits and their money. And the hell with the rest of the people of this country."[1] Accordingly, Sanders advised corporations to steer away from their profit-driven approach and move towards a more "moral economy."[2] In response to Sanders, Jeffrey Immelt, chairman and CEO of General Electric, immediately retorted that General Electric's so-called "corporate greed" is not destroying the moral fabric of

[1] Interview by The Daily News Editorial Board with Sen. Bernie Sanders (April 4, 2016), http://www.nydailynews.com/opinion/transcript-bernie-sanders-meets-news-editorial-board-article-1.2588306.
[2] *Id*.

America, but is rather positively contributing to it; GE "takes risks, invests, innovates and produces in ways that today sustain 125,000 jobs."[3]

The arguments presented by both Sanders and Immelt harken back to older, fundamental questions about what a corporation's proper objective is and how corporations should be governed in light of these objectives. In fact, determining the purpose of corporations has been the focus of legal debate among courts and scholars since the development and rise of the corporate entity, resulting in the formation of two competing corporate governance theories—shareholder wealth maximization and social responsibility. On one hand, proponents of shareholder primacy and shareholder wealth maximization stand firm in their belief that the corporation's primary, and in fact, only, constituency is the shareholder, the "owner" of the business.[4] Consequently, under this model, shareholder interests are prioritized and corporate managers are given the task of maximizing corporate profits in order to increase shareholder wealth.[5] Conversely, supporters of the corporate social responsibility theory take a broader approach to corporate governance, advocating the need to consider multiple, non-shareholder constituencies.[6] These theorists believe that large corporations should have a legal duty, a social responsibility, "to take into account not only the needs of the shareholders but also other groups affected by the corporations' actions, such as its employees, customers, or the communities in which they are based." [7]

So which corporate governance theory should prevail? The purpose of this paper is to trace the development of both doctrines and ultimately argue for a reassessed notion of governance; one that balances the two theories and encourages corporations to consider the effects shareholder profit maximization has on society. This paper is structured into three parts. In Part I of this essay, I explore the shareholder wealth maximization and public responsibility approaches, respectively. I trace the evolution of the shareholder primacy model, providing a brief history of its theoretical underpinnings. Additionally, I discuss the Berle- Dodd debate, the first modern legal discussion that set out the central conceptions behind the two governance theories.

In Part II, I demonstrate the support the corporate social responsibility model garnered among courts in the post-*Dodge* era generally, and specifically in Delaware, the mainstream of corporate law. I show how though the shareholder

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[3] Jeffrey R. Immelt, *GE CEO: Bernie Sanders Says We're Destroying the Moral Fabric of America. He's Wrong*, WASH. POST (April 6, 2016), https://www.washingtonpost.com/opinions/ge-ceo-bernie-sanders-says-were-destroying-the-moral-fabric-of-america-hes-wrong/2016/04/06/8499bc8c-fc23-11e5-80e4-c381214de1a3_story.html?utm_term=.8fdc2fb3dc3e.

[4] Margaret M. Blair, *Directors' Duties in a Post-Enron World: Why Language Matters*, 38 WAKE FOREST. L. REV. 885, 886-887 (2003).

[5] *Id*. at 887.

[6] C.A. Harwell Wells, *The Cycles of Corporate Social Responsibility: An Historical Retrospective for the Twenty-First Century*, 51 U. KAN. L. REV. 77, 78 (2002).

[7] *Id*.

primacy model was once the dominant corporate governance theory among legal scholars and judges, it increasingly began to lose favor as evidenced through case law.

Finally, in Part III, I analyze the two competing theories against the backdrop of the 2010 British Petroleum oil spill. I show how flaws in the shareholder primacy theory became evident in the aftermath of the environmental disaster, consequently necessitating a shift in the corporate governance model— one that considers broader social objectives in addition to shareholder centric norms. To avoid future calamities and corporate scandals, I argue for a change in the corporate governance model; while corporations should pursue economic motives, this should not be at the expense of non-economic or social objectives. Modern corporate governance treats shareholder primacy and corporate social responsibility as mutually exclusive. Rather than approaching corporate governance in this manner, my proposition lends itself to the notion that the two theories of governance can co-exist. I refer to this as the *hybrid approach*— a theory of governance that also forces corporations to consider the implications their choices will have on society. Under this approach, corporations are encouraged to pursue their economic motives, but only to the extent that they do not pose great danger to the public. By encouraging corporations to transition from a governance model that focuses exclusively on shareholder wealth to one that also incorporates social responsibility, the goal is to decrease the occurrence of corporate scandals and disasters.

