

# Observation

## Politics, Economics, and Corporate Power: The Challenge of Bureaucracy

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*In this essay Professor Deutsch addresses the question whether the legal system can make modern corporations accountable to societal ideals. Whether one believes the modern corporation can be made amenable to the popular will through law may depend upon one's conception of what defines and motivates the activities of individual citizens as members of the polity. In this context Professor Deutsch analyzes the Marxist conception of human self-definition and argues that one can understand both the persistence of corporate power and the possibility of controlling that power through law only by recognizing a richer conception of human self-definition.*

### I.

When I was a student, my corporations teacher often asked whether we had ever seen a corporation walking down the street. The query was devastating. We had learned quickly that, given the costs of litigation, the demands of profit maximization meant that corporate lawyers were paid to keep matters out of court, rather than to make law or right injustice, and that the principles of corporate law consequently were contained in remarkably few decided cases. But if those few decisions concerned an entity that existed only in the eyes of the law, it became increasingly difficult to avoid the conclusion that law, as it was applied in fact, was too artificial and uncertain to function as an effective control on corporate power.

That position was not a difficult one to take when I was a student. Existentialists proposed that the existence of things, and not their essence (or meaning), was all that one could grasp. A generation that solemnly accepted that proposition as a philosophical truth naturally would be disturbed that corporations were neither seen nor heard. It

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was but a short step from existentialism as a philosophical doctrine to acceptance of the reality presented in Hemingway's novels: a focus on the tangible, a view of the meaning of life as realized in action rather than thought and feeling, and the definition of a good life as the stylish demonstration of personal strength.

A focus on personal strength inevitably involved us in an ambivalent attitude toward combat. Hemingway's *Farewell to Arms* was our text on the futility of the war to end all wars. Yet *For Whom the Bell Tolls* was testimony that fighting for some things gave meaning to existence. For us, however, it was the Korean War—a conflict whose significance was as ambiguous as whether its resolution should be counted a victory or a defeat—that in the end provided the context in terms of which we defined ourselves. It was this context that enabled us to see *Perlman v. Feldmann*<sup>1</sup> as the case that, if properly understood, embodied all of corporate law.

Feldmann sold his controlling interest in a steel manufacturing corporation at a premium well above the market price shortly after the Korean War had begun. The purchaser was a corporation whose stockholders were users of steel. A shareholder sued, arguing that Feldmann, instead of selling, should have consummated the merger he had been negotiating prior to the sale of his stock interest. The first decision produced by the controversy, *Birnbaum v. Newport Steel Corp.*,<sup>2</sup> held that claims of fraudulent mismanagement did not give jurisdiction under section 10(b) of the Securities Exchange Act of 1934,<sup>3</sup> which bars fraud in connection with the purchase or sale of the corporation's stock. We read that decision as an example of the conceptually inadequate but politically necessary doctrinal distinctions required by the coexistence of dual state and federal sovereignties that made law in our federal system.

The transaction having withstood attack under standards embodied in the federal statutes, the Second Circuit held, in *Perlman*, that part of the premium received for control of the corporation constituted a violation of the controlling shareholder's common law fiduciary duties.<sup>4</sup> Given that steel was in short supply because of the Korean conflict, and that Feldmann took advantage of the resulting shortage, we could understand the result. Nor was it a surprise, in light of the con-

1. 219 F.2d 173 (2d Cir.), cert. denied, 349 U.S. 952 (1955).

2. 193 F.2d 461 (2d Cir.), cert. denied, 343 U.S. 956 (1952).

3. 15 U.S.C. § 78j(b) (1976).

