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SESSION ONE: THE EVOLVING ROLE OF THE BOARD OF DIRECTORS

Session One of the Paris Colloquium on Corporate Governance focused on the evolving role of the board of directors in the business corporation. The role of the board of directors has been a topic of extensive commentary and debate in recent years. The topic divides into a number of interrelated subissues.

First, the way in which a jurisdiction defines the purposes of the business corporation determines the constituencies which a board of directors must represent. A number of different constituencies could be considered significant enough to require board representation, including shareholders, employees, consumers, the general public, and environmental groups. Countries have not defined corporate purposes uniformly. In the United States, for example, it is assumed that the corporation is owned by the shareholders and that the fundamental corporate purpose, with some exceptions, is to maximize long-term profitability. In Germany, however, the principle of co-determination mandates that the interests of employees as well as shareholders be accommodated.

The second subissue is the role of nonmanagement or "outside" directors: members of the board who do not have a significant relationship with the full-time senior executives of the corporation. Outside directors have drawn increasing support as a means for the board to fulfill its responsibilities to all constituencies represented on the board.

The third critical subissue concerns the role of the board of directors in corporate governance. A board of directors may be a mere "rubber stamp" for management decisions, may actively manage the corporation, may render advice to management, and/or may monitor the performance of management in reaching corporate objectives. The literature in this area is extensive, with many commentators advocating that boards adopt a larger "monitoring" role. In reality, however, boards assume widely divergent roles depending upon such factors as the relevant country, legal structure, corporate culture, age and size of the corporation, and the extent of the public distribution of corporate stock.

The final subissue relates to the general structure of the board. Some corporations use a unitary or single-tier board structure, while others have adopted a two-tier board structure with a "management" board and a "supervisory" board. Additionally, corporations have used committees as a means of dividing up board responsibilities. The discussion of board committees is contained in Session Three of this Colloquium.

Professor Barthélémy Mercadal of the International Faculty chaired this

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session of the Colloquium. Dean Robert Mundheim, also a member of the International Faculty, opened the session by considering the purposes of business corporations. He then reviewed present-day methods for making management accountable and found each defective. He explained that the failure of these methods has focused attention on the board of directors and particularly on the outside directors as the appropriate means to fulfill a monitoring function. Dean Mundheim concluded by discussing some of the elements involved in creating an environment supportive of monitoring within the corporation.

Professor Friedrich Kübler, a member of the International Faculty, commented on Dean Mundheim's presentation from the perspective of the German corporation. He emphasized that an increasing number of countries have broadened the definition of the corporation's objectives to include not only the interests of the shareholders but also those of the employees. He also remarked that the German supervisory board has been successful in ensuring that managers meet their fiduciary responsibilities.

Mr. Pierre Louis Peaucelle examined the role of the board in the context of the French corporation, noting that the French Civil Code does not precisely define the respective powers of the board of directors and the President-Director General. Because the law is unclear, the role of the board is determined by other factors, such as the articles of the corporation and the corporation's size and financial structure. Mr. Gabriel Mathey then described the experience of a French company which had shifted to a two-tier board structure, with a directorate and a supervisory board.

A roundtable discussion of the issues raised by each of the presentations ensued. Excerpts of this discussion have been included in these proceedings.

Dean Mundheim:

I will address what I conceive to be the major task of this conference, which is to examine on a comparative basis the principles of corporate governance and structure for business corporations. Our understanding of these principles will be increased if we consider for a moment the purposes of business corporations. It seems to me that a purpose of all business corporations, at least those located in the countries of the International Faculty, is to produce goods and services efficiently. Stating the purpose of business corporations in this manner implies certain approaches to the problem of corporate governance. Other purposes, such as maintaining a particular level of employment, may indicate somewhat different approaches.

An underlying assumption of the corporation law in the United States is that a business corporation is owned by its shareholders and that these shareholders expect the corporation to maximize its long-term profitability. This assumption is embodied in the American Law Institute's (ALI) draft of the Principles of Corporate Governance and Structure [1]. The ALI is a prestigious, private U.S. institution comprised of distinguished scholars, judges and practioners. The purpose of its effort in the corporate governance field is to examine major areas of the law, restate the governing principles, and suggest directions for future developments.