II. STOCKHOLDER INTERESTS VS. PUBLIC RESPONSIBILITY

A. The Rise of the Natural Entity Theory: Correlate to Shareholder Primacy Model

The years after the American Revolution were characterized by the emergence and growth of corporations.[8] During colonial America, corporations were formed through corporate charters that were granted directly by the government only after strict compliance with filing requirements and various other regulatory provisions. [9] The creation of corporations through such state-sanctioned charters paved the way for the emergence of the artificial entity theory, which posited the idea that corporations were "artificial creations of the state" rather than the product of "private initiative [by] individual incorporators."[10]

As the United States began its transition from colonial America into the Industrial Revolution, the slow, administrative nature of the corporate charter

[8] VALERIE P. HANS, BUSINESS ON TRIAL: THE CIVIL JURY AND CORPORATE RESPONSIBILITY 80 (2000).
[9] *Id.*
[10] David Millon, *Theories of the Corporation*, 1990 DUKE L.J. 201, 206.

system rendered it unable to respond to the fast development of industrial and urban society.[11] Due to the rapid growth of manufacturing technologies, the charter system was soon replaced with general incorporation codes, which "dispensed with the need for a special act of the legislature" and instead ordained simple procedures that could be followed by any individual seeking to incorporate. [12] "The ready availability of corporate status"[13] sparked the growth and evolution of the corporate form, consequently facilitating the formation of a new corporate philosophy—the natural entity theory.[14]

Responding to the expansion of corporate wealth, the natural entity theory replaced the outdated idea that corporate power was "artificial"—or owing its existence to the states—and suggested that corporations were "the product of a combination of entrepreneurial initiative and the natural, impersonal forces of market competition."[15] The theory's focus on "entrepreneurial initiative" signified a new perception of the corporation; central to this perception was the idea that the corporation was formed by and under the control of a group of individual owners, the shareholders.

The notion that a corporation was a "natural entity [made up of] private individuals"[16] was further expanded in a 1886 Supreme Court decision. In *Santa Clara County v. Southern Pacific Railroad*, the Court notably stated:

> 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 all of the opinion that it does. [17]

By extending the constitutional safeguards of the Fourteenth Amendment to corporations, the Court recognized that the corporate entity was a "person"—a distinct legal being free from the State. The Court's holding, illustrating the shift to the aggregate view of the corporation, "focused on the property rights of the underlying shareholders to conceive of the corporation as simply an association of individuals."[18] In treating the corporation as a separate legal being governed by individuals, the court fundamentally aligned the corporation's interests with those of the individual shareholders. Like shareholders, corporations now had the

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[11] Hans, *supra* note 8, at 80.
[12] Millon*, supra* note 10, at 206.
[13] *Id*. at 208.
[14] *Id*. at 211.
[15] *Id*. at 213.
[16] *Id*.
[17] Santa Clara County v. S. Pac. R., 118 U.S. 394, 396 (1886).
[18] Stefan J. Padfield, *Corporate Social Responsibility & Concession Theory*, 6 WM. & MARY BUS. L. REV. 1, 26- 7 (2015).

"same rights as natural persons under the Fourteenth Amendment" to pursue their own interests.[19] This modified principle viewed corporate activity as being intrinsically private in nature and consequently encouraged the promotion of shareholder economic interests.[20] Thus, the theory of the corporation as a natural entity or aggregate of individuals can be conceptualized as the precursor to the shareholder primacy model.[21]

B. Berle's Stance on Corporate Governance

In 1932, Professor Adolph A. Berle and economist Gardiner Means published the book, *The Modern Corporation & Private Property*, which traced the evolution of large corporations and discussed the "separation of ownership and control," a defining characteristic of the modern corporation.[22] According to Berle, the separation between ownership and control was caused by the growing number of corporate shareholders and their resulting geographic diffusion, thus prompting a need to localize ownership in the hands of a group of directors.[23] Not surprisingly, the emergence of these two groups—shareholders and managers—resulted in two diverging interests. On one hand, the stockholders of the corporation aimed to maximize corporate profits with the hope of yielding higher stock returns, while on the other hand the directors attempted to use their managerial power for their personal benefit. [24] In order to rectify this problem and protect shareholders, management's role had to be reassessed. For Berle and Means, this meant that managers had to be treated not only as directors of the corporation, but also as shareholder "trustees."[25]

But what does being a "trustee" mean exactly? This question sparked the Berle-Dodd debate, one of the most famous debates among legal scholars that set out the two competing approaches with respect to corporate governance—shareholder wealth maximization and corporate social responsibility. Set against the backdrop of the Great Depression, Professors Berle and E. Merrick Dodd outlined their views with respect to a corporation's purpose and the function of corporate directors.

In his 1931 Harvard Law Review article *Corporate Powers as Powers in Trust* Berle asserted, "it is the thesis of this essay that all powers granted to a corporation or to the management of a corporation….are. . .at all times

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[19] Dale Rubin, *Corporate Personhood: How the Courts Have Employed Bogus Jurisprudence to Grant Corporations Constitutional Rights Intended for Individuals*, 28 QUINNIPIAC L. REV. 523, 551 (2010).

[20] Millon, *supra* note 10, at 213.

[21] Padfield, *supra* note 18, at 27-28.