4. 219 F.2d at 178. Sitting in diversity, the court looked to state law for the sources of its decision.

ceptual inadequacies of the *Birnbaum* rationale, that when the Second Circuit was faced with the need to describe *control* (a concept that defined the scope of the *Perlman* duty), a three-judge panel wrote three separate opinions which agreed only that there should be a full hearing in the district court.<sup>5</sup>

In a memorial essay dedicated to him, the example given of my corporations teacher's "substantive . . . sophistica[tion]" is his view of *Perlman* as "a freak case arising out of a failure of the pricing system to allocate resources."<sup>6</sup>

One can cite the prominent place of economic analysis in current law school curricula to justify characterizing reliance on economic terminology as "substantive sophistication" in analyzing the meaning of a judicial opinion. As lawyers learned during the New Deal, the use of expertise in procedural intricacies to justify substantive judicial decisions can be matched by the use of expertise in economic models to justify substantive administrative determinations. The essay written in honor of my teacher itself proposes that the problems created by shareholders' appraisal remedies be reset "into functional economic terms" and that "[i]f we are to have the remedy at all, the key point on which it should turn is the presence or absence of a market."<sup>7</sup>

How one determines the presence or absence of a market is an issue regarded as either so obvious or so technical that nothing need be said, just as no definition of "control" was attempted in *Perlman*. The analyses both in the memorial essay and in the *Perlman* opinion remain persuasive, however, despite failure even to adumbrate a concept fundamental to the result reached. The reason is captured in one of the essay's closing observations:

The dissenter's appraisal statutes are not remarkable as material for the crusader or reformer. Their major interest is intellectual.

Altogether, we can live along with the *status quo* under the appraisal statutes as they now are. They are in sickly condition. But in a world as awry as this one, they do not loom very important.<sup>8</sup>

A situation is acceptable, in other words, as long as its consequences are not regarded as sufficiently important to justify the effort required in changing the law or the socioeconomic structure. In terms

5. *Essex Universal Corp. v. Yates*, 305 F.2d 572 (2d Cir. 1962).

6. Manning, *The Shareholder's Appraisal Remedy: An Essay for Frank Coker*, 72 *YALE L.J.* 223, 225 (1962).

7. *Id.* at 260, 261.

8. *Id.* at 262 (paragraphs reversed in original).

of corporate power, for example, the cost of a mass-produced item to the consumer remains acceptable as long as the amount involved remains sufficiently small in terms of the consumer's total expenditures. Of course, the objection may be raised that consumers can unite to force the reduction of an unjustifiably inflated price, in which case the number of interested consumers required for an effective alliance would be only those who consume an amount of the product sufficient to make the amount by which corporate profits might be decreased both a matter of more than marginal interest and sufficiently large to cover costs of their organization.

Given his postulate that humans define themselves in economic terms, Marx could argue that the consumers constitute a potential class and that capitalist corporate power, since it represents the real interest of a very small group, will disappear once all socioeconomic classes have realized their interests. What this Article contends is that a more complex paradigm of self-definition than that proposed by Marx, a paradigm that encompasses groupings other than socioeconomic classes, permits explication of both the persistence of corporate power and the factors that make the multinational corporation a peculiarly disturbing phenomenon in the world of today.

## II.

The paradigm I propose is that of humans as social animals in a sense more comprehensive than the economic. The fundamentally human attribute—the only characteristic in terms of which we are wholly equal—is that of self-aware mortality. Our behavioral response to that characteristic is a purely individual matter, a fact that forms the basis for the existentialist argument that one cannot validly grasp the meaning of one's life prior to one's death. With respect to every other characteristic, however, we define ourselves in terms of group membership—we focus on qualities that make us more like some humans and less like others. An individual may feel that the meaning of his existence is entirely restricted to achieving the qualities characteristic of a particular group existing at a given time and place. Even those qualities may well undergo change if the group succeeds in achieving its goals. Moreover, as long as an individual identifies himself with more than one group, realization of the interests of any given group will fulfill only some of the goals in terms of which he determines the meaning of his life.

Marxism as a philosophical doctrine, an oversimplification of the Hegelian thought from which it was developed, restricts historically rel-

evant group membership to that of socioeconomic class. What that oversimplification makes possible, however, is a view of human history as a wholly understandable process, a vision that would allow all humans to know, and therefore act upon, their real interests. The fact is, however, that when people behave, they believe they are acting in accordance with their intentions. As a result, even a socioeconomic analysis of group behavior is incomplete in the absence of a political component that describes the ways in which groups attempt to implement their intentions.