Section 2.01 of the Institute's draft of the Principles of Corporate Governance and Structure assumes that a business corporation is owned by shareholders who expect the corporation to maximize the enterprise's long-term profitability [2]. The draft emphasizes long-term rather than short-term profits. Frequently, corporations find it necessary to absorb a short-term loss in order to maximize long-term profitability. For example, during the Kennedy years, when interest rates in the United States were lower than those in Europe and funds were flowing out of the United States at an unhealthy rate, Standard Oil of Indiana financed its foreign operations by borrowing overseas at higher interest rates [3]. It did so in order to forestall public criticism and the enactment of formal rules restricting the outflow of U.S. funds. In effect, the company took a short-term loss on the financing in order to retain the freedom to choose its own method of financing. More recently, United California Bank assumed the obligations of its failed Swiss subsidiary even though there was no legal obligation to do so. It absorbed a short-term loss to maintain its credibility in the international financial markets, in the belief that this action would preserve the long-term profitability of the bank.

Long-term profitability is a very broad principle, one which allows management great flexibility. However, this flexibility does not permit management to pursue every course of action which it might believe the corporation should in good conscience take. To free management to make such decisions, section 2.01 of the ALI draft contains three proposed exceptions to the principle of maximizing long-term profitability.

The first exception requires the corporation to act within the boundaries set by law to the same extent as a natural person. For example, the corporation may not bribe a government official in order to secure a lucrative contract. The second exception permits the corporation to take into account ethical principles that are generally recognized as relevant to the conduct of business. This exception, for example, permits separation payments to employees upon the liquidation of a business even though no such payments had been promised to the employees. Similarly, a business corporation would be permitted to terminate a profitable operation in the Union of South Africa because that country's apartheid policies require a treatmeent of employees that is repugnant to management. The third exception would permit the corporation to devote resources, within reasonable limits, to humanitarian, educational, and philanthropic purposes.

I believe that section 2.01 of the ALI draft fairly describes corporation law as it exists in the United States today. Corporation law in the United States emphasizes the profit maximization principle, but recognizes that the pursuit of long-term profits may necessitate short-term losses. In addition, management has some leeway to consider factors that do not enhance profitability.

A somewhat different picture emerges for corporations outside the United States, particularly those in Europe and Brazil. Under German constitutional law, for example, the principle of *Unternehmensinteresse* provides a somewhat broader basis for defining the objectives of the business enterprise. That concept assumes that there are a number of legitimate interests to be accommodated in determining the appropriate corporate action. At a minimum, these include the shareholders' interest in maximizing wealth and the workers' interest in good wages, decent working conditions, and job security. Other interests may also be relevant, such as the interests of the community in which the enterprise is located. Presently, however, only the interests of the shareholders and the employees are represented on the board of the German corporation. These two groups must bargain out, in good faith, appropriate corporate decisions. Except in an unusual case where the decision is specifically articulated as being for the sole benefit of one interest to the detriment of the other interests, it would appear that the business judgments of a German board will not be second-guessed by the courts.

A significant difference between the German system and the U.S. system is that in Germany both the interests of shareholders and the interests of employees are represented on the board of directors. It seems to me that the presence of a nonshareholder constituency on the board gives that group a greater opportunity to affect corporate decisions.

Originally, corporate ownership and control were closely linked. But the rise of the large, publicly held corporation has resulted in the divorce of ownership from control. In dealing with this development, modern corporation law attempts to provide mechanisms which ensure that management does its job efficiently and loyally. In other words, it attempts to make management accountable. I would like to focus briefly on a number of traditional mechanisms for making management accountable.

One such mechanism is the opportunity to displace management, to periodically review management's stewardship, and to vote, whether directly or indirectly, on whether to retain management. The effectiveness of this mechanism depends to some extent on full and fair disclosure of management performance. It also depends on an adequate opportunity for casting a vote, which implies some kind of proxy system [4]. Another avenue for determining whether or not to retain management is through market action, particularly the hostile tender offer [5].