[22] ADOLF A. BERLE, JR. & GARDINER C. MEANS, THE MODERN CORPORATION & PRIVATE PROPERTY, 120 (1932).

[23] *Id*. at 139.

[24] *Id*. at 121.

[25] *Id*. at 275.

exercisable only for the ratable benefit of all the shareholders as their interest appears."[26] Implicit in his belief was the idea that the foremost "purpose of the corporation is investment."[27] Therefore, those who control the corporation must do so in a way that exclusively yields profit; they do not "assume responsibilities to the community"[28] and their "lawyers do not advise them in terms of social responsibility."[29] Thus, under Berle's view directors are primarily accountable to the corporation's shareholders and satisfy the fiduciary duty owed to such shareholders only by way of maximizing stock profits. Accordingly, Berle's shareholder wealth maximization and shareholder primacy notions leave no room for other corporate constituencies, and refuse to recognize the concept of corporate social responsibility.

Berle's shareholder wealth maximization theory was far from novel and its historical roots traced back to the 1919 seminal case *Dodge v. Ford*. In determining whether Ford Motor Company's president and majority shareholder, Henry Ford, could withhold payment of special dividends to shareholders in order to reinvest surplus capital gains in the company, the Michigan Supreme Court held:

> 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 the non-distribution of profits among stockholders in order to devote them to other purposes.[30]

Though Ford wanted to use the remaining capital to expand production, hire more employees, lower the price of the cars to assist consumers, and "spread the benefits of this industrial system to the greatest possible number,"[31] the court rejected such socially responsible objectives. Rather, the court held that managers have a duty to oversee corporate activities in a manner that financially benefits the primary, and in fact, only constituency—the shareholders. Hence, the court's shareholder-centered conception "reduced the corporation to the purely private financial interests of its owners,"[32] and excluded interests beneficial to the public.

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[26] Adolf A. Berle, Jr., *Corporate Powers as Powers of Trust,* 44 HARV. L. REV. 1049, 1049 (1931).
[27] *Id*. at 1066.
[28] Adolf A. Berle, Jr., *For Whom Corporate Managers Are Trustees,* 45 HARV. L. REV. 1365, 1367 (1932).
[29] *Id*.
[30] Dodge v. Ford Motor Co., 170 N.W. 668, 684 (Mich. 1919).
[31] *Id*. at 671.
[32] Millon, *supra* note 10, at 224.

C. Dodd's Response: Consider Social Responsibility

Professor Merrick Dodd responded to Berle, offering an opposing view. In his 1932 Harvard Law Review article, *For Whom Are Corporate Managers Trustees*, Dodd acknowledges the court's assertion in *Dodge*— that the sole function of the corporation is to generate profits for the stockholders—and explains the holding in terms of the natural entity theory.[33] Because the natural entity theory holds that corporations are a "distinct legal person" comprised of an association of stockholders, it follows that the board of directors owes a fiduciary responsibility to its individual shareholders to manage the corporation in a way that maximizes shareholder gains.[34]

Though Dodd acknowledges this as the "traditional view" of corporate governance, he advocates for an interpretive departure from the classic natural entity model, demonstrating how the natural entity theory could provide a "theoretical basis for corporate social responsibility."[35] Dodd's construction of the natural entity theory relies on the premise that since the corporation is an entity independent of its shareholders, the corporation and its shareholders have naturally conflicting interests.[36] Furthermore, as managers are the employees of the corporation and not of its shareholders, managers should prioritize the corporation's interests over those of its shareholders.[37] By subordinating the shareholder's interests to those of the corporation's, Dodd proposed a seemingly avant-garde concept of corporate governance: corporations must not only consider their "profit-making function" [38] but also their social responsibility. Public welfare provides long-term benefits to a corporation, such that corporations ought to meet certain obligations that assist constituencies other than shareholders; this includes "employees of the corporation, consumers of the products, creditors, or communities in which the corporation's plants [are] located."[39]

Dodd further demonstrated corporations' recent gravitation towards the social responsibility model when citing Owen D. Young, CEO of General Electric Co. In discussing what a business executive's role in a corporation was, Young stated the following:

> There is a rise in the notion that managers are no longer attorneys for stockholders; they are becoming trustees of an institution…If I am a trustee, who are the beneficiaries of the trust? One group

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[33] E. Merrick Dodd, *For Whom Are Corporate Managers Trustees?,* 45 HARV. L. REV. 1145, 1146 (1932).
[34] *Id*. at 1146-1147.
[35] Millon, *supra* note 10, at 216.
[36] *Id*. at 218.
[37] *Id*.
[38] Dodd, *supra* note 33, at 1148.
[39] Millon*, supra* note 10*,* at 216.