Marxism's oversimplification of Hegelian thought lies in the claim that socioeconomic terms are sufficient for an analysis of the political component of human behavior. What makes the oversimplification acceptable is the elusive meaning Hegelian thought assigns to the political component. The concrete manifestation of political meaning is variously referred to as Spirit, World Spirit, or the Absolute. The last of these designations expresses the conjunction of the particular with the universal, the actualization of a synthesis of thesis and antithesis. As the first two designations make clear, however, it is impossible, given separate political entities, to determine at any particular moment whether the currently prevailing synthesis constitutes an international consensus or the will of a dominant state. The political component of human behavior, in short, though a necessary part of any complete description of human behavior, cannot be grasped in solely descriptive terms.

The solution to this dilemma is to use a metaphor, while remaining aware that the figure of speech may be inaccurate. Given Hegel's background as a theological student, for example, I would argue that political power in Hegelian thought performs the functions assigned by theology to the Divine Will and I would point to the fact that monarchs were legitimately invested with authority only when they were anointed as providing historical justification for use of this metaphor at the time Hegel was writing. Since relatively few of today's political entities are monarchies, however, the metaphor I propose to be relevant is God as Father rather than God as King.

Much of Western political philosophy can be viewed as a succession of interpretations of what Plato meant to convey in the dialogue known as *The Republic*. Consequently, I choose that dialogue as the context in which to apply the metaphor of political actors—whether individuals or entities—as members of an extended family. From a Marxist perspective, what is crucial about the society *The Republic* prescribes is that it consists solely of a small elite subsisting on the labor

of a vastly larger number of humans consigned to slavery. It is precisely this separation of politics and the economic task of securing a livelihood, however, that makes it possible for *The Republic* to serve as such an all-encompassing textbook of political reality. Thus, in interpersonal terms, the structure of Greek society permitted active political participants to know each other as full human beings rather than solely in their political or economic roles. What this social situation contributes to the metaphor is that, just as the Greek gods could be viewed either as a squabbling family or as aspects of a single human being, so *The Republic* can be read as a metaphor either for a single human being or a political entity.

It is the absence of a distinction between public and private self that makes the philosopher-king simultaneously a person who focuses his activities solely on grasping the essence of philosophical concepts and a politician recognized as a leader because he is trusted to achieve the life agreed upon as desirable by all. Once political power involved something more than concrete, individual human beings, however, its meaning became a matter more abstract than individual responsibility for the nature of one's life. As the franchise widened, political responsibility increasingly became a matter attributed to abstract entities rather than specific individuals. The office, in short, became eternal, although its occupants could not draw upon that attribute to surmount their own mortality.

### III.

That the perspective on human self-definition developed thus far helps in explicating the law of corporations is a proposition that can be tested only by examining cases. *In re Radom and Neidorff, Inc.*,<sup>9</sup> decided by the New York Court of Appeals in 1954, was described by Professor Chayes as an example of the "judicial solicitude for the lives of fictional persons, creatures of the law, . . . that reduces the brave new close-corporation lawyer to a helpless rage."<sup>10</sup> In that case the Court of Appeals upheld a lower court's refusal to entertain a petition for dissolution of a corporation, despite the existence of a statute specifically authorizing those petitions and a history of bitter conflict between the two stockholders.

Radom and Neidorff had run a successful business for thirty years. Radom, however, had long had unfriendly relations with his sister,

9. 307 N.Y. 1, 119 N.E.2d 563 (1954).