A second form of control is the articulation of normative standards of conduct – *e.g.* the duty of care and the duty of loyalty – with appropriate mechanisms for enforcing adherence to those standards of conduct. Appropriate mechanisms of enforcement in the United States include both criminal sanctions (such as the penalties for embezzlement [6] and insider trading [7]) and civil remedies (such as damages for harm to the corporation caused by failure to observe the articulated norms) [8]. In the United States, criminal violations may be prosecuted by a government agency such as the Department of Justice. Civil remedies may be enforced by a government agency such as the Securities and Exchange Commission (SEC), or by private suits, both derivative and class actions.

A third method of enforcing accountability is the disclosure obligations which are designed to inform both voting shareholders and the market [9]. Disclosure, however, also has a very direct impact on corporate conduct. Many years ago Justice Brandeis characterized sunlight as the best disinfectant [10]: people are often prepared to forgo certain activities if they must disclose those activities to the public. I imagine that all of us who have counselled corporate clients that a particular transaction must be disclosed have gotten the reaction: "Well, in that case, let us not do the transaction."

Each of these three approaches (and others which I do not have time to discuss) to assure accountability has defects. For example, management controls the proxy machinery, including formulation of the issues to be presented, and a widely scattered shareholder body normally has neither the interest nor incentive to monitor management carefully or undertake the expense of organizing shareholders to act together to oppose management. The failure of these approaches to ensure management accountability, either alone or in combination, has focused increasing attention on the board of directors as the locus for providing effective monitoring of operational management [11]. Within the board, particular attention has been directed to outside directors: those members of the board who do not have a significant relationship with the full-time senior executives of the corporation.

Under U.S. law, the business and affairs of the corporation are managed under the direction of the board [12]. The formulation "under the direction of the board" recognizes that boards of directors generally do not actively manage publicly held corporations. Rather, the task of day-to-day management is confined to the senior executives chosen by the board. The board generally acts as a unit, although functions are often delegated to committees [13]. Each member of the board has power and status equal to that of any other member of the board, although as a practical matter the chairman typically has special power to call meetings, set the agenda, and appoint committees. The typical U.S. board consists of some senior executives of the corporation, several advisers to the corporation (perhaps one of the corporation's outside counsel or investment banker), and some other members who have no other significant relationship with the senior executives of the corporation. It is the last category, the outside directors, upon which the monitoring concept focuses.

Monitoring by the board, and particularly by the outside directors, has at least two advantages over other techniques. First, communication of information can be tailored to meet the needs of the individual board members. Board members can ask very specific questions and obtain answers responsive to those questions. This is very different from, for example, the generalized set of disclosures, responsive to all of the shareholders' questions that one finds in a proxy statement [14]. Second, board responses to management shortcomings can be tailored to the specific situation. The board can fire particular management, can decide not to give raises or to give lower raises, or can provide incentives for management to carry out actions deemed necessary. These flexible responses cannot be developed as easily under the other mechanisms I have talked about.

Casting the board in a monitoring role is consistent with the overall structure and functioning of the corporation. Businesses maintain internal controls with respect to operations and finances. These controls converge at the office of the chief executive. This is the level at which a need for independent monitoring arises. While management is normally in the best position to exercise business judgement about the company's affairs, there are situations when its judgement may be tainted by personal interest. A means for correcting this situation may be afforded by bringing the conflict to the attention of the independent, outside directors. In other cases, management's judgment will be unreliable because it has psychologically committed itself to a certain course of action. A critical review of this course of action by a group of outside directors is a useful corrective device. Also, as a general matter, a careful review of management's business judgment is desirable whenever proposed action can be expected to have a significant impact on the corporation.

Monitoring is essentially a review of management's judgment. The outside directors are not expected to substitute their own views for those of management. Monitoring does not contemplate a hostile or adverse attitude toward management; rather, it requires that the outside directors be alert and that they be prepared to raise questions.

At this point I would like to discuss some techniques for monitoring. The likelihood of a board successfully implementing the monitoring concept depends primarily on the ability to create an environment supportive of monitoring. There are a number of elements involved in creating this kind of supportive environment.