> is. . . customers and the general public. Customers have a right to demand that a concern so large shall not only do its business honestly and properly, but. . .that it shall meet its public obligations and perform its public duties.[40]

Young's argument that directors of a corporation are above all fiduciaries to the corporation itself and not to its shareholders directly correlates with Dodd's interpretation of the natural entity theory. Fundamental to Young's claim is the idea that a corporation's vast economic and political power implicates a responsibility to be a "good citizen" [41] and serve the public honestly. This corporate objective is achieved by directing managers to "use their broad powers not only for the benefit of shareholders. . .but also for the good of the general public."[42]

Evidently, General Electric has long been the focus of issues involving corporate social responsibility. In the 1920s, GE's CEO elected to supervise GE in a manner that ran parallel to the social responsibility paradigm. Yet Sanders, in his recent controversy with Immelt, contests that GE's current CEO is governing GE in a way that directly runs afoul of corporate social responsibility. If the ideologies rooted in social responsibility include corporate actions that further social good and strategies that yield a positive impact on the environment, employees, and consumers, then GE "shutting down many of the major plants in this country, sending jobs to low-wage countries, and. . . doing a good job in avoiding paying taxes," [43] is in essence repudiating social responsibility.

Finally, it is important to note that Dodd's theory was at the forefront of the corporate governance debate at a time characterized by great economic recession. Taking widespread unemployment and a general loss of confidence in the business form into account, Dodd's solution depended on businesses recognizing their responsibilities to the community and directing "corporate managers to control the businesses in a way that fulfilled those responsibilities."[44] Similarly to Dodd, I advocate for an increase in a corporation's social responsibility. The shareholder-centric view, reinforced in both Berle's approach and the holding in *Dodge*, is too narrow to adequately address the behavior of corporations in recent years. Correspondingly, remedying corporate misdeeds should depend on considering a public responsibility model of corporate governance as well.

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40 Dodd, *supra* note 33, at 1154.
41 *Id*.
42 Millon, *supra* note 10, at 220.
43 Sanders, *supra* note 1.
44 Dodd, *supra* note 33, at 1153.

III. CORPORATE SOCIAL RESPONISBILITY IN MODERN ERA

A. U.S. Courts Side with Social Responsibility

Recall that the court in *Dodge* did not cite precedent when setting forth the shareholder primacy model, yet it nonetheless became the central theory of corporate law and continued to find favor among legal scholars in the late twentieth century. Equally aligned with Berle's view was that of American economist Milton Friedman. In his article *The Social Responsibility of Business Is to Increase Its Profits*, Friedman criticized the corporate social responsibility model for its "analytical looseness and lack of rigor," [45] stating that there is "one and only one social responsibility of business—to use its resources and engage in activities designed to increase its profits."[46] Friedman's view revolved around the idea that since shareholders are responsible for selecting the corporate executives, they are, in essence, their principals; in turn, the executives are called upon to serve the interests of their principal.[47] Even if directing expenditures towards social objectives like "reducing pollution," "preventing inflation," or hiring the "unemployed"[48] would be in the corporation's best interest, such objectives would directly conflict with shareholder welfare as the corporation's employees would be "spending someone else's money for a general social interest." [49] Consequently, under Friedman's view, corporate social responsibility was not just ineffective but was also theft.[50]

In spite of the overwhelming support the shareholder primacy model has found since *Dodge*, it is important to recognize that the shareholder wealth maximization standard is not settled law. In fact, none of the fifty states have statutes that impose profit maximization on corporations, yet every state has a statute that sanctions unprofitable corporate donations.[51] Furthermore, the American Law Institute Principles of Corporate Governance explicitly permits boards of directors to "take into account ethical considerations reasonably regarded as appropriate to the responsible conduct of the firm, even if shareholder wealth is not advanced," implicating that corporate managers are not proscribed from diverting profits for the benefit of the public.[52] Thus, the Principles explicitly authorizes corporations to set aside corporate resources to advance social and philanthropic purposes even if it is at the cost of shareholder profit.

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[45] Milton Friedman, *The Social Responsibility of Business Is to Increase Its Profits,* N.Y. TIMES, Sept. 13, 1970, at 29.
[46] *Id*. at 33.
[47] *Id*. at 30.
[48] *Id*.
[49] *Id*.
[50] Harwell, *supra* note 6, at 124.
[51] Einer Elhauge, *Sacrificing Corporate Profits in the Public Interest*, 80 N.Y.U.L. REV. 733, 738 (2005).
[52] Principles of Corporate Governance: § 2.01(b)(2) (2016).

In addition, a growing trend in corporate case law has advocated for a deviation from the profit maximization standard. In *A.P. Smith Mfg. Co. v. Barlow*[53], the court determined whether a New Jersey based manufacturing company could set aside corporate funds to make a charitable contribution to Princeton University. In responding to the defendant shareholders who argued that the company was barred from using corporate funds for purposes other than maximizing shareholder profits, the New Jersey court held:

> What promotes the general good inescapably advances the corporate wealth. . .corporate contributions to Princeton and institutions rendering the like public service are. . .a matter of direct benefit to the giving corporations…The benefits derived from such contributions are nation-wide and promote the welfare of everyone.[54]

The court accordingly upheld the donation, reasoning that since corporations had abundant corporate wealth it was fitting that such societal contributions were derived from them. This is especially the case when donations are given to organizations, like universities, which promote the "democratic system of business and government"[55] through the institution of education. Moving forward, it is evident that the court in *A.P. Smith* expanded the corporation's power to designate corporate resources for philanthropic donations.