10. Chayes, *Madame Wagner and the Close Corporation*, 73 HARV. L. REV. 1532, 1545-46 (1960).

Anna, who was married to Neidorff. When the latter died, brother and sister became the sole and equal stockholders in the company. Radom's petition for dissolution occasioned the controversial decision of the Court of Appeals. Although Professor Chayes obviously does not find the court's opinion persuasive, he suggests that the result might be justifiable because the brother offered his sister \$75,000 for her interest shortly after her husband's death; three years later accumulated profits were \$242,000, and a court-ordered dissolution would have produced no more than \$300,000 for the two stockholders. "But Radom," concludes Chayes, "would have had the going-concern value, since he had the skill and associations to continue to operate the business while his 'partner's' widow did not. Surely, when they organized the business the two men did not contemplate this kind of bet on survivorship."<sup>11</sup>

This analysis is striking, for several reasons: the result it approves remains one impossible to reconcile with the governing statute; nothing in the corporate documents contravened the existence of a bet; and the absence of any documentary evidence normally would place at least the burden of going forward on the sister opposing the petition. Insofar as the analysis is nevertheless persuasive, I suggest it is because of the reliance on numbers, which seem real because they cannot be affected by the wishes or desires of the individuals involved. The Marxist focus on accumulated capital as the source of individual human alienation is persuasive because the numbers in terms of which capital is presented are, in this symbolic sense, not only real but of equal applicability to all human situations.

What makes both Marxism and the justification offered for the *Radom* result inadequate is that much of human behavior, whether or not provoked by or responding to economic pressures, cannot accurately be reduced to numbers. If the *Radom* result *can* be justified, the determinative issue is how brother and sister should treat each other, rather than what two businessmen might or might not have wagered. Applying the language of relationship to the context of *Perlman v. Feldmann*, the generation facing the ambiguity inherent in the Korean conflict resolved it by acting on the conviction that the interests of the United States were sufficiently related to those of South Korea to justify the efforts required to protect Korea from an expansion of Soviet power.

Post-1950s generations drew from the thought of Herbert Mar-

11. *Id.* at 1547.

cuse<sup>12</sup> a generalization of this opposition to the expansion of the power wielded by organized institutions. The generalization was that all bureaucracies have the identical impact of severely restricting the individual autonomy of persons over whom they exercise control, and that expansion of bureaucratic power—whether abroad or at home, whether Communist or capitalist—therefore necessarily represents, at worst, tyranny, and, at best, unjust domination in the name of benevolent tutelage.

Such an argument, of course, assumes that all bureaucracies, like a Communist Party in a communist state, are immune from the accountability imposed by a court of law. Since the generalization encompasses private and economic as well as public and political bureaucracies, however, it also requires the assumption that the only important economic problem is how to achieve equitable distribution or allocation. As long as an increase in the availability of material goods broadens individual autonomy, in other words, the restrictions imposed on individual behavior by bureaucracies charged with the production and distribution of material goods may be both necessary and, in social terms, benevolent.

This increase in the availability of material goods does, however, have significant social consequences. Thus, as more and more resources are devoted to mass production, the relative cost of goods readily distinguishable from those mass-produced rises, eventually making conspicuous consumption of material goods a prohibitively expensive mechanism for the definition of personal identity. One consequence of this economic process, as is apparent in demonstrations staged for the media, is that personal identity is in more and more instances defined by the presentation of self to the public as a member of a group wholly devoted to a particular political goal. The particular goal in question, usually embodied in a symbol sufficiently compelling to persuade individuals to engage in the group activity, is often a response to arbitrary application of otherwise legitimate political power. Such protests often succeed in changing the status quo by imposing effective limits on the use of political power; most of these protests, however, are too short-lived to create new symbols sufficiently effective to justify application of political power in situations other than the one that led to the protest. Continuation of a shift of the behavior in terms of which individuals define themselves from the economic to the political sphere, because

12. *E.g.*, H. MARCUSE, ONE DIMENSIONAL MAN (1964).

it would produce more demonstrations, might therefore deplete the stock of effective political symbols available to the society.

A decline in the number of effective political symbols would result in a shift of power away from political entities; the contexts for social activities structured by political symbols, and therefore political authorities, would decrease, possibly to be replaced by contexts structured by corporate hierarchies. In any event, it is less likely that political authorities would be able effectively to control corporate activity. Even if this shift does not occur, however, the amount of political and economic power wielded by corporations today makes the question of their governance a significant one. The question presented, therefore, is whether any legal system can make possible effective regulation of the governance of corporate bureaucracies.