The first element is a critical mass of outside directors. The essential factor here is to have a sufficient number of outside directors so that they can discuss among themselves the various areas of concern and explore remedial actions. Various proposals have suggested different numbers of outside directors. A few years ago, Professor Leech and I suggested that a board of directors have at least three outside directors, depending on the work to be done [15]. In a more radical proposal, one which has not been adopted by many U.S. corporations, former SEC Chairman Harold Williams called for a board of directors comprised of all outsiders, with the exception of the chief executive officer. Presently, the ALI draft calls for a majority of outside directors [16].

This need for discussion defines the second step in creating a hospitable environment for monitoring: routine occasions for some or all of the outside directors to meet together without the intervention of inside directors. Meetings of the audit committee, for example (which is typically composed only of outside directors), offer a routine occasion for discussion among the outside directors.

The third element is the method of selecting outside directors. In the United States, outside directors are often nominated by a committee of outside directors. The ALI draft recommends that no officers or employees sit on the nominating committee and that a majority of those on the nominating committee have no significant relationships with senior executives [17]. The point here is that outside directors should not feel that they owe their selection to management.

The fourth element is that the outside directors and management should agree on the role of the outside directors. Without this mutual understanding, tension and hostility may prevail, which will diminish the efficiency of monitoring.

The fifth element is that management must ensure that outside directors receive an adequate flow of information in a form which indicates problems and alternative solutions. The outside directors must be provided with this information in a timely manner so that they may reflect on this information and develop a feel for the problems presented. As a corollary, the outside directors must have access to professional staff which will provide them with additional information and help the directors to understand the information transmitted. By "professional staff" I do not mean to imply that the directors must have a staff, inside or outside the corporation, assigned to them. Typically, directors can rely on the staff work provided by management. Of course, there may be occasions when separate professional help is necessary. In reviewing derivative litigation brought against management, the responsible committee of outside directors often retains separate counsel to advise it.

Finally, the outside directors' level of compensation should signify that the role of the outside director is significant and that a substantial time commitment and effort is required to fulfill that role adequately.

Please note that nowhere in my list have I suggested the need to split the outside directors off from the other directors in a way which would further emphasize their special responsibilities. The U.S. board functions as a unit, with each director's power and status equal to those of every other director. Creating a formal split in the board along the lines of the German board would be a sharp departure from current U.S. practice.

At this point, I would like to ask my colleague Fritz Kübler to comment on some of the issues which I have raised from the context of the German corporation.

Professor Kübler:

I have two observations relating to Dean Mundheim's comments. The first concerns the goal of commercial and business activity. Classical doctrine requires that the directors pursue the interests of the business corporation. More and more countries, such as Germany, Japan, and Switzerland, have broadened the definition of the corporation's objectives to include not only the interests of the shareholders but also those of the employees.

In Germany, this broadened definition of the corporation's interests was challenged on constitutional grounds. The Constitutional Court concluded that co-determination, that is, the participation of employees in the management of the corporation, is not an uncompensated taking of the shareholders' property rights. So long as promotion of employee interests is a proper goal of management activities, worker participation in the decision-making process is permissible [18].

My second observation concerns the supervisory board, which is a traditional element of the German corporation. These boards have been satisfactory in ensuring that managers meet their fiduciary responsibilities. No violations of these responsibilities appear in court decisions, at least with respect to large, publicly owned business corporations. This phenomenon can be easily explained. The corporation's supervisory board comprises mostly managers of other large German corporations. These people have a common interest in avoiding scandals which might cast doubt on existing corporation law, which is frequently quite favorable to management. Thus, the managers have developed a kind of professional morality that is generally respected. I believe that a similar situation exists in other European countries.

Professor Mercadal:

Thank you, Professor Kübler. Mr. Peaucelle will now discuss some of the practical problems encountered in the management and oversight of a French corporation.

Mr. Peaucelle:

Thank you very much, Mr. Chairman. I would like to examine the role of the board of directors, the manner in which the board fulfills that role, and the growing gap between the economic responsibilities and social responsibilities of the board. I know that you are all familiar with French corporation law, but I would remind you that French law calls for a management board, presided over by a President, Director General (PDG). The law, in theory, gives the same powers to the board as to the PDG.