In addition, in *Shlensky v. Wrigley*[56] the shareholders of the Chicago Cubs baseball team brought a derivative suit against the board of directors arguing that the board's refusal to install lights at the baseball field for purposes of scheduling night games was contrary to the team's financial interest and welfare. Deferring to the board's business judgment, the Illinois court ruled for the defendants, holding that, "the effect on the surrounding neighborhood might well be considered by a director who was considering the patrons who would or would not attend the games if the park were in a poor neighborhood." [57] In siding with the defendants' contention that night baseball might have a deteriorating effect on the neighborhood surrounding the field, the court appears to be devaluing shareholder wealth maximization and recognizing a corporation's duty to society.

B. Public Responsibility in Delaware Law: Challenging the Profit Maximization Model

Despite the holdings in *A.P. Smith* and *Wrigley*, which unequivocally suggest that directors do not need to treat shareholder wealth maximization as

[53] A.P. Smith Manufacturing Co. v. Barlow, 97 A. 2d 186, 190 (N.J. Ch. Div 1953).
[54] *Id*. at 189.
[55] *Id*.
[56] Shlensky v. Wrigley, 95 Ill. App. 2d 173 (1968).
[57] *Id*. at 780.

their sole normative objective, legal scholars still remained unpersuaded. In his article *In Defense of the Shareholder Wealth Maximization Norm: A Reply to Professor Green*, Stephen Bainbridge remained steadfast in his support for shareholder primacy and wealth maximization, referring to it as "the fundamental norm which guides U.S. corporate decision makers."[58] Bainbridge's central argument was that "the mainstream of corporate law remains committed to the principles espoused by the Dodge court;" [59] the "mainstream" being Delaware courts as they are still the primary makers of corporate law.[60]

Though Bainbridge's argument is seemingly persuasive on its face, case law coming out of Delaware courts in more recent years has not been entirely committed to the principles embraced by the *Dodge* court. In 1969, the Delaware Supreme Court in *Theodora Holding Co v. Henderson*[61] considered the validity of a $528,000 donation to a charitable organization whose mission was to help finance a camp for underprivileged boys.[62] In its analysis, the court looked to Delaware Code Title 8 § 122. Title 8 explicitly authorized donations that were made for "the public welfare or for charitable, scientific, or educational purposes."[63] Furthermore, in citing *A.P. Smith* which approved corporate giving for educational needs[64], the court upheld the donation in the present case on the basis that the "rehabilitation and education of deprived but deserving young people is peculiarly appropriate in an age when a large segment of youth is alienated even from parents who are not entirely satisfied with our present social and economic needs." [65] Thus, absent a showing of "failure of corporate purpose, a fraudulent disregard of the minority's rights, or some other fact…[indicating] an imminent danger of great loss resulting from fraudulent. . .management,"[66] the donation was a proper corporate gift of charitable nature.

Similarly, the Delaware court did not require exclusive shareholder profit maximization in the context of takeover battles. In its 1985 decision, *Unocal Corporation v. Mesa Petroleum Co*.[67], the Delaware Supreme Court addressed the issue of whether Unocal Corporation's board of directors had the power to repurchase stock from a group of its shareholders in order to oppose a takeover threat by Mesa Petroleum.[68] In determining whether this act was within the

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[58] Stephen M. Bainbridge, *In Defense of the Shareholder Wealth Maximization Norm: A Reply to Professor Green*, 50 WASH & LEE L. REV. 1423, 1423 (1993).
[59] *Id*. at 1424.
[60] *Id*.
[61] Theodora Holding Co v. Henderson, 257 A. 2d 398 (Del. Ch. 1969).
[62] *Id*. at 401-2.
[63] 8. Del. C. § 122 (9).
[64] Theodora, *supra* note 61, at 404.
[65] *Id.* at 405.
[66] *Id.* at 406 (quoting Warshaw v. Calhoun, 221 A.2d.487 (Del. 1966)).
[67] Unocal Corporation v. Mesa Petroleum Co, 493 A. 2d 946 (Del. 1985).
[68] *Id*. at 951.

bounds of the business judgment rule, the court balanced the “threat posed” to the corporation against the “nature of the takeover bid and its effect on the corporate enterprise.” [69] Relevant factors for a board to consider when ascertaining a takeover’s effect on the corporation include: “inadequacy of the price offered, nature and timing of the offer. . .and the impact on ‘constituencies’ other than shareholders (i.e. creditors, customers, employees, and even the community in general).”[70] The court even went on to say that the interests of the “basic stockholder” were not a “controlling factor” in the board’s analysis.[71] By emphasizing the existence of other constituencies and by placing such constituencies at the forefront of the board’s decision-making process, the court seemingly rejects the shareholder primacy model for the corporate social responsibility doctrine.