#### IV.

In 1955 the New York Court of Appeals wrote *Rosenfeld v. Fairchild Engine and Airplane Corp.*,<sup>13</sup> a decision that appears to be a conscious attempt to create a common law governing the political aspects of competition for corporate control. The question presented concerned the use of corporate funds by both incumbent management and successful insurgents in their proxy contest. A majority of four refused to accept the three-person dissent that treated as legal only those corporate expenditures “incurred in giving widespread notice to stockholders of questions affecting the welfare of the corporation,”<sup>14</sup> presumably because that holding would have prevented incumbent management from using corporate resources even for the purpose of making a contest with insurgents, who were not so limited, an equal one in financial terms.<sup>15</sup>

The formula written into law by the majority distinguishes between “personal power” and “policy” contests, and permits corporate funds to be spent only on the latter.<sup>16</sup> As in all attempts to create formulas effectively to control human behavior, the *Rosenfeld* words are sufficiently general to permit opportunities for evasion. However, the view of law dominant in the 1950s—centered at Harvard and embodied in the scholarly work of Henry Hart and the judicial opinions of Felix Frankfurter—stressed the primary importance of the process of creating rules rather than their substantive context. The fourth member of

13. 309 N.Y. 168, 128 N.E.2d 291 (1955).

14. *Id.* at 185, 128 N.E.2d at 300 (Van Voorhis, J., dissenting, joined by Dye & Fuld, JJ.).

15. *Id.* at 172-73, 128 N.E.2d at 293.

16. *Id.* at 173-74, 128 N.E.2d at 293.

the *Rosenfeld* majority, in a concurring opinion that demonstrates the possibility of focusing on process in arriving at a substantive result, rests on a technical ruling concerning allocation of the burden of proof.<sup>17</sup> The final comment of that opinion, however, leaves open the possibility that situations may arise in which proxy campaign expenditures will be “intrinsically unlawful,”<sup>18</sup> thus raising questions, not about the applicability of the majority’s formula, but about the meaning of the precedent in which it was announced.

Whatever one reads the *Rosenfeld* rationale to mean, the fact is that few courts have applied the formula it promulgated because, as a recent California opinion put it, “every contest involves or can be made to involve issues of policy.”<sup>19</sup> The relevant issue raised by the governance of corporate bureaucracies, therefore, is not whether the proper content of the judicial formula or the appropriate process leading to its promulgation can be established, but whether the formula will in fact be applied.

A situation in which judicially promulgated rules will be applied requires for its existence individuals for whom the advantages obtained from continued membership in the groups by which they define themselves (whether those groups be ethnic, religious, political, economic or vocational) are outweighed by the commitment to hold corporate entities to the goals prescribed by societal ideals—ideals that include a corporate promise, when the State recognizes its existence, of obedience to law. The burden faced by these individuals, whether lawyers or plaintiffs, is the awareness that the lawsuit they are initiating may well be based on so individual a weighting of values that it proves unacceptable to the court and/or the relevant groups. Marxists in the German legislature at the turn of this century, for example, were the predominant representatives of proletarian political interests in Europe. Yet each of them joined in voting credits for the conduct of World War I, thus placing loyalty to the country and the party above an important promise of Marxism to the working class: release from the obligation to fight other proletarians in bourgeois wars.

The Marxist definition of proletarian interests is incomplete, this Article has argued, precisely because it defines out of existence the political component of that concept. If my analysis of Hegelian thought is correct, however, that Hegel substituted the State for God as the abstraction into which the individual projects his need to control reality,

17. *Id.* at 175, 128 N.E.2d at 294 (Desmond, J., concurring).

18. *Id.* at 176, 128 N.E.2d at 295.

19. *Braude v. Havenner*, 38 Cal. App. 3d 526, 532, 113 Cal. Rptr. 386, 389 (1974).

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then even a definition that takes the political component into account will simply be changing the rhetoric that describes a persistent mystery. What this substitution of terminology would prevent is the individual self-awareness that may prove necessary if we are to use the legal system to impose effective checks on the power wielded by corporate bureaucracies.