In France, the board may manage or it may supervise. The Civil Code does not precisely define the respective powers of the board of directors, the PDG, and the deputy directors (who also may participate in the decision-making process). Because the law is unclear, a number of other factors determine whether the board manages or supervises. These factors include the articles of the corporation, which may limit the powers of the board or the PDG; the financial structure of the corporation; the traditions and history of the corporation; and the unwritten conventions governing the relationship between the shareholders and the board of directors. The sum of these competing influences will determine the role of the board.

Now let us consider the actual functioning of a French board of directors. The most important factor here is the size and financial structure of the corporation. If, for example, the business is owned and operated by an individual or a family, then a single person will make the decisions. He will, of course, ask his board of directors for advice, and he will probably have as directors people whose advice he values. But the final decision will be made by the controlling individual. This type of business structure is becoming increasingly outmoded in France.

A slightly different situation exists when the firm has a small number of stockholders. In this type of corporation there is a great need for consensus among the stockholders. Consequently, the role of the board is minimized since important decisions will be made by the directors after consultation with the stockholders.

This leads us to the large, publicly held corporation in which no single stockholder is controlling. In such a corporation, the co-optation system often permits the chairman to exercise tremendous influence over the board. The absence of a controlling shareholder frequently allows the chairman to play a decisive role in the co-opting of new directors. This power allows the chairman to shape the policies of the board, frequently limiting the board to rubber-stamping management's decisions.

Another category of corporation, the one I know best, is where at least 35% of the stock is held by a financial group or consortium. If the parent group controls a number of companies, monitoring duties will be split between the holding company's board and the subsidiary's board. In practice, either the management of the parent group or the managers of the different affiliates will jointly adopt a structure and strategic plan for the entire group. Actual monitoring of the planning process occurs at the holding company level: the parent's board ensures that decisions are made only after serious study and that the majority stockholder's interest is protected. The subsidiary's board is limited to a supervisory role – guaranteeing that the objectives of the subsidiary corporation are being pursued, that management is operating in an efficient and competent fashion, and that the law is obeyed. The subsidiary's board, in effect, monitors the interests of the subsidiary's minority stockholders. Although this division of labor was not contemplated by the legislature, the combined review by the parent and subsidary's boards does protect all interested parties.

The growing presence of large corporations in France has led us away from management by the individual to the more modern management by the group. Legislation, such as the 1966 statute, has constrained the actions of the board chairman. Consumers and government regulators, such as the Commission des Operations de Bourse, have demanded the disclosure of more and more information. These developments have forced the chairman to be a more respectful of the board. On economic questions, the chairman increasingly must defer to the board.

At the same time, French law makes the chairman solely responsible for matters pertaining to social issues. Labor negotiations, hiring and firing, and other matters are examples of social issues for which the chairman is responsible. This creates a problem in priorities: who should set policy for the corporation, the board or the chairman? Should the chairman plan for social questions and the board adapt its economic plans accordingly? Or should the reverse occur? The answer to these questions will, in large part, determine what role the board plays in managing the corporation, and how the board fulfills that role.

Professor Mercadal:

Thank you Mr. Peaucelle. Let me now give the floor to Mr. Mathey, who will describe his experience with a French company which has shifted from the traditional business corporation structure to a directorate and a supervisory board.

Mr. Mathey:

Thank you. Let me start by describing our company. CEDIS is a business corporation with a number of affiliates, having its headquarters in Besançon. At present we sell about 50000 different food and nonfood products. Except for the bottling of wines, we are purely a retail company and do no manufacturing. We have 8500 employees and 866 supermarkets with total selling area of 221000 square meters. The company was created in 1965 by the merger of four regional companies with an equity of 90 million francs. In 1977, CEDIS purchased as 93% interest in a fifth company.

I was Chairman of the Board of CEDIS from its inception in 1965 to my retirement in 1982. The board of directors consisted of myself and a number of directors from the original four companies. When the board members began to retire, we decided to give the management of CEDIS to a much younger team. In light of recent changes in the law and current trends in management, the board chose to adopt the structure of a supervisory board and a directorate. The old directors became members of the supervisory board. The directorate has five members and two deputy directors.