Finally, in the 1989 decision *Paramount Communications v. Time*[72], the Delaware Supreme Court weighed in on yet another merger battle. When Time’s board of directors proposed a tender offer to purchase Warner’s outstanding shares at $70 per share, Time’s shareholders brought suit to prevent the merger transaction. Rather than merging with Warner, the shareholders argued that Paramount’s bid to purchase Time’s outstanding stock at $200 per share was the proper business move as it represented the shareholders’ best financial interest; Paramount’s offer would accordingly increase the corporation’s short-term shareholder profits.[73] In determining whether the board’s decision to reject Paramount’s $200 per share offer was reasonable and within the bounds of the business judgment rule, the court held that, “directors are not obliged to abandon a deliberately conceived corporate plan for a short-term shareholder profit.” [74] Because the board’s judgment would yield long-term corporate benefits—including “global expansion”[75] and “the preservation of Time’s culture i.e. it’s perceived editorial integrity in journalism”[76]— the court approved it at the expense of short- term shareholder profits. Effectively, the Delaware court’s decision allowed for a reconsideration of the shareholder wealth maximization norm, permitting managers to pursue corporate goals that did not necessarily relate to immediate measurable profit.

Theodora Holding, *Unocal*, and *Paramount*, cases coming out of the “mainstream of corporate law,”[77] all indicate a departure from the pure profit

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[69] *Id*. at 955.
[70] *Id*.
[71] *Id*.
[72] Paramount Communications v. Time, 571 A. 2d 1140 (Del. 1989).
[73] *Id*. at 1141.
[74] *Id*. at 1154.
[75] *Id*. at 1149.
[76] *Id*. at 1152.
[77] Bainbridge, *supra* note 58, at 1424.

conception of a corporation and stand for the proposition that a corporation can, in fact, have both commercial and social responsibility purposes. While several preeminent scholars exclusively support the traditional corporate model of public corporations, the assertion that a corporation is not conducted solely to maximize shareholder wealth cannot be overlooked. Corporate social responsibility does not ignore the profit maximization model entirely, but rather vies for a medium; one that recognizes other constituencies as well as the shareholder. In other words, while profit maximization is a proper goal, it should not be attained at the expense of corporate employees, the environment, and even society as a whole. Thus, shareholder wealth and social responsibility are interdependent. This so-called *hybrid approach* is especially fundamental when placed against the backdrop of corporate misdeeds that rocked the early twenty-first century.

IV. CORPORATE SOCIAL RESPONSIBILITY'S ROLE IN REBUILDING TRUST

The early twenty-first century was characterized by an onslaught of corporate scandals. Beginning with the demise of Enron in 2002, the fraudulent activities of corporate managers were brought to the public's attention. [78] Large corporations, like Enron, were engaging in risky investments, inflating accounting figures, and avoiding full disclosures, undoubtedly revealing a problem in America's capitalist driven society.[79] Though such managerial practices were beneficial to the corporation and top managers at the time, the aggressive emphasis on profit maximization and unethical strategies employed to achieve such short-term profits, yielded long-term detrimental effects on the shareholders, creditors, employees, and the general public.[80] Before long, Enron's misleading practices resulted in share price collapse and Enron went from a prominent corporation to the biggest bankruptcy in U.S. history; four thousand employees lost their jobs and investors lost billions.[81] As Enron filed for bankruptcy, several other corporate scandals arose, including WorldCom, Adelphia, and Tyco.[82]

A. In re Oil Spill

Amidst the corporate scandals of the early 2000s and the subsequent financial crisis in 2008 and 2009, yet another corporate misdeed shook the nation,

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[78] Nancy R. Mansfield, Joan T.A. Gabel, & Kathleen A. McCullough, *The Shocking Impact of Corporate Scandal on Directors' and Officers' Liability*, 20 U. MIAMI BUS. L. REV. 211, 230 (2012).

[79] *Id*.

[80] Daniel J.H. Greenwood, *Enroronitis: Why Good Corporations Go Bad*, 2004 COLUM. L. REV. 773, 774 (2004).

[81] Mansfield, Gabel, & McCullough, *supra* note 78, at 230.

[82] *Id*.

once again illustrating the flaws in the widely accepted shareholder profit maximization model. On April 20, 2010, one of the worst environmental disasters occurred off the Louisiana coast due to an explosion onboard the *Deepwater Horizon*, a drilling vessel leased by British Petroleum (BP).[83] The initial explosion and the ensuing fire, resulted in the deaths of eleven workers, dozens of injuries, and the sinking of the vessel. [84] Due to difficulties in covering the seabed oil gusher for months, millions of barrels of oil were released into the Gulf of Mexico, resulting in the largest oil spill in United States history.[85] The basic cleanup effort took a number of years, involved the help of tens of thousands of employees, cost over fourteen billion dollars, and required the use of two million gallons of dispersants in order to rectify the effects of the spill. [86] Though the dispersants helped break up the oil slicks, the chemicals used were toxic and posed environmental risks that have lasted for years.[87]

Not surprisingly, litigation ensued soon after the accident and BP found itself caught in the middle of legal crossfire. In 2014, the Eastern District Court in Louisiana set out to determine the cause of the accident and the extent of BP's liability. In the case *In re Oil Spill*, [88] the court outlined the series of events leading up to the incident, starting off with an explanation of proper deep-water drilling procedure in the specified region and the subsequent risky decisions made by the BP executives. As the United States' expert testified, "drilling in the Macondo well did not go smoothly…many of the problems stemmed from the fact that the well encountered increasingly fragile sandstone…BP was aware of this issue, but did not always manage it properly."[89]

In addition to mismanaging the delicate drilling conditions, BP also failed to properly cap important seals and stoppers along the exterior of the well and chose not to run tests that could have diagnosed the issues caused by the hasty work.[90] Such important and erroneous judgments were found to have been driven by a desire to "save time and money, rather than to ensure that the well was secure." [91] A peek into BP's financial condition further corroborated this point; as

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[83] *In re* Oil Spill by Oil Rig Deepwater Horizon, 910 F. Supp. 2d 891, 900 (E.D. La. 2012).
[84] *Id*.
[85] Alice- Azania Jarvis, *BP Oil Spill: Disaster by Numbers*, INDEPENDENT (Sept. 13, 2010), http://www.independent.co.uk/environment/bp-oil-spill-disaster-by-numbers-2078396.html, (reporting 4.9 million barrels of oil released before the leak was capped on July 15).
[86] Michael E. Miller, *Study Suggests Chemical used in BP Oil Spill Cleanup is Capable of Injuring People and Wildlife*, WASH. POST (April 7, 2015), https://www.washingtonpost.com/news/morning-mix/wp/2015/04/07/study-suggests-chemical-used-in-bp-oil-spill-cleanup-capable-of-injuring-people-and-wildlife/?utm_term=.b4f75e925f9d.
[87] *Id*.
[88] *In re* Oil Spill, 21 F. Supp. 3d 657, (E.D. La. 2014).
[89] *Id*. at 673.
[90] *Id*.
[91] *Id*. at 693.

of April 9, 2010 BP was "sixty million dollars (60-70%) over budget and 54 days behind schedule on the Macondo well.[92] For each additional day the HORIZON remained at the Macondo well, BP lost approximately another one million dollars."[93]

The court conclusively established BP's liability by presenting a transcript of a phone call between a BP senior representative and an engineer that took place thirty-five minutes before the accident. In the phone call, the men discussed the results of a pressure test conducted on the drill pipe, indicating that it was not secure. Though they acknowledged that the negative test results were likely not accurate, neither took any further action. The court stated "upon determining that the well was not secure, the drill crew would have been in a position to circulate the well back to drilling mud and return it to state of overbalance. The blowout would have been avoided." [94]

Considering the totality of the circumstances—including the high-pressure position of the Macondo well, BP's failure to conduct and accurately read the pressure test results, the lack of proper casing, and the way in which executives handled the discrepant results of the pressure tests minutes before the explosion—the court held that BP's gross negligence caused the explosion and resulting oil spill. As the court concluded, "these instances of negligence, taken together, evince an extreme deviation from the standard of care and a conscious disregard of known risks."[95]

B. Corporate Social Responsibility Shines Amidst a Disaster

How could a corporation like BP, which prides itself in responsibly producing energy that poses no harm to the environment, be the catalyst for such a tragic accident?[96] The answer to this question once again involves the two competing theories of corporate governance. In her book, *The Shareholder Value Myth: How Putting Shareholders First Harms Investors, Corporations, and the Public,* Lynn A. Stout discussed the BP oil catastrophe in light of the shareholder wealth maximization and corporate social responsibility norms.[97]As an advocate for corporate social responsibility, Stout addressed the flaws in the shareholder primacy model, arguing that its focus on stock price maximization led corporations to ignore the long-term value of their business.[98] This concentration

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[92] *Id*.
[93] *Id*. at 675.
[94] *Id*. at 705.
[95] *Id*. at 743.
[96] *People and Values*, BP Global, http://www.bp.com/en/global/corporate/about-bp/people-and-values.html (last visited April 5, 2016).
[97] Lynn A. Stout, *The Shareholder Value Myth*, UTNE READER (July 2012), http://www.utne.com/politics/shareholder-value-myth-ze0z1207zsie.aspx?PageId=2#ArticleContent.
[98] Lynn A. Stout, *The Shareholder Value Myth*, EUROPEAN FINANCIAL REVIEW (April 2013), http://www.europeanfinancialreview.com/?p=883.