In our particular case, use of the directorate structuring allowed us to include two senior staff members with no equity in the company in the decision-making group. These were young, skilled people responsible in part for the success of the company. They are officially at the policy-making level.

Before changing the management structure, we studied the 1966 statute and the 1967 decree. Because the law did not precisely define the roles of the supervisory board and the directorate, we referred to the law on the board of directors. While the responsibilities of each member of the board of directors are specified by statute, the roles of the supervisory board members and the directorate are only vaguely defined. We chose to abolish the hierarchy of the usual board in favor of collective management by the directorate. Currently, decisions must be approved by a majority of the directorate; the chairman can be in the minority. The absence of formal structure is offset by an allotment of duties (unenforceable by third parties) among the directorate's members. Before the reorganization, the chairman and two executive directors controlled the major departments of the corporation. This division of power still exists, notwithstanding the fact that it violates the principle of equality of power among the directorate members. All members of the directorate are protected by working contracts allocated on the basis of their functions.

Originally, we had wanted to carefully define the relationship between the directorate and the supervisory board. We decided to eschew this approach, however, because we were afraid to create too rigid a framework. The one requirement which was placed in the corporation's Articles of Association was that the directorate must submit to the supervisory board a draft budget for the upcoming fiscal year and obtain the board's approval. In our company, this budgetary process is extremely important as it specifies, *inter alia,* the financing of the company, staffing requirements for the upcoming year, operating costs, margins and new investments. The supervisory board also has the authority to monitor the implementation of the budget and receive quarterly and annual reports concerning the company's accounts. Finally, the supervisory board (in addition to the directorate) has the power to convene the general assembly.

We have found our system satisfactory. I want to emphasize the need for a good working relationship between the chairman and the other members of the directorate. Without such cooperation the corporation will falter – no single individual can make the decisions necessary for the corporation's continued operation.

The legal status of the CEDIS structure is still unclear. There are a number of gaps in the existing law. The legislature has not properly evaluated the problems and malfunctions that are likely to arise in the operation of the new corporation. The vagueness of the statutes probably underlies the reluctance of many companies to adopt the new system of management.

Professor Mercadal:

Thank you very much, Mr. Mathey. The floor is now open to questions.

From the floor:

Can a useful comparison be made between the directorate and supervising board in France and the presence of outside directors on the U.S. board?

Mr. Mathey:

It is tempting to draw a parallel here, but the situations are quite dissimilar. In the United States, the outside directors are full participants on the board, with a special responsibility for oversight. The French case is just the opposite. Members of the directorate and supervisory board are insiders who are directly or indirectly linked to the capital and/or management of the company.

From the floor:

What are the implications of this distinction?

Mr. Mathey:

Personally, I would say that the French system of co-opting directors hinders progress of the type seen in the United States. I think we need changes in both legislation and attitudes. Such a change has begun without new legislation. More and more chairmen believe that two-thirds of the board of directors should be people who are very much involved with the functioning of the company and one-third should be outsiders. These outsiders would serve as the "moral bulwark" of the company.

Mr. Peaucelle:

I have one more comment to make. In the United States, there appears to be a consensus of opinion among legislators, the public, business leaders, and company employees on the basic goal and form of the corporation. This consensus simply does not exist in France. This difference may explain the different trends and solutions which have emerged in France to meet the problems of the corporation.

Dean Mundheim:

I would like to provide a little background on the expansion of the role of the outside director in the U.S. corporate scene. The development is relatively recent. Less than fifteen yars ago, Miles Mace, a professor at Harvard Business School, examined the board of directors in a book entitled *Myth and Reality* [19]. The "myth" was that directors acted independently and assumed responsible roles. The "reality" was that they rubber-stamped management's decisions. At about the same time a number of events caused great concern among the public. For example, the Penn Central Corporation, which had always been perceived as a reliable company, went bankrupt. The Securities and Exchange Commission report revealed that the board had done nothing to halt the slide toward bankruptcy [20]. Concurrently, it was discovered that U.S. corporations were making illegal or questionable payments both in the United States and abroad to further corporate objectives. A number of other problems in the areas of environmental protection and occupational safety also surfaced in this period.

As the public grew more concerned, corporations began to fear legislation and took steps to change the attitude and role of the outside director. Thus, public pressure and not legislation was the catalyst that effected change. As I understand it, the French situation at the present time is somewhat analogous.

Notes

[1] Restatement of Principles of Corporate Governance and Structure, section 2.01 (Tent. Draft No. 1, 1982).

[2] *Id.* The full text of section 2.01 is set out here for future reference.

§2.01. Corporate law should provide that the objective of the business corporation is to conduct business activities with a view to corporate profit and shareholder gain, except that, even if corporate profit and shareholder gain are not thereby enhanced, the corporation, in the conduct of its business:

(a) is obliged, to the same extent as a natural person, to act within the boundaries set by law,

(b) may properly take into account ethical principles that are generally recognized as relevant to the conduct of business, and

(c) may devote resources, within reasonable limits, to public welfare, humanitarian, educational, and philanthropic purposes.

[3] *See Sylvia Martin Foundation, Inc. v. Swearingen,* 260 F. Supp. 231 (S.D.N.Y. 1966).

[4] A proxy system permits the shareholder to exercise his voting rights through an agent. The term "proxy" may refer either to the agent or to the ballot cast by the agent. Companies subject to the reporting requirements of the Securities Exchange Act of 1934 (the "1934 Act") must comply with federal proxy rules. *See generally* section 14(a) of the 1934 Act, 15 U.S.C. section 78n(a) (1981), and Regulation 14A and Schedules 14A and 14B, 17 C.F.R. section 240, 14a-1,*et. seq.*

[5] A "tender offer" is an offer to purchase some or all of the shares of a corporation, usually at a premium above market price. Tender offers in which the target company is a 1934 Act reporting company are regulated by sections 13(d–e), 14(d–f) of the 1934 Act, 15 U.S.C. section 78m(d–e), section 78n(d–f) (1981).

[6] *See, e.g.,* 13 Cal. Penal Code sections §503–15 (West Supp. 1982).

[7] *See, e.g.,* section 10b of the 1934 Act, 15 U.S.C. section 78j(b) (1982); Rule 10b–5, 17 C.F.R. section 240.106–5; section 16(b) of the 1934 Act, 15 U.S.C. section 78p(b) (1982).

[8] *E.g.,* Model Business Corp. Act, section 48 (1979) (directors jointly and severally liable for improper dividend distributions and improper repurchase of outstanding shares).

[9] *See generally* L. Loss, Fundamentals of Securities Regulation 54–59 (1983).

[10] L. Brandeis, Other People's Money 92 (1914).

[11] *E.g.,* N. Leech and R. Mundheim, The Outside Director of the Publicly Held Corporation (Korn/Ferry International 1976), *reprinted in* 31 Bus. Law. 1799 (July 1976).

[12] *See, e.g.,* Model Business Corp. Act, section 42 (1978); Restatement of Principles of Corporate Governance and Structure, section 3.08 (Tent. Draft No. 1, 1982).

[13] *E.g.,* Model Business Corp. Act, Section 42 (1978); Restatement of Principles of Corporate Governance and Structure, section 3.08 (Tent. Draft No. 1, 1982).

[14] *See, e.g.,* the information required by the Securities Exchange Commission's Schedule 14A, 17 C.F.R. section 240. 14a–101.

[15] Leech and Mundheim, *supra* note 11.

[16] Restatement of Principles of Corporate Governance and Structure, section 3.03(a) (Tent. Draft No. 1, 1982).

[17] Restatement of Principles of Corporate Governance and Structure, section 3.06(a) (1) (Tent. Draft No. 1, 1982).

[18] BVerfGE 50, 290, 340 ss.

[19] M. Mace, Directors: Myth and Reality (1971).

[20] The Financial Collapse of the Penn Central Company, Staff Report of the Securities and Exchange Commission to the Special Subcommittee on Investigations, House Committee on Interstate and Foreign Commerce, 92d Cong., 2d Sess. (1972).