detrimentally affected both financial institutions in the early 2000s, which maximized share price through their fraudulent bookkeeping methods, as well as the practices of non-financial institutions such as BP. According to Stout, the BP disaster was due to the fact that "BP paid large dividends and kept its share price high by cutting safety corners to keep expenses down."[99]

The idea that public corporations belong to their shareholders and exist for one purpose only, to maximize shareholders' wealth, is largely to blame in this disaster. BP pledged its allegiance to shareholder interests by focusing its attention on inflating stock price. Though this was in the company's best short-term interest, it came at the cost of the environment and their obligations to society as a whole. Ultimately, their decision to save money by cutting the costs of safety procedures proved to be detrimental in the long-term, both to BP and to other constituencies as well; "when tragedy finally struck, the BP oil spill damaged not only the price of BP shares, but also BP bonds, other oil companies operating in the Gulf, and the Gulf tourism and fishing industries." [100]

Along with Stout stands Professor Lawrence E. Mitchell who also condemns management's focus on short- term profits. Referring to it as a "perennial problem in corporate governance,"[101] Mitchell argues that short- term managerial focus is predominately a result of corporate directors catering to shareholder interests. [102] Mitchell's problem with the traditional theory of corporate governance is that its narrow concentration fails to consider the long-term health of a corporation and the ways in which group welfare can be maximized.[103] Rather, the shareholder primacy norm concentrates on the individual and self- interested struggles upon which American capitalism is based.[104] To rectify the narrowness of the shareholder primacy model, Mitchell recommends creating a new fiduciary duty for the board of directors—the duty not to harm. [105] When faced with a corporate decision, the duty not to harm would require the board of directors to "weigh the interests of all constituent groups," not just those of the shareholders.[106]

Likewise, economist Margaret Blair presents her own proposal in *Directors' Duties in a Post-Enron World,* arguing that a modification in the board of directors' focus is exactly what the shareholder primacy norm needs to recognize.[107] Blair's thesis suggests that the board should shift its primary focus

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[99] *Id*.
[100] *Id*.
[101] Lawrence E. Mitchell, *A Critical Look at Corporate Governance*, 45 VAND. L. REV. 1263, 1268 (1992).
[102] *Id*. at 1283.
[103] *Id*. at 1268.
[104] *Id*. at 1269.
[105] *Id*. at 1313.
[106] *Id*. at 1316.
[107] Blair, *supra* note 4, at 889.

on short-term share value and instead concentrate on the general business of the corporation. This is accomplished by developing corporate strategies, "making sure the company invests in people,. . . ideas, and reputation," and most importantly, by building "a corporate culture that supports integrity and fair play."[108] Directing the focus towards the "general business of the corporation" would remedy the current, defective structure of corporate governance and encourage the board of directors to consider other constituent groups that are fundamental to the corporation's survival as well.

V. CONCLUSION: *HYBRID APPROACH*

Undoubtedly, the corporate scandals of the twenty-first century altered society's perception of corporations, revealing a fundamental distrust in the corporate form. Overcoming this distrust requires upholding a corporation's social responsibility and steering away from an ethos that focuses predominately on profit-maximization and encourages managers to exploit those around them for the benefit of shareholders. Despite the numerous other factors that led to the oil spill disaster, blatant indifference for society's welfare undeniably had a huge impact. If anything, the BP oil spill should illustrate that prioritizing short- run profits over long-term solvency is socially harmful. Rather, a business's integrity, reputation, and the ramifications of its practices are invaluable.

Because of this, an improved notion of corporate purpose and responsibility must be conceived, one that I refer to as the *hybrid approach*. Like Stout, Mitchell, and Blair, I argue for a corporate governance theory that is a compound of the shareholder-centric norm and social responsibility. This reexamined conception requires managers to acknowledge that shareholder primacy and corporate social responsibility are not mutually exclusive, but rather function interdependently. While shareholder wealth maximization is an important corporate purpose it cannot be the central or sole focus; most importantly, it cannot be pursued at the expense of other constituencies. Accordingly, my proposition recognizes that certain limitations on corporate power do in fact exist. If a corporate act yields short-term profit and benefits, yet poses potential detriments to the public, such harms are to be acknowledged and ultimately avoided. Corporate profits should be pursued in a way that poses the least amount of danger to the environment, the economy, and society as a whole. By keeping such social obligations in mind, corporations are free to pursue their economic incentives but are also directed to suspend any behavior that may have damaging societal effects.

With the *hybrid approach* in mind, imagine if BP had been forced to weigh seriously the potential disaster in non-financial terms; imagine if it was

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[108] *Id*.

part of their corporate responsibility to give serious thought to the local constituents in the community of *Deep Horizon*. Would the result have been different?

In the end, the decision to pursue social responsibility is left up to the discretion of corporate managers. Yet in light of the environmental disasters the twenty-first century has been troubled by and amidst concerns that profit-maximizing corporations are destroying the "moral fabric of America,"[109] the decision to do so is imperative.

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[109] Sanders, *supra* note 1.